

# Avago to Acquire LSI Corporation



## OBJECTIVE ANALYSIS SEMICONDUCTOR MARKET RESEARCH

**AVAGO**  
TECHNOLOGIES

LSI 

### **\$6.6 Billion Deal to Create Synergies and Diversification**

On Monday, 16 December 2013, Avago Technologies, a manufacturer of networking semiconductors announced plans to acquire LSI Corporation for \$6.6 billion in cash. LSI manufactures storage and networking chips. This represents a premium of roughly 40% over LSI's market capitalization prior to the announcement.

In a conference call the two companies' management expressed belief that the acquisition will be synergistic: Avago makes wired and wireless networking chips and LSI manufactures chips for wired networking and storage. Although both make wired networking chips, there is not significant overlap. Avago makes high-speed signaling and optical interface chips, and LSI's networking products consist mainly of ASICs and support software. There are probably numerous designs that use chips from both companies.

Avago CEO Hock Tan said that the companies' wired networking products fit together to provide a complete solution that does not already exist in the industry.

Because of this Avago's management expects combined post-acquisition revenues to be roughly the same as the sum of the two companies' current revenues, or about \$5 billion. Approximately half of this will come from wired and wireless networking products and over a third from storage. The balance of sales will result from semiconductors sold into industrial and embedded applications.

Acquisition financing will be made up of \$1 billion in cash from the two companies, \$4.6 billion in bank loans, and a \$1 billion investment by Silver Lake Partners who helped orchestrate the deal. Avago was previously privately held by Silver Lake, and after it was spun off in 2008, Silver Lake maintained a position on the board, although it sold off its ownership in the company by 2012.

The acquisition's timing was probably influenced by the current market's low bank interest rates.

#### **What's in it for Avago?**

Avago's wireless business, which accounted for nearly half of the company's last 12 months' revenues, is selling into a customer base that is consolidating, a fact

that management expects to result in an increasingly volatile marketplace. Since wireless will only contribute 25% of the combined company's revenues, Avago will be less exposed to this volatility. Management expects for the other product lines to have more consistent revenues.

### **Changes in Store for LSI?**

During a conference call Avago pointed out that LSI has higher gross margins than Avago, but that Avago has a higher operating margin. Since the companies are relatively similar in structure, LSI's lower operating margin will be an area of focus: Avago hopes to bring that number higher once LSI has been acquired. This should be a big part of the \$200 million in cost savings Avago plans to achieve by combining the companies.

### **A Non-Merger of Equals**

In most acquisitions a larger company buys out a smaller one. This deal is a little unusual in that respect, since both companies are roughly the same size: Avago's FY2012 revenues were \$2.4 billion and LSI's were \$2.5 billion.

According to Avago the biggest delays will come from regulatory issues in those countries whose approval is required. The companies have given themselves a loose target date by planning to close in the first half of 2014.

### **Long-Term Outlook**

Objective Analysis sees two ways this company could evolve over the long term. The first would be to maintain the same basic product lines, networking and storage, reaping the stability of diversification. The other would be to split along product and customer lines, with Avago eventually spinning off the storage business, a mixture of HDD chips, SSD controllers (the SandForce line) and RAID controllers.

Either approach makes sense. In either case we would not expect to see much impact to the two companies' customers. It's not at all clear which path Avago's management will choose. We will have to wait and see.

---

Jim Handy

### **OBJECTIVE ANALYSIS**

Semiconductor Market Research

[www.Objective-Analysis.com](http://www.Objective-Analysis.com)

[Forbes.com/sites/jimhandy](http://Forbes.com/sites/jimhandy)

[TheSSDguy.com](http://TheSSDguy.com)

[TheMemoryGuy.com](http://TheMemoryGuy.com)

PO Box 440

Los Gatos, CA 95031-0440

USA

+1 (408) 356-2549