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Zacks Small-Cap Research

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O2Micro International Ltd (OIIM-NASDAQ)

OIIM: Agreement With Feit Electric Could Boost Q4 Revenues and Earnings

Using an industry average value to trailing 12-month sales of 6.2 times and OIIM's $59.7 m trailing 12-month revenue, we would calculate an enterprise value of $368 million, a market cap of $406 million and a price of **$15.43 per share**, if the company could reach breakeven.

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, and smartphones. It has struggled to reach profitability and cash flow breakeven. The company trades at an **enterprise value of $4.2 million**, well below the value of its non-cash assets. It is beginning to gain traction in smartphones, which could allow it to regain its growth.

Current Price (11/01/19)	$1.62
Valuation	**$15.43**

SUMMARY DATA

52-Week High	**$1.80**
52-Week Low	**$1.19**
One-Year Return (%)	**-6.9**
Beta	**0.7**
Average Daily Volume (sh)	**64,566**
Shares Outstanding (mil)	**26.3**
Market Capitalization ($mil)	**$42.6**
Short Interest Ratio (days)	**1.0**
Institutional Ownership (%)	**38**
Insider Ownership (%)	**8**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**1.5**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/M**
P/E using 2018 Estimate	**N/M**
P/E using 2019 Estimate	**N/M**

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)
2017	15.0 A	14.5 A	15.5 A	15.2 A	60 A
2018	14.1 A	15.2 A	16.8 A	16.6 A	63 A
2019	12.8 A	14.3 A	16.0 A	16.2 E	59 E
2020					65 E

Earnings Per Share
(non-GAAP EPS before non-recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	-$0.04 A	-$0.04 A	-$0.04 A	-$0.06 A	-$0.18 A
2018	-$0.09 A	-$0.05 A	-$0.05 A	-$0.05 A	-$0.24 A
2019	-$0.13 A	-$0.08 A	-$0.02 A	-$0.04 E	-$0.25 E
2020					-$0.20 E

Zacks Projected EPS Growth Rate - Next 5 Years % **5**

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WHAT'S NEW

Agreement With Feit Electric Could Boost Q4 Results

On Oct. 30, 2019 O2Micro announced that it has entered into a strategic agreement with Feit Electric Company, Inc., a leading supplier of lighting products. This agreement allows Feit Electric to fully utilize O2Micro's patented Free Dimming technology in its general lighting products. In addition to being granted a license for O2Micro's free dimming patents, the hope is with Feit using O2Micro's technology, and marketing free dimming products, this category could expand both in the residential and commercial markets. Free dimming bulbs allow lights to be dimmed without a dimmer switch. In addition to licensing, we expect Feit may be buying free dimming chips from O2Micro and ultimately, other general and intelligent lighting products O2Micro provides. Feit is privately and held was founded in 1978 in Pico Rivera, California. It has over 100 employees and more that $100 million in annual sales and sells through stores such as Ace Hardware and Home Depot in the US. This agreement is an important step in expanding O2Micro's footprint in the US. To date virtually all of O2Micro's free dimming sales have been in Asia.



Source: Zacks Investment Research

Guidance for revenue for the fourth quarter of 2019 was only that it would be up sequentially. It appears that the partnership with Feit may include the payment of a licensing fee to be booked in Q4 and management indicated they are waiting for a ruling by the auditors as to how to account for it. If it were a one-time licensing fee, booked in revenues in Q4, it would not be broken out, but would affect guidance. There was no indication as to if there is to be a payment for past infringement, a one-time payment for patent licensing or if there would be ongoing payments based on Feit sales of free dimming products. As Feit is a private company, it does not want to disclose its specific financial arrangement with O2Micro for competitive reasons.

Q3 Results Beat Expectations

In the September quarter just announced the company beat the high end of its revenue guidance reporting $16.0 million in sales, down year over year by 5%, but up sequentially by 12.3%.

Intelligent lighting revenue grew due to the recovery in the Chinese TV market and O2Micro's many design wins in both 4K and 8K TVs, expansion of HDR monitors, and gaming, medical, and industrial

applications. Lower end TVs are using its new line of backlighting products with integrated MOSFETs. The company is also introducing new backlighting products for use in the industrial and automotive markets.

Battery management continued to grow with the increased use of lithium ion batteries. The global lithium-ion battery market has a CAGR over 10%. Customers are starting to design in O2Micro's first ARM-based products but due to the complexity of these designs, including firmware development, major revenue is not expected from these products until 2020.
Gross margin in the quarter was 51.4%, up sequentially from 50.1%, and up year over year from 50.5%. Management expects margin next quarter to in the range of 49% to 51%.

R&D declined in the quarter to $4.7 million, as the company reigned in expenses and SG&A declined to $4.6 million from $4.9 million in Q3, reducing operating expenses $375,000 sequentially. Total operating expenses in the quarter were $9.4 million, down from $10.2 million last year, and compared with $9.7 million in Q2 2018. For Q4 the midpoint of guidance is $9.9 million, up $500,000 sequentially with increased spending on R&D for new products, but still below the $10.4 million in last year's Q4.

The operating loss in Q3 decreased to $1.1 million versus $1.7 million last year and $2.6 million in Q2. This is the company's lowest quarterly operating loss since 2016. Adding back depreciation and amortization and stock-based compensation, the adjusted EBITDA looks to be a loss of $301,000.

Total other income was $1.2 million versus -$1.5 million last year, mostly from Excelliance stock marked to market and a realized gain from selling some of the stock. In Q3 2019, O2Micro sold 630,000 shares of Excelliance MOS Corp. (5299.TWO) at $3.80 per share for $2.4 million with a cost basis of $0.53 per share. O2Micro will continue selling stock in Q4.

The company reported a GAAP net loss of $256,000 versus last year's loss of $3.5 million last year. This yielded a GAAP loss per share of $0.01 versus $0.13 a year ago.

Non-GAAP net loss was a loss of $542,000 million, versus a loss of $1.4 million last year. The company reported a **non-GAAP EPS loss of $0.02, versus a loss of $0.05 last year**. In Q3 2019, the company repurchased 37,994 ADS units at a cost of $52,000.

On September 30, 2019, the company had $38.5 million in unrestricted cash and equivalents (or $1.46 per ADS), up $3.6 million sequentially. Net cash generated by operating activities in the quarter was $1.6 million. Capital expenditures were $156,000 and depreciation and amortization was $432,000.

The company believes it can be EBITDA positive between $16 million to $18 million in quarterly revenues, and profitable between $18 million to $20 million in revenues. The company expects "cash profitability" in Q4 2019.

Revenue By Segment

	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019
Consumer	40-45%	42-44%	49-51%	43-45%	46-48%	43-45%	44-46
Computer	10-15	15-17	8-10	6-8	6-8	6-8	6-8
Industrial	40-45	40-42	40-42	47-49	45-47	47-49	47-49
Communications	<5	0	0	0	0	0	0

One-Time Events in Q4

The company expects to continue to sell some Excelliance MOS stock in Q4 2019. It still holds 1 million shares. During Q2 it also sold two units of real estate in Taiwan for $2.2 million, but it collected and booked the sale in October. This will result in a gain on real estate of $495,000 in the fourth quarter.

VALUATION

Company Has Significant Upside If It Can End Cash Burn and Turn a Profit

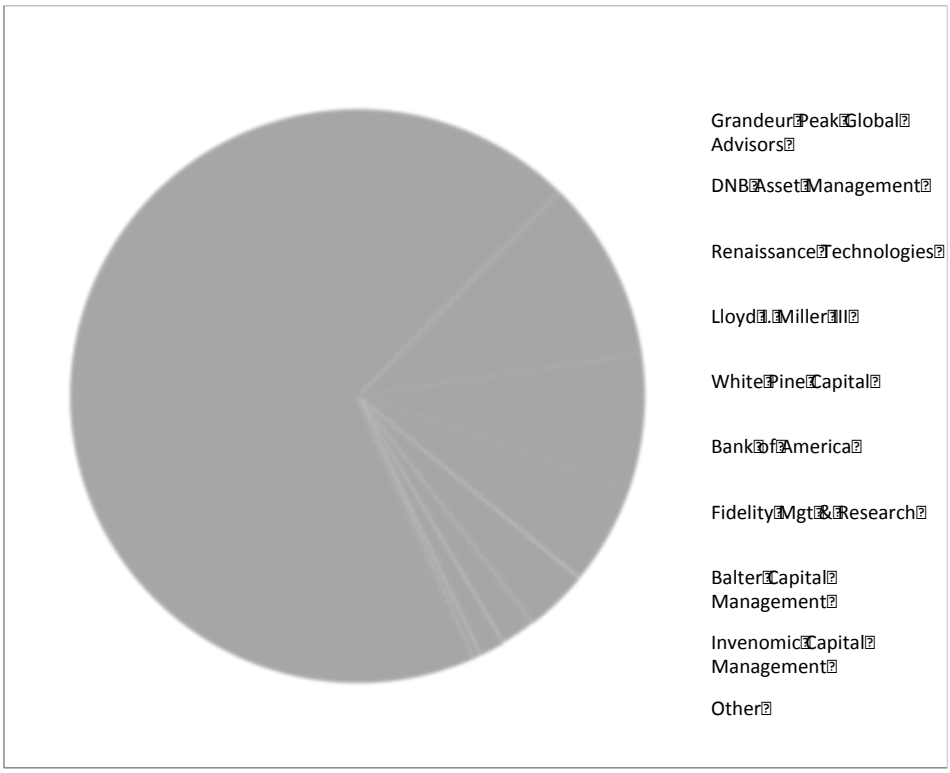
The company trades at an **enterprise value of $4.2 million**. At the end of Q3 2019, the company had $38.5 million (or $1.46 per ADS) in cash and equivalents, no debt, and valuable real estate in China and California. In California it owns a 37,180 square foot building where it has its USA operations, which was bought for $4.6 million in May 2004 and believe it is now worth at least $7 million. Plus it also owns other real estate in China and Taiwan. Also on the balance sheet are long-term investments in other companies, including 1 million shares of stock in Excelliance MOS (worth $4.2 million.) The company has a very high liquidation, as well as acquisition, value. Activists have tried to encourage a transaction with an acquirer, but the company has no interest in a sale and due to restrictions, it is difficult to force one.

Last May, Microchip Technology bought Microsemi for $10.15 billion, which was a valuation of 5.5 times its trailing twelve-month revenues of $1.845 billion. Two other comparable companies we had been using, Intersil and Linear Technology, were acquired at very high valuations. Intersil was acquired by Renesas for $3.2 billion at a valuation of 5.9xs the company's trailing $542.1 million in revenue. Analog Devices acquired linear Technology for $14.8 billion. This was 9.9 times its trailing four quarters of revenue of $1.5 billion.

Were we to use the average enterprise value to trailing twelve-month sales of 6.2 times and apply it to OIIM's trailing 12-month $59.7 million revenues, we would calculate an enterprise value of $368 million. Adding to it $38.5 million in cash gives us a market cap of $406 million or **$15.43 per share**. We believe that once the company shows sustainable revenue growth and cash breakeven, the market should afford it a valuation closer to this price.

	Competitors	EV	TTM Sales	EV/Sales
Monolithic Power Systems	**MPWR**	6,340	615	10.3
Cree Inc.	**CREE**	5,280	3,285	1.6
Microchip Technology	**MCHP**	32,880	5,460	6.0
Maxim	**MXIM**	15,650	2,210	7.1
Texas Instruments	**TXN**	111,420	14,750	7.6
Cirrus Logic	**CRUS**	5,280	1,190	4.4
	Average			6.2

OWNERSHIP



Source: Zacks Investment Research

RISKS

- O_2Micro has high exposure to the global demand for TVs, particularly those sold in China. It is depending on free dimming and high power LED lighting, 4K and 8K and other high end TVs, battery management, IoT, and successful penetration of and volume sales to the smartphone market to give it 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. Ramping revenues for this market has been difficult and has taken longer than expected.

- The firm is currently not at GAAP breakeven, is still operating cash flow negative, and has recently been unable to grow revenues.

- Given its large number of patents, litigation risk is a possibility as the company enforces its patents.

- It also has geopolitical risk as countries move to adjust tariffs for various products. It has been hurt by companies jockeying to avoid US tariffs by moving production sourcing to places like Vietnam and Mexico.

INCOME STATEMENT

	March Q1 18	June Q2 18	Sept Q3 18	Dec Q4 18	March Q1 19	June Q2 19	Sept Q3 19	Dec Q4 19E	2017	2018	2019E	2020E
REVENUE												
Net Revenue	14.1	15.2	16.8	16.6	12.8	14.3	16.0	16.2	60.2	62.7	59.3	65.2
Yr-to-yr Gr.	-6%	5%	8%	9%	-10%	-6%	-5%	-2%	6%	4%	-5%	10%
OPERATING EXPENSES												
Cost of goods sold	6.9	7.3	8.3	8.2	6.3	7.1	7.8	8.1	29.4	30.7	29.3	32.0
Gross Margin	7.2	7.9	8.5	8.3	6.4	7.1	8.2	8.1	30.8	32.0	29.9	33.2
% of Sales	51.2%	52.1%	50.5%	50.3%	50.5%	50.1%	51.4%	50.0%	51.1%	51.0%	50.5%	51.0%
R&D	4.8	4.7	5.2	5.0	5.1	4.8	4.7	5.0	18.0	19.8	19.7	20.1
SG&A	5.0	5.0	4.9	5.4	5.0	4.9	4.6	4.9	19.0	20.3	19.3	19.8
One-time expenses & Adj.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	(0.0)	(0.0)	0.0	0.0
Tot Operating Exp.	9.8	9.7	10.2	10.4	10.0	9.7	9.4	9.9	37.0	40.1	39.0	39.9
Operating Income	(2.5)	(1.8)	(1.7)	(2.1)	(3.6)	(2.6)	(1.1)	(1.8)	(6.2)	(8.1)	(9.1)	(6.7)
Interest income	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.3	0.4	0.4	0.2
Unrealized fair value on LT Investment	9.8	3.1	(1.7)	(1.4)	0.0	(0.2)	0.7	0.0	0.0	9.8	0.5	0.0
Foreign exchange loss	(0.2)	0.2	0.0	0.1	(0.1)	0.1	0.0	0.0	0.1	0.1	(0.1)	0.0
Gain on sale of real estate	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.5	0.0	0.0	0.5	0.0
Other (rent) - net	0.3	0.1	0.1	0.5	0.1	0.1	0.4	0.1	0.7	1.0	0.8	0.6
Total other Income	10.0	3.6	(1.5)	(0.7)	0.1	0.1	1.2	0.8	1.1	11.4	2.1	0.8
Pretax Income	7.5	1.7	(3.2)	(2.8)	(3.5)	(2.5)	0.1	(1.0)	(5.1)	3.3	(7.0)	(5.9)
Pretax margin	52.8%	11.5%	-18.9%	-16.6%	-27.6%	-17.4%	0.5%	-6.3%	-8.5%	5.2%	-11.8%	-9.0%
Taxes	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	1.0	1.1	1.2	1.1
Tax Rate	3.6%	15.2%	-8.9%	-12.0%	-8.5%	-11.6%	436.8%	-29.2%	-19.7%	34.9%	-17.5%	-18.7%
GAAP Net Income	7.2	1.5	(3.5)	(3.1)	(3.8)	(2.8)	(0.3)	(1.3)	(6.1)	2.1	(8.2)	(7.0)
Non-GAAP Net Income	(2.2)	(1.3)	(1.4)	(1.4)	(3.5)	(2.2)	(0.5)	(1.0)	(4.6)	(6.3)	(6.6)	(5.4)
GAAP EPS-Basic	$0.28	$0.06	($0.13)	($0.12)	($0.15)	($0.11)	($0.01)	($0.05)	($0.24)	$0.08	($0.31)	($0.27)
GAAP EPS-Fully dil.	$0.27	$0.06	($0.13)	($0.12)	($0.14)	($0.11)	($0.01)	($0.05)	($0.24)	$0.08	($0.31)	($0.27)
Non-GAAP	**($0.08)**	**($0.05)**	**($0.05)**	**($0.05)**	**($0.13)**	**($0.08)**	**($0.02)**	**($0.04)**	**($0.18)**	**($0.24)**	**($0.25)**	**($0.20)**
Share Out	26.0	26.0	26.0	26.0	26.3	26.4	26.3	26.3	25.8	26.0	26.3	26.3
Fully diluted shares	26.5	26.5	26.5	26.6	26.9	26.4	26.3	26.3	25.8	26.6	26.5	26.3
Yr-to-yr Gr.	2%	2%	3%	4%	2%	0%	0%	-1%	1%	3%	-1%	-1%

BALANCE SHEET

	Sept 30, 2019	June 30, 2019	Sept-June % Change	Sept 30, 2018	Yr-to-Yr % Change
CURRENT ASSETS					
Cash and cash equivalents	$19,217	$12,955	48.3%	$33,856	-43.2%
Restricted cash	34	34	0.0%	34	0.0%
Short-term investments	19,239	21,950	-12.4%	7,331	162.4%
Accounts receivable, net	12,358	11,143	10.9%	11,291	9.5%
Inventories	9,807	9,910	-1.0%	9,960	-1.5%
Prepaid expenses and other current assets	1,633	2,360	-30.8%	2,326	-29.8%
Total current assets	**62,288**	**58,352**	6.7%	**64,798**	-3.9%
LONG-TERM INVESTMENTS	4,805	6,463	-25.7%	13,104	-63.3%
PROPERTY AND EQUIPMENT, NET	17,139	17,365	-1.3%	13,703	25.1%
OTHER ASSETS	2,168	2,321	-6.6%	2,132	1.7%
Total other assets	24,112	26,149	-7.8%	28,939	-16.7%
TOTAL ASSETS	86,400	84,501	2.2%	93,737	-7.8%
CURRENT LIABILITIES					
Notes and accounts payable	3,978	2,839	40.1%	5,138	-22.6%
Income tax payable	536	384	39.6%	435	23.2%
Lease liabilities	916	975	-6.1%	0	NA
Accrued expenses and other current liabilities	5,335	4,420	20.7%	4,654	14.6%
Total current liabilities	10,765	8,618	24.9%	10,227	5.3%
OTHER LONG-TERM LIABILITIES					
Accrued pension liabilities	277	295	-6.1%	333	-16.8%
Deferred tax liabilities	717	673	6.5%	1,099	-34.8%
Lease liabilities	2,012	2,124	-5.3%	0	NA
Other liabilities	87	86	1.2%	86	1.2%
Total long-term liabilities	3,093	3,178	-2.7%	1,518	103.8%
Total liabilities	13,858	11,796	17.5%	11,745	18.0%
SHAREHOLDERS EQUITY					
Ordinary shares	33	33	0.0%	33	0.0%
Additional paid-in capital	143,136	142,775	0.3%	142,794	0.2%
Retained earnings (accumulated deficits)	(53,514)	(53,282)	0.4%	(42,780)	25.1%
Accumulated other comprehensive income	4,237	4,544	-6.8%	4,759	-11.0%
Treasury stock	(21,350)	(21,365)	-0.1%	(22,814)	-6.4%
Total shareholders equity	72,542	72,705	-0.2%	81,992	-11.5%
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	86,400	84,501	2.2%	93,737	-7.8%
Cash and equivalents	$38,456	$34,905	10.2%	$41,187	-6.6%
Change in cash and equivalents	(130)	(6,282)	-97.9%	375	-134.7%
Market value	42,682,140	37,161,960	14.9%	43,425,560	-1.7%
Enterprise value	4,192,140	2,222,960	88.6%	2,204,560	90.2%
DSO	66	62	6.5%	60	10.0%
Inventory Days	114	130	-12.3%	108	5.6%

ANNUAL CASH FLOW

	12 Months Ended December 31,					
	2018	2017	2016	2015	2014	2013
OPERATING ACTIVITIES						
Net loss	$ 2,088	$ (6,145)	$ (2,986)	$ (21,095)	$ (15,057)	$ (19,099)
Adjustments to reconcile net loss to net cash used in operating activities:						
Depreciation and amortization	1,641	1,667	1,682	2,446	3,718	4,685
Stock-based compensation	1,421	1,589	1,606	1,912	2,120	2,609
Loss on asset write-off	0	0	0	0	82	
Inventory write-downs	1,328	642	1,527	913	1,538	900
Net gain recognized on LT investments	(9,916)	0	0	0	0	0
Gain on sale of long-term investments	0	(20)	(948)	(8)	(436)	0
Impairment loss on long-term investments	0	0	0	4,953	83	0
Gain on disposal of property & eqt, net	(6)	(137)	(1,726)	(738)	(428)	(106)
Deferred income taxes	(155)	40	(1,231)	1,989	78	41
Other, net	0	0	0	0	(36)	(1)
Changes in operating assets and liabilities:						
Accounts receivable, net	(2,204)	(1,979)	(2,008)	1,592	3,235	(1,251)
Inventories	(2,286)	(697)	(1,140)	(1,933)	(2,963)	(200)
Prepaid expenses and other current assets	(1,031)	(139)	(6)	191	130	510
Deferred charges	(983)	(553)	(375)	(416)	(985)	(1,366)
Notes and accounts payable	2,122	(1,869)	996	1,202	(2,038)	413
Income tax payable	72	161	(2,065)	1,595	412	(124)
Accrued expenses and other current liabilities	(105)	186	(1,064)	(1,039)	577	(1,083)
Accrued pension liabilities	(20)	13	(4)	(11)	(12)	(25)
Other liabilities	(1)	3	(56)	(168)	(346)	(8,893)
Net cash used in operating activities	(8,035)	(7,238)	(7,798)	(8,615)	(10,328)	(22,990)
Acquisition of:						
Short-term investments	(11,197)	(8,505)	(28,797)	(7,128)	(22,346)	(15,496)
Long-term investments		0	0	0	0	(250)
Property and equipment	(1,272)	(704)	(673)	(724)	(1,004)	(743)
Decrease (increase) in:						
Restricted assets	0	0	0	0	0	10,000
Restricted cash	0	0	0	132	(1)	1
Other assets	(12)	22	40	82	116	108
Proceeds from:						
Sale of short-term investments	22,540	12,635	18,331	16,755	34,333	52,131
Sale of long-term investments	2,582	0	5,982	167	1,304	0
Return of capital from LT investment	0	1,163	17	370	0	0
Disposal of property and equipment	16	145	3,837	3,205	1,982	166
Net cash provided by investing activities	12,657	4,756	(1,263)	12,859	14,384	45,917
FINANCING ACTIVITIES						
Acquisition of treasury stock	(451)	(708)	(619)	(3,233)	(4,965)	(8,279)
Proceeds from:						
Exercise of stock options	10	29	2	31	44	25
Issuance of ordinary shares under the Employee Stock Purchase Plan	86	84	73	180	258	335
Net cash used in financing activities	(355)	(595)	(544)	(3,022)	(4,663)	(7,919)
EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATE	(374)	268	(261)	(1,092)	(617)	(613)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	3,893	(2,809)	(9,866)	130	(1,224)	14,395
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR	28,555	31,364	41,230	41,069	42,293	27,898
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	32,448	28,555	31,364	41,199	41,069	42,293
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS						
Cash paid for tax	$ 1,218	$ 818	$ 4,349	$ 1,068	$ 697	$ 1,064
Cash Flow	(3,599)	(2,364)	(2,076)	(9,628)	(8,338)	(10,971)
Free cash flow	(4,871)	(3,068)	(2,749)	(10,352)	(9,342)	(11,714)

HISTORICAL STOCK PRICE



Source: Zacks Investment Research

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