Transaction Rationales

Purchases / Increases

Buy Tokyo Electron (8035 JP)

We take advantage of the negative sentiment toward the semiconductor industry to re-initiate a position we liquidated in March 2024. Tokyo Electron is down about 40% since we have sold at a price close to its all-time high.

The rational for selling the stock in March was related to market exuberance around the AI theme that had pushed the stock price to levels that left us with no margin of safety. It was by no mean due to a lack of confidence in the company's fundamentals.

5-year Chart: TEL vs. the Bloomberg World Index and the Sector

Source: Bloomberg
Total return in USD
Data range 09.09.2019-09.09.2024
Note: past performance is not a reliable indicator of future results

Tokyo Electron has a strong position in most machines that equip semiconductor fabs and that are critical to process silicon wafers when manufacturing chips. The demand for TEL's tools will continue to grow in the long-term with advanced semiconductor powering the world digitalisation and most innovations being deployed nowadays, including AI.

Its high profitability is protected by a strong economic moat that is grounded on a technological know-how that few possess, on its scale and on the entrenchment of its relation with its customers. As a matter of fact, the chip manufacturers need to partner with suppliers like Tokyo Electron to develop the next generation of deposition, etching and resist coater tools that will be fit to make the smaller nodes of the future. Such co-developments create a symbiotic relationship that is a powerful barrier to entry in these oligopolistic markets and result in a high level of ROIC for equipment manufactures like TEL.

The industry has always been volatile and prone to violent shifts in market sentiment. The sharp correction driven by fears around geopolitics has confirmed that. Western governments are increasingly using technologies and semiconductor in particular as a weapon in their struggle against China. That could surely impact TEL's business in the short term if they were to be prevented to sell some of their most advanced tools to the Chinese. Nevertheless, we view these fears as overdone. Most advanced tools related to EUV processes were already not in sale in China and if legacy nodes chips were to be increasingly manufactured in Western countries, that would require massive investment in fab capacity triggering additional demand for equipment that TEL provides. Meanwhile the Chinese are decades away from developing etching and deposition technologies that could match the ones of TEL and its Western peers.

We use that volatility in our favour to buy at a stock price that offers a good margin of safety vs the earning power value of that high quality cyclical business (current normalised earnings yield at 5.5%).

Buy Entegris (ENTG US)

Entegris is leading supplier of filter solutions, specialty chemicals and other advanced materials for the semiconductor and other high-technology industries. Their systems help semiconductor companies to maximize manufacturing yields, reduce manufacturing costs and enable higher device performance by engineering advanced chemicals and improving contamination control.

Entegris' prospects look bright as there is an increase in demand for more advanced chemicals and materials as the semiconductors move toward smaller geometry and complex architectures. Critically higher material purity and stability is required by chip makers to limit defects in the fabrication of the most advanced chips.

5-year Chart: ENTG vs. the Bloomberg World Index and the Sector

Source: Bloomberg
Data range 14.08.2019-16.08.2024
Total return in USD
Note: past performance is not a reliable indicator of future results

Some of Entegris' technologies find no match in the world, and no other company possess a set of solutions and capabilities that is as broad as Entegris in the space of material and material handling for semiconductor. It dominates the high-end filtration tech field with market share that are above 75% (and 100% for the highest spec ones). These filters are critical to avoid micro contamination. Since the acquisition of AMTI (2014) it develops the most advanced chemicals in collaboration with fabs that are in search for solutions to push the physical limit of chip manufacturing and its latest acquisition of CMC (2023) gives it access to arguably the best and broadest chips planarization capabilities of the world. That unique portfolio of technologies gives the company a strong moat. These technologies are inherently hard to copy, Entegris' scale in the space enables it to invest more in R&D to compound their tech advance, and their relationship with semiconductor manufacturers is getting more entrenched (semi companies share their tech road map with them as they seek a reliable partner to develop innovation in the chem field years ahead of the launch of a new node).

The company will compound its value creation over time as the semiconductor market to continues expand and as Entegris' content per wafer increases as chips becomes more complex (architecture, size of the circuitry, new materials involved) and as it gains market share over time.

We think that the recent sell-off in the stock price post earnings release offer an opportunity to initiate a position in this fast growth and high quality franchise at a price offering decent margin of safety (Normalised earning power yield of 4.5%).

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Increase Amazon (AMZN US)

Amazon has been disrupting the traditional retail industry for more than two decades. After many years of heavy investments and thanks to innovative culture Amazon today not only dominates e-commerce but has also built a leading position in cloud services. Additionally, the firm has built a sizable advertising business in recent years that leverages off Amazon's retail operations and its vast data pool.

However, the Amazon story is likely to morph from a risky high growth/innovation story into a more predictable compounder with above average growth driven by rising margins and returning large amounts of cash to shareholders.

5-year Chart: Amazon vs. the Bloomberg World Index and the Sector

Source: Bloomberg — Data range 19.08.2019-15.08.2024
Total return in USD — Note: past performance is not a reliable indicator of future results

The company has numerous levers it can pull such as ongoing shift to a more profitable business mix, leveraging its vast distribution network through third party seller volumes and technology, and, finally, by returning excess cash to shareholders as cash flows grow faster than capex. While this shifting investment rationales may lead to some shifts in Amazon's investor base that can cause occasional volatility in the stock, management's increasing focus on profitability and (as we expect) capital allocation, essentially de-risk the Amazon investment case.

Therefore, we view the recent drop in the stock price as a good entry opportunity into this long-term growth story (increasingly from compounding). At current prices the stock offers a relative upside of 23%.

Increase Uber Technologies (UBER US)

We continue to build the position we initiated in June. The stock is only slightly up since (~+7%). The last quarterly earnings only brought elements that strengthen our conviction. The franchise is broadening, the profitability is on the rise, and they are gaining share to the ride hailing number 2 – Lyft. Since our initial purchase, the company has announced a few partnerships/deals (Instacart, BYD, Delivery Hero) that in our opinion reflect well on the management's business savviness. The current valuation (6% normalised yield) is far from reflecting the potential long-term earning power of the company.

5-year Chart: Uber Technologies vs. the Bloomberg World Index and the Sector

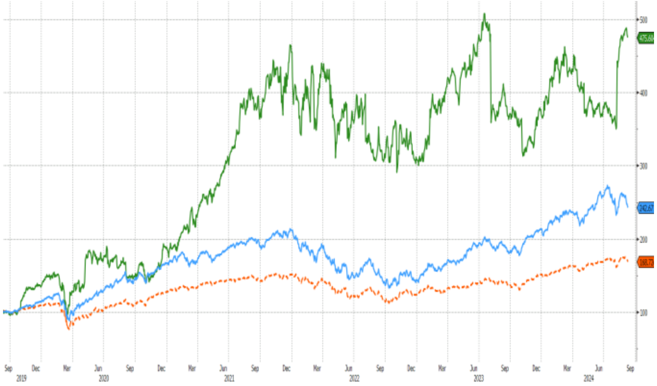
Source: Bloomberg — Data range 19.08.2019-15.08.2024
Total return in USD — Note: past performance is not a reliable indicator of future results

Sells / Reductions

Reduce Fortinet to a normal position (FTNT US)

To finance the initiation of Tokyo Electron, we take profit and sell some shares of Fortinet. The stock has had a nice ride up lately (+26% in the last 3 months) and is up 28% this year, outperforming the market by some 17% and the sector by 14%.

5-year Chart: Fortinet vs. the Bloomberg World Index and the Sector



Source: Bloomberg — Data range 09.09.2019-09.09.2024
Total return in USD — Note: past performance is not a reliable indicator of future results

Sell full position of Sika (SIKA SW)

Our view of Sika as a high-quality franchise as not changed and we have made money with the stock. But at current valuation multiple (Fwd P/E above 30x) it has a much lower margin of safety than Entegris as well as a lower long term compounding rate. We therefore think that SIKA is an appropriate source of cash to fund our initiation of Entegris.

5-year Chart: Sika vs. the Bloomberg World Index and the Sector

Source: Bloomberg — Data range 14.08.2019-18.08.2024
Total return in USD — Note: past performance is not a reliable indicator of future results

Sell Waters (WAT US)

5-year Chart: Waters vs. the Bloomberg World Index and the Sector

Source: Bloomberg
Total return in USD
Data range 19.08.2019-15.08.2024
Note: past performance is not a reliable indicator of future results

Since we took advantage of a significant decline in the stock price in 2023 the stock has rebounded strongly. However, our free cash flow estimates for 2029 have come down by more than 20% since the initial purchase. As a result of all of this, Waters stock now trades slightly above its 10-year averages. While the long duration nature of its cash flows warrants a large premium over the market, current multiples leave limited upside.

Therefore, we take profit to make room investments that offer a more attractive risk/return.

With kind regards,

Emerald Wealth Partners AG, Investment Office

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