



ANALYST QUICK NOTES

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Analog Devices Inc. (NGS: ADI: BUY)

Target Price: \$84

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Thesis

- ADI is benefiting from improving consumer revenue (iPhone) and continued strong margin trends in business-to-business (B2B) end markets.

Fiscal 1Q17 Outlook (reporting 2/15/17)

- Street: Revenue of \$872 million, non-GAAP EPS of \$0.74.
- Argus: Revenue of \$878 million, non-GAAP EPS of \$0.77.
 - At Argus estimates: up 14% y/y down seasonal 13% q/q from fiscal 4Q16 (holiday-build quarter).

Consumer Market Comeback

- A year ago, ADI cut 2Q16 revenue guidance citing weak customer demand for portable devices.
- This was the end of life for the iPhone 6 family; ADI builds force-touch controller, the most-significant upgrade from iPhone 6 to iPhone 6S.
- Consumer business of \$294 million in 4Q16 declined 7% year over year, but surged 58% sequentially.

Fiscal 2Q17 Guidance: What the Street Wants to Hear

- Our AAPL thesis is that the installed base is becoming sufficiently large that individual iPhone cycles will matter less, as services grow and upgrades become less seasonal.
- For ADI, we are modeling 23% q/q decline in consumer:
 - Much less of a sequential decline than in 2Q16 (down 36%).
 - Plus consumer business in 2Q17 modeled twice as big as in 2Q16.
- Modeling industrial and automotive to remain very strong.
- 2Q17 Street: Revenue of \$878 million, non-GAAP EPS of \$0.76.
- 2Q17 Argus: Revenue of \$898 million, non-GAAP EPS of \$0.80.
 - At Argus estimates: up 15% y/y and low singles q/q, and EPS up 39%.

Linear Technologies

- In July '16, ADI announced plans to acquire Linear Technology (NSM: LLTC) for \$60 per share, or \$14.8 billion.
- The deal will vault ADI to the #2 market-share position in analog chips, behind Texas Instruments.
- While this move is not without risks, we view it as a necessary step in a consolidating industry.

Capital Allocation

- In 2/16, the board announced a 5% hike in the quarterly dividend, to \$0.42.
- We look for a similar mid-single-digit hike to be announced with 1Q17 results.
- The board also increased the share-repurchase authorization to \$1 billion; at quarter end, the existing authorization stood at \$415 million.
- ADI now has gross cash of \$3.4 billion and net cash of \$1.7 billion.

Valuation

- Trading average is 20.6-times two-year forward P/E, vs. historical 19.4-times.
- However, relative P/E of 1.18 is below the five-year average of 1.23.
- Below calculated value of \$100 on DFCF, fair value of \$90.

Conclusion

- We look for accelerating growth and strong cash generation from improving operating leverage, supporting industry-leading performance and healthy returns to shareholders.
 - We are reiterating our BUY rating to a 12-month target price of \$84.
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