

TSMC Upside, IDT Adds a Technologist

TSMC (TSM, \$19.43 +0.66, rated *Not Compelling/Hold* on my latest *Chip Investment Ideas*)

Preannounced 1Q Upside: Late yesterday TSMC raised its guidance for 1Q due to demand strength for 28nm technology wafers and ‘customers’ active restocking of inventory.’ This technology node has been very relevant in recent quarters for products TSMC manufactures for smartphone-related companies such as Qualcomm and MediaTek among others, and I view this as good news at the margin for the overall smartphone market. However, I also think it is difficult to attribute such strength any more narrowly.

First of all, let’s keep this upside in perspective: revenue is now expected to drop sequentially by -0.7% this quarter rather than the original -8-7% in converted dollar terms compared to last quarter’s \$4.9B*. Certainly a meaningful improvement, but hardly growth. Also, the 28nm node is growing and TSMC is the primary beneficiary given the challenges most other foundries are having establishing the technology, fine-tuning its performance and yield, and ramping meaningful capacity. It accounted for 34% of sales at TSMC last quarter. And finally, there still may be some lingering benefits associated with Apple shifting its semiconductor manufacturing capacity away from Samsung to other suppliers that TSMC may benefit from either directly or indirectly. As I noted above, this is good news for smartphones in general, but there are a lot of moving parts to consider before trying to attribute the upside more narrowly to any specific company or market sub-sector.

I remain ambivalent with respect to TSM shares: I agree business is good and the company will likely outperform both the semiconductor industry and the foundry sector in terms of growth as it gains market share over the next few quarters, but its price-sales ratio of 4-5x and price-earnings ratio of 12-16x already credit performance with a premium, in my opinion. Nevertheless, I also agree there is room for potential upside as a momentum play on incremental growth.

(* *Specific guidance from TSMC calls for revenue of NT\$147B, gross margin of 47% and operating margin of 35%, up from revenue in a range of NT\$136-138B, gross margin 44.5-46.5%, and operating margin 32-34%. Last quarter it delivered NT\$145.8B at 29.541 NT\$/US\$ and guidance was offered at 30 NT\$/US\$.*)

IDT (IDTI, \$11.96 -0.09, rated *Not Compelling/Hold* on my latest *Chip Investment Ideas*)

Hires New CTO: Dr. Sailesh Chittipeddi joined IDT as CTO. I view the addition of such a technological heavy-weight as a positive for the company after last year’s departure of the CEO and CFO, failed acquisition of PLX Tech, and loss of R&D talent after activist shareholder issues. Nevertheless, I remain ambivalent with respect to the shares until I see some kind of favorable combination of business recovery and/or share price softening. Dr. Chittipeddi was the former CEO of Conexant Systems, holds five degrees including a PhD in physics and an MBA, and earned 64 patents and authored 40 publications. (And makes me wonder what I’ve been doing with my life. . .)

—**Dan K. Scovel**
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