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Zacks Small-Cap Research

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O2Micro International Ltd (OIIM-NASDAQ)

OIIM: A Small Fish in the Smartphone Pond

Using an industry average value to trailing 12-month sales of 6.1 times and OIIM's $61.4 m trailing 12-month revenue, we would calculate an enterprise value of $375 million, a market cap of $410 million and a price of **$15.20 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 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 (05/03/19)	$1.43
Valuation	**$15.20**

SUMMARY DATA

52-Week High	**$2.37**
52-Week Low	**$1.33**
One-Year Return (%)	**-4.3**
Beta	**0.7**
Average Daily Volume (sh)	**28,741**
Shares Outstanding (mil)	**26**
Market Capitalization ($mil)	**$37**
Short Interest Ratio (days)	**1.0**
Institutional Ownership (%)	**41**
Insider Ownership (%)	**8**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-0.7**
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	**Above 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	13.3 E	16.1 E	16.8 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	-$0.10 E	-$0.05 E	-$0.04 E	-$0.25 E
2020					-$0.15 E

Zacks Projected EPS Growth Rate - Next 5 Years % **8**

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WHAT'S NEW

Company Cuts Expenses After a Weak Q1

O2Micro revenues for Q1 came in at $12.8 million inline with its downwardly revised guidance of $12.5 million to $13 million. This is a decrease of 10% compared with last year, and 23% sequentially. Weakness in TV sales in China continues, but demand has been picking up as the inventory correction from the wafer shortages has been mostly resolved. O2Micro still expects revenues to improve in the latter half as design wins convert to ramping production, particularly in smartphones, and TV demand stabilizes.

Guidance for revenue for the second quarter of 2019 was sequentially flat to up 8% from Q1 2019, the midpoint of which is $13.3 million, which would be down 13% over last year. O2Micro still expects to see improvement in latter half of 2019. The second half usually accounts for 60% of TV sales and this year the company will see a production ramp for 8 cell phone designs with hopefully many more to follow if successful. As management said it is such a small fish in the large smartphone pond, even small penetration can produce large revenues for the company. Sales into the smartphone market will initially have gross margins below the corporate average of 50% but will improve with volume.

Gross margin in the quarter was 50.5%, up sequentially from 50.3%, and down year over year from 51.2%, due to product mix.

R&D increased to $5.1 million in the quarter, from $5.0 million in Q4, but still down from the peak in Q2 when spending ramped due to a push to complete new battery management products. In last year's quarter O2Micro spent $4.8 million. In Q2 O2Micro took steps to reduce R&D spending and lower its breakeven. Steps included reducing headcount, and prioritizing R&D to focus on more important products. In Q2, guidance for R&D is $4.3 million to $4.8 million excluding severance charges that should be $150,000 in total.

SG&A was $5.0 million, flat with last year and down from $5.4 million in Q4. In Q4 2018, the company had an extra one time expense of $200,000-$250,000 for logistics for the accelerated deliveries of orders.

Total operating expenses in the quarter were $10.0 million, $200,000 more than last year, and compared with $10.4 million in Q4 2018.

The operating loss in Q1 was $3.6 million versus $2.5 million last year and $2.1 million in Q4.

Other income was $72,000 versus $10 million last year when Excelliance IPOed and was marked to market. In Q1 2019, O2Micro sold 510,000 shares of Excelliance MOS Corp. (5299.TWO) at $3.69 per share for $1.9 million with a cost basis of $0.54 per share.

The company reported a GAAP net loss of $3.8 million versus last year's gain of $7.2 million last year. This yielded a GAAP loss per share of $0.15 versus a gain of $0.28 a year ago.

Non-GAAP net loss was a loss of $3.5 million, versus a loss of $2.2 million last year. The company reported a **non-GAAP EPS loss of $0.13, versus a loss of $0.08 last year**. In Q1 2019, the company repurchased 119,769 ADS units at a cost of $194,000.

On March 31, 2019, the company had $35.2 million in cash and equivalents (or $1.33 per ADS), down $3.3 million sequentially. During the quarter EBITDA was a negative $3.1 million. Net cash used in operating activity was $4,524,000. Capital expenditures was about $738,000 in the first quarter for R&D, information technology equipment, and tester upgrades.

The company has lowered its breakeven point. It believes it can be EBITDA positive between $16 million to $18 million in quarterly revenues (a reduction of $1 million), and profitable between $18 million to $20 million in revenues.

O2Micro continues its extensive R&D efforts and in Q1 it was awarded three new patents in battery management: US patent number 8,922,218 Detection circuits for batteries**,** US patent number 9,291,680 Circuits and methods for measuring a cell voltage in a battery, and US patent number 9,368,981 System and methods for current balancing.

The company is depending on a better second half due to higher sales of TV components as well as an increase in smartphones sales as previous design wins ramp into production volumes. If smartphone customers like the results, we expect more usage in future products and revenues from these large customers that could be very meaningful to tiny O2Micro. It currently has four design wins in initial production involving three key customers and four more design wins in prototype production that includes two additional customers. This includes products that are going into phones **for brand name carriers**. By Q3, the company expects to have at least eight design wins in production, with as many as **eight key customers** actively using or designing its products into their systems. These design wins involve chargers for applications including: high powered 2-cell charging, IoT product, wearables, and express charging as well as gas gauges and complex integrated custom product. So far they have been taking market share from Texas Instruments in high-end smartphones, MediaTek and Qualcomm for charging, and Dialog for DC/DC product. If all goes well, we should begin to see indications by year-end that these major customers will begin to use product in more of their devices.

Revenue By Segment

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

Q2 Guidance

O2Micro expects Q2 2019 revenue to be flat to up 8% sequentially. It is guiding for Q2 gross margin to be in the range of 49% to 51%, mainly based on the product mix. R&D expense, excluding stock-based compensation but including one-time severance payment charges of $150,000, is expected to be in the range of $4.3 million to $4.8 million. SG&A expense, excluding stock-based compensation but including one-time severance charges, is expected to be in the range all $4.5 million to $5 million. Stock-based compensation should be in the range of $300,000 to $400,000 for the quarter. Non-operating income should be in the range of $750,000 to $850,000, excluding the net gain or loss recognized on long-term investment. Based on the service income of subsidiaries in different countries, it expects its tax amount to be in the range of $250,000 to $350,000.

The company expects to continue to sell Excelliance stock and will sell some in Q2 2019. During Q2 it also sold two units of real estate in China for $2.2 million and this will result in a gain on investment of $600,000 in the quarter.

VALUATION

Company Has Significant Upside If It Can End Cash Burn

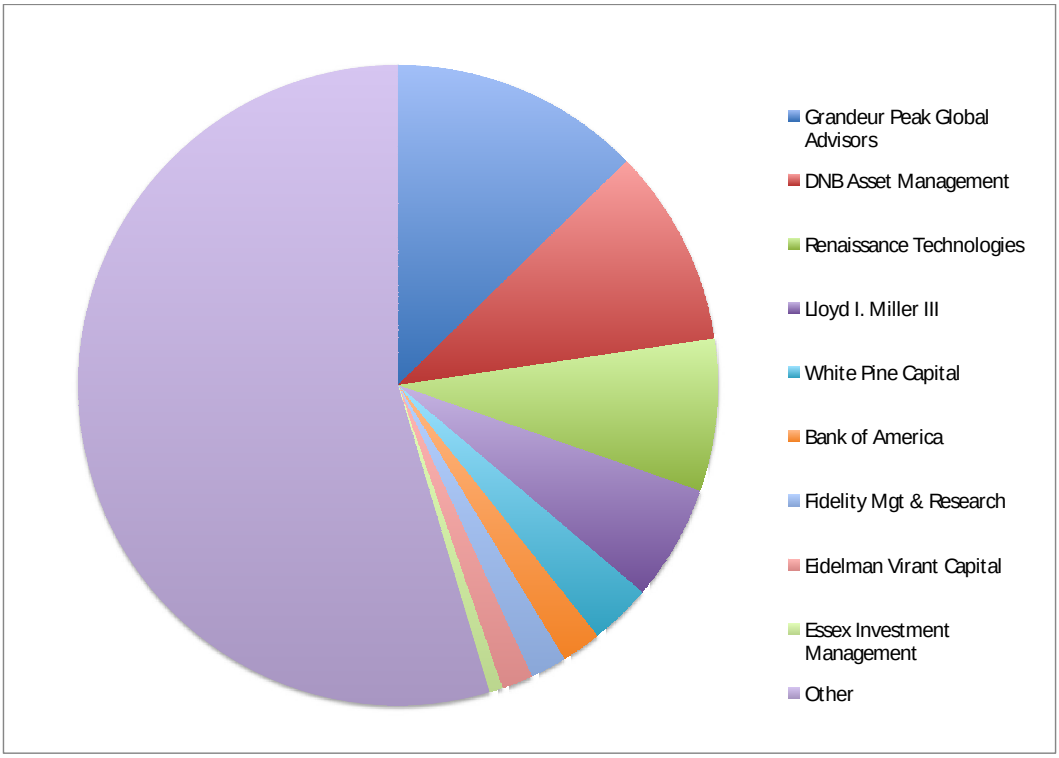
The company trades at an **enterprise value of $4 million**. At the end of Q1 2019, the company had $35.2 million (or $1.33 per ADS) in cash and equivalents, no debt, and valuable real estate in China and California. In California it owns a 37,180 square foot building where it has its USA operations, 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 approximately 2.2 million shares of stock in Excelliance MOS (worth $6.9 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 6.1 times and apply it to OIIM's trailing 12-month $61.4 million revenues, we would calculate an enterprise value of $375 million. Adding to it $35.2 million in cash gives us a market cap of $410 million or **$15.20 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**	6,240	582	10.7
Cree Inc.	**CREE**	6,460	1,590	4.1
Microchip Technology	**MCHP**	33,500	5,020	6.7
Maxim	**MXIM**	15,280	2,391	6.4
Texas Instruments	**TXN**	112,340	15,590	7.2
Cirrus Logic	**CRUS**	2,140	1,250	1.7
	Average			6.1

OWNERSHIP



RISKS

- O_2Micro has high exposure to the global demand for TVs, which can be hurt in recessions. It is depending on free dimming and high power LED lighting, 4K and 8K and other high end TVs, battery management, 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.

- The firm is currently not at GAAP breakeven, is still 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.

INCOME STATEMENT

	March Q1 18	June Q2 18	Sept Q3 18	Dec Q4 18	March Q1 19	June Q2 19E	Sept Q3 19E	Dec Q4 19E	2017	2018	2019E	2020E
REVENUE												
Net Revenue	14.1	15.2	16.8	16.6	12.8	13.3	16.1	16.8	60.2	62.7	58.9	64.8
Yr-to-yr Gr.	-6%	5%	8%	9%	-10%	-13%	-4%	1%	6%	4%	-6%	10%
OPERATING EXPENSES												
Cost of goods sold	6.9	7.3	8.3	8.2	6.3	6.6	8.0	8.3	29.4	30.7	29.3	31.9
Gross Margin	7.2	7.9	8.5	8.3	6.4	6.6	8.1	8.5	30.8	32.0	29.7	32.9
% of Sales	51.2%	52.1%	50.5%	50.3%	50.5%	50.0%	50.3%	50.6%	51.1%	51.0%	50.4%	50.8%
R&D	4.8	4.7	5.2	5.0	5.1	4.5	4.6	4.6	18.0	19.8	18.8	18.4
SG&A	5.0	5.0	4.9	5.4	5.0	5.0	5.0	5.1	19.0	20.3	20.1	19.8
One-time expenses & Adj.	0.0	0.0	0.0	0.0	0.0	0.2	0.0	0.0	(0.0)	(0.0)	0.1	0.0
Tot Operating Exp.	9.8	9.7	10.2	10.4	10.0	9.6	9.6	9.7	37.0	40.1	39.0	38.2
Operating Income	(2.5)	(1.8)	(1.7)	(2.1)	(3.6)	(3.0)	(1.5)	(1.2)	(6.2)	(8.1)	(9.3)	(5.3)
Interest income	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.3	0.4	0.3	0.2
Unrealized fair value on LT Investment	9.8	3.1	(1.7)	(1.4)	0.0	0.0	0.0	0.0	0.0	9.8	0.0	0.0
Foreign exchange loss	(0.2)	0.2	0.0	0.1	(0.1)	0.0	0.0	0.0	0.1	0.1	0.0	0.0
Gain on sale of real estate	0.0	0.0	0.0	0.0	0.0	0.6	0.0	0.0	0.0	0.0	0.0	0.0
Other (rent) - net	0.3	0.1	0.1	0.5	0.1	0.1	0.1	0.1	0.7	1.0	2.1	0.6
Total other Income	10.0	3.6	(1.5)	(0.7)	0.1	0.8	0.2	0.2	1.1	11.4	2.4	0.8
Pretax Income	7.5	1.7	(3.2)	(2.8)	(3.5)	(2.2)	(1.3)	(1.0)	(5.1)	3.3	(6.9)	(4.5)
Pretax margin	52.8%	11.5%	-18.9%	-16.6%	-27.6%	-16.5%	-8.1%	-6.0%	-8.5%	5.2%	-11.7%	-6.9%
Taxes	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	1.0	1.1	1.3	1.1
Tax Rate	3.6%	15.2%	-8.9%	-12.0%	-8.5%	-13.7%	-23.0%	-29.8%	-19.7%	34.9%	-19.2%	-24.5%
GAAP Net Income	7.2	1.5	(3.5)	(3.1)	(3.8)	(2.5)	(1.6)	(1.3)	(6.1)	2.1	(8.2)	(5.6)
Non-GAAP Net Income	(2.2)	(1.3)	(1.4)	(1.4)	(3.5)	(2.6)	(1.2)	(1.0)	(4.6)	(6.3)	(6.6)	(4.0)
GAAP EPS-Basic	$0.28	$0.06	($0.13)	($0.12)	($0.15)	($0.10)	($0.06)	($0.05)	($0.24)	$0.08	($0.31)	($0.22)
GAAP EPS-Fully dil.	$0.27	$0.06	($0.13)	($0.12)	($0.14)	($0.09)	($0.06)	($0.05)	($0.24)	$0.08	($0.31)	($0.22)
Non-GAAP	**($0.08)**	**($0.05)**	**($0.05)**	**($0.05)**	**($0.13)**	**($0.10)**	**($0.05)**	**($0.04)**	**($0.18)**	**($0.24)**	**($0.25)**	**($0.15)**
Share Out	26.0	26.0	26.0	26.0	26.3	26.0	26.0	26.0	25.8	26.0	26.1	26.0
Fully diluted shares	26.5	26.5	26.5	26.6	26.9	26.9	26.9	26.9	25.8	26.6	26.9	26.9
Yr-to-yr Gr.	2%	2%	3%	4%	2%	2%	2%	1%	1%	3%	1%	0%

BALANCE SHEET

	March 31, 2019	Dec 31, 2018	Mar-Dec % Change	March 31, 2018	Yr-to-Yr % Change
CURRENT ASSETS					
Cash and cash equivalents	$31,058	$32,414	-4.2%	$25,417	18.2%
Restricted cash	34	34	0.0%	36	-5.9%
Short-term investments	4,189	6,172	-32.1%	19,695	-370.2%
Accounts receivable, net	8,592	11,388	-24.6%	8,043	6.4%
Inventories	10,608	10,288	3.1%	9,662	8.9%
Prepaid expenses and other current assets	2,347	2,276	3.1%	1,685	28.2%
Total current assets	**56,828**	**62,572**	-9.2%	**64,538**	-13.6%
LONG-TERM INVESTMENTS	8,567	10,445	-18.0%	12,849	-50.0%
PROPERTY AND EQUIPMENT, NET	15,283	13,714	11.4%	13,751	10.0%
OTHER ASSETS	2,444	2,578	-5.2%	2,232	8.7%
Total other assets	26,294	26,737	-1.7%	28,832	-9.7%
TOTAL ASSETS	83,122	89,309	-6.9%	93,370	-12.3%
CURRENT LIABILITIES					
Notes and accounts payable	1,746	4,582	-61.9%	3,290	-88.4%
Income tax payable	444	413	7.5%	292	34.2%
Lease liabilities	727				
Accrued expenses and other current liabilities	3,188	4,181	-23.8%	3,761	-18.0%
Total current liabilities	6,105	9,176	-33.5%	7,343	-20.3%
OTHER LONG-TERM LIABILITIES					
Accrued pension liabilities	315	321	-1.9%	358	-13.7%
Deferred tax liabilities	735	681	7.9%	1,012	-37.7%
Lease liabilities	344				
Other liabilities	87	85	2.4%	88	-1.1%
Total long-term liabilities	1,481	1,087	36.2%	1,458	1.6%
Total liabilities	7,586	10,263	-26.1%	8,801	-16.0%
SHAREHOLDERS EQUITY					
Ordinary shares	33	33	0.0%	33	0.0%
Additional paid-in capital	142,424	143,115	-0.5%	142,128	0.2%
Retained earnings (accumulated deficits)	(50,440)	(45,912)	9.9%	(40,702)	19.3%
Accumulated other comprehensive income	4,844	4,674	3.6%	6,014	-24.2%
Treasury stock	(21,325)	(22,864)	-6.7%	(22,904)	-7.4%
Total shareholders equity	75,536	79,046	-4.4%	84,569	-12.0%
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	83,122	89,309	-6.9%	93,370	-12.3%
Cash and equivalents	$35,247	$38,586	-8.7%	$45,112	-28.0%
Change in cash and equivalents	(5,940)	(2,226)	166.8%	(1,064)	82.1%
Market value	38,836,000	40,698,000	-4.6%	35,214,410	9.3%
Enterprise value	3,555,000	2,078,000	71.1%	(9,933,590)	379.4%
DSO	70	62	12.9%	55	21.4%
Inventory Days	149	111	34.2%	124	16.8%

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



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