

First Read

SunPower Corp

Pivoting Back Towards the Core Competency

Mgmt meeting focuses on 2017 – and prospects for resi/commercial stability

We held our latest meeting with mgmt. at their California HQ to discuss prospects after the cut to the outlook with 2Q results. Overall, mgmt. was sober on its prospects and is focused on reducing costs and repositioning the company to hit its latest targets. Mgmt is in the midst of its wider ~10% reduction in Opex to realign its headcount with reduced deployment. Mgmt did not offer comfort on 2017, but instead emphasized the cycle was poised to turn in 2018 and particularly 2019 as the next 'peak' year in the ITC. Our Buy rating rests on this recovery, with margin improvement in particular.

Residential execution remains critical to story, but clarity is lacking

Following the near zeroing out of expectations for its Power Plant build with 2Q, the story has meaningfully shifted towards resi and commercial execution. However, we noted a lack of confidence on execution on this front as well given the more limited forward visibility on resi. While mgmt. was confident to grow in line with the industry average (~30%) YoY, it cautioned that resi market conditions appear to be constantly evolving with forward margin visibility of ~90-days. The higher efficiency panels makes these two (resi + comm) segments its core product offering, with confidence on (maintaining ~current levels for resi and C&I into 2017 despite this opacity. Further, distancing itself from recent scrutiny of SCTY, mgmt. emphasizes the diversity of its resi offerings across the US, Europe, and Japan/Australia. The focus is also principally on loans/direct sales vs. SCTY's leases, with loans garnering a greater level of industry penetration of late. Beyond the scope of our latest mgmt. meetings, we note recent expert meetings have indicated a shift towards emphasized 'exclusive' dealer relationships to remarket SPWR residential products in an effort to ensure execution on targets into 2017. Net-net, while forward visibility on orders is less than ideal here, mgmt. appears to be keenly aware of the need to succeed in this core niche.

Focusing on Power Plant biz: is zero margin on all 1.1 GW realistic? Just as surprising as mgmt's reduction in guidance was with 2Q, we think the latest reduction is overly conservative with mgmt. still expecting zero margin on ~all of its ~1.1GW (even with ~50% already booked). Further, mgmt. notes that even at zero margins, the upstream equipment committed to downstream development activities would have cash benefit attributable to it (albeit unclear on total; seems ~modest).

Valuation: Committed parent sponsor in Total; desire to maintain public float

Mgmt emphasized that its majority shareholder Total was clearly committed to the business through its past cycles, emphasizing its complementary acquisitions of late. They did further emphasize Total's desire to maintain a public float to provide employee alignment on execution and a public eye on execution. PT based on SotP valuation.

Equities

Americas
Semiconductors

12-month rating **Buy**

12m price target **US\$13.00**

Price **US\$10.10**

RIC: SPWR.O BBG: SPWR US

Trading data and key metrics

52-wk range	US\$30.77-9.84
Market cap.	US\$1.69bn
Shares o/s	167m (COM)
Free float	34%
Avg. daily volume ('000)	2,595
Avg. daily value (m)	US\$34.3
Common s/h equity (12/16E)	US\$1.28bn
P/BV (12/16E)	1.1x
Net debt / EBITDA (12/16E)	2.8x

EPS (UBS, diluted) (US\$)

	12/16E	
	UBS	Cons.
Q1	(0.30)	(0.30)
Q2E	(0.12)	(0.22)
Q3E	0.36	0.36
Q4E	0.34	0.48
12/16E	0.28	0.35
12/17E	0.63	0.63
12/18E	1.36	1.07

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Highlights (US\$m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	2,602	2,619	2,613	2,935	3,756	4,165	4,563	5,219
EBIT (UBS)	289	267	423	121	179	307	412	487
Net earnings (UBS)	292	251	357	40	94	215	312	376
EPS (UBS, diluted) (US\$)	2.10	1.54	2.65	0.28	0.63	1.36	1.84	2.07
DPS (US\$)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net (debt) / cash	(306)	(234)	(656)	(821)	(853)	(88)	211	543
Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
EBIT margin %	11.1	10.2	16.2	4.1	4.8	7.4	9.0	9.3
ROIC (EBIT) %	26.4	20.4	25.1	6.5	10.2	23.8	52.4	79.1
EV/EBITDA (core) x	6.5	13.0	8.3	5.8	4.7	3.6	3.0	2.6
P/E (UBS, diluted) x	9.7	21.3	10.5	35.6	16.0	7.5	5.5	4.9
Equity FCF (UBS) yield %	5.7	(1.0)	(19.9)	(12.7)	42.4	18.1	19.2	19.1
Net dividend yield %	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US\$10.10 on 01 Sep 2016 19:38 EDT

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Forecast returns

Forecast price appreciation	+28.7%
Forecast dividend yield	0.0%
Forecast stock return	+28.7%
Market return assumption	5.8%
Forecast excess return	+22.9%

Valuation Method and Risk Statement

Risks to SunPower (SPWR) include but are not limited to: inability to raise debt, equity, working capital, and other capital sources to finance development of solar projects; rising interest rates and financing costs; lack of liquidity and failure to meet liabilities and other obligations as due; inability to transact with its jointly-owned YieldCo entities in an accretive fashion; counterparty defaults; inability to transact with third parties and realize gross margins; supply/demand imbalances; increasing cost structure and failure of solar technology to achieve 'grid parity'; increased competition for project development opportunities pressuring realized margins; technological defects and obsolescence; loss of and/or infringement on intellectual property rights; losses from cyber-attacks; lack of raw materials and necessary components needed to manufacture solar modules; supply chain delays or interruptions; sudden removal of existing government subsidies such as tax rebates or feed-in tariffs.; unfavorable international, federal, state, or local legislation/regulation; unforeseen environmental liabilities for its hazardous materials used in solar manufacturing; natural disasters; labor strikes and other unrest; adverse changes to tax subsidies for solar generation, unfavorable weather (solar resource generation); sustained declines in oil prices; shareholder and class action litigation; insider and/or concentrated shareholder selling and below-average customer demand.

Our price target remains based on an EV/EBITDA-derived SotP valuation.

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12-Month Rating	Definition	Coverage ¹	IB Services ²
Buy	FSR is > 6% above the MRA.	47%	32%
Neutral	FSR is between -6% and 6% of the MRA.	38%	25%
Sell	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	Definition	Coverage ³	IB Services ⁴
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2016.

1:Percentage of companies under coverage globally within the 12-month rating category.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
SunPower Corp ¹⁶	SPWR.O	Buy	N/A	US\$10.10	01 Sep 2016

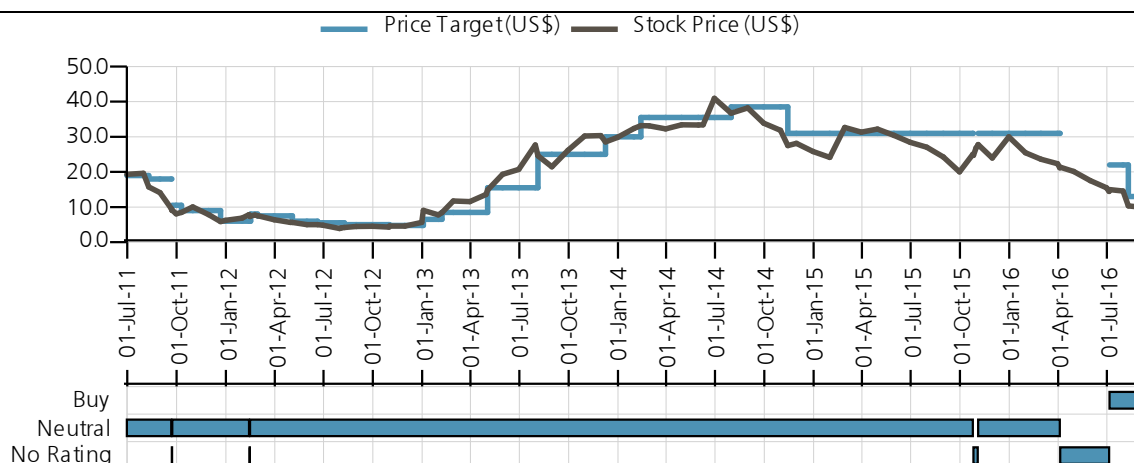
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SunPower Corp (US\$)



Source: UBS; as of 01 Sep 2016

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