



Microchip Technology Incorporated (MCHP)

Updated February 4th, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	\$72	5 Year CAGR Estimate:	15.7%	Market Cap:	\$40.0 B
Fair Value Price:	\$81	5 Year Growth Estimate:	12.0%	Ex-Dividend Date:	02/22/2022
% Fair Value:	89%	5 Year Valuation Multiple Estimate:	2.3%	Dividend Payment Date:	03/08/2022
Dividend Yield:	1.4%	5 Year Price Target	\$143	Years Of Dividend Growth:	19
Dividend Risk Score:	C	Retirement Suitability Score:	D	Last Dividend Increase:	9.1% ¹

Overview & Current Events

Microchip Technology develops, manufactures, and sells smart, connected and secure embedded control solutions used for a wide variety of applications. These include disruptive growth trends such as 5G, artificial intelligence, Internet of Things (IoT), and autonomous driving, amongst others, in key end markets such as automotive, aerospace and defense, communications. The company's strategic focus is that these solutions are cost-effective, offer high performance, with a wide voltage range operation, at extremely low power usage. Microchip Technology generates around \$6 billion in annual revenues and is based in Chandler, Arizona.

On February 3rd, 2022, Microchip Technology reported its Q3-2022 results for the quarter ending December 31st, 2021. Net sales were a record \$1.79 billion, up 30% from the comparable period last year and 6.8% higher sequentially. Higher revenues were again powered by exceptional execution on delivering Microchip's backlog and strong underlying demand despite the ongoing manufacturing capacity constraints amid supply chain constraints. Due to a higher production scale, GAAP gross margins reached a record of 65.6% for the quarter, leading to a record net income of \$358.8 million or \$0.62 per diluted share. On a non-GAAP basis, EPS was \$1.20 versus \$0.81 in Q3-2021. Non-GAAP results are more meaningful in Microchip's case due to the company's high share-based compensation, COVID-19 shelter-in-place restrictions on manufacturing activities, manufacturing excursion, high depreciation & amortization, and other factors. Based on Microchip's first-nine-month results and its Q4 non-GAAP EPS outlook of \$1.22 to \$1.28, we forecast non-GAAP EPS for FY2022 of \$4.51. We use non-GAAP figures to accurately value the stock and assess its future returns but all other figures in the table are GAAP-based, as officially shown in the company's filings with the SEC.

Microchip once again hiked its quarterly dividend 9.1% sequentially, or 29.7% year-over-year, to \$0.253.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$0.88	\$0.33	\$1.00	\$0.92	\$0.80	\$0.38	\$0.55	\$0.75	\$1.19	\$0.67	\$4.51	\$7.95
DPS	\$0.70	\$0.70	\$0.71	\$0.71	\$0.72	\$0.72	\$0.72	\$0.73	\$0.73	\$0.75	\$1.01	\$1.78
Shares²	382.6	389.2	396.6	401.9	406.8	434.4	465.8	472.4	477.8	519.2	565.4	800.0

Microchip Technology's EPS has struggled to improve meaningfully over the past decade despite the company growing its revenues relatively consistently. This has been mostly due to higher operating and R&D expenses, as well as increased financial expenses. However, with management's goal to expand margins while taking advantage of the ongoing sky-high demand for chips, EPS has started to snowball, as was the case in the company's latest results. The company is currently attempting to grow its production capacity to service its growing delivery backlog. Hence we expect EPS growth of around 12% in the medium term.

In terms of its dividend, Microchip has grown it for 19 years, quite marginally in some cases as in 2015-2016. Dividends have grown sequentially, by tiny increases QoQ. We forecast DPS growth of 12% moving forward to reflect the recent DPS growth acceleration, and management's intention to grow the dividend sequentially by around 9% going forward.

¹ Due to the company's multiple dividend increases intra-year this refers to the latest QoQ increase. YoY, DPS increased by 29.7%.

² Share count is in millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	18.2	61.5	21.6	27.7	38.4	113.2	64.5	62.3	50.2	118.5	16.0	18.0
Avg. Yld.	4.3%	3.5%	3.3%	2.8%	2.3%	1.7%	2.0%	1.6%	1.2%	0.9%	1.4%	1.2%

Microchip currently trades at a P/E of 16 based on our expected FY2022 non-GAAP EPS estimates. While the company is currently enjoying favorable market conditions and expanding margins, the high CAPEX needs of the industry could compress net income, as was the case in the past. That said, we remain optimistic for robust profitability moving forward, and believe that a slightly higher valuation multiple of around 18 better fits the stock. Investors should expect the currently tiny yield to remain a token to the stock's total return prospects.

Safety, Quality, Competitive Advantage, & Recession Resiliency

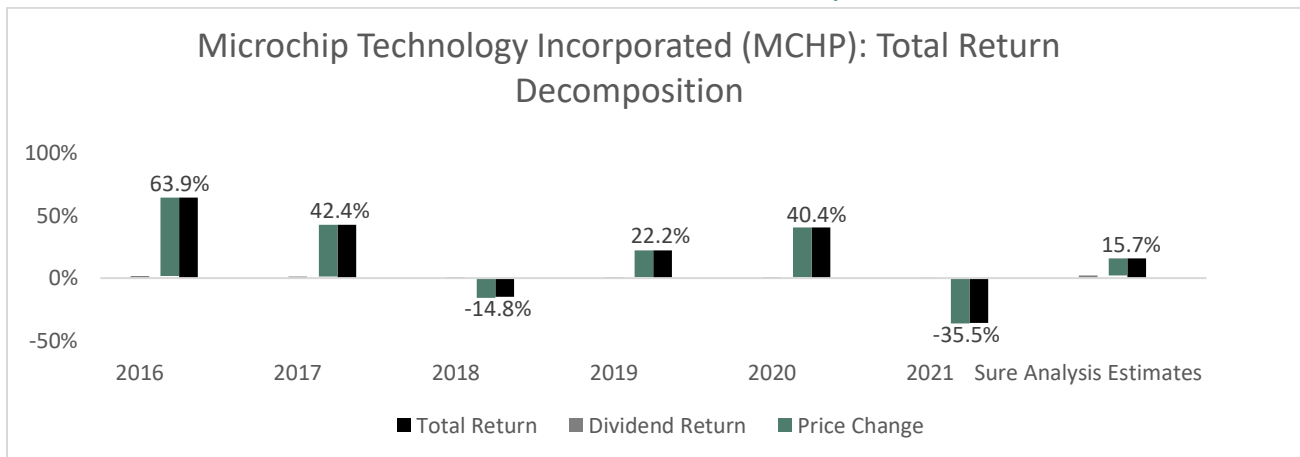
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	80%	212%	71%	77%	90%	189%	131%	97%	61%	112%	22%	22%

Microchip's dividend should quite safe, being multiple times covered by operating cash flows. The normalized payout ratio seems high only due to the company's GAAP results, which carry heavy stock-based compensation expenses and depreciation & amortization (a non-cash item). The company enjoys several qualities and positive catalysts, including a robust backlog that should provide stable and predictable cash flows moving forward, expanding margins, and a declining long-term debt position (currently \$7.86 billion vs. \$9.55 billion in 2019). Still, the company faces several noteworthy risks, including fierce competition, global industrial cyclicality effects, limited visibility to product shipments, and international risks such as FX fluctuations due to its global clientele. A global recession could adversely impact the company's results, though global demand for chips remains far ahead of supply capabilities, at least for now.

Final Thoughts & Recommendation

Microchip Technologies has rallied massively over the past decade, with the company's sales expanding during this time as a result of the increased demand for chips. With higher margins, the company should continue to grow EPS at a rapid pace as its production capacities increase to service its growing backlog. Additionally, management mentioned its commitment to growing the dividend sequentially, which should add to total returns. Along with the possibility for a multiple expansion following the stock's correction, we estimate annualized returns of 15.7% through 2027. Shares earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	1,383	1,582	1,931	2,147	2,173	3,408	3,981	5,350	5,274	5,438
Gross Profit	799	838	1,129	1,230	1,206	1,757	2,421	2,931	3,242	3,379
Gross Margin	57.8%	53.0%	58.4%	57.3%	55.5%	51.6%	60.8%	54.8%	61.5%	62.1%
SG&A Exp.	208	261	267	275	302	500	452	683	677	610
D&A Exp.	99	204	189	278	283	469	616	876	1,216	1,153
Operating Profit	397	211	462	428	356	374	954	748	694	1,000
Operating Margin	28.7%	13.3%	23.9%	20.0%	16.4%	11.0%	24.0%	14.0%	13.2%	18.4%
Net Profit	337	127	395	369	324	165	255	356	571	349
Net Margin	24.3%	8.1%	20.5%	17.2%	14.9%	4.8%	6.4%	6.7%	10.8%	6.4%
Free Cash Flow	350	409	563	572	647	984	1,213	1,446	1,476	1,824
Income Tax	43	25	37	(19)	(43)	(81)	482	(151)	(420)	(10)

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	3084	3851	4068	4781	5538	7687	8257	18350	17426	16479
Cash & Equivalents	636	528	467	608	2093	909	901	429	401	280
Accounts Receivable	170	230	242	274	290	478	564	881	934	998
Inventories	217	242	263	279	307	417	476	712	686	665
Goodwill & Int. Ass.	184	801	722	1076	1619	4447	3961	13350	12367	11465
Total Liabilities	1093	1918	1932	2720	3387	4416	4977	13063	11841	11142
Accounts Payable	50	76	74	87	79	149	144	226	247	292
Long-Term Debt	355	983	1021	1827	2453	2951	3068	10307	9482	8904
Shareholder's Equity	1991	1933	2135	2045	2151	3271	3280	5288	5586	5337
LTD/E Ratio	0.18	0.51	0.48	0.89	1.14	0.90	0.94	1.95	1.70	1.67

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	11.1%	3.7%	10.0%	8.3%	6.3%	2.5%	3.2%	2.7%	3.2%	2.1%
Return on Equity	17.7%	6.5%	19.4%	17.7%	15.4%	6.1%	7.8%	8.3%	10.5%	6.4%
ROIC	14.9%	4.8%	13.0%	10.5%	7.6%	3.0%	4.1%	3.2%	3.7%	2.4%
Shares Out.	203.5	205.8	217.6	223.6	217.4	234.8	248.9	249.9	256.2	270.6
Revenue/Share	6.80	7.69	8.87	9.60	10.00	14.51	15.99	21.41	20.59	20.10
FCF/Share	1.72	1.99	2.59	2.56	2.97	4.19	4.87	5.79	5.76	6.74

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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