



Qualcomm Inc (QCOM)

Updated May 4th, 2018 by Nate Parsh

Key Metrics

Current Price: \$52	5 Year CAGR Estimate: 8.4%	Quality Percentile: N/A
Fair Value Price: \$52	5 Year Growth Estimate: 4.0%	Momentum Percentile: N/A
% Fair Value: 100%	5 Year Valuation Multiple Estimate: 0.0%	Total Return Percentile: N/A
Dividend Yield: 4.4%	5 Year Price Target: \$60	Valuation Percentile: N/A

Overview & Current Events

“Quality Communications” was started in the living room of Dr. Irwin Jacobs in 1985. The company’s first product and service was a satellite used by long-haul trucking companies that could locate and message drivers. Qualcomm, as it is known today, develops and sells integrated circuits for use in voice and data communications. The chip maker receives royalty payments for its patents used in devices that are on 3G and 4G networks. Qualcomm has a current market cap of \$77.7 billion and had sales of almost \$16 billion in 2017.

Qualcomm reported 2nd quarter 2018 earnings on 4/25/2018. Adjusting for a charge related to tax reform, the company earned \$0.80 per share, \$0.10 above estimates. Revenue declined 13.2% year over year to \$5.2 billion, but came in \$10 million above expectations. Sales declined mostly due to the lack of royalty payments made by Apple’s manufacturers. Qualcomm has made some concessions in hopes of ending its feud with Apple, including offering a lower-cost license on devices that use the company’s patented products. The company has offered to drop its 5% fee on the first \$500 of a device’s selling price to 3.25% fee on the first \$400 of a device’s selling price. In other news, President Trump issued an order on 3/12/2018 that blocked Qualcomm from being acquired by Broadcom (AVGO) due to national security issues.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$2.25	\$1.90	\$2.46	\$3.20	\$3.71	\$4.51	\$5.27	\$4.66	\$4.44	\$4.28	\$3.55	\$4.32
DPS	\$0.60	\$0.66	\$0.72	\$0.81	\$0.93	\$1.20	\$1.54	\$1.80	\$2.02	\$2.20	\$2.43	\$2.96

Qualcomm’s earnings per share declined almost 16% during the last recession. Even with this sharp decline, the company has grown earnings per share at a rate of 6.6% per year over the last decade. Much of this growth has taken place in the early part of the current decade as royalty payments from 3G and 4G networks accelerated. The non-payment of royalties from Apple have had a significant impact on Qualcomm’s earnings recently.

Qualcomm increased its offer for NXP Semiconductors (NXPI) to \$127.50 per share from \$110. The company is still waiting for regulators in China to sign off on the deal though the country approved of a joint venture between the company and state-owned Dtang Telecom. China remains the lone regulatory body not to have signed off on the deal for NXP, possibly because of trade tensions between the country and the U.S. The \$44 billion dollar acquisition of NXP will help Qualcomm diversify its business into automotive and personal security markets. Given the dispute with Apple and the not-yet-completed NXP deal, we see EPS growing at the below average rate of 4% per year. At this growth rate, earnings per share could reach \$4.32 by 2023.

Qualcomm has increased its dividend for the past 16 years. The most recently increased the dividend 9%. If the company grows dividends at the same rate as earnings, then investors could receive \$2.96 per share in income by 2023.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	19.5	21	16.5	16.4	15.9	14.2	14.3	14.5	12.1	13.7	14.0	14.0
Avg. Yld.	1.4%	1.7%	1.8%	1.5%	1.6%	1.9%	2.0%	2.7%	3.8%	3.8%	4.4%	4.4%

Qualcomm had an average price-to-earnings multiple of 15.8 over the last 10 years. Given the uncertainty around its disagreement with Apple as well as its pending purchase of NXP, we assign target multiple of 14. A successful conclusion to either of these issues would likely mean a higher target multiple.

Qualcomm has only recently become a high yielding stock. The current 4.4% yield easily tops that of both the S&P 500 and the 10-year Treasury Bond. Investors looking for income could find Qualcomm’s dividend attractive and could be a “get paid as you wait for growth” type of scenario.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	31.5%	26.4%	25.1%	27.7%	28%	33.1%	32.5%	29.3%	26.4%	19.1%	20.8%	22.0%
Debt/A	26.9%	26%	31.8%	25.9%	22%	20.7%	19.4%	38.2%	39.3%	53%	48.5%	30.3%
Int. Cov.	---	---	---	---	---	---	---	---	---	---	---	---
Payout	26.7%	34.7%	29.3%	25.3%	25.1%	26.6%	29.2%	38.6%	45.5%	51.4%	68.5%	68.5%
Std. Dev.	41.7%	24.5%	34.3%	25.8%	23%	13.6%	12.4%	23.4%	23.5%	34.4%	32.7%	25.7%

Qualcomm suffered a severe decline in earnings during the last recession. While handheld devices have become more of a necessity amongst consumers, the company would likely see a decline in EPS due to their high costs. Qualcomm’s gross profits to asset ratio has declined steadily, but much of this is likely due to Apple’s lack of royalty payments. On the positive side, the company has around \$40 billion in cash and marketable securities on its balance sheet. Investment gains from these assets more than offset the company’s interest expense and give the company ample cushion to continue paying dividends even in the event of a protracted recession.

Qualcomm’s dividend growth has been impressive in recent years, but with earnings falling the payout ratio has started to climb. For much of the last 10 years, the payout ratio was ~30% of earnings. In order to see aggressive dividend growth, Qualcomm would need to show accelerated earnings growth.

Final Thoughts & Recommendation

Shareholders of Qualcomm can expect an annual return of 8.4% through 2023. This return is a combination of growth (4%) and dividends (4.4%). While we feel that the current multiple is an appropriate target, there is a possibility of P/E expansion if Qualcomm is able to resolve its dispute with Apple over royalties and earn Chinese approval for its purchase of NXP Semiconductors. Qualcomm is an interesting stock that is likely to see its total returns driven by the situations discussed previously rather than general market growth. While we don’t recommend it as an outright buy today, it certainly has potential because of its positive expected total return and non-market driven catalysts.

Total Return Breakdown by Year

