

Cody Willard's

Top 10



Supplier Stocks

Homerun stocks for every tech investor

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DUNKIN'DONUTS

By Cody Willard (with Ashwin Deshmukh and William Fox)

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Introduction

If you've been reading or listening to me over the past 10 years you know I think Apple will definitely get to \$1000. And that would be a little less than a double (the stock is at \$628 as I write this but has probably moved up by the time you read this). So the reward is definitely less asymmetrical than when I was buying the stock at \$7.

Which is precisely why I think it's time to look at Apple's supply partners. Their share prices will have a halo from being associated with the Apple ecosystem. Much of what Apple is going to do in the next 5-10 years is baked-in demand from consumers replacing their iPhones & iPads. So while Apple will likely run another 100% from these levels, the suppliers should go up disproportionately more. I want to be long the spillover effect from Apple into the names I've picked out in a new book I'm calling "Top 10 Apple Supplier Stocks".

To understand why we're talking about Apple's suppliers, let's look at another West Coast high-tech giant that has transformed the world: Boeing.

Over the last 20 years Boeing advanced the science of aeronautics, launched multi-billion dollar defense systems that saw a dozen wars, created futuristic widebody jets and returned 242% for its shareholders.

And the company that supplies Boeing the TV's that fit above the food tray gained 3285% .



If you're a subscriber of mine, you've no doubt bought in to the Apple story---and hopefully listened to me at any point over the last 5 years and bought some shares. The stock has run up so

much, 5200% in the last decade, that it begs the question: How much higher can it go? It's no accident that Apple's supply guru Tim Cook was chosen by Steve Jobs to carry on his legacy. Apple's supply chain is a huge competitive advantage that rivals are having an impossible time copying. When Apple's design team decides it wants something, whether it be retina screens or aluminum shells or lasers that machine microscopic holes, they buy all the capacity that exists. Even the cycle on which they pay suppliers is structured as to squeeze out every last penny.

After the shareholders who receiving the newly announced dividend and buyback, Apple's suppliers will be the biggest recipient of its massive war chest. Apple has shown a willingness to provide vendor financing and pay a premium when it wants a component; they are one of the few companies that can actually pass those costs along. And when you add in that a good deal of Cupertino's cash is overseas, the logic of spending on the supply chains in other countries rather than paying taxes in this one makes sense.

I've spent the last few months talking to the geekiest of the geeks, supply chain experts and those in the know when it comes to Apple's components. Steve Jobs figured out early on that the best way to execute his vision was to leave some revenue on the table for other companies, and outsource key parts of its value chain. This hasn't worked out so well for other companies like Boeing but Apple has taken supply management to an art form. Over the next decade I expect them to keep working with the companies on this list, and possibly even buying some of them outright.

Bottom line is that you should own Apple, it's firing on all cylinders and innovating even without its founder. But it makes sense to pay attention to the companies that help Apple create its magic. And the stocks I've highlighted are the ones that are best positioned to take advantage of the ever-continuing Apple boom.

Company

BRCM - Broadcom Inc.

Summary

Broadcom Corporation designs and develops semiconductors for wired and wireless communications. It provides a portfolio of system-on-a-chip (SoC) and software solutions for the manufacturers of computing and networking equipment, digital entertainment and broadband access products, and mobile devices, which enable the delivery of voice, video, data, and multimedia content to the home, office, and mobile environment.

Balance Sheet

Cash and Cash Equivalents:	4.1 B
Short Term Investments:	383 M
Long term Investments:	<u>676 M</u>
Total Cash:	5.1 B

Total Debt:	<u>1.2 B</u>
Net Cash:	3.9 B

Outstanding Shares:	545 M
Net Cash / Share:	7.15

Share Price:	38.4
Enterprise Value / Share:	31.25

Total Market Cap:	20 B
Enterprise Value:	16.1 B

2012 Sales Growth:	9.9%
2012 Earnings Estimate:	2.9
Enterprise Value Multiple:	10.7 Times Forward Earnings
Dividend & Yield:	.4 (1%)

Broadcom is a fabless semiconductor company (meaning that outsource the actual production) that makes some of the most integral components of the iphone & ipad. They are still growing their product line, and eating the lunch of the likes of Intel and texas instruments. And best of all it looks like they've convinced Apple to rely on them even more heavily.

Apple's history with Broadcom goes back to a video component they made for the ipod. Today, BRCM makes the socket for the iphone, and has been doing so for at least two generations of the

iphone (they are in the newest ipad as well). Apple is a big proponent of the wifi & Bluetooth standards, and that's exactly what Broadcom deals in. And I love to see when Apple not only continues a relationship with a supplier but buys the new, updated version of the component. Broadcom convinced apple to go with their newer BCM4330-802 chipset, which means that their product cycle is pretty well synced up to Apple's needs. And that really is the Holy Grail for Apple suppliers. So not only is Broadcom getting that huge revenue stream but it becomes ever more difficult for Apple to separate from them as time goes on.

And it probably doesn't hurt that Samsung uses the exact same chipset in their well reviewed Galaxy S II. In a war between two superpowers, you want to be the guy selling bullets. And with a couple of savvy acquisitions over the years, Broadcom has positioned itself to benefit from the coming battle in mobile payments via NFC (near-field-communications).

Broadcom is in fact so well tied to Apple that revenue fluctuations at one of BRCM's biggest suppliers, Taiwanese Semiconductor, is now considered a reliable signal of Apple's product pipeline. So anytime TSM reports a slew of rush orders, the market takes it as a sign that Apple (and by proxy Broadcom) is about to launch a new gadget. That's the kind of deep and well understood intergration into Apple's supply chain that I want to invest in.

Just like ARM I think Broadcom is probably too big to be an acquisition candidate. At an enterprise value of ~\$17 billion, almost \$4 billion in net cash, it probably wouldn't sell itself for anything less than \$25 billion. Instead BRCM bought back \$300M of its own shares last year and raised the dividend 12.5%. Plus they've shown a willingness to do overseas acquisitions, where most of their stockpile is, avoiding repatriation at American corporate tax rates. Add in Broadcom's growing exposure to the growing Android tablet market and the fact that you can buy the stock at 10x forward earnings, and it's clear why this is one of my favorite Apple derivative plays.

Company

FIO - Fusion-io, Inc.

Summary

Fusion-io, Inc. develops, markets, and sells storage memory platforms for data decentralization in the United States. Its platforms enhance the processing capabilities within a datacenter by relocating process-critical or active data from centralized storage to the server where it is being processed.

Balance Sheet

Cash and Cash Equivalents:	3.8 M
Short Term Investments:	216 M
Long term Investments:	<u>--0</u>
Total Cash:	219.8 M

Total Debt:	<u>6 M</u>
Net Cash:	213.8 M

Outstanding Shares:	81.6 M
Net Cash / Share:	2.62

Share Price:	28.6
Enterprise Value / Share:	26

Total Market Cap:	2.5 B
Enterprise Value:	2.3 B

2011 Sales Growth:	444%
2012 Earnings Estimate:	.24
Enterprise Value Multiple:	108 Times Forward Earnings
Dividend & Yield:	N/A

Fusion-io is the newest of our Apple Supplier picks, so new that it may not even be on your radar screen. But it absolutely deserves to be.

As one of the few companies that incubated in the dark ages (2002-2007) while the housing boom was underway, IPO'd last year. Demand was big but the stock didn't do much. The ultimate Apple pedigree, Steve Wozniak as chief scientist, doesn't hurt either.

Bonafides asides FIO has some serious heat on it, namely EMC. The storage behemoth is outright threatened by FIO's disruptive potential and has gone so far as to launch its own poor imitation (caveat: emc is a fantastic company with a long track record and their offering will no doubt get better over time). Imitation really is the sincerest form of flattery, as EMC's move didn't hurt FIO stock, but instead provided fuel with takeover rumors.

FIO offers an innovative product for the cloud. Here's what I said to my Marketwatch readers about the company:

Fusion-Io has a pretty interesting and unique product; they bundle flash memory, like the ones in the ipad3 Apple is premiering in two weeks that can be put right alongside existing servers. It's a pretty deceptively simple idea, but it basically enables servers to access data way, way quicker.

FIO products are already in Apple server farms and expect them to grow as Apple buys more land for more data hubs. The other big customer of FIO is Facebook, which just convinced Apple to join it in building a new server farm in Oregon.



DAN AGUAYO/THE OREGONIAN

(Facebook & Apple are building data centers practically next to each other, using FIO's products)

I want to keep seeing that triple-digit growth in revenue and can deal with losses in the short term. The more widespread FIO makes its products now, the bigger it will be when it achieves profitability. For this name you almost have to be willing to catch a falling knife on the day no one else wants it.

Company

QCOM - Qualcomm, Inc.

Summary

QUALCOMM Incorporated designs, develops, manufactures, and markets digital telecommunications products and services. It operates in four segments: Qualcomm CDMA Technologies (QCT), Qualcomm Technology Licensing (QTL), Qualcomm Wireless and Internet (QWI), and Qualcomm Strategic Initiatives (QSI). The QCT segment develops and supplies integrated circuits and system software based on code division multiple access (CDMA), orthogonal frequency division multiple access (OFDMA), and other technologies for use in voice and data communications, networking, application processing, multimedia, and global positioning systems.

Balance Sheet

Cash and Cash Equivalents:	4.9 B
Short Term Investments:	6.5 B
Long term Investments:	<u>10.4 B</u>
Total Cash:	21.8 B

Total Debt:	<u>--0</u>
Net Cash:	21.8 B

Outstanding Shares:	1.7 B
Net Cash / Share:	12.8

Share Price:	68
Enterprise Value / Share:	55.2

Total Market Cap:	115 B
Enterprise Value:	93.2 B

2012 Sales Growth:	29.2%
2012 Earnings Estimate:	3.76
Enterprise Value Multiple:	14.6 Times Forward Earnings
Dividend & Yield:	.86 (1.3%)

Qualcomm is the largest of our Apple supplier picks by market cap. The stock has been a monster win for early investors, up 12,000%+ since IPO. And even if you bought in the last 5 years you're looking at 60%+ gains right now. Not bad in totally flat markets.

Qualcomm has about 40% of the market in something called 'baseband chips'. The baseband manages all the radio business of the main chipset. Over the last decade the standard, for as

much regulatory as technological reasons, has become that device manufacturers keep the baseband as a separate 'stack', distinct from the main processor.

Before Qualcomm had their baseband chip in the iPhone Apple was using an Infineon chip. But after Verizon became the 2nd U.S. iPhone carrier, Infineon's fate was sealed, Qualcomm's technology simply plays better with Verizon's CDMA standard---after all, they invented it. Teardowns of the iPhone 4s reveal that Apple uses Qualcomm's MDM6610, and channel checks in Taiwan have highlighted the MDM9615 as being part of the iPhone 5 (or 4.5 s, who knows). This new chip will enable those brand-new super-fast LTE networks to run on the iPhone. And Nokia and Samsung are both looking into using the MDM9615 in their perennial game of trying to mimic Apple. Besides the baseband chip in the iPhone Apple uses a Qualcomm power management device (PM8028) & RF transceiver (RTR8605). The new iPad uses a similar baseband chip, the MDM9600.

So it shouldn't be much of a surprise that when Goldman Sachs surveyed the 13F filings of 105 hedge funds, thirty-three of them listed Qualcomm among their top 10 holdings (above that were, in order, Apple, Google, Microsoft & J.P. Morgan). Which should raise the question of whether Qualcomm is a crowded trade and all future growth is priced in. I think there are quite a few catalysts that could pump that stock higher from here.

There has been a major wireless scandal in India, one of the biggest potential CDMA markets outside the U.S. Politicians of the ruling party were caught taking bribes to sell spectrum for way below market value, cheating the Indian taxpayer out of billions of dollars---our bureaucrats seem tame by comparison. Reliance, one of the main companies embroiled in the scandal, and the biggest provider of CDMA in the subcontinent, has been hampered in building out its subscriber base & network capacity. This has been the trend across the industry really, as bureaucrats looking to save face have been holding back all kind of approval necessary for CDMA capex. This should begin to abate this year. And Qualcomm is looking to become a direct provider of CDMA access in key urban areas after winning a hard-fought battle for an ISP license.

The other big catalyst is Qualcomm encroaching on the territory of another one of our picks, Broadcom. BRCM & QCOM have definite overlap and it's in the WiFi chips that Broadcom is the industry leader. Qualcomm is betting that its \$3.1 billion acquisition of Atheros, and the 26% market share they got with it, will let them leapfrog Broadcom into 5g Wi-Fi. The wireless service providers that used to think of WiFi as cutting in to juicy data margins are building in automatic switching capacities in phones, just to relieve the burden heavy data usage has put on their network. There is unlikely to be any kind of meaningful capacity buildout for the wireless carriers so look for WiFi to become even more important. Broadcom has an enormous lead in their WiFi capabilities, and it's less of a zero sum game than most analysts think, so there's probably room for both companies to grow.

And even though Qualcomm has gone from large cap to mega cap in short order (it's roughly the same size as Cisco with roughly one-third the revenue) I think there's still meat on the bones. I'd feel confident buying the stock on the dips, management has shareholders' backs with a \$4 billion stock buy back in place AND is increasing the dividend 16% to 25 cents. The stock is up about

17% this year as well, basically tracking what Apple has done. I'm not sure if you'll get a pullback on earnings anytime soon, so you'll probably have to be really disciplined and be holding on for a macro hit to the market. Hopefully some Eurozone nation will cause a mini panic so you can pick up some Qualcomm on the cheap.

Company

ARMH - ARM Holdings, plc.

Summary

ARM Holdings plc designs microprocessors, physical IP, and related technology and software, as well as sells development tools to enhance the performance of high-volume embedded applications. Its products include 16/32-bit RISC microprocessors cores, such as specific functions comprising video and graphics IP, and on-chip fabric IP; embedded software; physical IP components for the design and manufacture of SoC integrated circuits, which comprise embedded memory, standard cell, input/output components, and analog and mixed-signal products.

Balance Sheet *

Cash and Cash Equivalents:	45 M
Short Term Investments:	496 M
Long term Investments:	<u>45 M</u>
Total Cash:	586 M

Total Debt:	<u>--0</u>
Net Cash:	586 M

Outstanding Shares:	458 M
Net Cash / Share:	1.2

Share Price:	29
Enterprise Value / Share:	27.8

Total Market Cap:	13 B
Enterprise Value:	12.4 B

2012 Sales Growth:	11.6%
2012 Earnings Estimate:	.69
Enterprise Value Multiple:	40 Times Forward Earnings
Dividend & Yield:	.17 (.6%)

For the past 5 years there hasn't been a semi company hotter than ARM thanks to its relationship with Apple. Even with Tech Bust 1.0 the stock is up ~1200%+ since inception and trades at a premium to its competitors. If you had bought the Dow at its all time closing high you'd be down ~5%; if you had bought ARM you'd have doubled your money. Arm's designs are used in both the iphone & new ipad, as well as most of the world's smartphones.



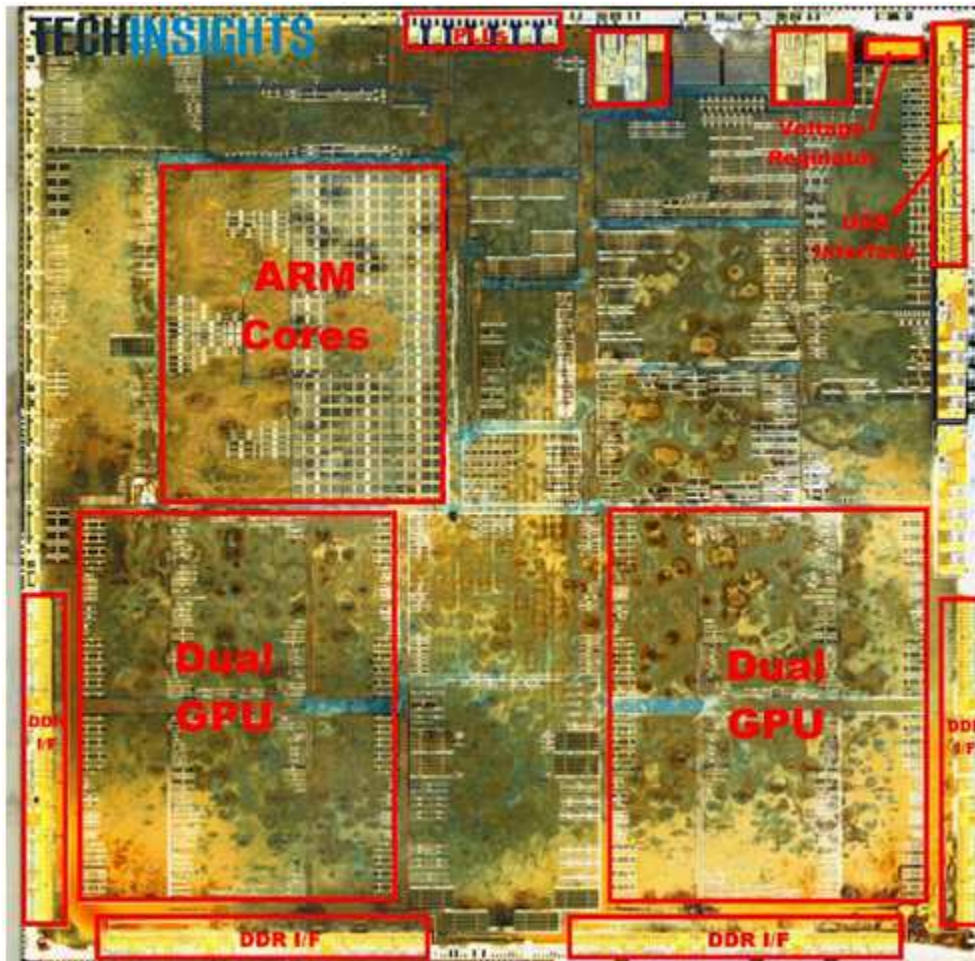
Buying the Dow at its all-time high vs ARMH (Source: Google Finance)

ARM actually started out as an Apple joint venture with VLSI Technology & Acorn Computers, both industry giants that went by the wayside. ARM specializes in low-power processors that have enabled Apple to make products that don't drain batteries and don't heat up. Apple pays ARMH a royalty for each iPhone sold, likely between 1.5-2% to license their chip architecture. And lots of other companies, from Xilinx to Altera do the same, which has put ARM inside 90%+ of the world's smartphones.

You can bet that Apple's love affair with ARMH will continue as its Mac product line keeps moving towards its iOS mobile products. There is speculation & some evidence that Apple has at least considered moving the chipset for its laptops from Intel to Arm. Capturing part of the notebook market would be a huge win for ARMH that would push its ~\$780 million revenue number up significantly and probably expand operating margins above the current ~30%. IHS iSuppli has a prediction of 22% of the global notebook market by 2015; while I think this is probably too high, even half that number would be an enormous catalyst for the stock. With almost half a billion in cash they definitely have capacity to attack not only notebooks but consumer electronics like the coming round of smart TVs.

As if that weren't enough, the ARM takeover chatter is nonstop. At various points over the last few years Texas Instruments, Intel and even Apple itself were all supposed to be close to a deal

to take over the British chip maker. That's well and good but the giant chipmakers haven't always been the most astute when it comes to the megadeal and ARM is getting to be Too Big To Takeover. Call it hubris or gumption or just believing the ride will never end but the premium management would likely demand would make for a ~\$26 billion takeover. That would rank as one of the largest takeovers—tech or otherwise—of all time. Even for one of the most likely acquirers, the \$134 billion Intel, a \$26 billion pill is tough to swallow.



The real estate ARM has in the new iPad (Source: UBM Tech Insights)

I do expect them to keep eating Intel's lunch though when it comes to the iPad. The company has no debt and is growing top and bottom line. Much like Corning, Arm is part of Apple's secret sauce, and wouldn't you know it, softee is trying to launch its own tablet platform knockoff. Best of all it even has a spiffy acronym, WARM---**Windows On ARM**. Balmer & Co have launched plenty of failed platforms before, but they (along with Apple) are the original students of Picasso's maxim "Good artists borrow, great artists stream". WARM may be anecdotal revenue to Microsoft that is more of a defensive enterprise play than anything else, but it will be a nice new revenue base for ARM over the next decade.

Company

GLW- Corning, Inc.

Summary

Corning, Inc., manufactures and markets specialty glass and ceramics products worldwide in five segments: Display Technologies, Telecommunications, Environmental Technologies, Special Materials and Life Sciences.

Balance Sheet

Cash and Cash Equivalents:	4.6 B
Short Term Investments:	1.1 B
Long term Investments:	<u>4.7 B</u>
Total Cash:	10.4 B

Total Debt:	<u>2.3 B</u>
Net Cash:	8.1 B

Outstanding Shares:	1.5 B
Net Cash / Share:	5.4

Share Price:	13.8
Enterprise Value / Share:	8.4

Total Market Cap:	21 B
Enterprise Value:	12.9 B

2012 Sales Growth:	1.5%
2012 Earnings Estimate:	1.35
Enterprise Value Multiple:	6 Times Forward Earnings
Dividend & Yield:	.3 (2.1%)

Corning holds the unique distinction of being identified by Apple as the supplier of the product everyone knows it supplies, Gorilla Glass. While GLW is left off the official supplier list, Apple touts “Corning employees in Kentucky and New York who create the majority of the glass for iPhone” as proof that it’s a domestic job creator.

When Steve Jobs had a conniption about his iphone getting scratched up in his pocket he flew to upstate new York and convinced corning to revive their stalled Gorilla Glass project. And GLW should be thankful everyday that the Job’s Reality Distortion Field was applied to them to so intensely. Sales of Gorilla Glass, the fastest growing segments of the company, hit \$700 million, about triple what they were for 2010. And with every other smartphone maker trying to copy Apple component-by-component, you can expect this number to balloon to north of \$1.5 billion

as the Samsungs place their own Gorilla Glass Orders. The next iteration, Gorilla Glass, should help margins expand as it's rolled out of the next couple quarters.

So until someone perfects a flexible, telescopic or holographic display, Apple will be sticking with Corning. And as their Mac product line converges with ios it's possible we could see Gorilla Glass incorporated into desktop & laptops.

With more than \$5 of cash per share you could buy all of Corning (ex takeover premium) for a little under \$12 billion. That's about 5.9x forward earnings, or very, very cheap. This isn't a fast money stock, it's basically tracked the broader indices this year, but as it adds cash to its coffers it will continue to be a good long-term bet.

Company

LVLT - Level 3 Communications, Inc.

Summary

Level 3 Communications, Inc. engages in the communications business in North America and Europe. It offers network and Internet services, including transport services, high speed Internet protocol services, dedicated Internet access, virtual private network services, and dark fiber services, as well as managed modem, an outsourced, turn-key infrastructure solution; and colocation services.

Balance Sheet *

Cash and Cash Equivalents:	928 M
Short Term Investments:	--0
Long term Investments:	<u>--0</u>
Total Cash:	928 M

Total Debt:	<u>8.3 B</u>
Net Cash:	-7.3 B

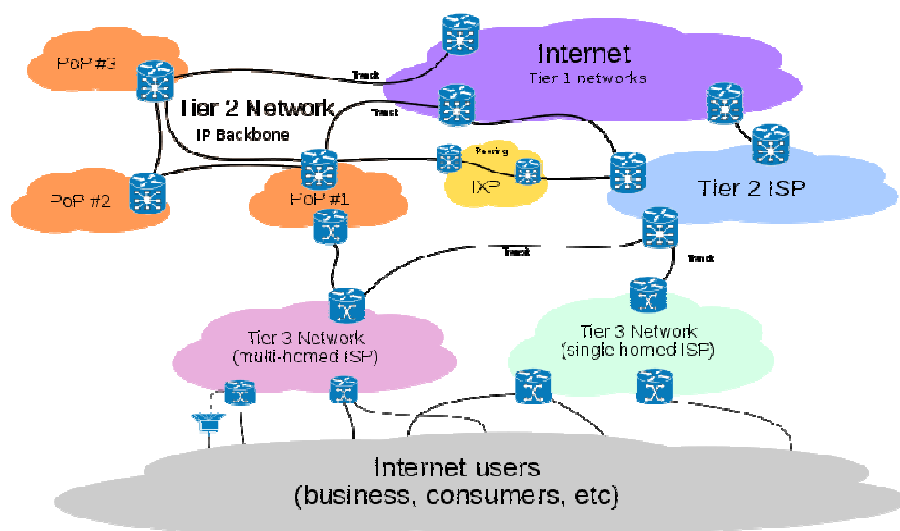
Outstanding Shares:	208 M
Net Cash / Share:	-35

Share Price:	26.5
Enterprise Value / Share:	61.5

Total Market Cap:	5.5 B
Enterprise Value:	12.8 B

2012 Sales Growth:	50.4%
2012 Earnings Estimate:	-1.39
Enterprise Value Multiple:	N/A
Dividend & Yield:	N/A

Last year Level3 merged with its main competitor Global Crossing, ending a huge value-destructing rivalry. That's been great for the stock; it's up more than 50% this year alone. And it's long-term prospects as backbone to the Apple ecosystem is very strong. As far a competitive moats & assets with enormous go, LVLT is king.



The graphic above illustrates what I mean. The purple cloud, ‘Tier 1 network’, that’s where Level 3 operates. It’s not much of a stretch to say that Level 3 is the Internet. As Apple builds its iCloud offerings, trying to subsume cable and other transmission networks, you can expect they’ll be paying Level3.

LVL3 has gone boom and almost bust so many times it’s hard to keep count. Founded by Warren Buffet’s friend (and landlord) Walter Scott, the company was a darling of the tech 90s, getting a huge multiple and becoming a mega cap. The thinking was that data was like oil and the pipelines that they flowed through could charge a toll. Billions of dollars of cable were laid and analysts projected data usage would progress geometrically year-over-year for perpetuity.

While not the instant multi-trillion dollar windfall, the logic has only shifted, not gone away all together. Level3 is the last man standing from the fiber wars and will benefit as capacity starts to be used up all the apps and media we’re downloading on our smartphones. And hundred-million fiber projects, like data centers in NYC & a direct connection between traders on the east coast and Midwest have been built out in the last few years. While there is tons of excess fiber most of it is not where it’s most needed---to relieve clogged wireless data networks. When I look at Level3 I see a company that is such a critical part of the App & Revolution infrastructure that it wouldn’t surprise me if an Apple or Google bid for the whole thing.

(Spread Networks spent \$300 million on this speculative fiber network from NYC to Chicago to shave milliseconds off trading time)

The really big overhang for LVL3 is the same one facing the U.S.—its debt. But even with that \$5.7 billion load I think Level 3 could---finally---start turning a profit in 2013. Even assuming a

bear case, taking revenue growth down to ~5% this year and ~7% the next, with redundancies eliminated from the Global Crossing merger and gross margins at ~60% would mean ~\$150 M of cash flow by the end of 2013. By that point I expect the stock to be much, much higher.

Company

MOLX - Molex, Inc.

Summary

Molex Incorporated designs, manufactures, and sells electronic components worldwide. It offers micro-miniature connectors, B-to-B connectors, SIM and SD card sockets, keypads, electromechanical subassemblies, internal and on-ground antennas, standard antennas, magnetic jacks, and subsystems for the telecommunications market; and power, optical, and signal connectors and cables for end-to-end data transfer, linking disk drives, controllers, servers, switches, and storage enclosures for the info-tech market.

Balance Sheet

Cash and Cash Equivalents:	607 M
Short Term Investments:	11 M
Long term Investments:	--0
Total Cash:	618 M

Total Debt:	<u>196 M</u>
Net Cash:	422 M

Outstanding Shares:	<u>176 M</u>
Net Cash / Share:	2.4

Share Price:	28.1
Enterprise Value / Share:	25.7

Total Market Cap:	4.9 B
Enterprise Value:	4.5 B

2012 Sales Growth:	-1.1%
2012 Earnings Estimate:	1.61
Enterprise Value Multiple:	16 Times Forward Earnings
Dividend & Yield:	.8(2.8%)

Molex is the world's Number 2 connector maker. That's just what it sounds like, their products plug other elements together. If you've ever taken apart your desktop PC to install a hard drive, those plastic two-socket female plugs are colloquially called molex connectors.

I'm highlighting the company because even though they are in a low-margin business, they are so necessary to chipmakers that they will benefit as long as Apple keeps growing.

Okay so it's not semiconductors but not all investments have to be flashy. Molex is integral enough that anyone buying it would cramp other semi manufacturers. And the industry itself is consolidating, Swedish conglomerate ABB just picked up Thomas & Betts. On top of this you get a nice, sustainable, 3.1% yield that represents about 48% of the company's overall earnings, so don't worry about Molex hoarding cash while lobbying for a repatriation loophole.

16x earnings is more than I'd like to pay for a low margin manufacturer, but in the time when return-of-capital is more important than return-on-capital, Molex is an Apple supplier that is almost completely unlikely to be innovated out of business and should generally track the growth in smartphones. Mr. Market seems to agree at the moment---YTD Molex has returned double what the Dow has. If they guide down or get hit with another situation like the Thailand flooding I'd feel confident stepping in and buying.

Company

NUAN - Nuance Communications, Inc.

Summary

Nuance Communications offers voice and language solutions for businesses and consumers worldwide. They offer transcription solutions and dictation services that automate the input and management of information through voice recognition technologies.

Balance Sheet

Cash and Cash Equivalents:	873 M
Short Term Investments:	10 M
Long term Investments:	<u>--0</u>
Total Cash:	883 M
Total Debt:	<u>1.2 B</u>
Net Cash:	-317 M
Outstanding Shares:	308 M
Net Cash / Share:	-1
Share Price:	26.3
Enterprise Value / Share:	27.3

Total Market Cap:	8 B
Enterprise Value:	8.3 B

2012 Sales Growth:	20.6%
2012 Earnings Estimate:	1.58
Enterprise Value Multiple:	17 Times Forward Earnings
Dividend & Yield:	N/A

Nuance is a proud member of the 3%---- it's not part of the 97% of suppliers that Apple discloses. No you won't find NUAN anywhere among the 156 companies that Apple lists in it's very-Apple-titled "Apple Suppliers 2011". But you'll definitely find its DNA in the iphone.

While not confirmed by Cupertino it's certain that apple is powering Siri, at least partly, with Nuance technology. Over the last decade Nuance rolled up so many voice recognition companies (and their patents) that Apple has no choice but to license their technology. In fact the research institute that originally spun out Nuance (**SRI** International) also spun out Siri----which Apple bought for ~\$400 million.

Over the years I've seen umpteen tech geeks claiming that some patent or technical sketch from apple heralded a monumental technology change. And usually this is just a good way to get some digital ink on the fan boy blogs. But with Nuance it has paid to pay attention to the geeks. When they highlighted Apple jobs postings for voice technology engineers in 2010 and concluded that voice recognition was coming to the iphone, they were absolutely right. So I trust

the same sources that have looked SDK (standard developer kit) code and see evidence of Nuance technology running on Apple's servers.

Apple won't even entertain questions about Nuance, For it's part, Nuance is slightly less tight lipped, stating that "Apple licenses Nuance's voice technology for use in some of its products.", which is probably about as much as Apple's legal department allows them to say.

And if (read: when) Apple launches a standalone tv, expect voice control, and Nuance, to be a big part of the equation. I actually like the possibility of this a lot, as Microsoft and Samsung are making noise (protesting really) that they already have voice controlled Tv options. Which we know won't be anything like the formula Steve Jobs said he 'cracked'.

Nuance has plenty of other business lines outside of Siri, its Dragon dictation product is one of the most popular apps on the iphone & it just bought out Transcend, a competitor in the medical transcription market, which should allow it to get even more of the healthcare enterprise market.

The most interesting prospect for Nuance is that they are a competitor to Google. When you talk in to your iphone and ask it to guide you to a restaurant, that's a search function. Right now Google's enormous profitability depends on 99% of searches being input by typing, not talking. Believe me when I say they see Nuance and voice recognition as an existential threat to their business model. Nuance is already generating revenue from partners like OpenTable & Fandango, getting a piece of date night sales. Enabling people to consume & spend the money ever more seamlessly is something you always want to be long.

You never want to chase stocks but really exercise caution with tech highfliers like Nuance (see: Netflix). The trick is to keep watching to make sure the story hasn't changed and pick up the name when everyone thinks it has and the momentum traders dump it wholesale. Nuance is up 36% over the last year but there were plenty of sharp down days you could have used to build a position on the cheap. I don't think a takeout is out of the question for this name, especially on a large decline, which means there is a kind of takeover-put for the stock.

Company

TXN - Texas Instruments Inc.

Summary

Texas Instruments Incorporated designs and sells semiconductors to electronics designers and manufacturers worldwide. The company's Analog segment offers high-performance analog products comprising standard analog semiconductors, such as amplifiers, data converters, and interface semiconductors; high-volume analog and logic products; and power management semiconductors and line-powered systems. Its Embedded Processing segment includes DSPs that perform mathematical computations to process and enhance digital data; and microcontrollers, which are designed to control a set of specific tasks for electronic equipment..

Balance Sheet

Cash and Cash Equivalents:	992 M
Short Term Investments:	1.9 B
Long term Investments:	<u>265 M</u>
Total Cash:	3.2 B

Total Debt:	<u>4.2 B</u>
Net Cash:	-1 B

Outstanding Shares:	1.1 B
Net Cash / Share:	-.9

Share Price:	32.9
Enterprise Value / Share:	33.8

Total Market Cap:	37 B
Enterprise Value:	38 B

2012 Sales Growth:	-1.9%
2012 Earnings Estimate:	1.76
Enterprise Value Multiple:	19 Times Forward Earnings
Dividend & Yield:	.68 (2%)

Texas instruments can sometimes look a stock stuck in the mud. Management is increasingly opaque about costs and growth potential. Wall street seems to have problems understanding exactly what it's place in the apple ecosystem is. With the Dow up about 7% in the last year TXN is down about 2%. But if you buy it cheap enough, and as part of a basket of other Apple suppliers, you should do pretty well over time.

TI makes the touch screen controllers for both the iphone and the 3rd generation ipad. They also have a small low-margin audio chip in the iphone. Despite many Asian suppliers trying to knock TI out of the iphone/ipad ecosystem Apple has been unwilling to go with anyone but them. Touchscreens are a de facto standard that won't go away till we move to hologram phones and Texas Instruments makes the best touchscreen controller. TI has been in the iphone since it launched but it pulled off a coup by replacing five other components with its elegantly packaged controller. And suppliers that can make Apple products simpler, or more Apple, are the ones that are going to see their relationships extended.

As I alluded to before, TXN doesn't do the best job of communicating to Wall Street. Right now with the overall markets booming it's not a problem. But management has missed on various metrics more than a couple times. Expenses for the previous quarter were \$918M vs an expected \$783M. In q4 of 2011 it slashed guidance, sending the shares down 6%. Then it beat in q1 of 2012, but lowered estimates again.

So jump over the disconnect between stocks as blips on a screen and real companies with underlying business. So imagine for a second that the above mess was said to you by a relative you had invested with. Let's make it your brother-in-law. You'd probably ask for your money back, right?

And that's why the stock is being held back even with the larger markets booming and the nasdaq at a 4 year high. Looking at 10 years chart the NASDAQ the tech index is up almost 70% while TI has barely notched a gain at all. TXN's products should be used for the time being by apple, and they are hard to duplicate. So if you're bullish on Apple, and can get TXN at a price, you can make money. It has more debt than I'd like, far more than most other tech names. It pays a yield close to treasuries which is considered among the safest in the industry--uninterrupted for 26 years, or since Steve Jobs 26th birthday.

Company

MFLX - Multi-Fineline Electronix, Inc.

Summary

Multi-Fineline Electronix, Inc. engineers, designs, and manufactures flexible printed circuit boards and related component assemblies for the electronics industry. The company offers integrated flexible printed circuits and component assembly solutions, such as design and application engineering, prototyping, high-volume fabrication, component assembly, and testing.

Balance Sheet

Cash and Cash Equivalents:	75 M
Short Term Investments:	--0
Long term Investments:	<u>--0</u>
Total Cash:	75 M

Total Debt:	<u>--0</u>
Net Cash:	75 M

Outstanding Shares:	<u>23 M</u>
Net Cash / Share:	3.2

Share Price:	27.2
Enterprise Value / Share:	24

Total Market Cap:	646 M
Enterprise Value:	571 M

2012 Sales Growth:	10.8%
2012 Earnings Estimate:	1.88
Enterprise Value Multiple:	13 Times Forward Earnings
Dividend & Yield:	N/A

Let me put you at ease if you haven't heard of this one before, not many people have. MFLEX makes the printed circuit boards (those green flat things the chips go on if you are going 'Office Space' on your computer and happen to open it up). It's not a particularly high-value item and MFLEX doesn't have the margins of some of our other picks but Apple has consistently used their boards for the iphone & ipad

Plus Mflex is becoming a kind of canary-in-the-coal-mine, it's being looked at as a pretty good gauge of what apple is doing. This past quarter many analysts based revised their Apple

numbers higher when Mlflex beat expectation. In fact MFLEX is now a more reliable indicator of iphone shipments than Verizon or AT&T handset numbers.

It's that kind of 1:1 correlation to the Apple ecosystem that I like. With more than \$3 net cash per share & an enterprise value of barely more than half-a-billion, I like the idea of buying MFLX over a contract manufacturer. With no net-debt and double-digit sales growth I wouldn't be shocked if someone buys the company to have that almost-certain Apple revenue.

Cody Willard writes [The Cody Word](#) for MarketWatch and posts the trades from his personal account at [TradingWithCody.com](#), a separate service not affiliated with MarketWatch. At time of publication, Cody was net long Apple, Fusion IO, Level 3, and Nuance.

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