Long Ideas Tech Canada

Photon Control: A Virtuoso Performer In The Semiconductor Industry

Apr. 04, 2021 9:44 PM ET | **Photon Control Inc. (POCEF)** | AMD, INTC, QCOM | 13 Comments | 16 Likes

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Summary

- Forecasts for the red-hot global semiconductor industry call for growth of over 8% in 2021 to around $470 billion, driving higher levels of demand for chip manufacturing equipment.
- Domestic semiconductor equipment vendors, such as Photon Control, are well-positioned to benefit from "silicon nationalism," a push by countries to develop manufacturing and become more self-sufficient in chips.
- Photon Control recently reported a record 2020 annual revenue of $64.7 million and has guided to even higher growth and profitability in 2021, making the current share price highly undervalued.

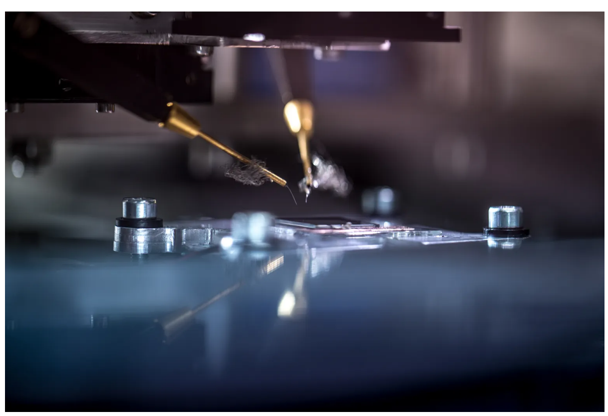


Photo by CasarsaGuru/E+ via Getty Images

The term “Virtuoso” is used to describe somebody with such outstanding talent and technical ability in a particular art or field that they are usually conferred elevated levels of adulation and recognition for their accomplishments. Typically, this description is reserved for high performers in music or athletics but when you consider the recent track record of Photon Control Inc. (OTCPK:POCEF), a leading manufacturer of fiber optic measurement solutions to the semiconductor industry, virtuoso may be the most fitting way to represent their outstanding execution as of late. Across the board on almost every metric, Photon Control is one of those extremely rare examples of a company firing on all cylinders.

Source: Corporate Website

There is a comprehensive overview of Photon Control in this recent article for readers requiring more background on the company. Since that was written, Photon Control has continued to impress, including delivering a record Q4 and full-year earnings announced in March. Before we dive into the details, let’s first set the stage by considering the macroeconomic backdrop.

The Market

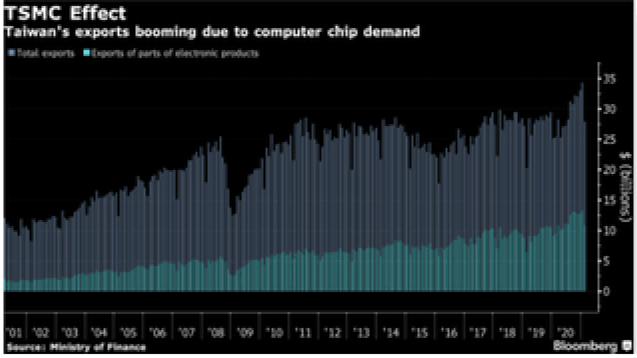
For an investor on the look-out for opportunities, recent events in the semiconductor industry are very compelling. The industry is in the 2nd year of a multi-year growth cycle, propelled by multiple technical drivers such as autonomous vehicles, 5G, IoT, AI, work from home, and high-performance computing. The Semiconductor Industry Association forecasts global chip sales in 2021 will grow over 8% from 2020 to around $470 billion, far exceeding the 5.1% growth between 2019 and 2020. This growth is driving increased capital intensity and higher levels of investment in chip technology and production.

Early this year though, companies that sell chips - like Intel (INTC), AMD (NASDAQ:AMD) and Qualcomm (NASDAQ:QCOM) - have been experiencing serious supply issues. Reasons include rapidly changing, complex semiconductor designs that have slowed production at chip factories (or “fabs”) and the lingering effects of the ongoing trade war with China that has choked supply. Automakers have been especially hard hit by the chip shortages, which could cut $1.5 - $2 billion from their 2021 earnings.

To address the problem, President Joe Biden ordered a review of critical product supply chains in the U.S., including semiconductors, to protect and strengthen American competitiveness. The U.S. now accounts for only about 12% of global semiconductor manufacturing capacity, down from 37% in 1990, thanks in part to other nations subsidizing the growth of their chipmakers. Now, the President’s recently unveiled $2 trillion American Jobs Plan, is seeking congressional approval for a $50 billion investment in strategically vital domestic semiconductor manufacturing and research.

This could help American companies better compete with foreign companies and level the playing field in the global race for semiconductor leadership. Some have likened this government support to how Operation Warp Speed spurred innovation in the pharmaceutical and biotech industries in the early days of the pandemic.

The effects of all this new attention were evident immediately. In March, Intel announced plans for a major manufacturing expansion starting with a $20 billion investment this year to build two new chip factories in Arizona. Taiwan Semiconductor Manufacturing Co., the world’s leading producer of advanced semiconductors, recently said it also plans to spend $100 billion over the next three years to expand its chip-making capacity, including in the U.S., to address booming demand for new technologies.

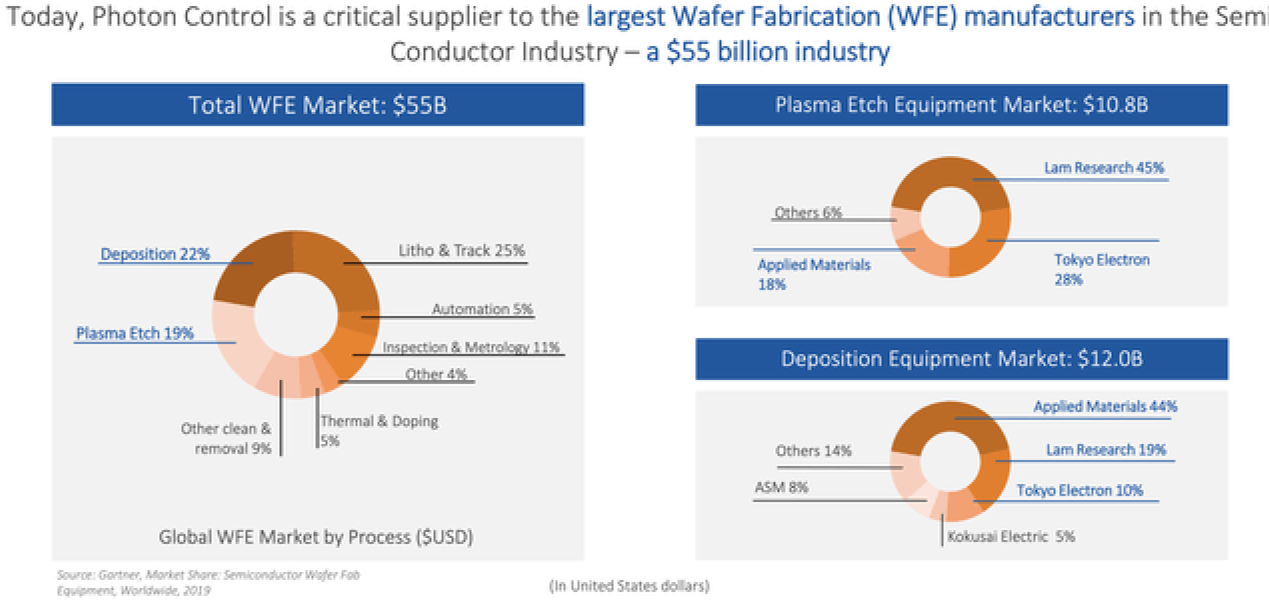


Source: Bloomberg

Adding to the drama and supporting the move to mitigate risk by repatriating chip-related supply, diplomats in the Biden administration recently confirmed that the U.S. is engaging in “strategic planning” with Australia to develop potential joint responses in case of a war with China over Taiwan, a key hub in the critical semiconductor industry.

A recent Bank of America report highlights how semiconductor equipment vendors are well-positioned to benefit from what they refer to as "silicon nationalism", a push by countries to develop domestic manufacturing and become more self-sufficient in chips. BofA believes fiscal 2021 changes to the CHIPS America Act, along with billions of dollars in matching funding from state and local authorities, will incent domestic investment in new chip foundries, R&D streams, and equipment.

The net result of all of these developments for investors should be the confirmation that the semiconductor industry is the place to look for lucrative investment opportunities. Furthermore, local suppliers who provide the products and services to support that forecasted huge growth in capital spending may be the surest bet. One of those innocuous but critical sectors is Wafer Fabrication Equipment (WFE), which is expected to grow in the mid to high teens percentage range in 2021. Photon Control, an essential supplier of precision products to the WFE market, is in a prime position to continue to benefit from this roaring demand.



Source: Corporate Presentation

Along with excelling in their primary WFE sector of Plasma Etch, Photon Control's new high-temperature probes are starting to make inroads in deposition, a growing focus, and opportunity for the company. Strategic acquisitions the company made in 2020 also open up new avenues for expansion. With that background, let's now explore the details behind the thesis that Photon Control is one of the most undeniable yet extremely undervalued investments in the red-hot semiconductor industry.

Q4 and Full Year 2020 Earnings

Note: *All figures referenced in Photon Control's financial analysis are in Canadian dollars, the reporting currency of the company.*

In their Q3 earnings call back in October, Photon Control had estimated full-year growth of around 15% in the WFE sector in 2020 thanks to a very healthy spending environment driven primarily by a recovery in the NAND memory market. As they reported on March 18th, the actual growth in their primary market turned out to be a record $60 billion overall. The accelerating capital spending momentum helped propel Photon Control to Q4 revenues of $14.9 million, exceeding its forecasted range of $12 - 14 million, and total annual revenue hitting a record $64.7 million, almost double that of 2019's $32.7 million.

Photon Control CEO Nigel Hunton had this to say about the results:

> “We are very pleased to announce a record year for Photon Control, and a strong finish to 2020, with Q4 revenues 69% higher than the comparable period in 2019. Throughout the year, we executed on our strategic objectives of outpacing semiconductor capital equipment growth and growing earnings faster than revenues. Compared to industry growth of approximately 18% in 2020, our revenues increased 98%, and earnings growth exceeded 500%, compared to 2019. Our relative outperformance is testament to the enabling role of Photon Control within the global semiconductor manufacturing industry, the strength of our customer partnerships with the world’s leading Original Equipment Manufacturers (“OEMs”), and the increasing importance of precise control of critical processes at successive technology nodes.”

Photon Control beat on gross margin too, clocking in at 60% and exceeding their guidance by 5%. They also reported $22.8 million of adjusted EBITDA, up over 200% from the prior period. This improved profitability was achieved despite Q4 having a substantial increase of $1.8 million in R&D invested back into the business, for a total of $5.7 million for the full fiscal year.

Photon Control is in excellent financial health. Working capital has grown steadily over the last six quarters and now sits at $50.6 million, including cash and cash equivalents of $48.4 million. The data below highlights Photon Control’s impressive performance over the last few periods:

Consolidated Statements of Income	FY2018	FY2019	Q1/20	Q2/20	Q3/20	Q4/20	FY/2020
(Unaudited, in thousands of CAD)	*FY to Dec.31*	*FY to Dec.31*	*to Mar. 31*	*to June 30*	*to Sept. 30*	*to Dec. 31*	*FY to Dec.31*
Revenue	**46,704**	**32,730**	**17,312**	**16,098**	**16,330**	**14,917**	**64,657**
Cost of sales	21,057	15,165	6,724	6,376	6,125	6,768	25,993
Gross profit	25,647	17,565	10,588	9,722	10,205	8,149	38,664
Operating expenses							
General and administrative	7,035	6,516	2,155	1,851	1,918	2,215	8,139
Research and development (Engineering)	3,525	4,404	1,255	1,154	1,507	1,794	5,710
Sales and marketing	2,529	1,902	687	920	1,028	1,014	3,649
Total operating expenses	13,089	12,822	4,097	3,925	4,453	5,023	17,498
Operating income	**12,558**	**4,743**	**6,491**	**5,797**	**5,752**	**3,126**	**21,166**
Finance income, net	356	654	154	27	7	24	212
Accretion expense on contingent consideration	(748)	(520)	(122)	(106)	(84)	(72)	(384)
Change in fair value of contingent consideration	(141)	(115)	(88)	(467)	(153)	(50)	(758)
Gain (Loss) on Sale of Assets	166	0	0	0	0	(2)	(2)
Foreign exchange (loss) gain	2,499	(1,264)	2,682	(1,518)	(483)	(951)	(270)
	2,132	(1,245)	2,626	(2,064)	(713)	(1,051)	(1,202)
Net income before taxes	**14,690**	**3,498**	**9,117**	**3,733**	**5,039**	**2,075**	**19,964**
Income taxes	4,007	1,127	2,478	1,060	1,432	917	5,887
Net income	**10,683**	**2,371**	**6,639**	**2,673**	**3,607**	**1,158**	**14,077**
Other comprehensive income:							
Unrealized gain (loss) from Fx translation of sub	-125	4	16	120	11	(41)	106
Total comprehensive income	**$10,558**	**$2,375**	**$6,655**	**$2,793**	**$3,618**	**$1,117**	**$14,183**
Basic and diluted earnings per share							
Weighted average common shares, basic	110,814,812	106,238,776	104,513,571	104,565,672	104,592,218	104,573,994	104,573,994
Weighted average common shares, diluted	111,738,931	106,614,958	104,925,738	105,212,341	105,629,671	105,284,879	105,284,879
Basic earnings per share	**$0.10**	**$0.02**	**$0.06**	**$0.03**	**$0.03**	**$0.01**	**$0.13**
Diluted earnings per share	**$0.09**	**$0.02**	**$0.06**	**$0.03**	**$0.03**	**$0.01**	**$0.13**

Source: Corporate Website and Author's Research

Both full-year and Q4 gross margins exceeded Photon Control's forecasts due primarily to customer mix and the strengthening of the Canadian dollar (revenue is predominantly in U.S. dollars while the cost base is principally in Canadian), which they believe will continue through 2021. The higher revenue volumes in 2020 helped gross margin by allowing the fixed costs of sales to be amortized over a larger base. Additionally, there were improved cost savings and variable cost of production through supply chain initiatives and lower cost supplies compared to 2019. In dollar terms, gross profit in 2020 rose by 120% to a record $38.7 million.

The balance sheet is stellar as well. Year-end inventory was $8.8 million, slightly down from Q3 2020 of $9.1 million, as Photon built slightly higher levels, partially in response to a general move in the industry to de-risk supply chains by building excess stock and in response to COVID-19. To improve efficiency, during Q4 the company acquired a system to expand warehouse storage and capacity. Manufacturing equipment was also purchased to support rapid prototyping capabilities to help reduce customer lead-time requirements.

Balance Sheet (TTM)			
Total Cash	38.04M	Current Ratio	4.39
Total Cash Per Share	0.36	Quick Ratio	3.74
Total Debt	970,591.47	Covered Ratio	-
Total Debt to Equity	1.93%	Book Value Per Share	0.45
Short Term Debt	-	Debt/Free Cash Flow	-
Long Term Debt	-	Long Term Debt/Total Capital	1.46%

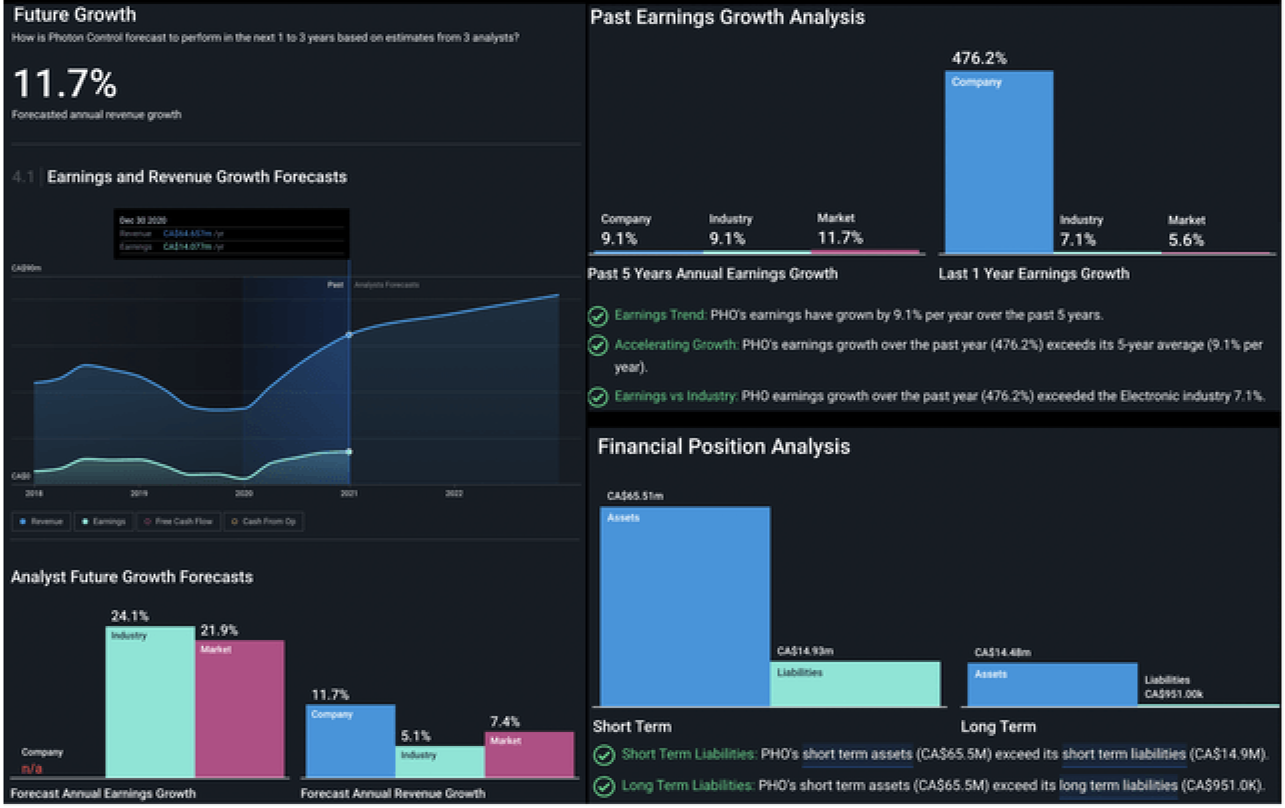
Cash Flow Statement (TTM)			
Net Operating Cash Flow	15.59M	Free Cash Flow	13.75M

Source: Seeking Alpha

Photon Control remains debt-free and is very well-positioned to continue executing on its growth objectives, including the record year-end backlog of over $30 million, which grew 10% Q-o-Q, and signals strong demand and solid growth through 2021. Another key metric to gauge longer-term revenue growth prospects is new product introductions (NPI), which CEO Hunton confirmed has remained over 30% of total revenues for both Q4 and FY2020. Let's take a look at the immediate prospects.

Near-Term Growth Forecasts

According to CEO Hunton, Photon Control's objective is to continue to outperform industry growth on the top-line and increase earnings faster than revenues on the bottom-line. For Q1 2021, the CEO expects demand in the semiconductor market to remain strong, echoed by their customers, with no second-half decline as was earlier feared.



Source: Simply Wall St.

Based on their order backlog and operating plan, Mr. Hunton expects strong quarterly revenues in the range of $16-18 million. For modeling purposes, the table below employs the CEO's Q1 revenue forecasts and averages out the previous four quarters for the other line items using a "percentage of revenue" calculation" to come up with the following estimated results:

Consolidated Statements of Income	Q1/20	%	Q2/20	%	Q3/20	%	Q4/20	%	Q1/21	%
(Unaudited, in thousands of CAD)	*to Mar. 31*		*to June 30*		*to Sept. 30*		*to Dec. 31*		*to Mar. 31*	
Revenue	**17,312**		**16,098**	**-7%**	**16,330**	**1%**	**14,917**	**-9%**	**18,000**	**21%**
Cost of sales	6,724	39%	6,376	40%	6,125	38%	6,768	45%	7,260	40%
Gross profit	10,588	61%	9,722	60%	10,205	62%	8,149	55%	10,740	
Operating expenses										
General and administrative	2,155	12%	1,851	11%	1,918	12%	2,215	15%	2,274	13%
Research and development (Engineering)	1,255	7%	1,154	7%	1,507	9%	1,794	12%	1,605	9%
Sales and marketing	687	4%	920	6%	1,028	6%	1,014	7%	1,025	6%
Total operating expenses	4,097	24%	3,925	24%	4,453	27%	5,023	34%	4,905	33%
Operating income	**6,491**	37%	**5,797**	36%	**5,752**	35%	**3,126**	21%	**5,836**	39%
Finance income, net	154	1%	27	0%	7	0%	24	0%	57	0%
Accretion expense on contingent consideration	(122)	-1%	(106)	-1%	(84)	-1%	(72)	0%	(106)	-1%
Change in fair value of contingent consideration	(88)	-1%	(467)	-3%	(153)	-1%	(50)	0%	(211)	-1%
Gain (Loss) on Sale of Assets	0	0%	0	0%	0	0%	(2)	0%	(1)	0%
Foreign exchange (loss) gain	2,682	15%	(1,518)	-9%	(483)	-3%	(951)	-6%	(147)	-1%
	2,626	15%	(2,064)	-13%	(713)	-4%	(1,051)	-7%	(408)	-3%
Net income before taxes	**9,117**	53%	**3,733**	23%	**5,039**	31%	**2,075**	14%	**5,428**	36%
Income taxes	2,478	14%	1,060	7%	1,432	9%	917	6%	1,612	9%
Net income	**6,639**	38%	**2,673**	17%	**3,607**	22%	**1,158**	8%	**3,816**	26%
Other comprehensive income:										
Unrealized gain (loss) from Fx translation of sub	16	0%	120	1%	11	0%	(41)	0%	(11)	0%
Total comprehensive income	**$6,655**	38%	**$2,793**	17%	**$3,618**	22%	**$1,117**	7%	**$3,805**	26%
Basic and diluted earnings per share										
Weighted average common shares, basic	104,513,571		104,565,672		104,592,218		104,573,994		104,573,994	
Weighted average common shares, diluted	104,925,738		105,212,341		105,629,671		105,284,879		105,284,879	
Basic earnings per share	**$0.06**		**$0.03**		**$0.03**		**$0.01**		**$0.04**	
Diluted earnings per share	**$0.06**		**$0.03**		**$0.03**		**$0.01**		**$0.04**	

Source: Author's Research

Echelon Capital Markets analyst Amr Ezzat, who covers Photon Control, is forecasting 2021 revenue and adjusted EBITDA of $74.6 million and $22.3 million, respectively. He sees even stronger performance in 2022 with revenue and EBITDA of $87.9 million and $32.4 million, respectively, thanks to the company's penetration into the deposition segment.

Ezzat believes Photon Control is currently very undervalued, trading at only around 10.1x and 7.0x 2021 and 2022 EBITDA estimates, respectively. He puts the valuation at 18.4x and 12.2x based on his projected 2021 and 2022 earnings estimates, respectively. He describes this as "exceptional valuation metrics by any standard…". For comparison, Ezzat said WFE component suppliers typically trade at a median of 23.5x next-twelve-months EBITDA.

Any way you look at it, the future appears bright for Photon Control.

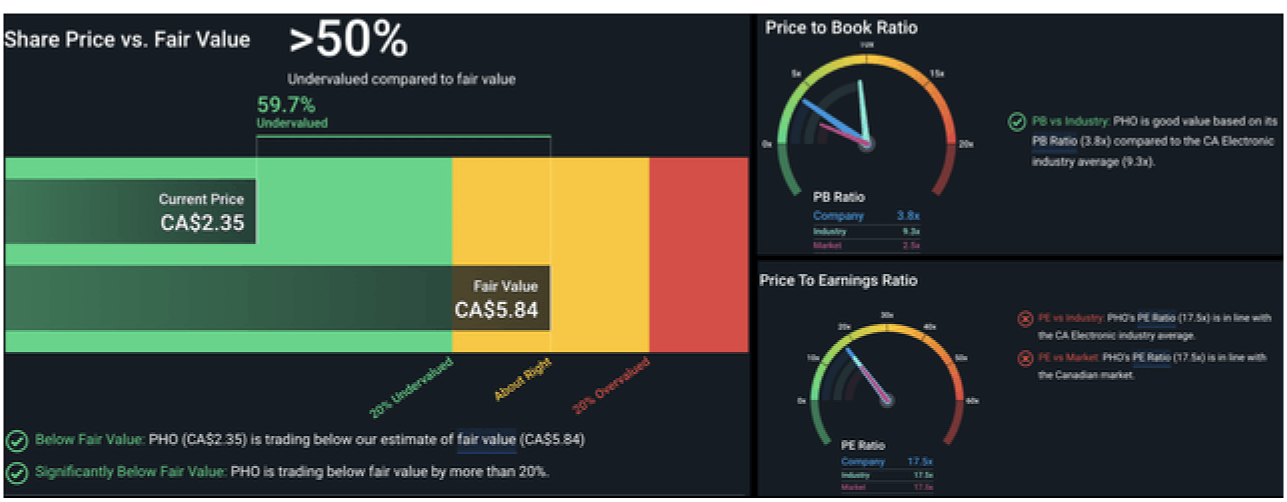
The Business Fundamentals and Valuation

The business fundamentals for Photon Control are solid across the board. In the analysis below, we see the company's consistently strong performance Q-o-Q compared to the industry and significantly beating similar companies in the Q4 numbers.

FUNDAMENTAL ANALYSIS	Photon Control Inc (to Sept/20)	Electrical Components & Equip. Industry (to Sept/20)	Photon Control Inc (to Dec/20)	Electrical Components & Equip. Industry (to Dec/20)	Electrovaya Inc. (to Dec/20)	dynaCERT Inc (to Dec/20)	GBLT Corp (to Dec/20)	Decisive Dividend Corp (to Dec/20)
PER SHARE DATA								
Earnings (TTM)	$0.13	($0.01)	$0.14	$0.00	$0.01	($0.05)	$0.00	($0.02)
Book Value	$0.47	$0.16	$0.61	$0.27	($0.08)	$0.06	($0.01)	$1.91
Cash Flow (TTM)	$0.15	$0.01	$0.16	$0.01	$0.01	($0.05)	$0.00	$0.31
VALUATION								
Price/Earnings	15.0x	117.0x	17.8x	105.1x	191.9x	---	---	---
Price/Sales (TTM)	3.6x	54.1x	4.0x	69.6x	14.2x	180.6x	0.8x	0.7x
Price/Book (MRQ)	3.3x	36.2x	4.0x	34.0x	---	8.9x	721.3x	1.5x
Price/Cash Flow (TTM)	13.1x	82.7x	15.6x	100.4x	159.0x	---	454.4x	9.0x
PROFITABILITY								
Gross Margin	60.02%	48.28%	59.80%	45.09%	33.45%	74.15%	8.08%	39.55%
Operating Margin	34.28%	-346.81%	32.74%	-469.80%	9.33%	-751.95%	0.37%	0.50%
Profit Margin	23.25%	-489.52%	21.77%	-576.84%	7.24%	-1342.05%	-0.21%	-0.53%
MANAGEMENT EFFECTIVENESS (TTM)								
Return on Assets	20.32%	-48.98%	20.39%	-54.17%	16.94%	-113.11%	-0.71%	-0.42%
Return on Equity	24.45%	-67.74%	24.81%	-70.02%	---	-130.50%	-91.51%	-1.15%
Return on Investment	23.51%	-65.48%	24.03%	-64.26%	---	-129.73%	-14.04%	-0.49%
FINANCIAL STRENGTH (MRQ)								
Debt to Capital	2.05%	63.99%	1.89%	76.37%	335.34%	0.65%	98.63%	53.64%
Current Ratio	5.0x	6.4x	4.4x	9.2x	0.5x	21.3x	1.0x	2.3x
Quick Ratio	4.2x	6.0x	0.2x	0.0x	0.0x	0.0x	0.0x	0.3x
SIZE								
Market Cap	$210.2M	$259.7M	$257.4M	$260.9M	$288.8M	$221.0M	$29.4M	$32.2M
Revenue	$58.6M	$15.0M	$64.7M	$16.8M	$20.3M	$1.2M	$37.3M	$47.9M
Shares Outstanding	104.6M	143.5M	104.6M	146	139.4M	381.0M	113.0M	11.6M
Employees	103	64	142	77	56	---	---	61
Revenue Growth	82.45%		97.55%					

Source: Author's Research

The strong ROA and ROI are an enticing draw for fundamental investors. The extremely low price-to-sales, price-to-book, and price-to-cash flow relative to the industry also scream out that the current share price is very undervalued. Simply Wall St., a FinTech startup that provides comprehensive investment research, employs "The Two-stage FCFE Model" to provide the following valuation assessment on Photon Control:

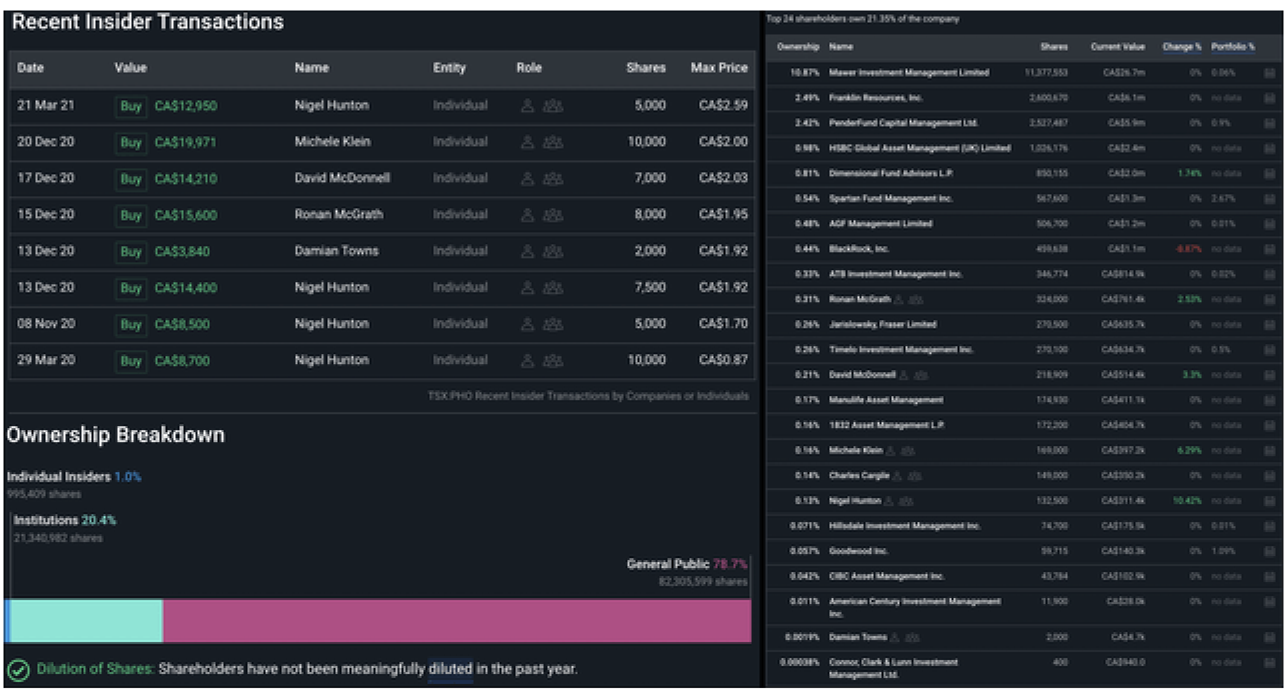


Source: Simply Wall St.

After the latest Q4 and full-year ER in March, bullish analyst ratings began to pour in. First, Desjardins analyst Kevin Krishnaratne initiated coverage of Photon Control with a Buy rating and provided a $3.50 price target. Echelon analyst Amr Ezzat, referenced earlier, also stayed bullish reiterating both his "Buy" rating and Top Pick Call while maintaining a $3.50 price target:

> "We believe Photon's balance sheet strength together with its leverage to an economic upcycle constitutes attractive risk-reward characteristics. Despite the strong stock performance since our late 2015 initiation, valuation remains exceptionally attractive with earnings growth keeping pace with stock performance," Ezzat said.

One big drag on the company is the high number of outstanding shares of over 109 million, with less than 23% held by institutions and insiders. The data below shows that insiders see the improving investment opportunity with their buying picking up over the last few quarters.



Recent Insider Transactions

Date	Value	Name	Entity	Role	Shares	Max Price
21 Mar 21	Buy CA$12,950	Nigel Hunton	Individual		5,000	CA$2.59
20 Dec 20	Buy CA$19,971	Michele Klein	Individual		10,000	CA$2.00
17 Dec 20	Buy CA$14,210	David McDonnell	Individual		7,000	CA$2.03
15 Dec 20	Buy CA$15,600	Ronan McGrath	Individual		8,000	CA$1.95
13 Dec 20	Buy CA$3,840	Damian Towns	Individual		2,000	CA$1.92
13 Dec 20	Buy CA$14,400	Nigel Hunton	Individual		7,500	CA$1.92
08 Nov 20	Buy CA$8,500	Nigel Hunton	Individual		5,000	CA$1.70
29 Mar 20	Buy CA$8,700	Nigel Hunton	Individual		10,000	CA$0.87

TSX:PHO Recent Insider Transactions by Companies or Individuals

Ownership Breakdown

Individual Insiders 1.0%
995,409 shares

Institutions 20.4%
21,340,982 shares

General Public 78.7%
82,305,599 shares

Dilution of Shares: Shareholders have not been meaningfully diluted in the past year.

Top 24 shareholders own 21.35% of the company

Ownership	Name	Shares	Current Value	Change %	Portfolio %
10.87%	Mawer Investment Management Limited	11,377,553	CA$26.7m	0%	0.06%
2.49%	Franklin Resources, Inc.	2,600,670	CA$6.1m	0%	no data
2.42%	PenderFund Capital Management Ltd.	2,527,487	CA$5.9m	0%	0.9%
0.98%	HSBC Global Asset Management (UK) Limited	1,026,176	CA$2.4m	0%	no data
0.81%	Dimensional Fund Advisors L.P.	850,155	CA$2.0m	1.74%	no data
0.54%	Spartan Fund Management Inc.	567,600	CA$1.3m	0%	2.67%
0.48%	AGF Management Limited	506,700	CA$1.2m	0%	0.01%
0.44%	BlackRock, Inc.	459,638	CA$1.1m	-0.87%	no data
0.33%	ATB Investment Management Inc.	346,774	CA$814.9k	0%	0.02%
0.31%	Ronan McGrath	324,000	CA$761.4k	2.53%	no data
0.26%	Jarislowsky, Fraser Limited	270,500	CA$635.7k	0%	no data
0.26%	Timelo Investment Management Inc.	270,100	CA$634.7k	0%	0.5%
0.21%	David McDonnell	218,909	CA$514.4k	3.3%	no data
0.17%	Manulife Asset Management	174,930	CA$411.1k	0%	no data
0.16%	1832 Asset Management L.P.	172,200	CA$404.7k	0%	no data
0.16%	Michele Klein	169,000	CA$397.2k	6.29%	no data
0.14%	Charles Cargile	149,000	CA$350.2k	0%	no data
0.13%	Nigel Hunton	132,500	CA$311.4k	10.42%	no data
0.071%	Hillsdale Investment Management Inc.	74,700	CA$175.5k	0%	0.01%
0.057%	Goodwood Inc.	59,715	CA$140.3k	0%	1.09%
0.042%	CIBC Asset Management Inc.	43,784	CA$102.9k	0%	no data
0.011%	American Century Investment Management Inc.	11,900	CA$28.0k	0%	no data
0.0019%	Damian Towns	2,000	CA$4.7k	0%	no data
0.00038%	Connor, Clark & Lunn Investment Management Ltd.	400	CA$940.0	0%	no data

Source: Author's Research and Simply Wall St.

Photon Control's free cash flow of $2.5 million for 2020 versus negative $1.0 million for 2019, along with the overall cash balance which increased to $48.4 million from $46.6 million at the end of the previous quarter, puts them in an enviable position. Management believes the best use of their growing cash stockpile is to continue investing in the business to capitalize on favorable industry dynamics, as well as look for acquisition targets and strategic partnerships to accelerate their growth strategy. Internal opportunities include investing in R&D and optimizing manufacturing capacity to enable 100% on-time responsiveness to customer demand.

Those are worthwhile pursuits and the company has certainly demonstrated its ability to find value through acquisition and partnership but in the meantime, rather than let that cash idle, Photon Control should consider repurchasing shares to reduce the public float. This would help increase the share price, not just to reward existing shareholders but to provide a higher return if future equity raises are needed to fund higher value, strategic M&A. The more of the public float that can be soaked up the more we can expect the share price to grow steadily and hold the gains. With a market cap of around $274 million and an enterprise value of only $226 million, improvements are required in the capital structure to bring in more long-term investors.

The Strategic Direction

According to CEO Hunton, the company will focus on strategies to bolster growth and innovation through new products and partnerships to expand markets and customer footprint. Photon Control has enjoyed a great deal of success already in pursuit of that objective. In the Q4/FY earnings call, Mr. Hunton reported that last year's acquisition of the Micronor assets is paying off early. The over $1 million in revenues Micronor contributed to Photon Control's 2020 numbers was well ahead of the plan the company laid out when they acquired the business. New sales into the life sciences, energy, and aerospace sectors is providing Photon Control with much-needed exposure and a greater understanding of these markets.

Micronor’s solid base of technology, expertise, and focus has also helped Photon Control penetrate the energy sector, both in fusion reactors and in transformers. A recent news release from Fusion For Energy (F4E), the European Union organization coordinating the International Thermonuclear Experimental Reactor (“ITER”) p, recognized Micronor’s contributions: Micronor is one of the many technology companies participating in this bold energy project, which is attempting to demonstrate magnetic fusion as a large scale and carbon-free source of energy from future fusion power plants. Micronor’s innovative technology and engineering expertise were used to develop an optical encoder solution beyond industry standards to measure accurate position in extreme conditions.

The other key 2020 investment was the exclusive worldwide license and distribution agreement with FiSens in Germany for fiber Bragg grating (“FBG”) sensor solutions, which was developed for alternative industries, such as wind turbines, but is also deployable in applications for the semiconductor market. FBG is still early in its development so will require more evaluations and prototyping to ensure it meets the unique and stringent semiconductor industry standards and specifications.

Revenues are only expected for the end of 2021 but Photon Control is seeing success with the new technology in a life science application. Overall, the company is very excited about the technology, possibly the smallest form factor in the market, but also about the partnership. Photon Control believes the key to success is to learn from FiSens on what they're doing well, leverage that expertise to support their own engineering groups, and gain insights on where the company should be looking for their next acquisition. If FBG provides the expected benefits, Photon Control thinks it could be widely adopted and generate new earnings as a game-changer in the industry.

As for the emerging opportunities, some of the new technology within the deposition sector (such as atomic layer deposition) require high temperatures. In the last ER call, CEO Hunton mentioned design wins for their new high-temperature probes, with initial shipments to a leading OEM. This is an area that represents future growth but requires more time to ramp up from qualification to volume production.

The semiconductor industry is dynamic and drives innovation but it's also risk-averse to technology. In terms of cycle time, typically OEMs will evaluate a product for three to six months before putting it through an end-user trial for another three to six months. That means it could be up to 12 months as a prototype before any revenue is ever recognized. The key within that cycle is to make sure those products are focused on solving challenges that customers have so they prioritize that technology. There are also RF environments now being included that bring additional opportunities for fiber optics in the future.

From a geographic perspective, Photon Control increased revenues in Asia, thanks to strong selling by their new distributors. The company thinks their big opportunity is still in Korea, which is continuing to invest and is considered a global powerhouse. For Photon Control, having at least one strategic hub that can meet the demand to maintain 100% on-time delivery and support that growth is key to building a stronger position in the Asia Pacific region.

Conclusion

According to their CEO Nigel Hunton, the go-forward plan for Photon Control is to continue investing in the business through R&D, recruiting, and developing their engineering talent. They also will continue close collaboration with key customers to meet their needs on KPIs, like faster turnaround development cycles for novel solutions to address their challenges. The company expects these efforts will continue to strengthen and gradually increase its market share, which is already healthy and growing. Strategic acquisitions and partnerships will also continue to be a focus area for the company.

Photon Control has been executing at a virtuoso level for the past year and looks to continue that hot steak through 2021 in the sizzling, dynamic, growth-fueled semiconductor industry. The prospects for future success are clearly established. Now the share price needs to keep pace and better reflect the huge potential this company has. Any efforts by leadership to encourage greater institutional investment or reduce the float would more immediately reward their long-term investors. As the company continues to look for acquisitions, it may become evident that the greatest ROI Photon Control can generate is by buying more equity in their own company.

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