

Brooks Automation: BRKS

Hunter Sanna

Sector: Technology

Industry: Semiconductor Equipment /Material

Current Price: \$23.01

Target Price: \$ 32.56

Company Description: Brooks Automation Inc. operates in the provision of automation and cryogenic solutions for multiple markets, including semiconductor capital equipment and life science biological sample management. They currently operate through two segments which are Brooks Semiconductor Solutions and Brooks Life Science System. The semiconductor segments includes atmospheric and vacuum robots, as well as tool automation systems. The Life Science Systems segments automates cold sample management system for biological sample storage, preparation, handling, consumables and parts and support services.

BUY

Current Price: \$23.01
 Target Price: \$32.56
 Market Cap: \$1.58B
 Volume: 1,226,197
 Shares Sold Short: 3.04%
 Days to Cover SI: 2.66
 EBITDA Margin: 21.97%
 ROIC: 9.04%
 WACC: 6.4%
 Dividend Yield: 1.6%

Catalysts:

- Short Term: Continue to drive sales in a niche market.
- Mid Term: Advance growth within the Life Science Systems segment.
- Long Term: Improvement on profitability with margin expansion as the Life Science segment grows.



Thesis:

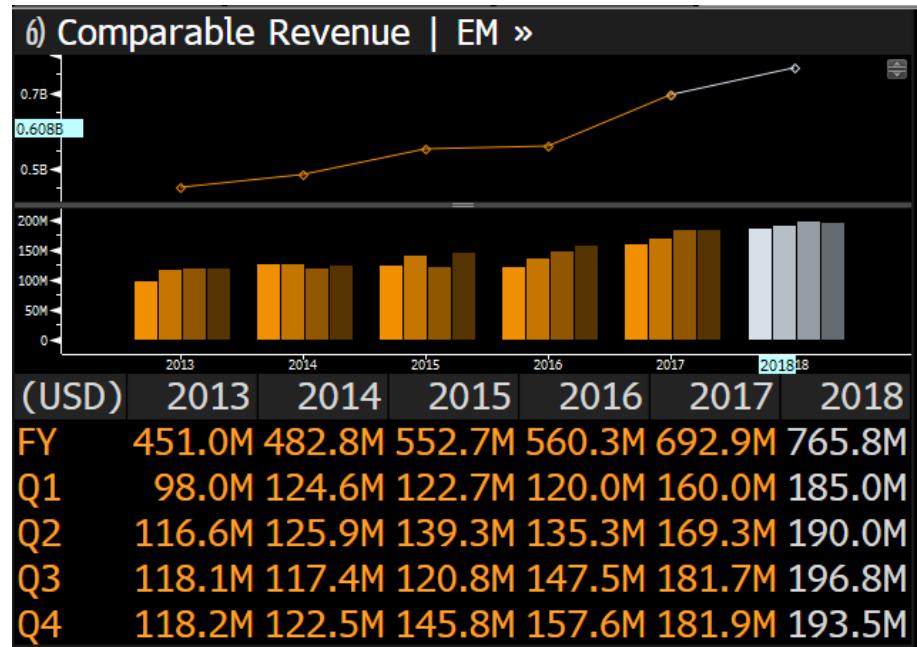
Brooks Automation is well positioned to expand and execute their long term strategy looking forward. With demand for semiconductors at an all time high, and the life science segment of the company growing fast and is well positioned to beat earnings for the current year.

Earnings Performance:

Brooks Automation experienced the eighth consecutive quarter beating estimates due to their portfolio of strong market leading technology. Total revenues totaled at \$182 million up 7% from March and 23% year over year. This growth was driven by an 8% increase in the semiconductor segment and a 6% increase within the Life Science segment. Growth was experienced in both segments due to strong momentum in the capital equipment space, as well as expanding market share in key growth segments. Management has proven to be able to continue to cut costs and improve efficiency while they advance product development and sales activity.

Within the Life Science segment revenue reached \$37 Million, an increase of 6% from Q2 and representing organic growth at 27% year over year. Gross margins this quarter came in relatively soft at 38% a two percent decrease from the previous quarter. This was a result of softness within the storage and infrastructure business. Management expects to return these margins back to 40% where they have been steady. Along with strong earnings within this segment, \$42 million of new contracts have been signed this quarter which added some additional backlog.

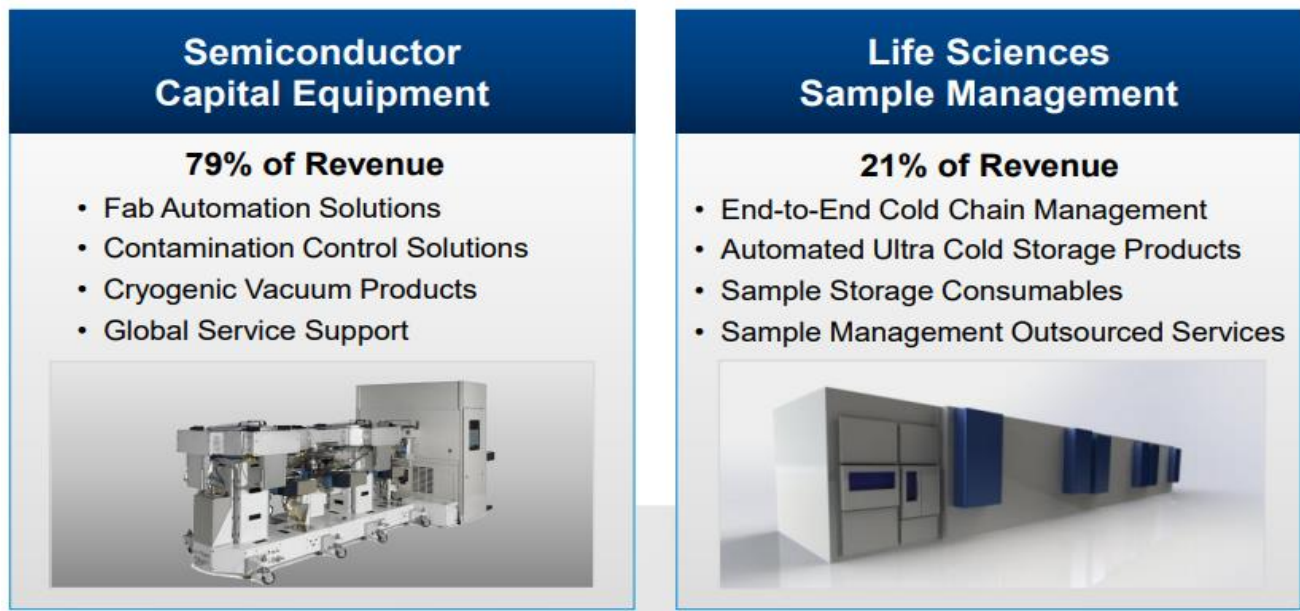
The semiconductor business produced revenue totaling \$145 million an increase of 8% from the previous quarter. This increase was primarily due to etch/dep vacuum, ccs, and ap products, which are key high growth areas within the business. This quarter BRKS also reached gross margins above 40%, which was caused by added value products and an emphasis on reducing fixed costs.



Market Segments:

Semiconductors:

Brooks semiconductor segment currently makes up most of their revenue at around 79% of total revenue and producing operating margins of 16%. Within this segment management has been successful in breaking down this segment into two major sub-segments; Stable leadership and Tech Drivers. The stable leadership segment mainly consists of ATM Robots, cryopumps, and services. The stable leadership sub-segment is approximately 55% of the total semi business and has been labeled as a “slow growth” category due to exiting the atmospheric robot business joint venture with Yasakawa in 2015. The “slow” segment has been projected to have a decline of 1% in sales but, will be offset by the Tech Drivers sub-segment. The Tech Drivers sub-segment consist of wafer-level packaging, contamination control, and dep & etch. The “fast growth” sub-segment has been refocused by management and has done exceptionally well this year producing an overall growth rate of 39%. This sub-segment currently is growing faster than the WFE market growth rate of 16%, with CAGR in deposition & etch at 21%, wafer-level packing at 26%, and contamination control respectively at 42%. This leaves BRKS to have strong organic growth of 20% this year. Brooks is a leading manufacturing within the semiconductor business and supplies to many major companies such as, Lam Research, Applied Materials, Samsung, and TSMC. Management projects a 2-8% CAGR until 2019 which will attribute to growth of the overall company.



Life Science Systems:

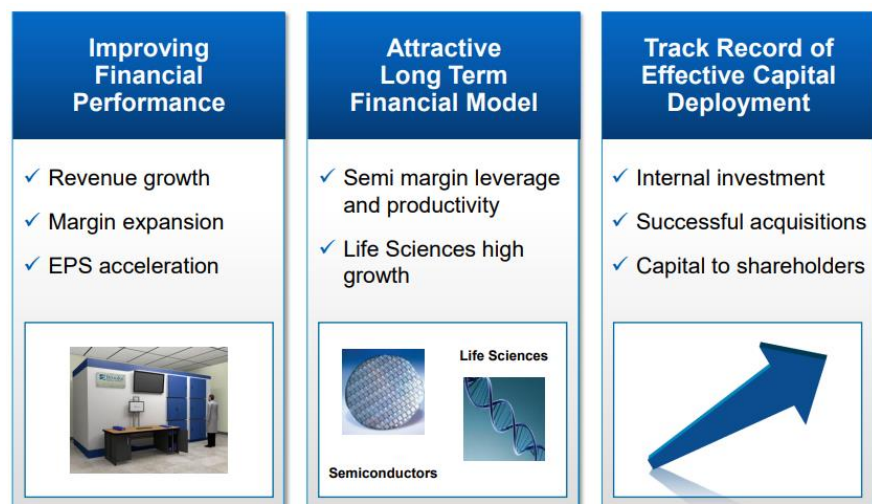
The Life Science segment is growing well as recurring sales increase. Currently, this segment is responsible for 21% of total revenue, but with management’s long term strategy we should see this segment create more revenue in the future. Currently, operating profits in this segment remain low at around 5%, but there is major room to grow and management projects these margins to reach 15%+ by 2019. The Life Science segment can be further broken down into end-to-end cold chain management (tools), automated ultra-cold storage products, sample storage products, sample storage consumables, and sample management outsourced services. A major part of the sales within this segment are recurring sales which recently reach \$42 million, up \$7 million after Q3. Storage solutions represents the majority of the life science segment at around 43% of their total sales, and has seen very strong momentum to have a projected growth rate year over year of 50% in 2018. Tools makes up 39% of their total sales within this segment and has strong expectations to start growing due to BRKS install base. Growth within the tool segment is expected to be the highest at 55%

year over year growth. The consumable sub-segment makes up 18% of sales and expected to see flat line growth of around 1%. Being innovative is a must and continually releasing new products such as B3 Cryo which produced \$5 million in revenue this year will help sales in the future. In the most recent quarter Brooks had international market penetration and gained 26 new customers. Their clients are diversified into pharmaceutical/biotech, healthcare/biobanks, and academic/government, selling too many significant players such as AstraZeneca, Johnson & Johnson, University of Cambridge and the National Cancer Institute. Recently an exciting new product was released. It is a new universal instrument which can cap and de-cap 96 sample tubes of various types and is the first in the market that can do that. Management plans to have a strong growth focus to increase this segment to be a greater percentage of their revenue.

Growth Strategy:

Moving forward Brooks has a motivated management team that has continue to grow their business especially within the life science segment. The strategy moving forward for BRKS is to extend their leadership in core markets, advance growth of the life science segment, drive margin expansion, and have a balanced and disciplined capital deployment. Currently, BRKS is a market leader within the semi business operating

as market leaders within three of the four businesses they partake in. The life science segment is still growing but they are leading within the automation infrastructure marketplace and will continue to do so moving forward. A large part of this strategy is to have the life science segment increase revenue to make up around 30% of their business. Management projects the long term growth rate in this segment to be around 20% which could really drive value creation for the business. Operating margins have been a point of emphasis for Brooks and management has been driving to cut fixed costs and continue to deliver better margins each quarter. The life science segment may have a low operating margins at this point but, with this being a relatively new segment the opportunity for growth is available. The currently capital deployment strategy is to grow the organically at 42%, inorganically at 40%, and give shareholders a return which makes up 18% of their capital deployment. Many businesses have been acquired to grow the life science division, and have been successful due to a high criteria to be acquired. The target focus for acquisitions is to expand the cold chain capabilities of BRKS as well as the storage services and informatics of the company. To help with acquisitions BRKS has a 7 year secured senior term loan of \$200 million with an interest rate of LIBOR +250bps, but have yet to use it and operate with no debt.



Competitors:

Create Template	FINAL F...	fund1	FUND UP...	Fund v2	FUND				
Name	Ticker	Mkt Cap	P/E	EBITDA to Net Sales:Q	Sls 3Yr Avg	Rev - 1 Yr Gr:Q	SI % Eqty Flt	ROIC/WACC Ratio	
Median		2.85B	20.09	26.79%	13.17%	27.74%	2.73%	1.45	
100) BROOKS AUTOMATION INC	BRKS US	1.68B	23.19	13.68%	13.17%	15.44%	3.11%	0.70	
101) ADVANCED ENERGY INDU...	AEIS US	2.85B	14.04	30.72%	-1.88%	39.53%	2.73%	3.97	
102) MKS INSTRUMENTS INC	MKSI US	5.20B	20.09	26.79%	26.69%	27.74%	2.73%	1.45	

Due to the nature of the business I split BRKS competitors based on the two segments they focus in. The main competitors that operate in the semiconductor space are AEIS and MKSI. On a P/E scale Brooks beats competitors and leads the market. The EBITDA margin for Brooks is lagging against competitors but has room to grow because of a current low operating profit within the life science segment. Also the competitors only operate within the semi space so there will be some skewed data against these competitors. The average three year sales is in line with the industry but in 2015 BRKS had a negative sales growth in the first half of the year which has caused some softness. Revenue growth is strong for Brooks at 15% but, against competitors is soft mainly due to the giant demand within the semi segment many of these companies have been booming due to the spike in sales.

Name	Ticker	Mkt Cap	P/E	EBITDA to Net Sales:Q	Sls 3Yr	Rev - 1 Yr Gr:Q	SI % Eqty Flt	ROIC/WACC Ratio	
Median		5.23B	30.83	14.53%	8.43%	12.26%	2.15%	0.86	
100) BROOKS AUTOMATION INC	BRKS US	1.68B	23.19	13.68%	13.17%	15.44%	3.11%	0.70	
101) BRUKER CORP	BRKR US	5.32B	39.38	15.38%	-4.22%	10.59%	2.57%	1.25	
102) CHARLES RIVER LABORAT...	CRL US	4.88B	23.04	23.15%	13.24%	9.05%	3.27%	1.16	
103) CATALENT INC	CTLT US	5.23B	36.65	13.04%	4.47%	23.00%	1.74%	0.61	
104) PAREXEL INTERNATIONAL...	PRXL US	--	--	11.72%	2.52%	3.15%	1.61%	1.02	
105) THERMO FISHER SCIENTI...	TMO US	74.44B	30.83	22.54%	12.40%	13.92%	1.05%	0.56	

Within the life science segment Brooks competes very well on many levels. On a price to earnings metric they are near the bottom of the list but, taking into account the semiconductor side of the business that makes up a majority of their revenue this is normal to be below healthcare companies. The EBITDA margin is below industry median and competitors due to the softness in margins within the life science segment, but positively speaking there is room to grow these margins just as competitors do. Sales growth relative to competitors have had an increase and is at the top of their class within sales.

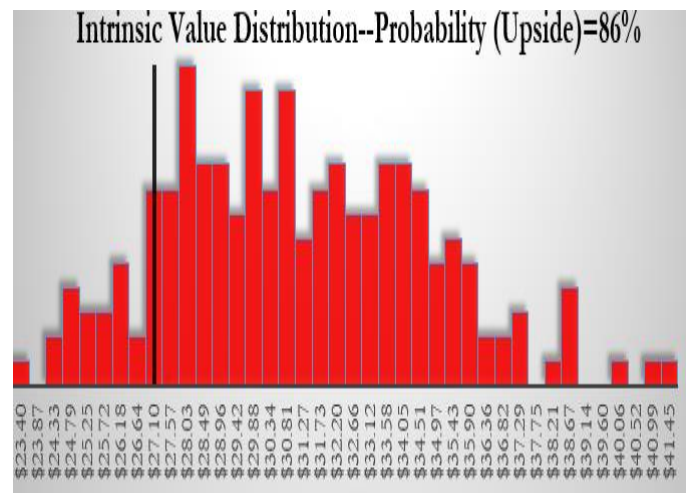
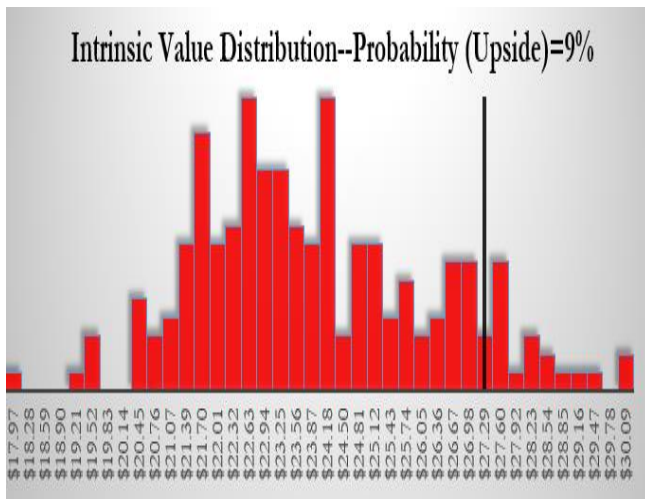
Ownership:

Throughout the past year BRKS has seen a large change in positions within hedge funds. These managers a year ago made up less than one percent of the total ownership but now accounts for around 8% of the stocks ownership. As hedge fund managers are buying into the stock investment advisor are selling their shares, with a change around 9% over the year. Hedge fund managers see as this company has growth potential that will bring for the price is worth the buy at this time. Although the heavy sell off within the advisors it has had little effect on the stock's price. Due to a low short interest and days to cover respectively at 3.04% and 2.66 days to cover this shows that many people do not feel the need to short this stock due to the growth capability.

Compare Current Stats Against	12/03/16				
Ownership Type	11/27/16	Curr ↓	Change		
11) Investment Advisor	92.06	83.29	-8.77	✓	
12) Hedge Fund Manager	0.97	7.74	+6.77	■	
13) Individual	3.22	2.89	-0.33	■	
14) Pension Fund	1.18	2.42	+1.24	■	
15) Insurance Company	1.04	1.18	+0.14	■	
16) Bank	0.18	0.83	+0.65	■	

What-If Analysis:

By running a what-if analysis one can have an idea of what return a stock can have given different scenarios. Though my scenario analysis I gave Brooks a conservative growth rate converging to 2% in ten years and increase operating margins by 3% to 78%. Given these conditions one would see a return of around 10% and a target price of 32.56. This would be a realistic case for BRKS given the expansion of the life science segment. A bear case would be growth converting to 1% and operating margins not changing staying at 82.5%. This would be the case if the semi demand sharply decreases as well as the life science system. This scenario would have a price decrease of -12.58% for a price of \$23.28. This scenario is unlikely to happen given the space the company operates in but it is possible.



Conclusion:

Brook's Automation is poised for growth in the future given the market the company operates in. Semiconductor demand has been high this year and looking forward should continue to grow. The life science segment is where value will be created due to a long-term strong growth rate and high operating margins that will drive revenues higher.

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