

Qualcomm stock analysis

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Executive summary

RISK – QCOM is sued all over the world for its highly profitable licensing business.

CERTAINTTY – legal costs will be high.

RISK – losing licensing court battles would lower future earnings power.

RISK – 5G adoption and QCOM’s market.

CERTAINTTY – competitors are not sleeping with Apple and Samsung in-sourcing.

RISK – yes, QCOM can make \$7 in EPS per share in 2021 based on 5G. However, as 5G slows down in 2024, competition ramps up, who knows where will EPS be.

CERTAINTTY – expect volatility in earnings and cash flows – not a value investment.

RISK – 5G adoption will not be smooth and can be delayed, don’t get confused by the marketing

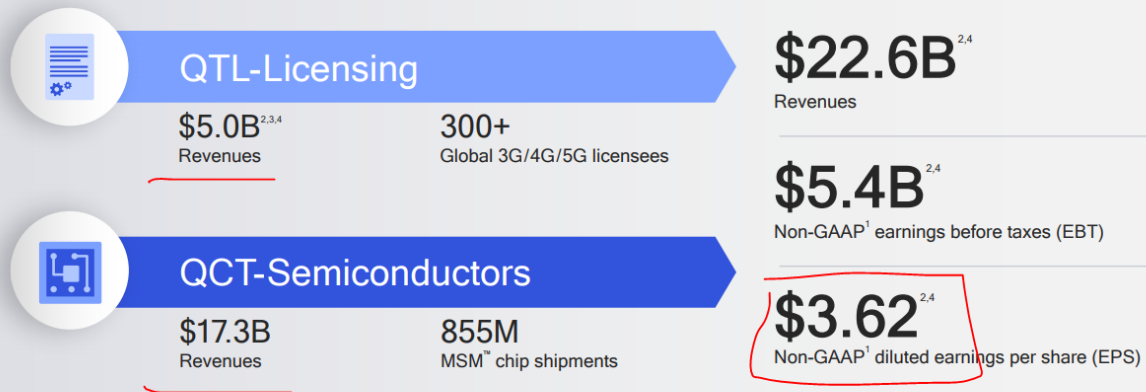
Summary – it is a semiconductor company that spent \$50 billion on buybacks that didn’t help, it is betting on the 5G boom and litigating with customers and the whole world. Have fun!

This analysis will be an example of an exploratory research process. I will start with what the company has to say about itself and the investor presentation.

Company overview

There are two businesses with QCOM, one is the licensing the other the semiconductors. The licensing business is a high margin one and makes 2/3 of EBITDA.

## Key fiscal 2018 results



We have strongly positioned ourselves for future growth

When the NXP acquisition fell through, they went on a crazy buyback program, it didn't help much as the stock didn't go anywhere in the last 8 years practically.

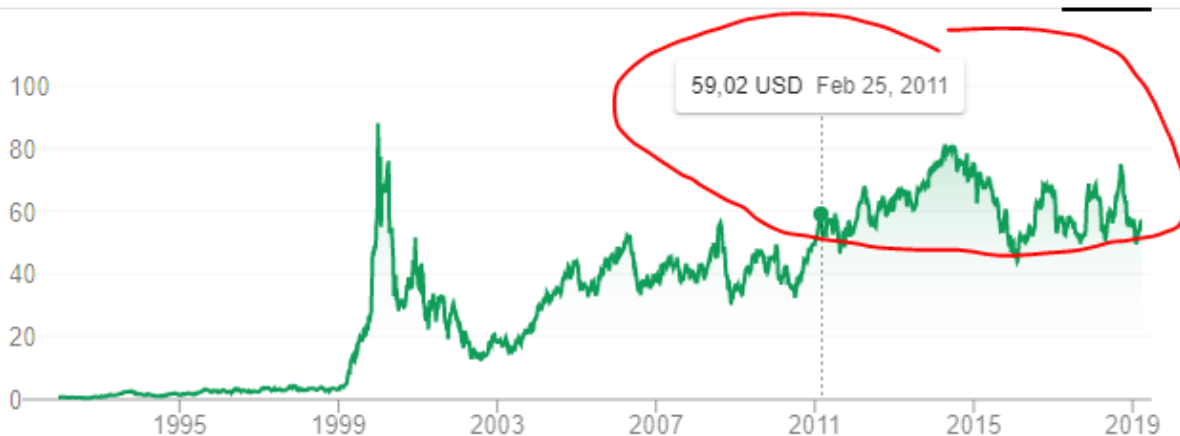
QUALCOMM, Inc.  
NASDAQ: QCOM

+ Follow

**58,09** USD +0,28 (0,48%) ↑

Closed: 2 Apr, 16:15 GMT-4 · Disclaimer  
After hours 58,09 0,00 (0,00%)

1 day 5 days 1 month 6 months YTD 1 year 5 years Max



Open	57,98	Div yield	4,27%
High	58,53	Prev close	57,81
Low	57,66	52-wk high	76,50
Mkt cap	70,31B	52-wk low	48,56
P/E ratio	-		

## Stock repurchase plan and capital policy

\$86.5B cumulative return of capital to stockholders



### Stock repurchase plan

- We have completed \$22B of the \$30B authorization\*

\*As of Q1FY19



### Capital policy

- No change to the quarterly dividend of \$0.62 at this time
- Continued focus on improving return on invested capital (ROIC)
- Long-term commitment to strong investment-grade rating
- Expect to target total liquidity of \$8B-\$10B

Note: Liquidity defined as cash and cash equivalents plus commercial paper and revolving credit facility availability

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The business plan is to grow the semiconductor and licensing revenues through innovative and sector leading products.

## Operational update



### 5G product leadership



### Investment discipline

- Cost plan – on track\*
- Focused product roadmap



### Adjacent growth

- RFFE – modem to antenna solutions
- Automotive –>\$5.5B pipeline
- C&N – Wi-Fi 6 leadership



### 5G licensing framework

- 35+ licensees have 5G agreements



### Core business execution

- 100+ Qualcomm® Snapdragon™ 855 mobile platform design wins in development

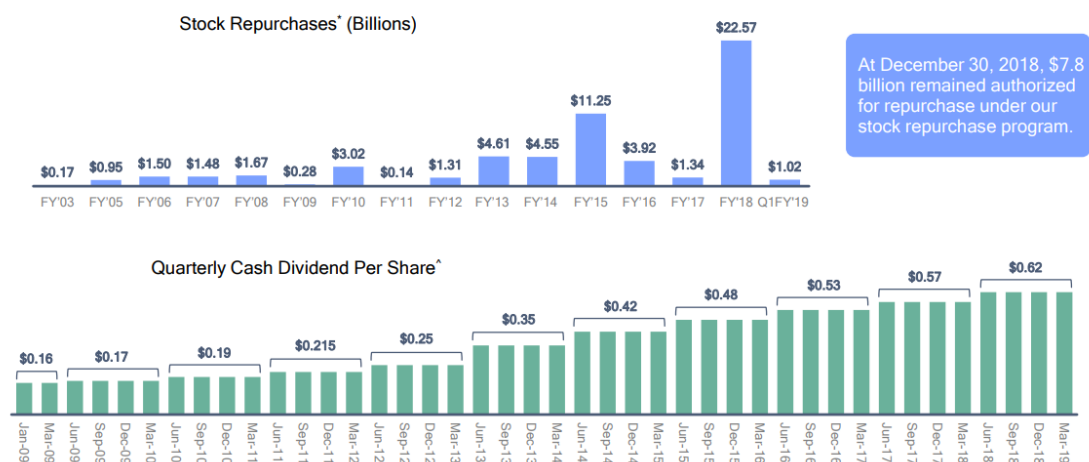
\*Excluding litigation costs that are in excess of the baseline spend.  
Qualcomm Snapdragon is a product of Qualcomm Technologies, Inc. and/or its subsidiaries.

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They have spent \$53 billion on buybacks in the last 10 years which is 75% of the current market cap. The number of shares outstanding went down 27%, from 1.67 billion to 1.22 billion.

# Cumulative \$86.5 billion returned to stockholders

As of January 30, 2019



\* Gross repurchases before commissions.  
 \*\* Based on date payable. Note: Please visit our website: <http://investor.qualcomm.com/dividends.cfm> for the complete dividend and stock split history list.

I will never understand the logic of the above but ok.

## Financial strength

In Billions	Dec '17 <sup>(2)</sup>	Dec '18
Total cash, cash equivalents & marketable securities	\$39.9	\$10.4 <sup>^</sup>
Total assets	\$64.4	\$34.2
Stockholders' equity	\$23.9	\$3.6
Debt*	\$22.8	\$16.4
EBITDA <sup>**</sup> (3)	\$0.4	\$1.1
Adjusted EBITDA <sup>**</sup> (3)	\$1.9	\$1.4

They have dried up their balance sheet with the buybacks, not indicating financial strength to me.

The question now is, will QCOM reach the cash flow levels it enjoyed in the past thanks to 5G and whatever is going on in the internet of things. Over the past 6 years, all of QCOM's metrics have been declining, from revenue, margins, cash flows etc.

**Qualcomm Inc** QCOM | ★★★★★

**Financials**

	2009-09	2010-09	2011-09	2012-09	2013-09	2014-09	2015-09	2016-09	2017-09	2018-09	TTM
Revenue USD Mil	10,416	10,991	14,957	19,121	24,866	26,487	25,281	23,554	22,291	22,732	21,539
Gross Margin %	69.5	68.0	67.4	62.9	60.5	59.7	58.9	58.6	56.1	54.9	54.6
Operating Income USD Mil	2,226	3,283	5,140	5,682	7,230	7,550	5,776	6,495	2,614	742	1,456
Operating Margin %	21.4	29.9	34.4	29.7	29.1	28.5	22.8	27.6	11.7	3.3	6.8
Net Income USD Mil	1,592	3,247	4,260	6,109	6,853	7,967	5,271	5,705	2,466	-4,864	2,187
Earnings Per Share USD	0.95	1.96	2.52	3.51	3.91	4.65	3.22	3.81	1.65	-3.32	1.60
Dividends USD	0.66	0.72	0.81	0.93	1.20	1.54	1.80	2.02	2.20	2.38	2.43
Payout Ratio % *	69.4	36.7	30.0	30.2	29.3	35.4	47.7	57.4	82.8	—	151.8
Shares Mil	1,673	1,658	1,691	1,741	1,754	1,714	1,639	1,498	1,490	1,463	1,400
Book Value Per Share * USD	12.17	12.94	16.03	19.10	22.30	23.24	21.79	20.76	21.23	18.92	2.99
Operating Cash Flow USD Mil	7,172	4,076	4,900	5,998	8,778	8,887	5,506	7,400	4,693	3,895	2,489
Cap Spending USD Mil	-761	-426	-593	-1,284	-1,048	-1,185	-994	-539	-690	-784	-710
Free Cash Flow USD Mil	6,411	3,650	4,307	4,714	7,730	7,702	4,512	6,861	4,003	3,111	1,779
Free Cash Flow Per Share * USD	3.83	2.20	2.55	2.99	3.77	4.98	2.63	4.24	2.54	3.75	—
Working Capital USD Mil	9,757	6,665	9,004	10,343	14,342	16,400	15,999	15,670	32,686	6,148	—

\* Indicates calendar year-end data information

Source: Morningstar - [QCOM](#)

Will things turn around? Possibly, but I am looking for trends that will last forever, not a quarter or two or maximally a year or two.

QCOM's future

QCOM has been guiding for a \$7 earnings per share year in 2019. But things don't look rosy.

**Fiscal 2019 Earnings Per Share (EPS) guidance\***

	Fiscal 2019 EPS (est.) <sup>(2)</sup>	Fiscal 2019 Accretion from NXP <sup>(2)</sup>	Accretion from Share Repurchase
GAAP diluted EPS	\$4.47 - \$5.22	\$0.08	\$1.26
Less: Diluted EPS attributable to QSI	\$0.02	N/A	\$0.01
Less: Diluted EPS attributable to share-based compensation	(\$0.73)	(\$0.16)	(\$0.16)
Less: Diluted EPS attributable to other items <sup>(1)</sup>	(\$1.57)	(\$1.26)	(\$0.09)
Non-GAAP diluted EPS	\$6.75 - \$7.50	\$1.50	\$1.50
Less: Diluted EPS attributable to income from customers involved in licensee disputes	\$1.50 - 2.25		
Non-GAAP EPS, before impact of expected licensing resolutions	\$5.25		

(1) Other items excluded from Non-GAAP in fiscal 2019 consist primarily of acquisition-related items.

(2) Fiscal 2019 estimated EPS and EPS accretion assume close of the pending NXP acquisition. Estimated amortization of intangible assets included in other items was based on a preliminary purchase price and are subject to change when the formal valuation and other studies are finalized. The differences that will occur between the preliminary estimates and the final purchase accounting could be material.

Sums may not equal totals due to rounding

\* Guidance as of Jan 31, 2018.

QCOM's future also depends on the FTC and Apple lawsuits. If they win, the royalties would boost QCOM, but Apple has already switched to Intel modems and making their own chips, so it is not really a great long-term deal there. If they get the money, they would probably do more buybacks that we have seen as not a great long-term story, again.

### Growth, 5G opportunity and long term earnings

Analysts estimate growth for QCOM based on positive things going on in the 5G sector but those things haven't happened yet. FY 2020 earnings are estimated to be \$4.5 in a good scenario.

I think much of the stock price has been protected by the latest \$22 billion buyback, if not this would bleed.

The promise is the following, QCOM's CEO:

"Snapdragon platform continues to outperform industry benchmarks and is well-positioned to successfully enable the low latency, high reliability and security requirements of 5G. We continue to extend this expertise with handset OEMs and adjacent industries of compute IoT and auto."

The above is based on 130,000 patents the company has. The expectations are limited for 2019 but the management is extremely positive for 2020 and 2021 as 5G rolls out. The [expectations](#) are that 22% of phones are on 5G in 2022 and 50% in 2025.

### The 5G product

From where I am looking at this, 5G chips, semiconductors etc. are a commodity. You can software it a bit, license it etc. but at some point, you will reach the human needs for speed and satisfy those. At that point, it will be a price battle and everybody will bring the price down. It is not an environment I would feel good investing as it can change so fast. There is always the one or two boom years that excite investors, but this is not value investing. I rather make my money with more certainty.

Apple and Samsung are insourcing their production – this could be very painful and Huawei isn't really in a good spot at the moment.

Plus, the marketing machine is already selling 5G for 2020, but real application could come a few years later that would be very detrimental to producers. Delays allow the competition to catch up and lower prices.

### My investing opinion

Charlie Munger makes investing really simple, he tells us not to do stupid things. For a value investor a stupid thing would be to invest somewhere with no margin of safety, exactly what QCOM is.

I think that QCOM will reach earnings per share of \$7 somewhere in the 5G boom. I have probably read about 10 bullish analyses on QCOM projecting a stock price of \$105 when that happens. However, when they make that kind of money, every graduate from any tech university plus Samsung and all others will be after the profits. This will lead to the current situation probably repeating itself.

**Qualcomm Inc** QCOM | ★★★★★

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A few years of wonderful earnings followed by nasty surprises alongside the semis cycle. On the stock price, when they make \$7, it will be about next year, not about the current \$7. Like it was the case with the buybacks that led nowhere.

I could be smart about the licencing, 5G snapdragon chip, saving energy, Apple becoming a customer again, but this is not value investing. As a value investor I see \$53 billion of buybacks gone nowhere. Remember, investing is about what will happen next. Value investing is about a margin of safety and long term business earnings.



I stick to being the boring, unexciting investor as that is what makes me money.

QCOM doesn't offer a margin of safety and its future depends on 5G adoption (timing), and on litigation outcomes (betting). Timing and betting is not what a value investor does.