

Infineon

Price EUR15.34

Heading to the right direction - we are increasingly confident about the mid-term

Fair Value EUR17.5 vs. EUR16 (+14%)

BUY

Bloomberg	IFX GY
Reuters	IFXGn.DE
12-month High / Low (EUR)	15.6 / 9.4
Market Cap (EURm)	17,366
Ev (BG Estimates) (EURm)	17,609
Avg. 6m daily volume (000)	4,455
3y EPS CAGR	17.4%

Today, we take advantage of a better visibility on FQ4 2016e/FY17e to adjust our mid-term estimates of model, and take into account the solid momentum on both Automotive and Industrial sector. Overall, we raise our top-line growth estimates which leads to FY17e and FY18e EPS estimates to increase by 2%. We continue to think that the profile of Infineon is slowly but continuously improving from an investor perspective while the valuation metrics remain attractive. Following adjustments to our model, we reiterate our Buy recommendation and raise our FV from EUR16 to EUR17.5.

	1 M	3 M	6 M	31/12/15
Absolute perf.	1.6%	18.0%	25.2%	13.6%
Semiconductors	3.2%	26.3%	27.1%	22.6%
DJ Stoxx 600	-1.1%	5.6%	1.5%	-7.1%

YEnd Sept. (EURm)	09/15	09/16e	09/17e	09/18e
Sales	5,795	6,496	7,045	7,622
% change		12.1%	8.4%	8.2%
EBITDA	1,658	1,840	2,114	2,331
EBIT	898.0	995.4	1,199	1,341
% change		10.8%	20.4%	11.9%
Net income	680.0	912.0	991.8	1,105
% change		34.1%	8.7%	11.4%

	09/15	09/16e	09/17e	09/18e
Operating margin	15.5	15.3	17.0	17.6
Net margin	11.7	14.0	14.1	14.5
ROE	13.3	14.1	14.1	14.7
ROCE	18.6	14.4	15.3	16.7
Gearing	-4.7	4.8	-4.6	-14.2

(EUR)	09/15	09/16e	09/17e	09/18e
EPS	0.60	0.81	0.88	0.98
% change	-	33.6%	8.8%	11.4%
P/E	25.4x	19.0x	17.5x	15.7x
FCF yield (%)	0.5%	3.4%	4.2%	5.0%
Dividends (EUR)	0.18	0.20	0.20	0.20
Div yield (%)	1.2%	1.3%	1.3%	1.3%
EV/Sales	3.0x	2.7x	2.4x	2.2x
EV/EBITDA	10.3x	9.6x	8.1x	7.1x
EV/EBIT	19.1x	17.7x	14.3x	12.3x

ANALYSIS

- Fundamentals remain very supportive in Automotive. We raise our FY17e and FY18e estimates for the ATV division.** This branch represents about 40% of the overall business of Infineon. Despite automotive volumes might be seen as a concern by some investors in the short term, we remind that most of the growth in the automotive sector comes from content increase (more semiconductor devices per car) while higher volume of cars remain a small part of that. With the current visibility we have so far, we remain confident about a short term growth in this market segment while, on the longer term, we believe that 1/ the current footprint of Infineon in this segment, 2/ the strong and leading product portfolio in autonomous driving (ADAS) and Electric Vehicles (xEV), and 3/ the right R&D strategy with a solid IP portfolio in the next generation power semi materials of Gallium Nitride (GaN) and Silicon Carbide (SiC) that will be used in xEV, will help to consolidate a leading position and allow the group to gain market share. As such, we raise our FY17e and FY18e growth estimate for the Automotive division (~40% of sales) to +9.5% and +9% respectively (vs. previous conservative growth estimates of +5.3% and +4.3%), i.e. an outperformance of more than 2ppts compared to the automotive semiconductor market.
- Industrial power control: Infineon is set to remain the leader. We also adjust higher our IPC growth estimates for FY17e and FY18e.** Following the acquisition of International Rectifier, Infineon is now a clear market leader in power semi-conductors. The group boasts a market share of almost 19.5% (in 2015) while the second player has only one-third of it. Again, the R&D effort in GaN and SiC will help the group to consolidate its leading position and be boosted by the strong momentum. As such, we also expect Infineon to gain market share in this segment. The acquisition of Wolfspeed during summer 2016 was also a sign that the group is actively investing in future technologies in order to maintain its competitive hedge. While we have a 2015/2018e CAGR of +7.3% for industrial sector market, we now apply a FY17e and FY18e growth of 8%/8.5% respectively (vs. +4.2%/+4.2% previously) for the IPC division (c. 18% of sales). We recall, that in Power semiconductor, Infineon is uninterruptedly gaining market share since 2006. At that time, the German group had a market share of 8.5% which increased to 12.3% before the acquisition of IRF, the one helping Infineon to achieve the 19.5% level today.
- However, we adopt a slightly more cautious scenario regarding Power Management (PMM) and Chip Card & Security (CCS) divisions.** While we are convinced that the group will now be able to gain market share in Automotive and Industrial sector, we also believe Chip Card business (13% of sales) will slow down due to current high penetration rate of Chip Cards in the US and in China, two of the most dynamic regions so far. As such, we now apply a 6.0% and 5.0% growth for FY17e and FY18e for CCS division (vs. +6.9% and +6.2% previously). Similarly, we adopt a more cautious scenario for the PMM division (c. 31% of sales) which includes a "consumer" share of Infineon business as well as network infrastructure revenue and sales of power supply components for servers. We were previously using growth rate of +7.0% and +6.0% for FY17e/FY18e respectively, we now apply growth rate of 6.0% for both FY17e and FY18e.
- A 2015/2018e CAGR of 9.6% on revenue and margin improvement to come.** Following the adjustments we detailed previously, our top-line estimates shows a growth pattern of +12.1%/+8.4%/+8.2% over FY16e/ FY17e/FY18e or an average growth rate of +9.6% over the period. Regarding margins, we continue to believe that there will be an improvement thanks to 1/ the Dresden 300mm fab reaching break-even during Q4 2017 (we estimates this should help to improve operating margin by about 100bp), 2/ the pruning of legacy IRF activity/assets (mainly the Wales fab to be sold in FY17, we estimates that it should help by at least 50bp), and 3/ the positive impacts of higher volumes since Infineon is an IDM (it owns the fabs) and is sensitive to volume variations (BG ests. c. +60bp on operating margin by 2018e). As such, our FY18e operating margin comes out at 17.6%, or 210bp higher than 15.5% achieved in FY15. Overall, our new EPS estimates



are 2% higher on average compared to our previous estimates. As such, our model now points to a 17.4% EPS growth on average over FY16e to FY18e (vs. +16.8% previously).

VALUATION

- **In our view, the profile of Infineon is slowly but continuously improving from an investor perspective.** The group is now mainly focused on the two most growing market segments among a sluggish semiconductor industry: Automotive and Industrial sector. It owns strong footprint in these segments and outpaces competitors thanks to a clear strategy and rigorously selected investments in technology development. As such, the group is now a clear leader in Power Semiconductor and perfectly positioned to respond to the high demand of Electric vehicle and robotization of the industrial sector with investments in next generation power semi materials of GaN and SiC. In addition, the group also re-engineered some of its Cellular Infrastructure technology (77 GHz P2P connection) to accelerate the development of radars for ADAS, as such it is also a leader in ADAS components, another strong catalyst of automotive market. While an exposition to the Automotive market might be seen as a sign of cyclicity on the top line, we think that with most of the growth coming from content increase (vs. car production) makes it more stable than before. Finally, the group also managed to afford operational leverage with the continuous development of the 300mm fab which will be soon at breakeven.
- **And yet, with this improving profile and strong momentum, Infineon's share performance remains below SOX Index' performance over a 6 months period (25.2% vs. 27.1% respectively) leading to current attractive valuation.** Based on our estimates, Infineon's shares trade at a 2016e/2017e P/E ratios of 19.0x/18.3x respectively and a **2016e/2017e PEG ratios of 1.1x/1.1x.**
- **Following the previously mentioned adjustments in our model and updates of our valuation methods (we uses both a DCF and SOTP based on peer ratios), we raise our FV from EUR16 to EUR17.5.**

NEXT CATALYSTS

- 23 November 2016: FY16 results

New detailed P&L

[EURm]	1Q16	2Q16	3Q16	4Q16e	FY16e	FY17e	FY18e	CAGR
Total Group	1556	1611	1632	1697	6496	7045	7622	+9.6%
Seq. growth	-2.6%	+3.5%	+1.3%	+4.0%	+12.1%	+8.4%	+8.2%	
Y/Y growth	+15.4%	+8.6%	+2.9%	+6.2%	+12.1%	+8.4%	+8.2%	
Cost of goods sold	-998	-1045	-1034	-1048	-4125	-4318	-4619	
Gross margin	35.9%	35.1%	36.6%	38.2%	36.5%	38.7%	39.4%	
SG&A	-200	-195	-200	-204	-799	-888	-938	
R&D	-198	-195	-197	-203	-793	-866	-930	
Other operating income*	60	52	53	51	216	226	205	
Adj. EBIT	220	228	254	293	995	1199	1341	+14.3%
adj. operating margin	14.1%	14.2%	15.6%	17.3%	15.3%	17.0%	17.6%	
EBIT	166	174	193	257	790	969	1133	
operating margin	10.7%	10.8%	11.8%	15.1%	12.2%	13.8%	14.9%	
Net financial result	-12	-18	-12	-25	-67	-58	-56	
Income tax	-2	21	3	-35	-13	-118	-151	
tax rate	-1.3%	13.5%	1.7%	-15.0%	-1.8%	-13.0%	-14.0%	
Net income (loss)	153	180	186	191	710	792	926	
Adj. Net income (loss)	194	207	246	265	912	992	1105	
Adj. Dil. EPS (in EUR)	0.17	0.18	0.19	0.23	0.81	0.88	0.98	+17.4%

Source: Bryan Garnier & Co. ests. * Reintegration of IRF acquisition related D&A and other income & expenses

[Click here to download document](#)



Analyst :
Dorian Terral
33(0) 1.56.68.75.92
dterral@bryangarnier.com

Sector Team :
Richard-Maxime Beaudoux
Thomas Coudry
Gregory Ramirez

Bryan Garnier stock rating system

For the purposes of this Report, the Bryan Garnier stock rating system is defined as follows:

Stock rating

BUY	Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
NEUTRAL	Opinion recommending not to trade in a stock short-term, neither as a BUYER or a SELLER, due to a specific set of factors. This view is intended to be temporary. It may reflect different situations, but in particular those where a fair value shows no significant potential or where an upcoming binary event constitutes a high-risk that is difficult to quantify. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

Distribution of stock ratings

BUY ratings 55.8%

NEUTRAL ratings 32.5%

SELL ratings 11.7%

Research Disclosure Legend

1	Bryan Garnier shareholding in Issuer	Bryan Garnier & Co Limited or another company in its group (together, the "Bryan Garnier Group") has a shareholding that, individually or combined, exceeds 5% of the paid up and issued share capital of a company that is the subject of this Report (the "Issuer").	No
2	Issuer shareholding in Bryan Garnier	The Issuer has a shareholding that exceeds 5% of the paid up and issued share capital of one or more members of the Bryan Garnier Group.	No
3	Financial interest	A member of the Bryan Garnier Group holds one or more financial interests in relation to the Issuer which are significant in relation to this report	No
4	Market maker or liquidity provider	A member of the Bryan Garnier Group is a market maker or liquidity provider in the securities of the Issuer or in any related derivatives.	No
5	Lead/co-lead manager	In the past twelve months, a member of the Bryan Garnier Group has been lead manager or co-lead manager of one or more publicly disclosed offers of securities of the Issuer or in any related derivatives.	No
6	Investment banking agreement	A member of the Bryan Garnier Group is or has in the past twelve months been party to an agreement with the Issuer relating to the provision of investment banking services, or has in that period received payment or been promised payment in respect of such services.	No
7	Research agreement	A member of the Bryan Garnier Group is party to an agreement with the Issuer relating to the production of this Report.	No
8	Analyst receipt or purchase of shares in Issuer	The investment analyst or another person involved in the preparation of this Report has received or purchased shares of the Issuer prior to a public offering of those shares.	No
9	Remuneration of analyst	The remuneration of the investment analyst or other persons involved in the preparation of this Report is tied to investment banking transactions performed by the Bryan Garnier Group.	No
10	Corporate finance client	In the past twelve months a member of the Bryan Garnier Group has been remunerated for providing corporate finance services to the issuer or may expect to receive or intend to seek remuneration for corporate finance services from the Issuer in the next six months.	No
11	Analyst has short position	The investment analyst or another person involved in the preparation of this Report has a short position in the securities or derivatives of the Issuer.	No
12	Analyst has long position	The investment analyst or another person involved in the preparation of this Report has a long position in the securities or derivatives of the Issuer.	No
13	Bryan Garnier executive is an officer	A partner, director, officer, employee or agent of the Bryan Garnier Group, or a member of such person's household, is a partner, director, officer or an employee of, or adviser to, the Issuer or one of its parents or subsidiaries. The name of such person or persons is disclosed above.	No
14	Analyst disclosure	The analyst hereby certifies that neither the views expressed in the research, nor the timing of the publication of the research has been influenced by any knowledge of clients positions and that the views expressed in the report accurately reflect his/her personal views about the investment and issuer to which the report relates and that no part of his/her remuneration was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in the report.	Yes
15	Other disclosures	Other specific disclosures: Report sent to Issuer to verify factual accuracy (with the recommendation/rating, price target/spread and summary of conclusions removed).	No

A copy of the Bryan Garnier & Co Limited conflicts policy in relation to the production of research is available at www.bryangarnier.com

London	Paris	New York	Munich	New Delhi
Beaufort House	26 Avenue des Champs Elysées	750 Lexington Avenue	Widenmayerstrasse 29	The Imperial Hotel Janpath
15 St. Botolph Street	75008 Paris	New York, NY 10022	80538 Munich	New Delhi 110 001
London EC3A 7BB	Tel: +33 (0) 1 56 68 75 00	Tel: +1 (0) 212 337 7000	Germany	Tel +91 11 4132 6062
Tel: +44 (0) 207 332 2500	Fax: +33 (0) 1 56 68 75 01	Fax: +1 (0) 212 337 7002	+49 89 2422 62 11	+91 98 1111 5119
Fax: +44 (0) 207 332 2559	Regulated by the	FINRA and SIPC member		Fax +91 11 2621 9062
Authorised and regulated by the	Financial Conduct Authority (FCA) and the			Geneva
Financial Conduct Authority (FCA)	Autorité de Contrôle prudentiel et de			rue de Grenus 7
	resolution (ACPR)			CP 2113
				Genève 1, CH 1211
				Tel +4122 731 3263
				Fax+4122731 3243
				Regulated by the FINMA

Important information

This document is classified under the FCA Handbook as being investment research (independent research). Bryan Garnier & Co Limited has in place the measures and arrangements required for investment research as set out in the FCA's Conduct of Business Sourcebook.

This report is prepared by Bryan Garnier & Co Limited, registered in England Number 03034095 and its MIFID branch registered in France Number 452 605 512. Bryan Garnier & Co Limited is authorised and regulated by the Financial Conduct Authority (Firm Reference Number 178733) and is a member of the London Stock Exchange. Registered address: Beaufort House 15 St. Botolph Street, London EC3A 7BB, United Kingdom

This Report is provided for information purposes only and does not constitute an offer, or a solicitation of an offer, to buy or sell relevant securities, including securities mentioned in this Report and options, warrants or rights to or interests in any such securities. This Report is for general circulation to clients of the Firm and as such is not, and should not be construed as, investment advice or a personal recommendation. No account is taken of the investment objectives, financial situation or particular needs of any person.

The information and opinions contained in this Report have been compiled from and are based upon generally available information which the Firm believes to be reliable but the accuracy of which cannot be guaranteed. All components and estimates given are statements of the Firm, or an associated company's, opinion only and no express representation or warranty is given or should be implied from such statements. All opinions expressed in this Report are subject to change without notice. To the fullest extent permitted by law neither the Firm nor any associated company accept any liability whatsoever for any direct or consequential loss arising from the use of this Report. Information may be available to the Firm and/or associated companies which are not reflected in this Report. The Firm or an associated company may have a consulting relationship with a company which is the subject of this Report.

This Report may not be reproduced, distributed or published by you for any purpose except with the Firm's prior written permission. The Firm reserves all rights in relation to this Report.

Past performance information contained in this Report is not an indication of future performance. The information in this report has not been audited or verified by an independent party and should not be seen as an indication of returns which might be received by investors. Similarly, where projections, forecasts, targeted or illustrative returns or related statements or expressions of opinion are given ("Forward Looking Information") they should not be regarded as a guarantee, prediction or definitive statement of fact or probability. Actual events and circumstances are difficult or impossible to predict and will differ from assumptions. A number of factors, in addition to the risk factors stated in this Report, could cause actual results to differ materially from those in any Forward Looking Information.

Disclosures specific to clients in the United Kingdom

This Report has not been approved by Bryan Garnier & Co Limited for the purposes of section 21 of the Financial Services and Markets Act 2000 because it is being distributed in the United Kingdom only to persons who have been classified by Bryan Garnier & Co Limited as professional clients or eligible counterparties. Any recipient who is not such a person should return the Report to Bryan Garnier & Co Limited immediately and should not rely on it for any purposes whatsoever.

Notice to US investors

This research report (the "Report") was prepared by Bryan Garnier & Co Limited for information purposes only. The Report is intended for distribution in the United States to "Major US Institutional Investors" as defined in SEC Rule 15a-6 and may not be furnished to any other person in the United States. Each Major US Institutional Investor which receives a copy of this Report by its acceptance hereof represents and agrees that it shall not distribute or provide this Report to any other person. Any US person that desires to effect transactions in any security discussed in this Report should call or write to our US affiliated broker, Bryan Garnier Securities, LLC, 750 Lexington Avenue, New York NY 10022. Telephone: 1-212-337-7000.

This Report is based on information obtained from sources that Bryan Garnier & Co Limited believes to be reliable and, to the best of its knowledge, contains no misleading, untrue or false statements but which it has not independently verified. Neither Bryan Garnier & Co Limited and/or Bryan Garnier Securities LLC make no guarantee, representation or warranty as to its accuracy or completeness. Expressions of opinion herein are subject to change without notice. This Report is not an offer to buy or sell any security.

Bryan Garnier Securities, LLC and/or its affiliate, Bryan Garnier & Co Limited may own more than 1% of the securities of the company(ies) which is (are) the subject matter of this Report, may act as a market maker in the securities of the company(ies) discussed herein, may manage or co-manage a public offering of securities for the subject company(ies), may sell such securities to or buy them from customers on a principal basis and may also perform or seek to perform investment banking services for the company(ies).

Bryan Garnier Securities, LLC and/or Bryan Garnier & Co Limited are unaware of any actual, material conflict of interest of the research analyst who prepared this Report and are also not aware that the research analyst knew or had reason to know of any actual, material conflict of interest at the time this Report is distributed or made available.