

Bloomberg	AMS SW
Reuters	AMS.S
12-month High / Low (CHF)	39.3 / 23.0
Market Cap (CHFm)	2,217
Ev (BG Estimates) (CHFm)	2,469
Avg. 6m daily volume (000)	466.2
3y EPS CAGR	9.5%

Yesterday, ams gave more details regarding the acquisition of Heptagon during a conference call. Today, we are convinced that the acquisition was the only solution left to ams in order to maintain its slot in Apple's smartphones. With the future being sensor fusion, ams had to propose a truly innovative value-added solution to Apple, including a complete advanced integrated module embedding at least true-tone and ToF sensors. Stuck in this battle, competing with STMicroelectronics (Neutral, FV EUR6.5), we believe ams struck the decisive blow by acquiring Heptagon. The question is, was it worth taking such a scorched earth approach? We think so! Nevertheless, the acquisition impacts our near- and mid-views. As such, we trim our FV to CHF27 (vs. CHF29 previously) and keep our Neutral recommendation.

	1 M	3 M	6 M	31/12/15
Absolute perf.	-10.9%	8.4%	-1.3%	-10.0%
Semiconductors	0.3%	6.2%	30.8%	24.2%
DJ Stoxx 600	-0.3%	1.2%	-1.2%	-5.9%

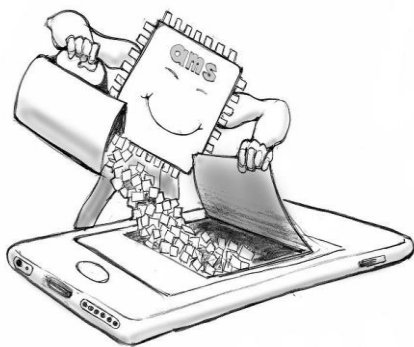
YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	623.1	545.8	660.2	792.8
% change		-12.4%	20.9%	20.1%
EBITDA	195	152	194	253
EBIT	162.2	95.9	152.5	214.8
% change		-40.9%	59.1%	40.9%
Net income	148.7	94.9	116.2	168.1
% change		-36.2%	22.5%	44.7%

	2015	2016e	2017e	2018e
Operating margin	26.0	17.6	23.1	27.1
Net margin	23.9	17.4	17.6	21.2
ROE	21.8	14.9	16.8	19.6
ROCE	18.7	11.5	15.6	21.1
Gearing	19.3	35.7	12.4	-3.6

(EUR)	2015	2016e	2017e	2018e
EPS	2.08	1.05	1.86	2.73
% change		-49.6%	77.1%	47.3%
P/E	13.4x	26.7x	15.1x	10.2x
FCF yield (%)	3.6%	0.4%	6.6%	8.4%
Dividends (EUR)	0.32	0.49	0.33	0.42
Div yield (%)	1.1%	1.8%	1.2%	1.5%
EV/Sales	3.5x	4.2x	3.3x	2.5x
EV/EBITDA	11.2x	15.1x	11.0x	8.0x
EV/EBIT	13.5x	23.8x	14.1x	9.4x

ANALYSIS

- Grabbing more market share in the iPhone.** Following our first take published yesterday morning ([see here](#)), we now have more details regarding the acquisition, but also on business momentum in the near term. First, regarding the deal: we learned that Heptagon's top customer represents about 80% of Heptagon's business. We have the strong conviction that this customer is Apple. Management also says that, on the basis of the combined revenue of 2017e, this customer would then represent about 30% of the business. Given that Apple represents about 20% of ams sales before the deal, this confirms our first thought regarding the name of the client. This customer is the one that provided a strong commitment which we believe is a multi-year commitment. After this deal, ams should be 3 to 4x larger than its main competitor (our investment strategy focuses on small but highly verticalised players in the semiconductor industry, [see here](#)).
- Earn-out to be paid only if Heptagon delivers expected top-line growth.** Another clarification during the conference call: the USD270m earn-out payment is linked to top-line growth, not margins. In this payment, the portion of cash will be more important than stock part (incl. stock from treasury) and it is said to kick in at a USD200m level (however we have no detail regarding the expected performance level required to trigger the payment).
- This confirms our view that the acquisition will not be accretive before 2018e at best.** During the conference call, the group said that Heptagon's margin should remain in negative territory during H1 2017, then possibly move to positive territory as of H2 2017. This makes sense if we expect a design-in in the iPhone. As such, it is possible to see a (very limited) positive impact on EBIT as of FY17. However, we note the very cautious tone of management when making this comment. In our view, this confirms that the acquisition will not be accretive before 2018e at EPS level, at best (including all the impacts of the acquisition).
- ams' standalone business and FY17e expectations are not impacted by the acquisition nor the short term slowdown.** According to the management, 2017 should be a strong year, this is not new but we had a confirmation that the deal will not impact the opportunities the next year. In addition, ams says to work hard on the yield issue impacting Q4 and expects it to be resolved by Q1 2017, i.e. it should have a limited impact on Q1 2017 and FY17e then. We understand it is due to problems linked to the rapid ramp up of an industrial product at a manufacturing partner's site. As such, neither the yield problem nor the Heptagon acquisition impacts our view on FY17e. Conversely, Heptagon adds new opportunities and the acquisition should not be seen as signalling a slowdown according to ams. Nevertheless, we now adopt a more cautious approach when modelling FY17e on a standalone basis (details given below).
- To sum up, our view is that ams has been put under pressure by one of its largest customer** (we believe it is Apple) to offer a highly integrated solution including two very important technologies, namely ambient light sensors and Time of Flight (ToF), into a single package able to offer a bezel-free (no visible frame around the screen) smartphone. Currently, the iPhone 7 uses ToF components from STMicroelectronics (Neutral, FV EUR6.5) and an Ambient Light Sensor from ams. With the needs for more integrated sensors, a trend called Sensor Fusion (resulting in products named sensor hubs), we think that ams has no other choice than invest in a differentiating technology in order to offer higher value-added products than ST. The solution is the strategic acquisition of Heptagon, currently working with ST on Wafer-Level optic packaging to supply Apple.



VALUATION

- **Expensive for investors but necessary to support the LT development of ams.** We have tuned our model in order to include 1/ the impact of the stronger than expected Q3 2016, 2/ the impact of the lower-than-expected Q4 2016, 3/ a more cautious approach regarding FY17e and FY18e on a standalone basis. We move away from the FY19e group target of revenue close to EUR1bn but given latest update, we believe a more cautious approach is required when modelling FY17e and FY18e. The result is a negative impact of 3% on average on our 3Y EPS estimates (details are given in the table below). We also modelled the impact of the acquisition of Heptagon, but because the deal is not closed yet, we do not include these impacts in our estimates. However, it **is included in our new FV of CHF27 vs. CHF29.**
- **Given 1/ sales momentum heading to a muted quarter, 2/ the risks linked to the execution of the integration of Heptagon, 3/ a possible softer demand than expected in FY17e and FY18e leading to fall short of the FY19e plan and 4/ a limited upside, we reiterate our Neutral recommendation.**
- Based on our estimates, ams' shares are trading on 2017e P/E and PEG ratios of 15.1x and 1.5x respectively.

NEXT CATALYSTS

- Early February 2017: FY16 and Q4 results.

Our new estimates – P&L

[in EURm]	1Q16	2Q16	3Q16e	4Q16e	2016e	2017e	2018e
Sales	137	132	147	130	546	660	793
Seq. growth	-7%	-4%	11%	-12%	-12%	21%	20%
Gross profit (IFRS)	74	71	78	63	286	366	452
Gross margin	54%	53%	53%	49%	52%	56%	57%
R&D	-33	-32	-37	-35	-137	-135	-151
% of sales	-24%	-24%	-25%	-27%	-25%	-21%	-19%
G&A	-24	-25	-23	-23	-95	-99	-111
% of sales	-17%	-19%	-16%	-18%	-17%	-15%	-14%
Other op. income	2	2	32	2	38	7	8
% of sales	2%	2%	22%	2%	7%	1%	1%
EBIT (IFRS)	20	17	50	7	94	139	198
Operating margin	14%	13%	34%	6%	17%	21%	25%
Adjusted EBIT	28	24	28	15	96	152	215
Operating margin	21%	18%	19%	12%	18%	23%	27%
Financial result	-5	4	-2	-1	-4	-7	-7
% of sales	-4%	3%	-1%	-1%	-1%	-1%	-1%
Income Tax	-1	-1	8	0	5	-16	-23
Income tax rate	-5%	-6%	16%	-6%	6%	-12%	-12%
Net Profit (IFRS)	14	20	56	6	95	116	168
Net margin	10%	15%	38%	4%	17%	18%	21%
Adj. Dil. EPS	0.21	0.28	0.37	0.19	1.05	1.86	2.73
EPS seq. growth	-51%	33%	32%	-49%	-50%	77%	47%

Sources: Bryan, Garnier & Co ests.

[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 57.3%

NEUTRAL ratings 31.2%

SELL ratings 11.5%

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.