

Flex Ltd.

Management meeting takeaways; does FLEX deserve to trade at a discount? No

Reiterate Rating: BUY | PO: 30.00 USD | Price: 24.51 USD

Focus on growing margins through cycle

We hosted in-person investor meetings in NYC with CEO Revathi Advaiti and CFO Paul Lundstrom. FLEX is trading at a meaningful discount to some peers, which we think is unwarranted. We walked away more confident in our thesis and opportunities for further revenue and margin growth. Management targets end markets where it can provide value to customers, and targets consistent margin improvement through cycle, which can come from revenue growth and/or productivity improvement. Even in a flat revenue environment, there is enough productivity growth and mix shift happening in order to sustain margin growth. We think that mid-teens (say 15% y/y) growth for EPS in F25 would be a good outcome in a weak macro. We reiterate our Buy rating on long-term improving mix, margin growth, and capital returns. We increase our PO to \$30 (from \$28) on 12x (prior 11x) F25 EPS of \$2.45 (unchanged). We make no changes to our estimates. We use a slightly higher multiple on more confidence in revenue and margin growth.

Well positioned with hyperscale to capture AI demand

Hyperscale customers want a partner that can reduce their end-to-end lead time and support new product launches. FLEX supports multiple hyperscalers and recently won a large contract (which is AI focused and relates to a new-generation product). FLEX is about halfway through this program ramp and expects a full revenue run rate in F26. FLEX makes all of the mechanical structures associated with racks/enclosures in-house and populates them with servers, storage, etc. It provides services to integrate the racks with value-added solutions. For example, FLEX is developing its own reference designs for cooling, which hyperscalers can use for their platform. FLEX also takes care of recycling components for hyperscalers. FLEX has been investing in power for datacenters for many years and has its own product to support both embedded power and facilities power. While margins are better on the power side, both the IT part (in CEC) and power (in Industrial) are accretive to respective segment margins.

Expect significant working capital unlock; buybacks

While FLEX is not going to lever up to buy back stock, management expects significant cash generation from working capital unlock (over the long term, net inventory days should reduce from 72 days to 60 days, which would generate about \$1bn of cash). FLEX needs to keep \$2bn of cash on hand to run the business. At the end of F3Q, Nexttracker had about \$350mn of cash and about \$150mn of debt. FLEX has guided for \$500mn of buybacks in F4Q, and we expect buybacks to continue beyond that.

Estimates (Mar) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	1.96	2.36	2.51	2.45	2.93
GAAP EPS	1.94	1.75	2.04	2.01	2.46
EPS Change (YoY)	24.8%	20.4%	6.4%	-2.4%	19.6%
Consensus EPS (Bloomberg)			2.51	2.46	2.89
DPS	0	0	0	0	0
Valuation (Mar)					
P/E	12.5x	10.4x	9.8x	10.0x	8.4x
GAAP P/E	12.6x	14.0x	12.0x	12.2x	10.0x
EV / EBITDA*	7.4x	6.3x	5.7x	6.3x	5.9x
Free Cash Flow Yield*	5.7%	3.2%	5.8%	4.2%	4.5%

* For full definitions of *IQmethod*SM measures, see page 7.

08 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	28.00	30.00

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Stock Data

Price	24.51 USD
Price Objective	30.00 USD
Date Established	8-Feb-2024
Investment Opinion	B-1-9
52-Week Range	14.14 USD - 25.96 USD
Mkt Val (mn) / Shares Out (mn)	10,323 USD / 421.2
Free Float	99.1%
Average Daily Value (mn)	140.03 USD
BoFA Ticker / Exchange	FLEX / NAS
Bloomberg / Reuters	FLEX US / FLEX.OQ
ROE (2024E)	18.7%
Net Dbt to Eqty (Mar-2023A)	9.6%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BoFA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BoFA ESGMeter Methodology".

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Timestamp: 08 February 2024 10:34AM EST

AI: Artificial Intelligence

CEC: Communications, Enterprise and Cloud end market

I-t: long-term

PO: price objective

iQprofileSM Flex Ltd.

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	11.5%	12.7%	12.8%	10.5%	12.0%
Return on Equity	24.7%	22.0%	18.7%	16.4%	17.8%
Operating Margin	4.5%	4.7%	5.8%	5.0%	5.2%
Free Cash Flow	592	335	602	436	462

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	1.1x	0.9x	1.0x	1.0x	0.9x
Asset Replacement Ratio	0.9x	1.2x	1.0x	0.9x	1.0x
Tax Rate	12.1%	10.8%	15.8%	17.5%	17.5%
Net Debt-to-Equity Ratio	29.3%	9.6%	12.8%	22.1%	16.1%
Interest Cover	12.4x	7.1x	8.8x	9.4x	12.5x

Income Statement Data (Mar)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	26,041	30,346	27,988	27,154	28,372
% Change	7.9%	16.5%	-7.8%	-3.0%	4.5%
Gross Profit	1,957	2,330	2,523	2,206	2,420
% Change	11.2%	19.1%	8.3%	-12.6%	9.7%
EBITDA	1,652	1,942	2,148	1,938	2,058
% Change	-2.6%	17.6%	10.6%	-9.8%	6.2%
Net Interest & Other Income	(94)	(204)	(185)	(144)	(119)
Net Income (Adjusted)	945	1,090	1,105	995	1,126
% Change	19.0%	15.3%	1.4%	-9.9%	13.2%

Free Cash Flow Data (Mar)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	945	1,104	1,211	995	1,126
Depreciation & Amortization	483	501	526	588	574
Change in Working Capital	(396)	(584)	(405)	(434)	(503)
Deferred Taxation Charge	0	0	0	0	0
Other Adjustments, Net	(8)	(71)	(179)	(180)	(180)
Capital Expenditure	(432)	(615)	(550)	(533)	(556)
Free Cash Flow	592	335	602	436	462
% Change	10.6%	-43.4%	79.8%	-27.7%	6.0%
Share / Issue Repurchase	0	0	0	0	0
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	475	(306)	(396)	0	(1,275)

Balance Sheet Data (Mar)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	2,964	3,294	2,648	2,112	1,083
Trade Receivables	3,371	3,739	3,681	3,645	3,887
Other Current Assets	8,002	8,988	8,394	8,821	9,371
Property, Plant & Equipment	2,125	2,349	2,314	2,260	2,242
Other Non-Current Assets	2,863	3,025	3,161	3,161	3,161
Total Assets	19,325	21,395	20,199	20,000	19,743
Short-Term Debt	949	150	3	3	3
Other Current Liabilities	9,762	10,705	9,533	9,491	9,779
Long-Term Debt	3,248	3,691	3,431	3,431	2,156
Other Non-Current Liabilities	1,159	1,143	1,104	1,104	1,104
Total Liabilities	15,118	15,689	14,071	14,029	13,042
Total Equity	4,207	5,706	6,127	5,970	6,700
Total Equity & Liabilities	19,325	21,395	20,198	19,999	19,742

* For full definitions of iQmethodSM measures, see page 7.

Company Sector

Electronics Manufacturing Services

Company Description

Flex is a global provider of vertically-integrated supply chain services starting from PCB fabrication, design, engineering and manufacturing services through after-sales support.

The core business includes the Reliability Solutions and Agility Solutions segments

Investment Rationale

Our positive view is based on (1) structural mix shift to higher margin end markets, (2) management's medium-term target of growing core business revenues at high single digits CAGR and growing operating margin to 5.0%, 3) consistency of FCF and good FCF yield, 4) management's focus on shareholder value creation, and 5) growth opportunity from new end markets

Stock Data

Average Daily Volume

5,713,362

Quarterly Earnings Estimates

	2023	2024
Q1	0.54A	0.57A
Q2	0.63A	0.68A
Q3	0.62A	0.71A
Q4	0.57A	0.55E

Takeaways from management meetings

We hosted in-person investor meetings in NYC with CEO Revathi Advaiti, CFO Paul Lundstrom, and David Rubin and Suzannah Williams from investor relations.

- FLEX has created significant value for shareholders with its spin-off of Nextracker (ticker: NXT).
- Management stressed that this spin-off was the correct thing to do. The Nextracker business did not have meaningful synergies with core FLEX. Over the years, management had improved margins at Nextracker and believed that it was in shareholders' best interest to spin off that business.
- Management stressed that from a revenue growth and profitability standpoint, core FLEX is well positioned, similar to competitor Jabil (ticker: JBL). It believes that the company has revenue growth opportunities in multiple end markets, including cloud/AI, healthcare, automotive, and industrial.
- FLEX is well positioned to support hyperscale in both the IT domain as well as in the power space.
- FLEX recently won a large hyperscale contract, which will be supported out of its facility in Mexico. FLEX had been working with the customer for two years before it won this particular contract. FLEX has a large facility in Mexico that is able to support the large power needs of this project.
- Capex investments over the years have tracked to what FLEX laid out at its analyst day three years ago. Investments have supported ramps in healthcare (for example, continuous glucose monitor devices), ramps in automotive, and growth in its cloud business (which has grown much faster than the targeted 20% y/y growth).
- The macro environment remains weak. In Industrial, both the residential and commercial renewables markets are soft. Industrial devices (for example, energy meters, circuit breakers) are slow, but there is not a lot of inventory buildup in this segment. The market for power remains strong.
- In automotive, FLEX is well levered to internal combustion engine (ICE), hybrid, as well as electric vehicles (EVs). In EVs, FLEX is well diversified from a geography and original equipment manufacturer (OEM) standpoint. The EV market is somewhat uncertain given some program delays.
- The Agility segment saw strong margin growth over the past several quarters from 1) intentional mix shift to higher-margin parts of the business (including lifestyle and Cloud within CEC), 2) un-intentional mix shift (lower revenue from lower-margin end markets such as telecom), 3) productivity gains (factory footprint, factory productivity, overhead productivity), and 4) unwinding of the impact of inflation pass-through (which helps margin rate but hurts revenues)
- The consumer devices segment within Agility has lower margins, and FLEX has de-emphasized that business.
- In the long term, FLEX has lowered the factory break-even costs in the Agility segment and manages well the fixed/variable costs in order to manage decremental margins through the cycle. Agility segment margins should continue to benefit in F4Q24 from restructuring activities taken throughout F3Q.
- The Lifestyle business within Agility targets high-end consumer appliance brands, and this affords a better margin profile.
- Within the CEC end market, there are three pieces: The communications part has been soft and has lower margin. The Enterprise IT part is also seeing softness. The Cloud business is seeing strong growth and offers higher margins.



- Reliability segment margins have been pressured given investment in program ramps; however, margins should improve over time. Over time, segment margins can get above 6.0%, and perhaps in the very long term into the high single digits. Management is not guiding to these margin targets, but it believes that the end markets can support these margins over time.
- Within Reliability, Health Solutions offers higher margins. This business has higher capital intensity and requires Food and Drug Administration (FDA)-regulated facilities. So the company enjoys barriers to entry. The customer contracts in this segment are 6-10 years long. Management believes that margins in Healthcare can grow over time.
- In Automotive, FLEX is displacing some Tier-1s, and while margins in this segment are somewhat thinner, management believes that margins can grow over the next few years.
- In Industrial, FLEX is seeing softness in residential solar. But margins in Industrial should improve over the next few years.
- FLEX is helping its customers with regionalization of manufacturing and ensuring continuation of supply.
- In terms of capex, management prefers modular expansion of existing facilities, which are already pre-wired with the supply chain. Big manufacturing hubs include Mexico, China, Malaysia, parts of Eastern Europe, and the US (Austin Texas and South Carolina).
- M&A target areas could include datacenter liquid cooling related, connectors for cooling, embedded power and facilities power related, and related to value-added services.

Model

Exhibit 1: FLEX Income Statement

We model F25 revenue/EPS of \$27bn/\$2.45

(\$ in millions except per share data)	F2024E				F2025E				F2022	F2023	F2024E	F2025E	F2026E
	1Q24A	2Q24A	3Q24A	4Q24E	1Q25E	2Q25E	3Q25E	4Q25E					
Sales	7,336	7,471	7,103	6,078	6,432	6,643	7,025	7,054	26,041	30,346	27,988	27,154	28,372
Cost of Sales	6,722	6,795	6,391	5,557	5,915	6,106	6,452	6,476	24,084	28,016	25,465	24,949	25,951
Gross Profit	614	676	712	521	518	537	573	578	1,957	2,330	2,523	2,206	2,420
Operating Income	377	439	477	329	315	328	352	356	1,169	1,441	1,622	1,350	1,484
Interest & Other Expense, net	51	43	38	53	36	36	36	36	94	204	185	144	119
Pretax Income	326	396	439	276	279	292	316	320	1,075	1,237	1,437	1,206	1,365
Taxes	41	58	86	41	49	51	55	56	130	133	226	211	239
Rate	13%	15%	20%	15%	18%	18%	18%	18%	12%	11%	16%	18%	18%
Minority interest	27	35	44	0	0	0	0	0	14	14	106	0	0
Net income before FAS 123R	258	303	309	235	230	241	260	264	945	1,090	1,105	995	1,126
Non GAAP EPS (ex FAS)	\$0.57	\$0.68	\$0.71	\$0.55	\$0.55	\$0.58	\$0.64	\$0.68	\$1.96	\$2.36	\$2.51	\$2.45	\$2.93
Non GAAP NI (incl FAS)	217	258	270	207	202	213	232	236	853	957	952	883	1,014
Non GAAP EPS (incl FAS)	\$0.48	\$0.58	\$0.62	\$0.49	\$0.48	\$0.52	\$0.58	\$0.61	\$1.77	\$2.07	\$2.16	\$2.17	\$2.64
Diluted Shares - NON GAAP EPS (MM)	455	448	436	425	420	412	404	389	483	462	441	406	384
As % of Revenue													
Cost of Sales	91.6%	91.0%	90.0%	91.4%	92.0%	91.9%	91.8%	91.8%	92.5%	92.3%	91.0%	91.9%	91.5%
Gross Profit	8.4%	9.0%	10.0%	8.6%	8.0%	8.1%	8.2%	8.2%	7.5%	7.7%	9.0%	8.1%	8.5%
SG&A	3.2%	3.2%	3.3%	3.2%	3.2%	3.2%	3.2%	3.2%	3.0%	2.9%	3.2%	3.2%	3.3%
Operating Earnings	5.1%	5.9%	6.7%	5.4%	4.9%	4.9%	5.0%	5.0%	4.5%	4.7%	5.8%	5.0%	5.2%
Interest & Other Expense	0.7%	0.6%	0.5%	0.9%	0.6%	0.5%	0.5%	0.5%	0.4%	0.7%	0.7%	0.5%	0.4%
Pretax Earnings	4.4%	5.3%	6.2%	4.5%	4.3%	4.4%	4.5%	4.5%	4.1%	4.1%	5.1%	4.4%	4.8%
Net income before FAS 123R	3.5%	4.1%	4.4%	3.9%	3.6%	3.6%	3.7%	3.7%	3.6%	3.6%	3.9%	3.7%	4.0%
Year-Over-Year Growth													
Sales	0%	-4%	-8%	-19%	-12%	-11%	-1%	16%	8%	17%	-8%	-3%	4%
Cost of Sales	-1%	-5%	-11%	-19%	-12%	-10%	1%	17%	8%	16%	-9%	-2%	4%
Gross Profit	13%	13%	20%	-12%	-16%	-21%	-20%	11%	11%	19%	8%	-13%	10%
SG&A	12%	6%	5%	-17%	-15%	-12%	-6%	16%	8%	13%	1%	-5%	9%
Operating Earnings	14%	17%	28%	-10%	-16%	-25%	-26%	8%	13%	23%	13%	-17%	10%
Interest & Other Expense	34%	-14%	-36%	-7%	-29%	-16%	-5%	-32%	-14%	117%	-9%	-22%	-18%
Pretax Earnings	12%	22%	40%	-10%	-14%	-26%	-28%	16%	17%	15%	16%	-16%	13%
Net income before FAS 123R	1%	5%	8%	-10%	-11%	-21%	-16%	12%	19%	15%	1%	-10%	13%
Non GAAP EPS (ex FAS)	4%	8%	14%	-3%	-3%	-14%	-9%	23%	25%	21%	6%	-2%	20%
Non GAAP EPS (incl FAS)	-3%	1%	10%	7%	1%	-10%	-7%	25%	25%	17%	4%	1%	22%
Diluted Shares - NON GAAP EPS (MM)	-3%	-3%	-5%	-7%	-8%	-8%	-7%	-8%	0%	0%	0%	0%	0%

Source: Company reports, BofA Global Research estimates

BofA GLOBAL RESEARCH



Price objective basis & risk

Flex Ltd. (FLEX)

Our price objective is \$30 based on 12x F25E EPS of \$2.45. This multiple is above the median 9x of the long-term trading range of 6-13x. We believe that this multiple is justified as it balances near-term risk from lower revenues related to weaker end markets, and margin headwind from component shortages, and higher logistics costs, versus longer-term expectation of improving mix, revenue growth and margins.

Downside risks: Unexpected downturn in the global economy, margin headwind from higher logistics costs, weaker-than-expected end markets, new program ramps taking longer than expected, share gains by competitors, unexpected restructuring and longer than expected time to pass through rising component costs.

Analyst Certification

I, Ruplu Bhattacharya, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - IT Hardware and Technology Supply Chain Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Amphenol	APH	APH US	Wamsi Mohan
	Apple Inc.	AAPL	AAPL US	Wamsi Mohan
	Corning Inc.	GLW	GLW US	Wamsi Mohan
	Dell Technologies Inc.	DELL	DELL US	Wamsi Mohan
	Flex Ltd.	FLEX	FLEX US	Ruplu Bhattacharya
	HP Inc.	HPQ	HPQ US	Wamsi Mohan
	International Business Machines Corp.	IBM	IBM US	Wamsi Mohan
	Jabil Inc.	JBL	JBL US	Ruplu Bhattacharya
	Nutanix Inc	NTNX	NTNX US	Wamsi Mohan
	Roku, Inc.	ROKU	ROKU US	Ruplu Bhattacharya
	Seagate Technology	STX	STX US	Wamsi Mohan
	TD Synnex Corp	SNX	SNX US	Ruplu Bhattacharya
	TE Connectivity Ltd.	TEL	TEL US	Wamsi Mohan
	Teradata Corporation	TDC	TDC US	Wamsi Mohan
	Western Digital Corporation	WDC	WDC US	Wamsi Mohan
NEUTRAL				
	Arrow Electronics Inc.	ARW	ARW US	Ruplu Bhattacharya
	Avnet Inc.	AVT	AVT US	Ruplu Bhattacharya
	CDW Corp	CDW	CDW US	Ruplu Bhattacharya
	Concentrix Corporation	CNXC	CNXC US	Ruplu Bhattacharya
	Hewlett-Packard Enterprise	HPE	HPE US	Wamsi Mohan
	Pure Storage	PSTG	PSTG US	Wamsi Mohan
	Sensata Technologies Holdings Plc	ST	ST US	Wamsi Mohan
UNDERPERFORM				
	DigitalOcean	DOCN	DOCN US	Wamsi Mohan
	NetApp Inc.	NTAP	NTAP US	Wamsi Mohan
	Sanmina Corporation	SANM	SANM US	Ruplu Bhattacharya
	Vishay Intertechnology, Inc.	VSH	VSH US	Ruplu Bhattacharya
	Vizio	VZIO	VZIO US	Wamsi Mohan

iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

iQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

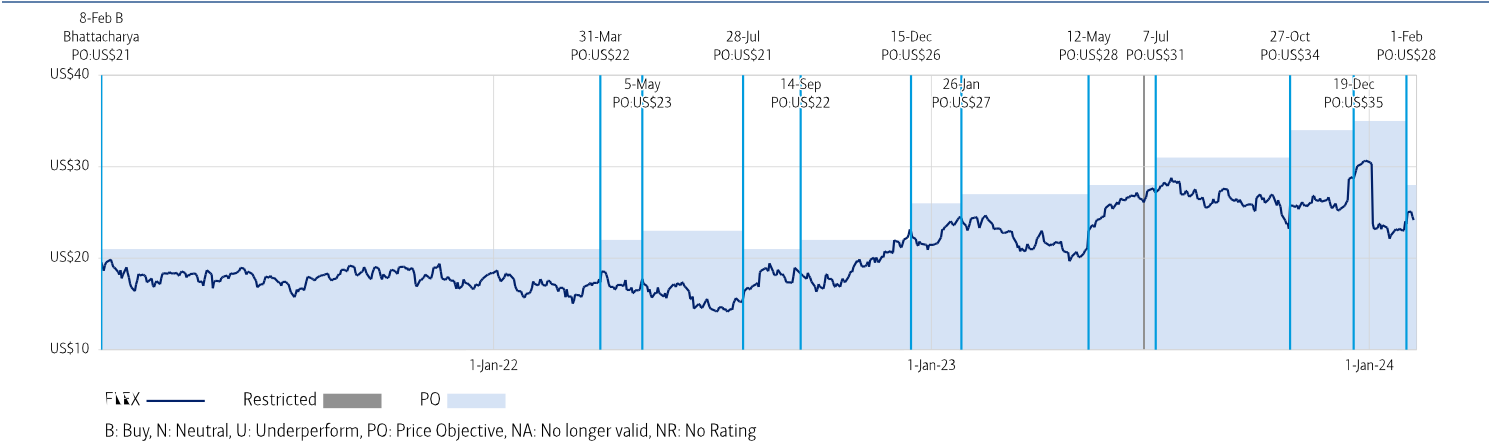
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Disclosures

Important Disclosures

Flex Ltd. (FLEX) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Electronics Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	32	54.24%	Buy	13	40.63%
Hold	11	18.64%	Hold	3	27.27%
Sell	16	27.12%	Sell	4	25.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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