

BUY

ANALYSIS OF SALES/EARNINGS

Financial Summary

Changes	Previous	Current
Rating	—	Buy
Target Price	—	\$33.00
FY19E Rev (net)	\$212.0	\$213.0
FY20E Rev (net)	—	\$243.0
FY19E EPS (net)	\$1.25	\$1.30
FY20E EPS (net)	—	\$1.75

Price (08/07/19):	\$27.40
52-Week Range:	\$30 - \$21
Market Cap.(mm):	782.7
Shr.O/S-Diluted (mm):	28.6
Enterprise Val. (mm):	\$602.9
Avg Daily Vol (3 Mo):	126,289
Net Cash/Share:	\$6.29
Dividend / Yield:	\$0.00 / 0.0%
Book Value/Share:	\$10.17
Cash/Share:	\$5.87

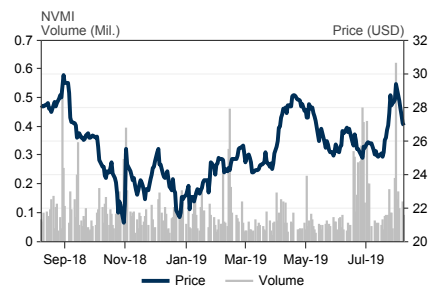
Prices updated intraday 08.07.19

EPS (net)	2018A	2019E	2020E
Q1	\$0.54	\$0.37A	\$0.38
Q2	\$0.46	\$0.32A	\$0.44
Q3	\$0.52	\$0.27	\$0.42
Q4	\$0.59	\$0.35	\$0.50
FY (Dec)	\$2.11A	\$1.30	\$1.75
P/E	13.0x	21.1x	15.7x

Results and estimates exclude stock options expensing

Rev (net)	2018A	2019E	2020E
Q1	\$62.6	\$56.7A	\$57.7
Q2	\$61.9	\$51.1A	\$61.1
Q3	\$63.6	\$50.0	\$59.3
Q4	\$63.1	\$55.2	\$64.9
Rev (net)	\$251.1A	\$213.0	\$243.0

Price Performance



Foundry Strength, Broad Customer Mix, and Increasing Capital Intensity Trends Set Up Sustainable Growth Trends

Summary

On Wednesday, Nova Measuring Instruments reported 2Q19 (June) earnings results ahead of expectations and provided an outlook that supports our favorable thesis on the name. In the near term, the company is poised to benefit from an accelerated spend in the advanced foundry market for 7/5nm capacity. We also believe the company remains well positioned to benefit from a more balanced customer spend, as memory (particularly in China) comprised the larger percentage of product revenues and we expect Nova to benefit from a broader memory recovery in 2020. Finally, we believe the company's recent new product introductions are positioning it favorably for next-generation manufacturing challenges in both memory and foundry. We believe capital intensity trends continue to rise for Nova and these products will help support sustainable growth over the next few years. In total, we emerged with our thesis intact, and we maintain our Buy rating on the shares.

Key Points

- From a near term industry standpoint, the company is benefiting from an accelerated uptick in advanced foundry (TSMC) spending, particularly at the leading-edge 7/5nm nodes. We believe the company is benefiting from this accelerated spending from TSMC (and others) and this will provide a boost over the next few quarters (we suspect December through the early parts of 2020) and into 2020 as a whole.
- One of the key parts of Nova's evolution over the past few years is its increased presence on the memory front, where it is now almost 50/50 between memory and foundry/logic. In the June quarter, memory shipments stayed elevated at 65% (and foundry/logic at 35%). While broader memory spending has declined incrementally since the beginning of the year, we believe Nova is seeing strength emerging from the Chinese memory segment, both in NAND and DRAM. We believe Chinese memory in both of these markets has accelerated their respective production line ramps (although we believe yields could still be an issue) and this is likely to carry into 2020 as well. In total, we believe a recovery in memory in 2020 will supplement the other growth areas for Nova as well.
- We have noted that the company's recent product introductions (materials characterization, dimensional analysis) provide the company with a roadmap to address next generation manufacturing challenges. This roadmap also provides the company with the ability to drive sustainable growth over the next few years as the industry transitions occur. Notably, next generation memory and logic manufacturing require 1) 3D scaling (both device and transistor structures), 2) device scaling, and 3) new materials. For example, going from the current FinFET transistor structure to a gate-all-around (GAA) or nanowire structure at 3nm will present new manufacturing challenges, both on the dimensional end and on the materials front (new materials for the gate). We believe this industry transition plays into the sweet spot of Nova's new product introductions and these increasing capital intensity trends will also help drive sustainable growth over the next few years. Memory presents its own challenges from increasing layers in 3D NAND and smaller device scaling in DRAM (which potentially requires new materials and additional OCD analysis as well). The company's technology and product portfolio are positioning Nova to benefit from these emerging manufacturing challenges.

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Investment Thesis

Our favorable thesis on the name is based on the following: 1) market position in the OCD metrology market; 2) increasing capital intensity in OCD metrology; 3) market share gains (particularly in the foundry and 3D NAND segments); 4) strong operating model metrics; and 5) attractive acquisition candidate.

New Estimates

Following the call, we are making minor revisions to our FY19 (Dec) estimates while maintaining our FY20 forecasts. For FY19, given that its outlook was generally in line with ours, we are tweaking up our estimates to \$213 million in revenue (up from \$212 million) and pro-forma EPS of \$1.30, excluding options (up from \$1.25). We believe the December quarter is likely to see a step up from tools we expect to be delivered to TSMC.

For FY20, we are maintaining our current estimates of \$243 million in revenue (+14% y-o-y) and pro-forma EPS of \$1.75, excluding options. We expect product (systems) revenue to grow +18% y-o-y, while services is projected to grow +4% y-o-y. We believe memory will be the larger percentage of revenues for the year (55%) with the remainder being foundry/logic (45%). We expect foundry strength to be more predominant in the first half of 2020 given TSMC's ramp of 5nm.

Target Price Methodology/Risks

Our \$33 target price is based on 15x our FY20 EPS estimate of \$1.75, excluding options, plus approximately \$7 in net cash per share exiting 2020. Risks to the target price include: 1) volatility of the semiconductor spending trends, 2) scale relative to competitors, 3) lack of presence with Intel (logic), 4) competitive pressures in the OCD metrology market, 5) near-term increase in R&D limits operating leverage, and 6) business operations and incorporation located in Israel.

Company Description

Nova Measuring Instruments is a leading provider of process control metrology solutions serving the semiconductor industry. The company offers both integrated and stand-alone metrology solutions and is a leading player in the emerging optical critical dimension (OCD) metrology market.

Nova Measuring Instruments Ltd. Income Statement (\$ in millions except per share data) December Fiscal Year	2018				2019					2020					
	1QA	2QA	3QA	4QA	2018A	1QA	2QA	3QE	4QE	2019E	1QE	2QE	3QE	4QE	2020E
Revenues	\$62.6	\$61.9	\$63.6	\$63.1	\$251.1	\$56.7	\$51.1	\$50.0	\$55.2	\$213.0	\$57.7	\$61.1	\$59.3	\$64.9	\$243.0
Cost of Revenues	\$26.1	\$26.0	\$25.8	\$27.1	\$105.0	\$24.6	\$22.5	\$23.0	\$24.3	\$94.4	\$25.3	\$26.6	\$25.8	\$28.0	\$105.7
Stock Options Compensation	\$0.2	\$0.2	\$0.3	\$0.3	\$0.9	\$0.2	\$0.2	\$0.2	\$0.2	\$0.8	\$0.2	\$0.2	\$0.2	\$0.2	\$0.7
Gross Profit	\$36.4	\$35.7	\$37.5	\$35.7	\$145.2	\$31.8	\$28.4	\$26.9	\$30.7	\$117.7	\$32.2	\$34.4	\$33.4	\$36.7	\$136.7
Research & Development	\$10.9	\$11.5	\$11.4	\$10.0	\$43.7	\$12.5	\$11.0	\$11.6	\$11.9	\$47.0	\$12.1	\$12.2	\$11.9	\$12.3	\$48.5
Selling & Marketing	\$6.0	\$7.2	\$6.7	\$7.0	\$27.0	\$6.9	\$6.3	\$6.3	\$6.3	\$25.8	\$6.3	\$6.4	\$6.3	\$6.6	\$25.7
General & Administrative	\$2.1	\$2.0	\$2.0	\$2.0	\$8.1	\$1.4	\$2.0	\$1.8	\$1.8	\$7.0	\$1.8	\$2.0	\$2.0	\$1.9	\$7.7
Stock options expensing	\$0.7	\$0.8	\$1.0	\$1.0	\$3.4	\$1.0	\$0.9	\$1.0	\$1.0	\$3.8	\$1.0	\$1.0	\$1.0	\$1.0	\$4.0
Total Operating Expenses	\$19.7	\$21.4	\$21.1	\$20.0	\$82.2	\$21.9	\$20.1	\$20.7	\$21.0	\$83.6	\$21.3	\$21.6	\$21.2	\$21.9	\$86.0
Total Operating Income (incl. Stock-based comp)	\$16.7	\$14.3	\$16.4	\$15.7	\$63.1	\$9.9	\$8.2	\$6.2	\$9.7	\$34.1	\$11.0	\$12.8	\$12.1	\$14.8	\$50.7
Total Operating Income (excl. stock based comp)	\$17.5	\$15.3	\$17.7	\$17.0	\$67.4	\$11.2	\$9.3	\$7.4	\$10.9	\$38.8	\$12.1	\$13.9	\$13.3	\$16.0	\$55.3
Interest and Other Income	\$0.4	\$0.5	\$0.9	\$1.2	\$3.0	\$1.0	\$0.9	\$0.8	\$0.8	\$3.5	\$0.8	\$0.9	\$0.9	\$0.9	\$3.6
Interest and Other Expense	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	
Total Interest Income and Other (Expense)	\$0.4	\$0.5	\$0.9	\$1.2	\$3.0	\$1.0	\$0.9	\$0.8	\$0.8	\$3.5	\$0.8	\$0.9	\$0.9	\$0.9	\$3.6
Pretax Income	\$17.1	\$14.8	\$17.3	\$16.9	\$66.0	\$10.9	\$9.1	\$7.0	\$10.6	\$37.6	\$11.8	\$13.7	\$13.1	\$15.7	\$54.3
Income Tax (Benefit) Non-GAAP	\$2.5	\$2.4	\$3.4	\$1.1	\$9.5	\$1.5	\$1.0	\$0.4	\$1.6	\$4.5	\$1.8	\$2.1	\$2.0	\$2.4	\$8.1
Net Income From Operations (incl. stock based comp)	\$14.6	\$12.4	\$13.8	\$15.8	\$56.5	\$9.4	\$8.1	\$6.7	\$9.0	\$33.2	\$10.0	\$11.6	\$11.1	\$13.4	\$46.1
Net Income From Operations (excl. stock based comp)	\$15.4	\$13.3	\$14.8	\$16.9	\$60.5	\$10.4	\$9.0	\$7.8	\$10.0	\$37.3	\$11.0	\$12.6	\$12.1	\$14.4	\$50.1
Shares Outstanding (Basic)	27.9	28.0	28.0	28.0	28.0	27.9	27.9	27.9	27.9	27.9	27.8	27.7	27.8	27.8	27.8
Shares Outstanding (Diluted)	28.7	28.8	28.8	28.7	28.7	28.6	28.6	28.7	28.8	28.6	28.7	28.6	28.7	28.8	28.7
Continuing Operating EPS (Pro-forma-Diluted Excl. Stock based comp)	\$0.54	\$0.46	\$0.52	\$0.59	\$2.11	\$0.37	\$0.32	\$0.27	\$0.35	\$1.30	\$0.38	\$0.44	\$0.42	\$0.50	\$1.75
Extraordinary Items	\$0.1	\$0.1	\$0.0	\$0.1	\$0.3	(\$1.0)	(\$1.0)	\$0.0	\$0.0	(\$2.0)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Amortization of Intangibles	(\$0.7)	(\$0.7)	(\$0.7)	(\$0.7)	(\$2.6)	(\$0.7)	(\$0.7)	(\$0.7)	(\$0.7)	(\$2.6)	(\$0.7)	(\$0.7)	(\$0.7)	(\$0.7)	(\$2.6)
Reported Net Income	\$14.1	\$11.8	\$13.2	\$15.2	\$54.2	\$7.8	\$6.5	\$6.0	\$8.3	\$28.6	\$9.4	\$11.0	\$10.5	\$12.7	\$43.5
Reported EPS	\$0.49	\$0.41	\$0.46	\$0.53	\$1.89	\$0.27	\$0.23	\$0.21	\$0.29	\$1.00	\$0.33	\$0.38	\$0.36	\$0.44	\$1.52
As a % of Revenue															
Gross Margin	58.1%	57.7%	58.9%	56.6%	57.8%	56.1%	55.5%	54.0%	56.0%	55.3%	56.2%	56.5%	56.5%	56.8%	56.2%
Research & Development	17.4%	18.5%	17.9%	15.8%	17.4%	22.0%	21.5%	23.2%	21.5%	22.0%	21.0%	20.0%	20.0%	19.0%	20.0%
Selling & Marketing	9.6%	11.6%	10.6%	11.2%	10.7%	12.3%	12.3%	12.6%	11.4%	12.1%	11.0%	10.5%	10.7%	10.2%	10.6%
General & Administrative	3.4%	3.2%	3.1%	3.2%	3.2%	2.5%	3.9%	3.5%	3.4%	3.3%	3.2%	3.2%	3.4%	3.0%	3.2%
Operating Income	26.6%	23.1%	25.8%	24.9%	25.1%	17.6%	16.1%	12.4%	17.7%	16.0%	19.0%	20.9%	20.5%	22.8%	20.8%
Pretax Income	27.3%	23.9%	27.2%	26.8%	26.3%	19.3%	17.8%	14.1%	19.2%	17.7%	20.4%	22.4%	22.0%	24.2%	22.3%
Tax Rate (% of Pretax Income)	14.7%	16.3%	20.0%	6.7%	14.4%	14.0%	11.1%	5.0%	15.0%	11.9%	15.0%	15.0%	15.0%	15.0%	15.0%
Net Income	23.3%	20.0%	21.7%	25.0%	22.5%	16.6%	15.8%	13.4%	16.3%	15.6%	17.4%	19.0%	18.7%	20.6%	19.0%
Y/Y Growth															
Revenue	15%	10%	18%	10%	13%	-9%	-17%	-21%	-13%	-15%	2%	20%	19%	18%	14%
Operating Expenses	16%	26%	19%	5%	16%	11%	-6%	-2%	5%	2%	-3%	7%	3%	4%	3%
Continuing Operating EPS	6%	-16%	11%	31%	7%	-35%	-34%	-51%	-43%	-41%	6%	44%	66%	49%	39%
Q/Q Growth															
Revenue	9%	-1%	3%	-1%	NA	-10%	-10%	-2%	10%	NA	5%	6%	-3%	9%	NA
Operating Expenses	3%	9%	-2%	-5%	NA	9%	-8%	3%	1%	NA	1%	2%	-2%	3%	NA
Continuing Operating EPS	21%	-15%	12%	14%	NA	-40%	-14%	-18%	34%	NA	12%	16%	-5%	20%	NA

Source: Company reports and Stifel estimates

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Nova Measuring Instruments Ltd. (NVMI) as of August 06, 2019 (in USD)



*Represents the value(s) that changed.

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