

ISGAM AG, Beethovenstrasse 48, CH-8002 Zurich, Switzerland
 T: +41 44 286 6060 F: +41 44 286 6065 E: enquiry@isgam.ch

Stock Highlight for the Quarter to 31 March 2021

This quarter we would like to focus on ASML Holding N.V., a Dutch technology company founded in 1984 which develops, produces, and markets semiconductor manufacturing equipment.

ASML is one of the largest suppliers of semiconductor manufacturing equipment specializing in photolithography systems used to produce semiconductors.

ASML's products include EUV (extreme ultraviolet) lithography systems, DUV (deep ultraviolet) lithography systems, refurbished systems, and metrology and inspection systems. ASML serves clients worldwide and its products are used at every major semiconductor manufacturer including Intel, Samsung, and Taiwan Semiconductor. ASML has been part of the information technology sector of the European share portfolio since November 2019.



Historical performance (total return in %)
 Source: Bloomberg Finance L.P.

ASML is the world's sole supplier of extreme ultraviolet (EUV) lithography equipment used in laying down circuitry, the most critical step in manufacturing the latest generation of chips (i.e. Apple Bionic chips). ASML is also a market leader in deep ultraviolet (DUV) lithography equipment which still produces most of the layers in a customer device today and will remain important for future devices.

This unique technological advantage gives ASML strong pricing power and the extensive technical expertise needed to develop lithography tools serves as a major barrier to entry. For example, ASML now sells its EUV machines for well over \$100 million each but it had first to invest roughly \$10 billion in developing the EUV technology;

this represents a significant barrier to entry as competitors do not have the scale or resources to compete at this cutting-edge. Besides, ASML's business strategy relies on innovation through collaboration. ASML innovates through partnerships by developing new technology and machines in close collaboration with its customers to build what they will need in the future (i.e. in 2012, ASML's top three customers, Intel, Samsung, and Taiwan Semiconductor, committed to help fund a portion of research and development for EUV technologies and acquired an aggregate 23% minority equity stake in ASML).

In the same way, ASML works closely with its suppliers, trusting them to manufacture parts and modules for its systems.

Despite ASML being a cyclical company, we remain confident the company can perform well in the current volatile environment. For instance, ASML experienced limited impact from Covid-19 on its manufacturing capability despite the challenges posed by absenteeism, transportation and support logistics related to the pandemic. Semiconductors are elementary components of many promising technologies and play a crucial part in shaping the interconnected and intelligent network future. The end market continues to grow as large and mature markets such as PCs and smartphones generate a steady growth from wired and wireless infrastructure as well as servers/data centers. Emerging opportunities involving automotive electrification, autonomous driving, Internet of Things, 5G, artificial intelligence, and the cloud will continue to drive demand in semiconductors in at least the next five years.

We have strong conviction in ASML because it is a well-managed company under the leadership of Peter Wennink, the CEO of ASML since 2013. He has been working for ASML since 1999 and most of the members of ASML's executive team have more than a decade of experience at ASML. Peter Wennink strongly improved the company's market position in the lithography segment by taking a technology lead over the past decade resulting in market share gains at the expense of competitors such as Nikon and Canon.

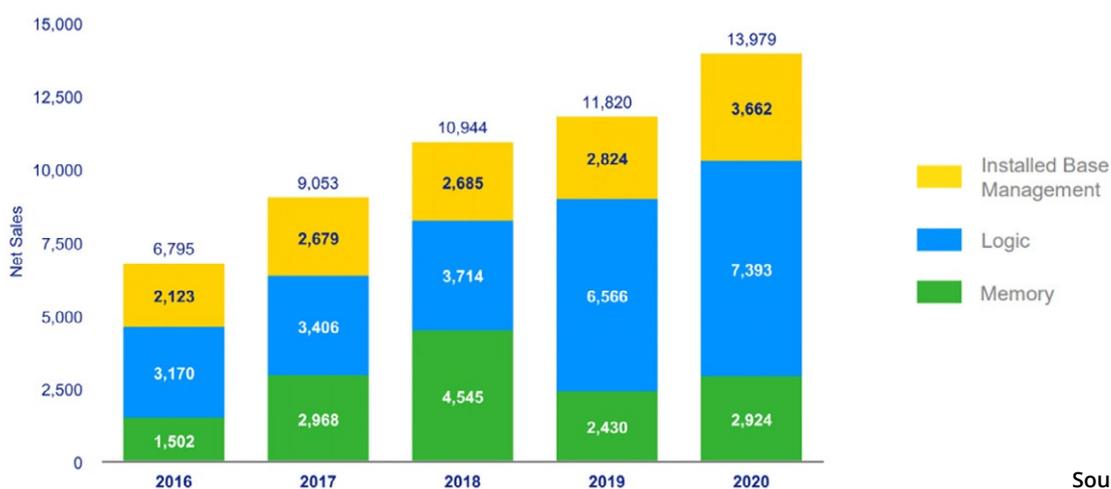
Under Wennink's tenure, ASML completed several strategic and focused mergers and acquisitions to further support growth and technological advancement.

For example, in 2013 ASML acquired a manufacturer of light sources, Cymer, to accelerate the development of the next-generation lithography technology EUV. In 2016, HMI, a major wafer inspection equipment provider, was acquired to further enhance the lithography product portfolio with e-beam inspection technology to identify pattern defects in EUV lithography. In 2017, ASML acquired a minority stake in Zeiss to secure the extension of EUV imaging technology, strengthening the combined businesses. Last year, ASML closed the acquisition of Glas Group, a manufacturer of ceramic and optical modules, which are important to support the future roadmap of EUV and DUV products.

Year-to-date, ASML is up 30.05% (as of March 31, 2021) and is part of our top 3 contributors to return of the European share portfolio and the best performing stock of the information technology sector of the European share portfolio.

Notwithstanding the significant outperformance this year, we believe ASML still has upside potential. In fact, despite the Covid-19 pandemic, ASML reported strong quarterly results in the fourth quarter of 2020, well ahead of expectations, reflecting the strong global demand for a digital infrastructure. In 2020, ASML net sales grew to a record €14.0 billion at 45.6% gross margin and €3.7 billion net income resulting in an EPS of €8.49. ASML anticipates revenue growth of 12% in 2021 but the consensus estimates are already above that, as continued growth is expected in 2021 due to strong logic demand and recovery in memory.

Total net sales € million by End-use



Source: ASML Holding NV

We also like the fact that ASML opted to integrate climate issues into its long-term business strategy. ASML aims to drive a renewable energy strategy by taking all steps required to lower its carbon footprint, reduce waste, and improve the energy efficiency of its products. As such, ASML decided to target zero emissions from its operations and supply chain by 2025 and committed to minimize waste and maximize the use of resources by cutting the amount of waste per revenue by 50% by 2025 (compared to 2019). In addition, ASML supports and contributes to the 2030 ambition defined in the United Nations Sustainable Development Goals (SDGs) to drive the transformation toward sustainability.

Of course, ASML is exposed to downside risks through potential weaker than expected global macroeconomic environment. A slower-than-expected EUV adoption rate, a slowdown in the semiconductor capex cycle, and a decline in the intensity of lithography capex could all negatively impact the company. Given the cyclical nature of the semiconductor industry, ASML could be affected by lower demand for chip-embedded devices such as smartphones, servers, and personal computers. The dependence on a limited number of suppliers for key components exposes ASML to possible disruptions to its supply chain.

Additionally, as semiconductors are at the heart of economic growth and a vital component of the technological innovation, the geopolitical risk should not be discounted.

As a conclusion, we think ASML's business model would be very difficult to disrupt as ASML operates in a quasi-monopoly as the leading provider of photolithography equipment. The company exhibits considerable scale and technological superiority relative to its competitors. Its technical expertise and large research and development budget (\$2.2 billion in 2020) serve as barriers to entry and give ASML a strong pricing power. Furthermore, in the last few years, ASML has focused on operational efficiency to improve profitability throughout industry cycles, which is now reflected in its solid balance sheet and financial position.

Thus, its debt position is not an issue as ASML generates strong cash flows and sits on a significant cash position which is appropriate given the cyclical nature of the semiconductor equipment industry. As a result, we believe ASML is uniquely positioned to benefit from the major trends driving the industry and to shape the semiconductor landscape by pushing technology to new limits.

In subsequent quarterly reports we will bring you further case studies in our "Highlights" series. As always, please do not hesitate to contact us if you have any questions or comments, about the contents of this report or your portfolio in general.

Portfolio Management Team ISGAM AG

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