MARKET DIGEST

U-Block, Strong H1 2017 Results, Buy

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U-Block delivered today strong results with unchanged 2017 guidance. This should support the share price as market was pessimistic on U-Block's ability to return to strong profitable growth and to meet its 2017 guidance. Consolidated revenues from chips and modules for positioning and wireless connectivity rose by 7.9% to CHF 193.8mn. Revenue growth was slightly negatively impacted by -0.3% foreign exchange.

By region, Asia Pacific improved by 25.3% to CHF 103.4mn, EMEA by 8.5% to CHF 49.9mn and USA revenues decreased by 20.7% to CHF 40.6mn. When compared to second half year 2016, the growth rates amounted to 8.0% for Asia‑Pacific, 9.1% for EMEA and 3.9% for Americas.

In Asia, the economic environment was strong, with production capacity in the electronics industry running at limits. Growth was driven by strong product sales in all categories. Several customers reported large scale operational expansion, while new applications, such as wearables and the smart bike.
In the USA, revenues declined by 20.7% as a direct result of the slowdown in 2016, which led to lower business activity at the beginning of the year. Compared to H2 2016, revenues increased by 3.9%. The migration to new LTE‑based cellular standards generated new traction as the industry has now opted for the M1 standard for M2M applications. There was a strong increase in sales of LTE based modules, with sales of CDMA based products declining. Demand in the automotive sector remained strong.

The EMEA region delivered 8.5% growth vs H12016. Strong demand in the industrial and automotive sectors supported growth. In car communication and navigation, smart meters, industrial controls, road pricing and asset tracking were the main business drivers. Gross profit improved from CHF 82.5mn to CHF 87.4mn, with gross profit margin remaining high at 45.1%. Operating profit (EBIT) was up by 6.1% CHF 29.5mn with EBITDA margin at 20.8%. Net profit declined by 2.6% CHF 18.0mn, due to foreign exchange impact. Net cash flow from operations was at CHF 22.1mn, corresponding to 11.4% of revenue. The balance sheet remained solid, with a healthy equity ratio of 58.1%.

For 2017, U‑Block is guiding EBIT as before between CHF 60mn and CHF 65mn, based on revenue predictions between CHF 410mn and CHF 425mn, with unchanged assumptions for foreign exchange rates. Medium to long/term perspectives expect continued growth.

We estimate that the company can achieve a revenue CAGR of 14% over 2017-22E and should reach an EPS CAGR in excess of 17% over 2017-22E. We believe market fears are exaggerated as U-block experienced a short term or cyclical slowdown and the structural long growth story remains. Furthermore, there is downside protection with U-block likely becoming a strategic M&A target. It currently trades at an EV/EBITDA 2018 of 11.6x and a 12m P/E of 23.5x. Looking at a group of peers or similar companies (Telit, Sierra Wireless, Melexis, Nordic Semi-conductor), U-blox is not overvalued. If U-block is able to deliver on its top-line guidance with EBIT margins around 16%, it could trade again at 13x EV/EBITDA.

We are keeping our Buy rating initiated early February 2017 and our 12m target price of CHF 230.

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