

Arm Holdings

FQ3 preview: all eyes on content growth

Maintain Rating: BUY | PO: 80.00 USD | Price: 73.27 USD

N-t trends mixed, but I-t intact; maintain Buy/\$80 PO

ARM will report FQ3'24 (DecQ) results and FQ4 (MarQ) guide after market close on Wed, February 7. Overall, we expect: 1) in-line to modestly better FQ3 results on upbeat iPhone/Android results, offset by continued weak Auto/IoT environments; and 2) in-line FQ4 outlook on sub-seasonal handset units (Apple/Qualcomm), offset by strong Arm content growth in smartphones and cloud. While near-term unit trends are more mixed, we point to royalty rate expansion (2.3% in CY25E from just 1.7% in CY23) as key to our Arm investment thesis and highlight continued penetration of higher-value systems at customers, such as TCS products at MediaTek (Dimensity 9300) and Neoverse CSS at Faraday (HPC vendor). Importantly, v9 adoption rate is still in its early days at ~10% of total royalties (per FQ2'24 call), suggesting significant transition benefits are still ahead. Moreover, the ramp of edge AI in smartphones should help accelerate mix shift toward more expensive, richer content CPUs (such as Snapdragon 8 Gen 3 which saw robust DecQ growth on AI features) vs. mid-/low-tier CPUs. In turn, we see royalty growth to start meaningfully inflecting higher in FQ4 (+31% YoY) as comps get easier and as v9 transition/content growth play out (up >30% YoY for the next nine quarters). Net-net, we maintain our ests. into the print and maintain Buy and \$80 PO on 44x CY25E P/E or high-end of peers but justified given superior growth profile and asset light model.

Royalty acceleration to drive growth; Licensing lumpy

For FQ3 we model \$761mn sales, including \$452mn in royalties (+8% QoQ, +6% YoY) vs. \$447mn cons. (+7% QoQ) and \$308mn in licensing. For FQ4, we expect \$490mn in royalties (+8% QoQ, +31% YoY) vs. \$476mn cons. (+6% QoQ) and \$288mn in licensing sales. Looking into CY24/FY25E, we forecast smartphone units to stabilize and grow modestly YoY, contributing to Royalties sales growth of ~40% YoY on content gains.

Client: unit outlook slows, but content growth continues

In DecQ, iPhone 15 cycle tracked better than prior gen (excl. extra week impact YoY). QCOM saw strong China Android ramps, alongside a successful Samsung (GS24) launch which utilizes its highest-end CPU (rich Arm content). MediaTek also saw the strongest QoQ handset growth in DecQ in nearly 20 years on its flagship v9 SoCs (+70% YoY). Though MarQ/JunQ point to sub-seasonal trends on slow China demand and the lack of new Android launches, we highlight continued Arm v9 transition (only 10% adoption today), as well as shift toward premium-tier CPUs (edge AI), enriching Arm content.

Infrastructure: cloud ramp continues into CY24E

Infrastructure growth is driven both by units (cloud share gains) and content growth (increasing royalty rate). NVDA's Arm-based Grace CPU (4nm) is now fully ramping in data centers, alongside Ampere's AmpereOne (5nm), taking share from x86 INTC (Intel 7) and AMD (5nm) counterparts. AWS has also unveiled its latest Arm-based Graviton4 which should ramp throughout CY24E. Overall, we see Arm Infra. sales to grow >50% YoY for the next 7-8 quarters, contributing to a potential doubling of sales in FY25E.

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Stock Data

Price	73.27 USD
Price Objective	80.00 USD
Date Established	15-Dec-2023
Investment Opinion	C-1-9
52-Week Range	46.50 USD - 79.94 USD
Mkt Val (mn) / Shares Out (mn)	75,119 USD / 1,025.2
Free Float	0%
Average Daily Value (mn)	495.43 USD
BofA Ticker / Exchange	ARM / NAS
Bloomberg / Reuters	ARM US / ARM.OQ
ROE (2024E)	23.2%
Net Dbt to Eqty (Mar-2023A)	-38.4%

ARM – Arm Holdings
AMD – Advanced Micro Devices
AWS – Amazon Web Services
INTC – Intel
NVDA – Nvidia
QCOM – Qualcomm
HPC – High-Performance Computing
CPU – Central Processing Unit
GPU – Graphics Processing Unit
SoC – System on Chip
GS – Galaxy S
AI – Artificial Intelligence
nm – nanometer
TCS – Total Compute Solution
CSS – Compute Subsystem
PC – Personal Computer
OEM – Original Equipment Manufacturer

Price objective basis & risk

Arm Holdings (ARM)

We assign a \$80 PO, which is based on 44x our CY25E non-GAAP EPS. This is at the high end of peers trading at 30x-36x and is justified, in our view, given Arm's superior growth profile.

Downside risks: 1) historically cyclical nature of semiconductor units, 2) high exposure to mature smartphone market, 3) competition against established x86 in the data center, 4) emerging competition from RISC-V in low-end consumer markets, 5) rising geopolitical tensions and deterioration of Arm China relationship, 6) ongoing Qualcomm/Nuvia litigation, 7) small trading float

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Arm Holdings (ARM) Price Chart



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Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

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

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

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