

Lattice to Acquire Silicon Image

Silicon Image (SIMG, \$5.90 +0.02, Hold, Target Price \$7, 2015: \$0.24 on \$230M, 2016: \$0.27 on \$247M)

Lattice Semiconductor (LSCC, \$6.59 -0.03, Rated Hold/Not Compelling in my latest *Chip Investment Ideas*)

LSCC Buys SIMG: LSCC announced plans to acquire SIMG early this morning for \$7.30 per share totaling \$600M in an all cash deal via a tender offering. This reasonably-priced deal offers LSCC significant benefits, while SIMG sides-steps its current MHL hiccup at major customer Samsung while 60GHz wireless opportunities continue to germinate ahead of a ramp that may not occur for another year or two.

This is a wonderful acquisition for LSCC in terms of scale, IP, gross margin, market expansion, and ‘stickiness’ of its product offering—all at a not unreasonable price. LSCC adds SIMG’s \$250M in sales to its \$370M in a giant step to achieve its goal of \$1B in annual sales; it gets valuable IP in terms of HDMI, MHL and 60GHz wireless; it gets accretive gross margins; it significantly increases its exposure to consumer electronics markets, which is one of its objectives; and it gets a longer-tail of the product lifecycle by adding SIMG’s ASSPs and royalty streams. The scale itself buys leverage at both customers and vendors, as well as expected cost savings.

A tender offer for SIMG shares is to be launched in 10 days and expected to close by the end of March (subject to regulatory approvals); the deal is expected to be immediately accretive on a non-GAAP basis; and \$32M in annual savings are expected to be realized by the end of the first year. The combined entity is expected to generate non-GAAP gross margin of 56-60% and operating margin over 20%. LSCC has cash of \$257M, SIMG has \$148M, and Jefferies is offering a \$350M term loan. Neither company carries debt at this time. 3Q results for LSCC and SIMG, respectively, included: revenue of \$86.6M and \$70.3M; gross margin at 58.7% and 61.1%; net income margin of 10.9% and 12.5%; share counts of 121M and 79.7M; total assets at \$502M and \$272M; and shareholder equity at \$434M and \$207M. The deal values SIMG at just over 2-times sales, which also approximates where LSCC is trading.

This deal appears to be about scale, in my opinion. Both companies have competitive offerings generating respectable profits, but are stymied in a persistently low-growth business environment. The combined entity will approximately double each company’s relevance and leverage to their respective customers and suppliers. G&A synergies are obvious, S&M synergies could be meaningful, and at least some incremental manufacturing cost savings appears reasonable, in my opinion—all of which could realistically result in the advertised \$32M in annual cost savings. But the very different product offerings would appear to limit R&D synergies to the sharing of technology and site-consolidation in Sunnyvale and Shanghai: LSCC can add SIMG’s high-speed interfaces to its programmable FPGA devices and SIMG will likely be able to accelerate time-to-market with preliminary FPGA implementations, but other than that there doesn’t appear to be much overlap available to leverage and/or trim.

I give this combination an enthusiastic two-thumbs-up for LSCC, although my enthusiasm is tempered from a SIMG perspective due to the limited synergies associated with disparate products and technologies—which is reflected in the lack of a more significant valuation premium associated with the price of the deal, in my opinion.

—**Dan K. Scovel**
Semiconductor Analyst

Tokeneke Research LLC
Rowayton, CT 06853
dscovel@tokenekereseearch.com
www.tokenekereseearch.com
203-554-4621

Copyright © 2015 Tokeneke Research LLC. All rights reserved. This report is for information purposes only and does not constitute a solicitation or an offer to buy or sell any security or to participate in any investment or trading strategy. Opinions expressed in this report reflect the judgment of Tokeneke Research LLC on the topics addressed as of the date of the report, and are subject to change without notice. Tokeneke Research LLC makes every effort to use reliable and comprehensive information but makes no representation that the information in this report is accurate or complete, nor does it undertake to update or revise this report at any time or for any reason. This report contains forward-looking statements that involve risks and uncertainties, both known and unknown, as well as assumptions that, if they do not fully materialize or prove incorrect, could cause actual results to differ materially from those expressed or implied by such forward-looking statements. Actual results and trends may differ materially from historical results or those projected in any such forward-looking statements depending on a variety of factors. This report does not provide individually tailored investment advice and has been prepared without regard to the specific individual financial situation, objectives and needs of those who receive it. Securities discussed in this report may not be suitable for the reader. Tokeneke Research LLC and/or Dan Scovel may have a long or short position in the securities of a company or companies mentioned in this report and, at any time, may change that position. Tokeneke Research LLC accepts no liability whatsoever for any loss or damage of any kind arising out of the use of any part, or all, of this report. All company and product names mentioned in this report may be trademarks or registered trademarks of their respective holders and are used for identification purposes only. Reproduction or distribution of this report, even for internal distribution, is strictly prohibited unless specifically authorized by Tokeneke Research LLC.