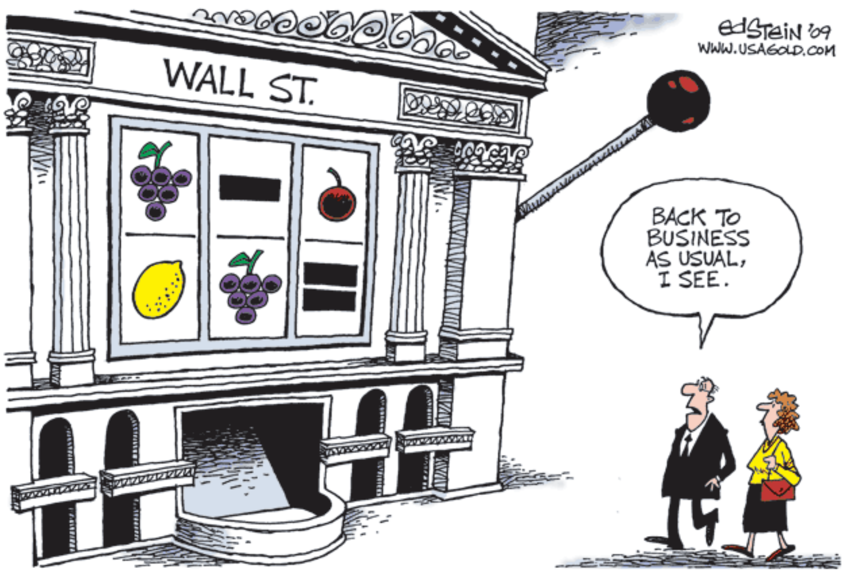
June 9, 2017

NVIDIA:

The Moment that Separates the Gamblers from the Investors

NVDA to Trade back to $130

Take your profits and move on to Google (Alphabet) (NASDAQ:GOOGL). Exposure to the identical array of "sexy businesses" with less risk on the downside.



Six months ago when NVDA had a trading frenzy and was at $119 Citron predicted a quick fall back to $90…the stock soon his $95 and Citron called the cover.

****Note:** We have been long time NVDA lovers. Two years this week when traders/analsyts/ and TV commentators were frothing over Ambarella, it was Citron who said that NVDA was the real buy and not AMBA…..we know how that played out. http://www.citronresearch.com/wp-content/uploads/2015/07/Ambarella-Ridiculousness-explained-final-c.pdf

In the recent frenzy in NVIDIA shares, it has added more to its market cap than the total valuation of its competitor AMD. Now it is fueled by an irresponsibly bullish number from Citi.

Just seven months ago, their analyst team had a $90 price target. But yesterday, their target is doubled $180 ... despite the weakness in NVDA's core gaming business.

** **Note:** The Citi (multi-year) bear case of $100 --where the stock was trading just **one month ago** -- shows a lack of respect for the stock market in general and the respected and stiff competition it is going to face in is emerging business.

While we are fans of NVDA emerging business in auto, gaming, and AI … have the prospects of these technology doubled in value in 6 months or is this an example of analysts chasing stock price?

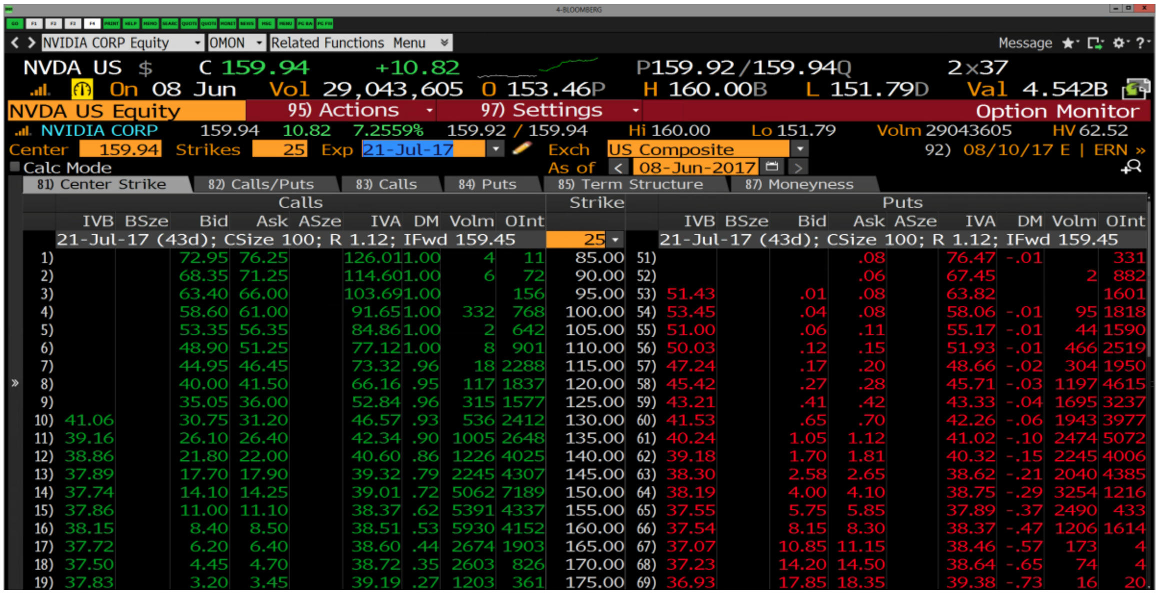
We view the company as two franchises:

- a Core Franchise, comprised of Gaming, Professional visualization, and OEM & IP, which will generate revenue of $6.1bn in FY18, and

- an Emerging Franchise, comprised of AI, Datacenter and Autonomous Driving / Auto Platform, which will generate revenue of $1.9bn in FY18, per our estimation.

The Casino is Open

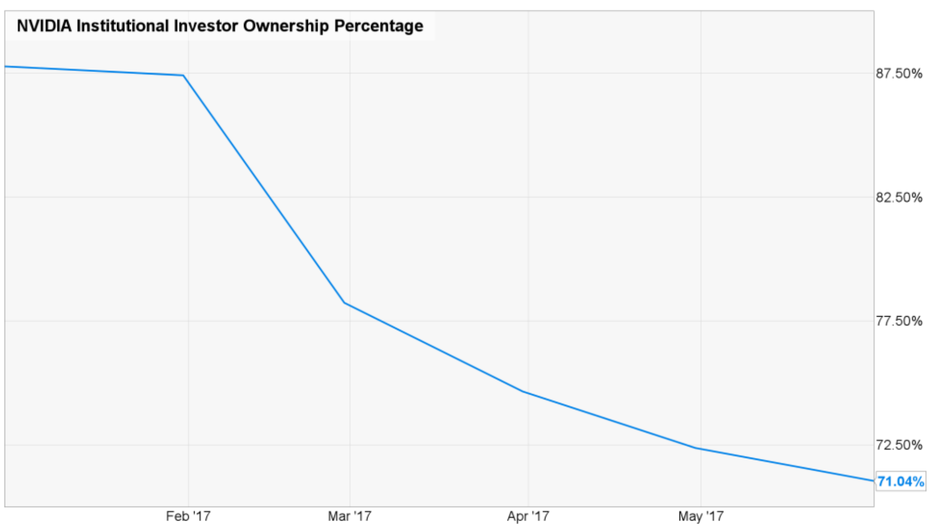
Citron notes a phenomenon that should scare anyone who thinks about buying NVDA at these prices. As institutional ownership is going lower, the amount of action on call options is exploding.



	Calls IVB	Calls BSze	Calls Bid	Calls Ask	Calls ASze	Calls IVA	Calls DM	Calls Volm	Calls OInt	Strike		Puts IVB	Puts BSze	Puts Bid	Puts Ask	Puts ASze	Puts IVA	Puts DM	Puts Volm	Puts OInt
1)			72.95	76.25		126.01	1.00	4	11	85.00	51)				.08		76.47	-.01		331
2)			68.35	71.25		114.60	1.00	6	72	90.00	52)				.06		67.45		2	882
3)			63.40	66.00		103.69	1.00		156	95.00	53)	51.43		.01	.08		63.82			1601
4)			58.60	61.00		91.65	1.00	332	768	100.00	54)	53.45		.04	.08		58.06	-.01	95	1818
5)			53.35	56.35		84.86	1.00	2	642	105.00	55)	51.00		.06	.11		55.17	-.01	44	1590
6)			48.90	51.25		77.12	1.00	8	901	110.00	56)	50.03		.12	.15		51.93	-.01	466	2519
7)			44.95	46.45		73.32	.96	18	2288	115.00	57)	47.24		.17	.20		48.66	-.02	304	1950
8)			40.00	41.50		66.16	.95	117	1837	120.00	58)	45.42		.27	.28		45.71	-.03	1197	4615
9)			35.05	36.00		52.84	.96	315	1577	125.00	59)	43.21		.41	.42		43.33	-.04	1695	3237
10)	41.06		30.75	31.20		46.57	.93	536	2412	130.00	60)	41.53		.65	.70		42.26	-.06	1943	3977
11)	39.16		26.10	26.40		42.34	.90	1005	2648	135.00	61)	40.24		1.05	1.12		41.02	-.10	2474	5072
12)	38.86		21.80	22.00		40.60	.86	1226	4025	140.00	62)	39.18		1.70	1.81		40.32	-.15	2245	4006
13)	37.89		17.70	17.90		39.32	.79	2245	4307	145.00	63)	38.30		2.58	2.65		38.62	-.21	2040	4385
14)	37.74		14.10	14.25		39.01	.72	5062	7189	150.00	64)	38.19		4.00	4.10		38.75	-.29	3254	1216
15)	37.86		11.00	11.10		38.37	.62	5391	4337	155.00	65)	37.55		5.75	5.85		37.89	-.37	2490	433
16)	38.15		8.40	8.50		38.51	.53	5930	4152	160.00	66)	37.54		8.15	8.30		38.37	-.47	1206	1614
17)	37.72		6.20	6.40		38.60	.44	2674	1903	165.00	67)	37.07		10.85	11.15		38.46	-.57	173	4
18)	37.50		4.45	4.70		38.72	.35	2603	826	170.00	68)	37.23		14.20	14.50		38.64	-.65	74	4
19)	37.83		3.20	3.45		39.19	.27	1203	361	175.00	69)	36.93		17.85	18.35		39.38	-.73	16	20

Translation: The market is pricing lottery tickets -- $160 calls -- not an investment in future prospects on NVDA in common stock.

Meanwhile the institutions are exiting stage left:



* We would venture to say Softbank owns their stock around $10

Why Move your Money from NVDA to Google?

NVDA buyers at these prices are obviously in it for the Emerging Franchise: AI, Datacenter, and Autonomous Driving. Google has major exposure to all three markets and can be considered a legitimate category leader in all 3, with the GPU vs TPU battle still to be decided

https://cloud.google.com/blog/big-data/2017/05/an-in-depth-look-at-googles-first-tensor-processing-unit-tpu

But, while the frenzy sorts itself out, Google has a far higher value core business. What happens if these businesses take longer to mature? As we have seen with technology before, adoption rates and pricing are far from certainties. In the meantime, would you rather “own the internet”, or "make chips for video game consoles"?

NVDA shareholders need to breathe, take some profits and really look at the competitive landscape and valuations they are paying. What might seem like "a 20 point move" might seem like a number on a scoreboard -- it is actually the valuation of AMD. Unless of course this is a casino...

2017 vs 2014	**Google**	**NVIDIA**
Stock Price Gain	74.02%	**761.27%**
Market Cap Growth (3 Years)	77%	**640%**
Enterprise Value Growth (3 Years)	81%	**1008%**
Revenue Growth	67%	63%
Free Cash Flow	129%	158%

Ahead of its Skis: A Portrait

Thoughts to consider before investing in NVDA anything higher than $130

1. The current multiple represents a 10-year peak both on an absolute and relative basis to the group.

2. **Competition coming to the Data Center setting** – Intel (Knight's Mill), AMD (Naples), Google (TensorFlow), XLNX (FPGA), and a multitude of well-funded startups.

3**. Growth decelerating in NVIDIA's largest segment**, Gaming, while +49% y/y, is slowing rapidly (-24% q/q), despite tons of channel commentary about shortening lead times. Gaming is still 55% of revenues despite slowing rapidly.

4. **Accounts receivable is exploding** – DSOs, historically ~35 days, blew out to 46 days. (could be a sign of a company trying to keep up with an exploding stock price)

5. **Inventories bloated** – grew 3% q/q despite sales -11% q/q. Were already significant. (Another sign of a business chasing a stock price)

6. **Valuation** – peak multiple on potentially peak earnings. Even assuming continued strong growth of 30% y/y, 6.2x EV/Sales and >30x EPS is exceedingly rich for a cyclical business

7. **Wall Street Analysts** – just raising estimates as the price goes higher is nothing more than Wall St. FOMO

Cautious investing to All