

Dialog Semiconductor

Price EUR35.36

No more juice, but buybacks and upcoming analyst day might provide a temporary refill

Fair Value EUR40 vs. EUR37 (+13%)

BUY

Bloomberg	DLG GR
Reuters	DLGS.DE
12-month High / Low (EUR)	39.9 / 24.4
Market Cap (EURm)	2,706
Ev (BG Estimates) (EURm)	2,012
Avg. 6m daily volume (000)	5.40
3y EPS CAGR	9.2%

	1 M	3 M	6 M	31/12/15
Absolute perf.	3.1%	23.6%	17.8%	13.3%
Semiconductors	-3.1%	2.0%	31.4%	20.3%
DJ Stoxx 600	-3.4%	-1.2%	-1.2%	-9.4%

YEnd Dec. (USDm)	2015	2016e	2017e	2018e
Sales	1,355	1,197	1,374	1,631
% change		-11.7%	14.7%	18.7%
EBITDA	360	285	366	455
EBIT	317.7	216.3	293.8	382.7
% change		-31.9%	35.8%	30.3%
Net income	238.4	163.0	228.2	305.6
% change		-31.6%	40.0%	33.9%

	2015	2016e	2017e	2018e
Operating margin	23.4	18.1	21.4	23.5
Net margin	17.6	13.6	16.6	18.7
ROE	17.3	20.3	12.9	14.6
ROCE	46.9	40.4	48.6	63.4
Gearing	-54.0	-62.6	-66.7	-70.8

(USD)	2015	2016e	2017e	2018e
EPS	3.02	2.09	2.94	3.94
% change		-30.7%	40.5%	33.9%
P/E	13.0x	18.8x	13.3x	10.0x
FCF yield (%)	7.9%	8.4%	5.7%	7.5%
Dividends (USD)	0.00	0.00	0.00	0.00
Div yield (%)	NM	NM	NM	NM
EV/Sales	1.8x	1.9x	1.5x	1.1x
EV/EBITDA	6.8x	7.8x	5.6x	4.0x
EV/EBIT	7.7x	10.3x	7.0x	4.8x

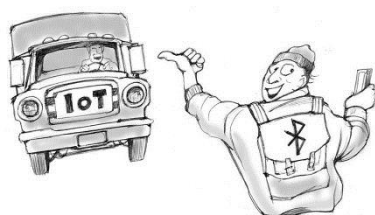
Yesterday's conference call was the final confirmation of the scenario we first discussed in March. Very low expectations for the iPhone 7 provided an easy comparable base (helped by the group's low guidance), leaving room for welcome news, such that the Dialog share enjoyed a +20% ride over the last three months. Nevertheless, we believe that the iPhone 7 source is drying up but the second tranche of the share buyback provides a temporary refill. We update our model and raise our FV to EUR40 vs. EUR37. Ahead of the analyst day scheduled next week (Friday 11 November) we maintain our Buy recommendation.

ANALYSIS

- What happened?** Yesterday, Dialog reported particularly strong Q3 sales at USD346m thanks to a Q4 order pulled in Q3 in order to accommodate a customer regarding Chinese holidays (about USD20m) but this was not a surprise (unaudited sales had been published in early October). The good part of the publication concerned margins. Over Q3, opex rose slightly compared with Q2 (note that Q3 sales were up 41% seq.), as such the group reported adjusted EPS 11% above expectations. For Q4, the group is guiding for revenue in the range of USD345m to USD375m, i.e. up 4% seq. at mid-range and yielding FY16e sales of about USD1.19bn (down 12% yoy), well above the latest company guidance of FY16e down 15%.
- Mobile Systems and BT to support Q4 growth.** In detail, we understand that Q4 should harbour strong momentum in BT. The target of 45/50m units was somewhat confirmed during the conference call leading us to believe that Q4 Connectivity sales (c. 11% of total sales) momentum will be stronger than in Q2 when this division showed sales up 38% seq (BG ests. +45% seq.). Overall, the pipeline is said to be very strong and note that the group had design wins in Q3, including Pokémon Go Plus tool and Tile products (which are proof of low energy consumption with battery life up to 1 year). As such, Q4 should also benefit from normal seasonality in the Mobile Systems division (c. 80% of sales). However, we believe that sequential growth will be impacted by the Q4 order (about USD20m) pulled in Q3 and, as such, result in sequential growth of 5%.
- Normal seasonality likely for H1 2017 and a strong H2 2017.** Combining all impacts, we understand that Q1 2017 should be down sequentially at a normal rate (down 25/30%) but up yoy. As such, Q1 2016 should not be seen as a new model for seasonality pattern but as an artefact and the strong traction that we currently see in the iPhone 7 is expected to remain strong. As such, we understand that things will change during H2 2017. The group should benefit from market share gains in the iPhone (we expect a mixed-signal products, maybe related to the new iPhone screen) leading to higher content per Apple phone and higher ASP while volume increases are not included in management expectations for a rebound in 2017 (which is a good thing in our view). Also, BT should remain a strong contributor to growth as should some design wins in China (in Power Conv.), which offset the MediaTek partnership which is set to generate lower revenues from Q4 2016. We understand that Power conversion and especially Rapid Charge will also play a strong role as of 2017 (which is not surprising given Dialog's solid product portfolio and 70% market share here).
- Overall, the 2017 outlook is unchanged.** To sum up, we see no major deviation in the actual management message and believe that it is also mostly in line with Street's expectations so far. 2017 will be a year of significant market share gains in the iPhone while business in other divisions should remain strong especially BT Smart and rapid charge which should offset weakness in the MediaTek partnership in China.

VALUATION

- So is the glass half full or half empty then?** Yesterday's publication and conference call confirmed our view that the group was overly cautious for the end of the year (we discussed this [during Q2 publication](#)). In addition to that, during the conference call, management reiterated its confidence regarding FY17 growth. So, everything confirms our scenario, nevertheless, the share's good ride in recent months (+20% over 3m) now limits upside potential. Hopefully, management will use its wildcard, the share buyback programme, to maintain positive momentum on the stock. The group plans to buy back about 2.1% to 2.8% of equity through a second tranche and we remind that the



total allowance is for 10% (the first tranche was about 1.7%). In addition to the strong Q3 results, this provides some additional upside. **We update our model to take into account all these impacts and raise our FV to EUR40 from EUR37 which points to an upside potential of 13%. Ahead of the analyst day scheduled next week (Friday 11 November) we maintain our Buy recommendation.**

- Based on our estimates, Dialog' shares are trading on 2017e P/E and PEG ratios of 12.8x and 1.4x respectively.

NEXT CATALYSTS

- 11th November 2016: Analyst day
- Late February/Early March 2017: Q4 and FY16 results (not confirmed yet)

Our new P&L

[USDm]	1Q16	2Q16	3Q16	4Q16e	FY16e	FY17e	FY18e
Total Group	241	246	346	364	1197	1374	1631
<i>Q/Q growth</i>	-39.2%	1.8%	40.7%	5.4%	-11.7%	14.7%	18.7%
<i>Y/Y growth</i>	-22.4%	-22.4%	4.6%	-8.3%	-11.7%	14.7%	18.7%
Cost of goods sold	-134	-132	-187	-196	-649	-747	-887
Gross margin	44.6%	46.3%	46.0%	46.1%	45.8%	45.6%	45.6%
SG&A	-36	-31	-33	-49	-150	-143	-153
R&D	-58	-60	-64	-62	-244	-251	-292
Other operating income	16	9	10	4	40	55	51
Adj. EBIT	30	33	73	80	216	294	383
<i>adj. operating margin</i>	12.4%	13.5%	21.2%	21.9%	18.1%	21.4%	23.5%
EBIT	151	23	61	57	292	234	300
<i>operating margin</i>	62.6%	9.3%	17.8%	15.6%	24.4%	17.0%	18.4%
Net financial result	-2	1	0	1	0	1	2
Income tax	-4	-9	-15	-13	-41	-53	-62
<i>tax rate</i>	-2.7%	-34.0%	-24.0%	-23.0%	-13.9%	-22.5%	-20.5%
Adj. Net income (loss)	22	27	55	59	163	228	306
Net income (loss)	143	17	46	44	250	182	239
Dil. Adj. EPS (in USD)	0.28	0.34	0.71	0.76	2.09	2.94	3.94

Source: Bryan, Garnier & Co. ests.

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