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HEARD ON THE STREET

The Chip Stocks That Don't Need a Smartphone Supercycle

Complexity of new devices means Broadcom, Qorvo and Skyworks can sell more chips per phone



The fortunes of many chip makers depend heavily on the next upgrade cycle of Apple's iPhone. PHOTO: STEFAN WERMUTH/REUTERS

By Dan Gallagher

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The big question among tech investors is just how super the coming smartphone “supercycle” will be. The smarter bet would be to focus on companies that will grow quickly whether the cycle is truly super.

Smartphones today aren't the growth business they once were. Even with big redesigns from Apple and Samsung, global smartphone unit sales are expected to rise only 4% this year compared with 2% last year, according to IDC. All things are relative, of course. Apple's stock price jumped 24% in the first quarter—its best performance in years—partly on hopes of a supercycle to be sparked by the 10th anniversary iPhone later this year. But Wall Street currently expects that supercycle to translate to a gain of just 4% in iPhone unit sales for 2017, following a 7% drop last year.

Fortunately, demand for certain chips that are vital for today's smartphones don't follow the same sort of curve. These are the radio-frequency chips made by companies including Broadcom, Qorvo and Skyworks Solutions and used for tasks such as filtering signal interference and boosting data speeds. Today's smartphones need to send messages, surf the web, process videos and backup data over the air, all at once—while working across different cell networks. That makes each new generation a more complex device than its predecessor.

That complexity creates a lot of opportunity. Ed Snyder of Charter Equity estimates that Apple's current iPhone 7 has a little over \$24 in RF chips per device, which is up more than 33% compared with the iPhone 6 just two years ago. He expects Apple to spend more than \$30 per iPhone on RF chips by next year. Broadcom, in its most recent earnings call last month, confirmed that the Samsung Galaxy S8 contains a greater number of the company's chips than its predecessor.

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And it isn't just high-end phones. Chinese smartphone manufacturers targeting middle and lower tiers are taking up a greater share of global smartphone sales, and their customers also have similar demands for performance. Tim Arcuri of Cowen estimates that RF spending per device has doubled in lower-end phones designed for the Chinese market over the past two years.

All three stocks have already made strong gains since the start of the year. That puts Broadcom and Skyworks around 15 times forward earnings, with Qorvo around 13 times. But while that is slightly above their three-year averages, the multiples are in line with chip peers, and each company still has good growth prospects beyond this year's smartphone cycle. There is still enough time for investors to tune in.

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