

STMicroelectronics

Price EUR7.22

Q3 adjusted results a penny above expectations, while Q4 outlook is supportive

Fair Value EUR6.5 (-10%)

NEUTRAL

Bloomberg	STM FP
Reuters	STM.FR
12-month High / Low (EUR)	7.5 / 4.6
Market Cap (EUR)	6,581
Ev (BG Estimates) (EUR)	5,928
Avg. 6m daily volume (000)	2,315
3y EPS CAGR	33.4%

	1 M	3 M	6 M	31/12/15
Absolute perf.	1.1%	22.7%	38.8%	16.9%
Semiconductors	0.1%	3.0%	29.9%	22.8%
DJ Stoxx 600	0.5%	0.1%	-1.6%	-6.6%

YEnd Dec. (USDm)	2015	2016e	2017e	2018e
Sales	6,897	6,977	7,102	7,261
% change		1.2%	1.8%	2.2%
EBITDA	910	977	1,143	1,286
EBIT	174.0	251.0	404.1	531.3
% change		44.3%	61.0%	31.5%
Net income	175.0	178.8	303.8	411.6
% change		2.2%	69.9%	35.5%

	2015	2016e	2017e	2018e
Operating margin	2.5	3.6	5.7	7.3
Net margin	2.5	3.1	4.3	5.7
ROE	2.2	3.8	6.5	8.6
ROCE	5.1	4.7	8.2	11.5
Gearing	-10.5	-14.0	-18.4	-23.0

(USD)	2015	2016e	2017e	2018e
EPS	0.20	0.20	0.34	0.47
% change	-	2.4%	68.9%	37.1%
P/E	36.4x	35.5x	21.0x	15.3x
FCF yield (%)	4.1%	5.8%	7.5%	9.1%
Dividends (USD)	0.40	0.24	0.30	0.39
Div yield (%)	5.5%	3.3%	4.2%	5.5%
EV/Sales	0.9x	0.8x	0.8x	0.8x
EV/EBITDA	6.7x	6.1x	5.0x	4.3x
EV/EBIT	35.0x	23.6x	14.1x	10.3x

Q3 sales came out at USD1.797bn, up 5.5% seq., in line with company guidance and broadly in line with expectations. The gross margin improved from 33.9% in Q2 to 35.5% in Q3, yielding Adjusted EBIT of USD119m and adjusted EPS of USD0.11, i.e. a penny above expectations for Adjusted EPS of 0.10 (BG ests. USD0.08). In addition, the group continues to enjoy healthy demand in the market it serves and Q4 2016 revenue guidance is ahead of the street's estimates with revenues set to grow 3.2% (+/- 350bp) sequentially, i.e. sales slightly above USD1.850bn, while current forecasts were for USD1.802bn (BG ests. USD1,868m) and GM is expected to be close to 37.0% vs. cons. at 36.1%.

ANALYSIS

- ST reported Q3 adjusted results in line with the street's expectations.** The company reported Q3 revenues of USD1.797bn, up 5.5% seq. (+1.9% yoy or +3.4% excluding businesses undergoing a phase-out) compared with group's guidance for a revenue up 5.5% sequentially (+/- 350bp) to about USD1.800bn, and consensus expectations at USD1.804bn or revenue up 5.9% sequentially. Gross margin came in at 35.8%, about 30bps above company's guidance (35.5%) and the street's forecasts of GM at 35.5% (BG ests. 35.4%). Combined R&D and SG&A (net of grants) in Q3 decreased slightly to USD524m vs. USD537m in Q2 2016. As a result, adjusted EBIT was above expectations at USD119m (cons. USD103m/BG ests. USD97m) (non-adjusted EBIT of USD90m) and **Adjusted EPS came in at USD0.11 (non-adjusted EPS of USD0.08), i.e. a penny above the consensus** (cons. USD0.10/BG ests. USD0.08). Finally, the group generated positive cash flow of USD100m in Q3 compared with USD47m in the previous quarter. Inventory levels were down -2% to USD1.238bn vs. USD1.266bn at the end of Q2 2016.
- Almost all of ST's business enjoyed strong momentum in Q3.** The group says that it has been helped by a continuous pervasiveness of its products in flagship smartphones, especially Time-of-Flight technology. Also, the STM32 family of microcontroller is said to have a continuous strong traction in Internet of Things applications. Finally, the automotive products sales is growing yoy and the industrial sector remains supportive. The Automotive and Discrete group (ADG) revenue in Q3 stood at USD704m (flat yoy and down 2.4% seq.). The Analog & MEMS Group (AMG) revenue stood at USD403m (down 2% yoy but up 7.2% compared to Q2 2016). The Microcontrollers & Digital ICs Group (MDG) revenue came out at USD587m (flat compared to Q3 2015 but up 5.6% seq.). And revenue from other products (mainly imaging) was up significantly in Q3 to USD103 compared to USD50m in Q2 2016 and USD57m in Q3 2015. The group also reiterated that, during the quarter, the acquisition of NFC and RFID reader assets from ams (Neutral, FV CHF27) has been completed.
- Q4 2016 revenue guidance also came out above expectations.** The demand in smartphone market is said to be strong and we believe this is mainly due to a design in of Time-of-Flight product in the Apple iPhone 7. The industrial and automotive market are also said to have sustained strong momentum. As such, STMicroelectronics expects Q4 2016 sales to increase sequentially by 3.2% (+/-350bp) to about USD1.855bn, above the consensus forecast for revenue of USD1.802bn (BG ests. USD1.868bn). Regarding the gross margin, it is expected to come out at a level of about 37.0%, up 120bps compared to Q3 2016 and 90bps above Street's expectations. As such, for the FY16, ST should see a 1% growth of its top-line and improving margin as we expected.

VALUATION

- Based on our estimates, STMicroelectronics' shares are trading on 2017e EV/Sales and EV/EBIT ratios of 0.6x and 21.0x respectively.

NEXT CATALYSTS

- Today: Q3 results conference call (9:30am, CET)
- Late January 2017: FY16 and Q4 results.



Reported Q3 2016 vs. estimates

[USDm]	BG ests. 3Q16e	Consensus 3Q16e	3Q16 Actual	Actual vs. Cons.
Net revenue	1,794	1804	1797	-0.4%
% change (seq)	5.3%	5.9%	5.5%	-40bp
% change (yoy)	1.7%	2.3%	1.9%	-39bp
Gross Margin	35.4%	35.5%	35.8%	30bp
SG&A + R&D (net)	-537	-	-524	-
Adj. EBIT (Non-GAAP)	97	103	119	16.1%
% of revenue	5.4%	5.7%	6.6%	94bp
Adj. EPS (in USD)	0.08	0.10	0.11	10.0%

Sources: Thomson Reuters I.B.E.S; Bryan, Garnier & Co ests.

Guidance Q4 2016 vs. estimates

[USDm]	BG ests. 4Q16e	Consensus 4Q16e	4Q16 Guidance	Guid. vs. Cons.
Net revenue	1868	1802	1855	2.9%
% change	4.1%	-0.1%	3.2%	328bp
Gross Margin	37.8%	36.1%	37.0%	90bp
Adj. EPS (in USD)	0.14	0.10		

Sources: Thomson Reuters I.B.E.S; Bryan, Garnier & Co ests.

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