

Pivotal Systems Corporation

Poised for semiconductor industry recovery

Pivotal Systems (PVS:ASX) provides gas flow control (GFC) solutions for the production of semiconductors. The company sells its products predominantly to OEM semiconductor processing tools which are then sold to Integrated Device Manufacturers (IDM's) for use in fabrication plants globally. The company has manufacturing facilities in the USA and Korea. The group's strategy is to leverage established relationships across its IDM customer base for new semiconductor processes while gaining increased acceptance by major Original Equipment Manufacturers (OEM's) in new applications or tool sets and in particular high temperate applications. These client-led new products will be key to future market share gains. Repair and upsell opportunities are also arising as existing GFC's in the field come off warranty. Key drivers of the business are end market semiconductor demand and IDM/OEM capex spend. Key industry forecasting group SEMI has forecast record industry capex spend in CY21 with growth of 11% on-top of the 6% expected in CY20. The company ended June 30 with US\$9.1m (A\$13.2m) in cash, which based on the June quarter cash burn of US\$1.8m represents 5-quarters of cash at the current burn rate.

Business model

PVS supplies gas flow control (GFC) solutions to the semiconductor industry. Semiconductors are essential components of most electronic circuits and gas flow control is critical for gas flow and chamber condition in today's wafer processing. PVS sells the hardware/software to IDM and OEM manufacturers. Over time PVS is looking to gradually diversify away from low flow (Etch) GFC sales towards the company's high temperature products. The company is also expecting increased repair & upsell opportunities as existing GFC's in the field come out of warranty, with its Korean upgrade centre qualified in Q2CY20.

Recent company commentary

PVS reported 1HCY20 unaudited revenue of US\$10.1m, +26% on the PCP, and expects growth in 2HCY20 off this base. The company finished the quarter with US\$9.1m in cash and cash burn from operations of US\$722k/month, implying 13-months' cash runway. Management expects further growth in CY21 based on industry forecasts from SEMI®, which has forecast global sales of semiconductor manufacturing equipment by OEM's to increase 6% in CY20 and 11% in CY21. In terms of revenue mix 1HCY20 saw low flow Etch sales accounting for 99% of revenue, an OEM/IDM split of 94%/6% and repair revenue of US\$325k (3% of sales).

Peer group hardware/software-based technology

While there are no direct ASX listed peers for PVS, investors should look at niche small cap hardware/software-based technology players who are loss making with similar challenges (funding, working capital, low gross margin and dealing with multinationals). Companies that come to mind include Shekel Brainweigh, Micro-X and Orbital Engine. For industry trends OEM's such as LAM Research (NASDAQ:LRCX) and Applied Materials (NASDAQ:AMAT) and Tokyo Electron (TYO:8035) should be monitored.

Historical earnings and ratios

Year end	Revenue (US\$m)	Gross Profit (US\$m)	EBITDA Adj.*(US\$)	NPAT Rep.	EPS Adj.*(c)	GP% (c)	EV/Sales (x)
12/16a	8.17	1.64	(2.70)	(4.71)	nm	20%	13.4
12/17a	15.44	3.87	(1.10)	(3.63)	nm	25%	7.1
12/18a	20.30	6.13	0.01	(4.05)	nm	30%	5.4
12//19a	15.30	1.73	(7.20)	(9.90)	nm	11%	7.2

Source: Company data *EBITDA and NPAT adj for one-time, non-cash items

Technology - hardware

4 September 2020

Share details

ASX Code	PVS
Share price (3-Sep)	\$1.07
Market Capitalisation	\$122.0M
Shares on issue	114.0M
Net cash at 30/06/2020	US\$9.1M (A\$13.2M)
Free float	60.5%

Share performance (12 months)



Upside Case

- Move to high tech high temperature GFC products
- Mix shift to IDM's over concentrated OEM market
- Repair and upsell opportunities

Downside Case

- Slowdown in semiconductor demand
- Unable to secure required funding
- New technology not embraced

Catalysts/upcoming events

- Final CY20 result (Late Feb 2021)
- Continued expansion into the Chinese IDM and OEM market

Comparable companies (Aust/NZ)

Shekel Brainweigh (ASX:SBW), Micro-X (ASX:MX1), Orbital Engine (ASX:OEC)

Top 5 shareholders

Firsthand Venture Group	39.5%
Perennial Value Management Ltd	12.5%
LHC Capital Partners	9.7%
Anzu Partners	6.3%
Enterprise Partners Management	5.4%

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FINANCIAL SERVICES GUIDE

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