

Melexis

Price EUR62.60

Q3 results and conference call confirmed our view

Fair Value EUR48 (-23%)

SELL

Bloomberg	MELE.BB
Reuters	MLXS.BR
12-month High / Low (EUR)	65.9 / 40.9
Market Cap (EURm)	2,529
Ev (BG Estimates) (EURm)	2,466
Avg. 6m daily volume (000)	38.00
3y EPS CAGR	5.6%

Only few more information have been given yesterday during the conference call. Melexis confirmed that R&D investments will increase from Q4 and also in FY17 adding pressure on operating margin as we expected. Overall, our investment case does not change following this call, we are convinced that, despite the company continues to deliver, Melexis valuation metrics are too high. We reiterate our Sell recommendation and our FV of EUR48.

ANALYSIS

- Margins in Q3 have been boosted by improvements in yields and product mix.** In Q3, we have seen a strong improvement in gross margin (from 45.3% in Q2 to 46.4% in Q3) mainly thanks to the resolution of the problem causing low yield at manufacturing level and also due to positive effect of product mix and higher volumes (sales in Q3 were EUR114.5m vs. EUR112.3m in Q2). We believe that most of the positive impacts of the improving yield have been passed and we expect to see lower gross margin in Q4. Nevertheless, our expectations are slightly higher than Melexis guidance for a FY16 GM at 45%, indeed, including a GM of 45.0% in Q4, our FY16e expectations is close to 45.4%.
- R&D efforts to be accelerated from Q4.** As expected, the group announced that R&D efforts will be accelerated as of Q4. Indeed, the current low level of R&D of about 13.9% of sales is far from Melexis target of 15%. However, during the call, it has been clearly stated that the R&D level would increase, both in absolute and relative terms. As such, we expect R&D expenses to represents 14.8% of sales in Q4e (also taking into account seasonality), then 15% from FY17e. In our view, this is due to the need to strengthen the expertise of Melexis and accelerate innovation in a rapidly moving market. We remind that the group's product portfolio is particularly strong in Body and Transmission but we also believe it need innovation to better fit needs for electric vehicle and autonomous cars.
- Inventory level up 11% in Q3 but we are said not to worry about it...** According to the management, the significant increase of inventory (+11% seq.) we highlighted in our first take yesterday was due to 1/ a catch up following the yielding problem at manufacturing lines and 2/ the preparation for a stronger demand Q4. Following the conference call, it looks like there is nothing to worry about at this point but we will keep a close eye on inventory level during the next publications.

VALUATION

- Overall, Q3 publication and conference call did not changed our view.** The group continue to perform as expected at top-line level and will have some pressure from opex due to the requirement to invest more heavily in R&D. We fine tuned our model, with a very limited impacts on our estiamtes (1% at EPS level on average) and no impact on our FV. **We reiterate our Sell recommendation given the very high valuation metrics.**
- Based on our estimates, Melexis' shares are trading on 2017e P/E and PEG ratios of 23.9x and 4.2x respectively.

NEXT CATALYSTS

- 8th February 2017: FY16 and Q4 results

	1 M	3 M	6 M	31/12/15
Absolute perf.	-3.7%	6.9%	33.4%	24.8%
Semiconductors	-0.6%	4.3%	29.8%	23.1%
DJ Stoxx 600	-0.7%	0.6%	-1.0%	-6.2%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	400.1	452.9	499.3	541.1
% change		13.2%	10.2%	8.4%
EBITDA	130	139	157	170
EBIT	107.6	112.7	124.3	134.7
% change		4.8%	10.3%	8.4%
Net income	99.1	95.3	107.8	116.8
% change		-3.8%	13.2%	8.4%

	2015	2016e	2017e	2018e
Operating margin	26.9	24.9	24.9	24.9
Net margin	24.8	21.0	21.6	21.6
ROE	40.9	36.1	34.6	32.1
ROCE	52.5	47.8	46.8	45.8
Gearing	-24.2	-24.0	-27.8	-31.5

(EUR)	2015	2016e	2017e	2018e
EPS	2.45	2.36	2.67	2.89
% change	-	-3.8%	13.2%	8.4%
P/E	25.5x	26.5x	23.5x	21.6x
FCF yield (%)	3.0%	3.0%	3.3%	3.7%
Dividends (EUR)	1.29	1.84	1.48	1.61
Div yield (%)	2.1%	2.9%	2.4%	2.6%
EV/Sales	6.2x	5.4x	4.9x	4.5x
EV/EBITDA	18.9x	17.7x	15.6x	14.2x
EV/EBIT	23.0x	21.9x	19.6x	17.9x



Our new estimates – P&L

[in EURm]	2015	1Q16	2Q16	3Q16	4Q16e	2016e	2017e	2018e
Sales	400	109	112	115	117	453	499	541
Seq. growth	20%	7%	3%	2%	2%	13%	10%	8%
Gross profit	192	49	51	53	53	206	234	254
Gross margin	48%	45%	45%	46%	45%	45%	47%	47%
R&D	-57	-15	-16	-16	-17	-64	-75	-81
% of sales	-14%	-13%	-14%	-14%	-15%	-14%	-15%	-15%
G&A	-19	-5	-5	-5	-5	-20	-23	-26
% of sales	-5%	-4%	-5%	-5%	-4%	-4%	-5%	-5%
S&M	-9	-2	-2	-2	-2	-9	-11	-12
% of sales	-2%	-2%	-2%	-2%	-2%	-2%	-2%	-2%
EBIT	108	28	28	30	28	113	124	135
Operating margin	27%	25%	25%	26%	24%	25%	25%	25%
Financial result	2	-1	0	-1	1	-1	2	3
% of sales	0%	-1%	0%	-1%	1%	0%	1%	1%
Income Tax	-10	-4	-5	-4	-4	-16	-19	-21
Income tax rate	-10%	-14%	-16%	-13%	-15%	-15%	-15%	-15%
Net Profit	99	23	23	25	24	95	108	117
Net margin	25%	21%	21%	22%	21%	21%	22%	22%
Dil. EPS	2.45	0.57	0.57	0.62	0.60	2.36	2.67	2.89
EPS seq. growth	17%	4%	1%	9%	-4%	-4%	13%	8%

Sources: Bryan, Garnier & Co. ests.

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

Sector Team :
Richard-Maxime Beaudoux
Thomas Coudry
Gregory Ramirez

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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
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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
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