

Global Company Highlight: Taiwan Semiconductor Manufacturing Co.



Kevin Walkush, Portfolio Manager

MARCH 2021

Company Highlight Series

jenseninvestment.com



Ticker:
(TSMC)

Year Founded 1987

Headquarters Hsinchu, Taiwan

Entered Strategy 2020

Taiwan Semiconductor Manufacturing Company (TSMC) is the world's leading semiconductor chip foundry. As a foundry, TSMC manufactures chips on behalf of customers with the most cutting-edge manufacturing capabilities as defined by node size. The smaller the node or circuit size, the more capable the chip, i.e., more processing power and energy efficiency. TSMC can manufacture at the smallest node size, providing its customers, such as Apple, Nvidia, and AMD, a competitive edge in their products. Both sides benefit from this arrangement that enables each to build differentiated leadership in their respective markets. In the case of TSMC, they can leverage their dominant position to “out-invest” competitors and thus realize pricing power and consolidate their leadership position. It also helps to eliminate risk for both parties as TSMC does not take on product risk, and its partners do not have to assume capital expenditure risk. Consequently, TSMC has earned a top position in the Jensen Global Quality Growth Strategy.

Know What You Own

TSMC's success is built on a foundation of strong and durable competitive advantages. First and foremost, the company is innovative. The company could not execute without technology commercialization and manufacturing expertise that has been honed since the company's founding in 1987. Compounding this competitive advantage, the company also enjoys economies of scale due to the fixed cost nature of the business; switching costs due to the lack of alternatives for customers; and high entry/competitor barriers fueled by technical expertise, experience, and substantial capital expenditures required to build capacity to meet demand.

Fueling the company's competitive advantages are strong underlying growth drivers. Long-term secular technology trends, such as 5G, the cloud, the Internet of Things (IoT), and increasing semiconductor content in products, especially automobiles and industrial products, increase demand for TSMC's capabilities. The company realizes further growth as it consolidates its share and distances itself from competitors that cannot compete as effectively.

TSMC's competitive advantages and growth drivers combine to enable it to generate strong returns evidenced by double-digit revenue and earnings per share growth,¹ which we expect to accelerate over the next few years due to the robust growth drivers described above. Key to this growth is TSMC's reinvestment in the business. TSMC spends over 30% of its revenue on capital expenditures to expand capacity and build capabilities.² Despite this high level of spending, the company generates significant cash flow to cover its need and still has excess cash to return to shareholders via its investor-friendly dividend policy.

¹ TSMC and Jensen Investment Management.

² Ibid.



A cornerstone of a Jensen Strategy company is an effective management team, and we give TSMC’s executive team and board of directors top marks as effective stewards of the business and shareholder capital. In short, the company would not be in its position today without such strong leadership.

Outlook

We continue to monitor risks to the business. Overbuilding and excess capacity have been a hallmark of the traditional semiconductor business. We consider this risk mitigated for TSMC for two reasons. First, as a foundry, TSMC can fill capacity with another customer’s orders if one falters. Second, we believe that future demand for chips will be robust and sustainable for many years and that TSMC can efficiently maintain its high capacity utilization. Additionally, geopolitical tensions between China, the United States, and Taiwan could escalate and adversely impact the business. We find this to be a relatively low risk, but if tensions do escalate, the company is building a global footprint that can provide flexibility to shift manufacturing to different geographies if necessary.

We are pleased to have TSMC in the Jensen Global Quality Growth Strategy and look forward to it continuing to contribute to the Strategy’s success.

The company discussion in this article is solely intended to illustrate the application of our investment approach and is not to be considered a recommendation by Jensen. The specific security identified is taken from a representative account of the Jensen Global Quality Growth Strategy and does not represent all of the securities purchased and sold for the Strategy. Our views expressed herein are subject to change and should not be construed as a recommendation or offer to buy or sell any security and are not designed or intended as a basis or determination for making any investment decision for any security. Our discussions should not be construed as an indication that an investment in a security has been or will be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance of any security discussed herein.

The information contained herein represents management’s current expectation of how the Jensen Global Quality Growth Strategy will continue to be operated in the near term; however, management’s plans and policies in this respect may change in the future. In particular, (i) policies and approaches to portfolio monitoring, risk management, and asset allocation may change in the future without notice and (ii) economic, market and other conditions could cause the Strategy and accounts invested in the Strategy to deviate from stated investment objectives, guidelines, and conclusions stated herein.

Certain information contained in this material represents or is based upon forward-looking statements, which can be identified by the use of terminology such as “may”, “will”, “should”, “expect”, “anticipate”, “target”, “project”, “estimate”, “intend”, “continue”, or “believe” or the negatives thereof or other variations thereon or comparable terminology. Due to various risks and uncertainties, actual events or results or the actual performance of a client account may differ materially from those reflected or contemplated in such forward-looking statements.

This information is current as of the date of this material and is subject to change at any time, based on market and other conditions. Jensen Investment Management, Inc. is an investment adviser registered under the Investment Advisers Act of 1940. Registration with the SEC does not imply any level of skill or training. Although taken from reliable sources, Jensen cannot guarantee the accuracy of the information received from third parties.

© 2020 Jensen Investment Management. The Jensen Quality Universe is a trademark of Jensen Investment Management. All rights reserved.

JENSEN
INVESTMENT MANAGEMENT

5500 Meadows Road, Suite 200
Lake Oswego, OR 97035
800.221.4384

jenseninvestment.com