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Technology Hardware
Taiwan

TSMC

#Flashnote

Buy

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Upward Revision Continues

- The earnings call turned out to be a mixed event. The market should welcome TSMC's upward revision in 2026E revenue (40%+ yoy now) and capex ($60-64b), but 2Q26A/3Q26E GM fell below our and some bulls' aggressive estimates, though still beating the guidance in 2Q26E. Without updated numerated guidance, TSMC's updated 3yr capex (2026-28E) and AI revenue CAGR (high-50%s) are both higher than what the firm has expected. If TSMC's view is proven current, we believe TSMC can sustain well above 30%+ revenue CAGR, which could accelerate in 2028E driven by more new capacity expansion in 2027E. TSMC remains the cheapest leading logic-chip compute name in our coverage, trading at 17x/12x our 2027/28E P/E. We reiterate our BUY rating and TP of TWD3,500/$700.

- In terms of capex, TSMC raised its 2026E capex to $60-64b vs $56b guided last qtr. We believe the key upside driver is related to ASML's FY26E revenue guidance raise yesterday (from €36-40b to €43-45b), which we believe partially driven from installation-based revenue. We believe TSMC is undergoing the upgrade process of its installed EUV scanners to gain higher throughput, which takes place in its existing fabs and is not constrained by the new cleanroom. Management also indicated tool inflation, though we believe a price hike is still more related to throughput improvement and to a lesser extent a like-to-like price increase. For longer-term, TSMC indicated "more significantly higher than the past 3-yr capex vs what they said 3mths ago". This echoes our 2026-28E capex raise to $230-240b from $220-230b.

- TSMC added $100b capex plan in the US and brings its US capex plan to $265b with 4x more additional fabs planned. This is likely to be another 2x front-end wafer fabs and 2x back-end fabs, in our view. At the same time, TSMC reiterated 13x new wafer fabs in Taiwan from now and 3x new N3 fabs is under construction globally. As for back-end, R&D line for CoPoS is ready, but it takes another year for technology to mature before entering HVM. We are expecting CoPoS capacity to only increase more rapidly in 2028E, though we do not rule-out a pull-in in 2H27E. Despite TSMC welcoming advance back-end capacity and technology such as EMIB-T from other suppliers, which can help to open up more front-end wafer business for TSMC because of its own constraints (in the back-end), we see TSMC aggressively trying to gain this back in the next few years.

- For 3Q26, sales guidance of $44.6-45.2b beat our/consensus $43-44b, but GM of 65-67% is short of our bullish expectation of 68%+. N2 depreciation starts to hit margins by 3-4ppts. OPM guidance is 56-58%. Net-net, GP and operating profit are in line with our expectation and street consensus. For FY26, 40%+ revenue guidance suggests $50b+ revenue in 4Q26E, another mid-to high-single digit above our and consensus estimates. As for 2Q26, sales of $40.2b, GM of 67.7% and OPM of 60.3% all topped its guidance though margins are slightly below our estimates. EPS was TWD27.5, +23% QoQ/+77% YoY and beat our/street TWD26.5/24.3. Overseas fab, mainly in the US, started to hit GM by 2-3ppts in 2Q and will expand to 3-4ppts overtime. For longer-term GM, we estimate the company can keep at high-60%s GM, especially after its annual price hike.

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