Zacks Small-Cap Research

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O2Micro International Ltd (OIIM-NASDAQ)

OIIM: Zacks Company Report – Company Guides to Up Yr/Yr Q3 Revenues, the First Since 2013

Using an average enterprise value to trailing 12-month sales of 5.0 times and applying it to OIIM's Q2 $53 m revenue run rate, we would calculate an enterprise value of $264, a market cap of $312 m and a price of **$12.15 per share.**

Current Price (08/02/16)	$1.70
Valuation	**$12.15**

OUTLOOK

O_2Micro International is a fabless semiconductor firm that designs, develops and markets high performance integrated circuits primarily for power management and battery management for TV backlighting, LED lighting, and portable tools and appliances. It has had declining revenues and losses for the past few years, but may have reached stability and is guiding to revenue growth in Q3 of 2016. The company trades at a negative enterprise value of $4 million, far less than the value of its assets. There are activists involved in the stock.

SUMMARY DATA

52-Week High	**$2.49**
52-Week Low	**$1.27**
One-Year Return (%)	**-23.1**
Beta	**0.59**
Average Daily Volume (sh)	**30,910**
Shares Outstanding (mil)	**26**
Market Capitalization ($mil)	**$43**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**42**
Insider Ownership (%)	**8**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-18.5**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/M**
P/E using 2016 Estimate	**N/M**
P/E using 2017 Estimate	**N/M**
Zacks Rank	**N/A**

Risk Level	**Average**
Type of Stock	**Small-Value**
Industry	**Elec Comp-Semis**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2014	16.5 A	17.4 A	15.4 A	14.3 A	64 A
2015	13.1 A	14.7 A	13.7 A	13.4 A	55 A
2016	13.0 A	13.2 A	14.3 E	14.5 E	55 E
2017					60 E

Earnings per Share
(EPS is non-GAAP earnings before non-recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2014	-$0.08 A	-$0.10 A	-$0.09 A	-$0.09 A	-$0.36 A
2015	-$0.11 A	-$0.09 A	-$0.07 A	-$0.10 A	-$0.37 A
2016	-$0.08 A	-$0.06 A	-$0.07 E	-$0.05 E	-$0.26 E
2017					-$0.09 E

Zacks Projected EPS Growth Rate - Next 5 Years % **N/A**

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WHAT'S NEW

The Full Range of Q3 Guidance is For Year over Year Revenue Growth

O2Micro reported **Q2 2016 revenues of $13.2 million versus $14.7 million** a year ago, within the company's guidance. More importantly, the revenue guidance for Q3 was for revenues in the range of up 4-12% sequentially (or $13.8 to $14.8 million) versus $13.7 last year. This means that currently the company is fairly confident of up revenues no matter where in the range they fall. Management also believes that Q4 2016 should be flat to up sequentially and thus be at least $13.8 million in revenues versus a $13.4 million revenue quarter in 2015. That would make two quarters in a row of year over year revenue growth. Its current cost structure would show cash breakeven at $16.5-17.5 million in quarterly revenues and profitability breakeven at $18.5-9.5 million. At quarter end the company had $47.5 million in cash and equivalents (or $1.85 per ADS) up $1 million due to the sale of real estate in the quarter despite cash burn from operations.

Revenue Breakdown

	Q2 2015	Q2 2016
Consumer	50-55	50-55
Computer	10-15	10-15
Industrial	30-35	35-40
Communications	<5	<5

In Q2 2016, gross margin was 50.7% versus 49.6% last year and 48.8% in Q1 2016. The company expects gross margins to move around somewhat as new products that are periodically introduced as they initially have lower margins and disrupt the company average. Management has given Q3 gross margin guidance of 49-51%, the same as Q2 guidance.

R&D was $3.8 million, flat with last year, and SG&A came in at $5.0 versus $6.3 million. This was a total expense reduction of $1.4 million, reducing operating losses to $2.1 million in 2016 versus $2.9 million in 2015. The company has guided to operating expenses in a range of $8.9 million to $10.0 million in Q3 2016, a mid-point decline of $1.1 million from Q2 2015. R&D spending was particularly low in Q1 because some development projects were pushed off. It is expected to be remain at $4.0-$4.5 per quarter for the rest of the year.

Interest income was down to $76,000 versus $199,000 last year in line with Q1 2016.

Currency exchange caused a loss of $303,000 versus last year's loss of $152,000.

In last year's other income number there was sale of real estate netting a gain of $201,000. In the 2016 June quarter, the company booked a gain of $413,000 from the sale of X-FAB stock. And in Q3 the company tells us to expect a one-time gain on the sale of one unit of a Shanghai office park of $1.85 million. In Q4 the company is considering selling more of its long term investments, which, if sold, could contribute another $500,000 to $600,000 to other income in that quarter.

Taxes paid were $237,000 versus $287,000.

The GAAP net loss was $2.0 million versus $2.7 million or a loss of $0.08 versus a loss of $0.10. Shares outstanding were 25.7 versus 26.1 and the company bought 104,000 shares in the quarter.

On a non-GAAP basis the company reported a loss of $0.06 in Q2 2016 versus a loss of $0.09 a year ago.

Business continues strong in battery management as more and more appliances and tools become untethered from electrical cords and as lead battery users move to lithium. This quarter it exceeded its goal to be 20-25% of total revenues in 2016. This could bring up overall margins as battery products have a 60% gross margin.

The backlighting business is improving as major international Tier 1 television manufacturer is now in mass production for its 4k TVs and another manufacturer should be brought on shortly. These 4k TVs use more units and generate more revenue per TV set, and are growing as a portion of the total TV market. The company is also has had success in the automotive market where it has achieved design wins. The global market for vehicles in 2015 was 89 million units.



Q3 2016 Forecast

For Q3, the mid-point of the range is $14.3 million in revenues versus $13.7 million, up 4%. With increased spending we expect the operating loss to be the same or more than Q2, but the gain from the sale of real estate should show a decline in the net loss. On a GAAP basis we are looking for a loss of $0.01 versus a loss of $0.09 last year. Non-GAAP EPS could be a loss of $0.07 flat with last year.

VALUATION

Company Has Significant Upside If It Can Grow

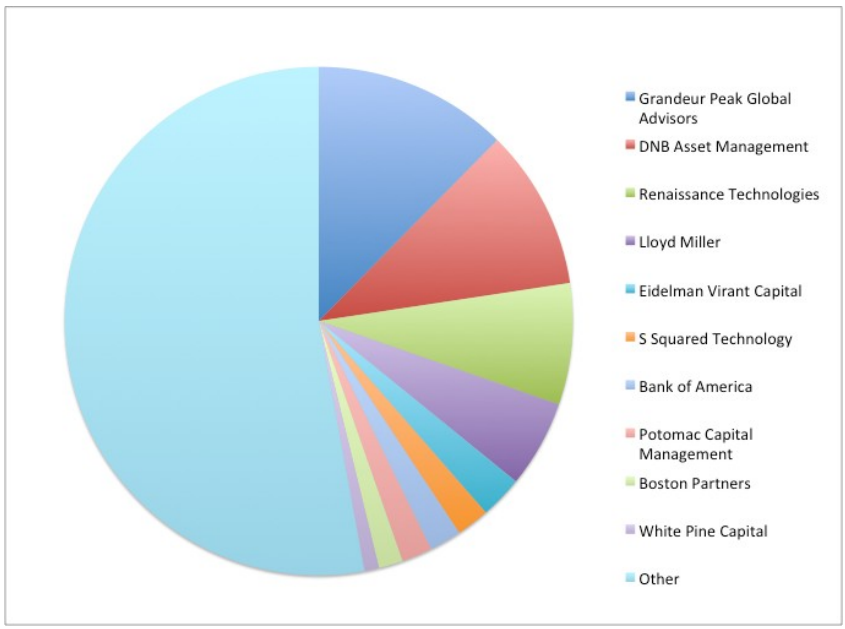
The company trades at a negative enterprise value of $4 million. The company has $47.5 million (or $1.85 per ADS) in cash and equivalents, no debt and valuable real estate in China and California. In California it owns a 37,180 square foot building where it has its USA operations, which was bought for $4.6 million in May 2004. It also owns other real estate in China. It also has long-term investments in other companies. Activists have tried to encourage a transaction with an acquirer but the company has no interest in a sale.

Were we to use the average enterprise value to trailing twelve-month sales of 5.0 times and apply it to OIIM's Q2 $53 million revenue run rate, we would calculate an enterprise value of $264 million. Adding to it $47.5 million in cash gives us a market cap of $312 million or **$12.15 per share**. We believe that once the company shows some revenue growth while continuing to cut losses, the market will afford it a valuation closer to this price. Year over year revenue growth could occur next quarter.

	Competitors	EV	TTM Sales	EV/Sales
Intersil	**ISIL**	$1,810	$518	3.5
Microsemi	**MSCC**	6,470	1,530	4.2
Monolithic Power Systems	**MPWR**	2,700	356	7.6
Cree Inc.	**CREE**	2,480	1,610	1.5
Microchip Technology	**MCHP**	11,990	2,170	5.5
Linear Technology	**LLTC**	13,230	1,420	9.3
Maxim	**MXIM**	10,610	2,190	4.8
Texas Instruments	**TXN**	71,060	12,900	5.5
Cirrus Logic	**CRUS**	2,960	1,150	2.6
	Average			5.0

OWNERSHIP

There are a number of activist hedge funds still involved in the stock as shown below.



RISKS

- O_2Micro has exposure several stagnant and declining markets such as standard TVs and notebooks. It is depending on General LED lighting, battery management, and successful penetration of and volume sales to the smartphone market to give it meaningful revenue and margin growth.
- It may be difficult for the company to capture market share in smartphones and tablets as a new entrant in an established field competing primarily with giant Texas Instruments and other larger firms.
- The firm is currently not at breakeven and is cash flow negative and has declining revenues.
- Given its large number of patents, litigation risk is a possibility as the company enforces its patents.
- Despite years of declining business the company has not been able to right size itself into a profitable entity. Activists have taken a position and encouraged the company to seek a sale or more drastic cost cutting action to realize value for shareholders. However to date this effort has not been successful and may never be.

PROJECTED INCOME STATEMENT

	March Q1 15	June Q2 15	Sept Q3 15	Dec Q4 15	March Q1 16	June Q2 16	Sept Q3 16E	Dec Q4 16E	2014	2015	2016E	2017E
REVENUE												
Net Revenue	13.1	14.7	13.7	13.4	13.0	13.2	14.3	14.5	63.6	54.8	55.0	60.0
Yr-to-yr Gr.	-20%	-16%	-11%	-7%	-1%	-10%	4%	8%	-14%	-14%	0%	9%
OPERATING EXPENSES												
Cost of goods sold	6.5	7.4	6.6	6.6	6.6	6.5	7.1	7.0	30.9	27.1	27.3	28.0
Gross Margin	6.6	7.3	7.1	6.7	6.3	6.7	7.1	7.3	32.7	27.7	27.7	32.0
% of Sales	50.0%	49.6%	51.0%	50.4%	48.8%	50.7%	50.0%	50.4%	51.5%	50.5%	50.3%	53.3%
R&D	4.5	3.8	4.7	4.8	3.8	3.8	4.2	4.2	21.9	17.8	16.0	17.0
SG&A	5.7	6.3	5.8	5.5	4.9	5.0	5.2	5.2	24.7	23.3	20.2	20.2
One-time expenses & Adj.	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0	3.0	1.1	0.0	0.0
Tot Operating Exp.	10.1	10.2	10.5	11.4	8.6	8.8	9.4	9.4	46.6	42.3	36.2	37.2
Operating Income	(3.6)	(2.9)	(3.4)	(4.7)	(2.3)	(2.1)	(2.2)	(2.1)	(13.9)	(14.6)	(8.5)	(5.2)
Interest income	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1		0.7	0.3	0.0
Foreign exchange loss	0.0	(0.2)	0.8	0.0	(0.2)	(0.3)	0.0	0.0		0.7	(0.5)	0.0
Gain on sale of real estate	0.3	0.2	0.3	0.0	0.0	0.0	0.0	0.0		0.8	0.0	0.0
Other - net	0.1	0.2	0.1	0.4	0.2	0.2	2.1	0.0		0.7	2.5	0.2
Gain/loss on long term investments	0.0	0.0	0.0	(5.0)	0.0	0.4	0.0	0.5		(5.0)	0.9	0.0
Total other Income	0.6	0.4	1.3	(4.4)	0.1	0.4	2.2	0.6	2.9	(2.0)	3.2	1.0
Pretax Income	(3.0)	(2.5)	(2.1)	(9.1)	(2.2)	(1.7)	(0.1)	(1.5)	(10.9)	(16.6)	(5.3)	(4.2)
	-22.6%	-16.7%	-15.1%	-68.1%	-16.8%	-13.1%	-0.4%	-10.5%	-17.2%	-30.3%	-9.6%	-7.1%
Taxes	0.2	0.3	0.3	3.8	0.2	0.2	0.2	0.2	1.2	4.6	0.8	0.0
Tax Rate	-8.1%	-11.7%	-13.9%	-10.9%	-9.2%	-13.7%	-311.9%	-13.2%	-10.8%	-28.0%	-15.8%	-11.0%
GAAP Net Income	(3.2)	(2.7)	(2.4)	(12.9)	(2.4)	(2.0)	(0.3)	(1.7)	(12.1)	(21.2)	(6.1)	(4.2)
Non-GAAP Net Income	(2.9)	(2.3)	(1.9)	(2.5)	(2.0)	(1.7)	(1.8)	(1.3)		(9.7)	(6.7)	(4.2)
GAAP EPS-Basic	($0.12)	($0.10)	($0.09)	($0.50)	($0.09)	($0.08)	($0.01)	($0.07)	($0.44)	($0.82)	($0.24)	($0.17)
GAAP EPS-Fully dil.	($0.12)	($0.10)	($0.09)	($0.50)	($0.09)	($0.08)	($0.01)	($0.07)	($0.56)	($0.82)	($0.24)	($0.17)
Non-GAAP	**($0.11)**	**($0.09)**	**($0.07)**	**($0.10)**	**($0.08)**	**($0.06)**	**($0.07)**	**($0.05)**	**($0.36)**	**($0.37)**	**($0.26)**	**($0.09)**
Share Out	26.5	26.1	25.9	25.6	25.7	25.7	25.5	25.3	27.2	26.0	25.5	25.3
Fully diluted shares	26.5	26.1	25.9	25.6	25.7	25.7	25.5	25.3	27.2	26.0	25.5	25.3
Yr-to-yr Gr.	-5%	-5%	-5%	-4%	-3%	-2%	-2%	-1%	-5.1%	-4.5%	-1.9%	-1.0%

BALANCE SHEET

	June 30, 2016	March 31, 2016	% Change
CURRENT ASSETS			
Cash and cash equivalents	$37,475	$35,924	4.3%
Restricted cash	32	32	0.0%
Short-term investments	10,028	10,580	-5.2%
Accounts receivable, net	6,880	5,337	28.9%
Inventories	9,216	9,328	-1.2%
Prepaid expenses and other current assets	1,464	1,388	5.5%
Assets held for sale	1,956	6,924	-71.8%
Total current assets	**67,051**	**69,513**	-3.5%
LONG-TERM INVESTMENTS	4,861	4,331	12.2%
PROPERTY AND EQUIPMENT, NET	13,904	14,077	-1.2%
OTHER ASSETS	2,231	2,375	-6.1%
Total other assets	20,996	20,783	1.0%
TOTAL ASSETS	88,047	90,296	-2.5%
CURRENT LIABILITIES			
Notes and accounts payable	2,746	2,951	-6.9%
Income tax payable	334	469	-28.8%
Deferred tax liabilities	1,030	2,278	-54.8%
Accrued expenses and other current liabilities	3,244	2,859	13.5%
Total current liabilities	7,354	8,557	-14.1%
OTHER LONG-TERM LIABILITIES			
Accrued pension liabilities	272	275	-1.1%
Other liabilities	122	149	-18.1%
Total long-term liabilities	394	424	-7.1%
Total liabilities	7,748	8,981	-13.7%
SHAREHOLDERS EQUITY			
Preference shares at $0.00002 par value per share; Authorized 250,000,000 shares;	33	33	0.0%
Additional paid-in capital	142,038	141,646	0.3%
Retained earnings (accumulated deficits)	(42,716)	(40,750)	4.8%
Accumulated other comprehensive income	5,928	5,258	12.7%
Treasury stock	(24,984)	(24,872)	0.5%
Total shareholders equity	80,299	81,315	-1.2%
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	88,047	90,296	-2.5%
Cash and equivalents	$47,503	$46,504	2.1%
Change in cash and equivalents	$999	(5,928)	-116.9%
Market value	43,644,100	35,207,630	24.0%
Enterprise value	(3,890,900)	(11,328,370)	-65.7%
DSO	42	37	13.5%
Inventory Days	128	129	-0.8%

ANNUAL CASH FLOW

Consolidated Statements of Cash Flows - USD ($) $ in Thousands	12 Months Ended		
	Dec. 31, 2015	Dec. 31, 2014	Dec. 31, 2013
OPERATING ACTIVITIES			
Net loss	$ (21,095)	$ (15,057)	$ (19,099)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	2,446	3,718	4,685
Stock-based compensation	1,912	2,120	2,609
Loss on asset write-off		82	
Inventory write-downs	913	1,538	900
Gain on sale of long-term investments	(8)	(436)	
Impairment loss on long-term investments	4,953	83	
Gain on disposal of property and equipment, net	(738)	(428)	(106)
Deferred income taxes	1,989	78	41
Other, net		(36)	(1)
Changes in operating assets and liabilities:			
Accounts receivable, net	1,592	3,235	(1,251)
Inventories	(1,933)	(2,963)	(200)
Prepaid expenses and other current assets	191	130	510
Deferred charges	(416)	(985)	(1,366)
Notes and accounts payable	1,202	(2,038)	413
Income tax payable	1,595	412	(124)
Accrued expenses and other current liabilities	(1,039)	577	(1,083)
Accrued pension liabilities	(11)	(12)	(25)
Other liabilities	(168)	(346)	(8,893)
Net cash used in operating activities	(8,615)	(10,328)	(22,990)
Acquisition of:			
Short-term investments	(7,128)	(22,346)	(15,496)
Long-term investments			(250)
Property and equipment	(724)	(1,004)	(743)
Decrease (increase) in:			
Restricted assets			10,000
Restricted cash	132	(1)	1
Other assets	82	116	108
Proceeds from:			
Sale of short-term investments	16,755	34,333	52,131
Sale of long-term investments	537	1,304	
Disposal of property and equipment	3,205	1,982	166
Net cash provided by investing activities	12,859	14,384	45,917
FINANCING ACTIVITIES			
Acquisition of treasury stock	(3,233)	(4,965)	(8,279)
Proceeds from:			
Exercise of stock options	31	44	25
Issuance of ordinary shares under the Employee Stock Purchase Plan	180	258	335
Net cash used in financing activities	(3,022)	(4,663)	(7,919)
EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATE	(1,092)	(617)	(613)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	130	(1,224)	14,395
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR	41,069	42,293	27,898
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	41,199	41,069	42,293
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS			
Cash paid for tax	$ 1,068	$ 697	$ 1,064
Cash Flow	(9,628)	(8,420)	(10,971)
Free cash flow	(10,352)	(9,424)	(11,714)

HISTORICAL STOCK PRICE



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