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US Semiconductor Equipment

What are Investors Asking? Downside Scenarios

CITI'S TAKE

Following the sharp correction in semiconductor and hardware technology stocks this week, including ~10% pullback in the semi-cap group, investors have increasingly focused on potential downside scenarios. While we had cautioned ahead of SEMICON West that select component shortages could constrain equipment industry shipments and limit upside to 2027/28 WFE expectations (see here), we believe these constraints are broadening to include gas delivery, DRAM, PC boards, and magnets components. Although the current cycle is being fueled by strong AI demand, we see parallels to the 2020-22 Covid period, when supply shocks and shortages of ICs and subsystems constrained WFE growth despite robust underlying demand. Based on our sensitivity analysis across 2028 WFE scenarios and applying 2020-22 trough P/E multiples, we estimate the Big Three equipment stocks (AMAT, KLAC, LRCX) have ~10% additional downside potential in our WFE-scenario base case and ~30% downside potential in our bear case (see Figure 1).

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Figure 1. Big Three Downside Scenario Analysis

	WFE Share % (2025)	2028 WFE Scenarios $260	2028 WFE Scenarios $285	2028 WFE Scenarios $300	2026 $155
AMAT	17.0%				
Semiconductor System Revs ($M)		$46,800	$51,300	$54,000	$29,637
Applied Global Services Revs ($M)		$9,643	$9,643	$9,643	$7,291
Other Revs ($M)		$1,736	$1,736	$1,736	$1,490
Total Revs ($M)		$58,179	$62,679	$65,379	$38,418
EPS $		$23.54	$25.74	$27.08	$14.55
Trough P/E		**Bear**	**Base**	**Bull**	**Downside %**
P/E	15x	$353	$386	$406	8%
P/E	13x	$306	$335	$352	**-11%**
P/E	11x	$259	$283	$298	-31%
KLAC	8.1%				
Semiconductor Process Control System Revs ($M)		$18,460	$20,235	$21,300	$10,906
Services Revs ($M)		$3,991	$3,991	$3,991	$3,071
PCB & Component Revs ($M)		$2,083	$2,083	$2,083	$1,575
Total Revs ($M)		$24,534	$26,309	$27,374	$15,551
EPS $		$7.50	$8.13	$8.51	$4.51
Trough P/E		**Bear**	**Base**	**Bull**	**Downside %**
P/E	18x	$135	$146	$153	4%
P/E	16x	$120	$130	$136	**-12%**
P/E	14x	$105	$114	$119	-29%
LRCX	13.2%				
System Revs ($M)		$35,620	$39,045	$41,100	$19,819
Customer Support Business Group Revs ($M)		$12,019	$12,019	$12,019	$9,581
Total Revs ($M)		$47,639	$51,064	$53,119	$29,400
EPS $		$13.66	$14.83	$15.56	$7.82
Trough P/E		**Bear**	**Base**	**Bull**	**Downside %**
P/E	16x	$218	$237	$249	8%
P/E	14x	$191	$208	$218	**-10%**
P/E	12x	$164	$178	$187	-29%

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Source: Citi Research, FactSet

See Appendix A-1 for Analyst Certification, Important Disclosures and Research Analyst Affiliations

Figure 2. Big Three P/E Valuation Multiples



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Source: Citi Research, FactSet

Applied Materials Inc

(AMAT.O; US$375.58; 1; 22 Oct 26; 16:00)

Valuation

We value AMAT at $710 using a 28x P/E multiple on 2028E EPS. We view a 28x multiple, above AMAT's 3-year average multiple of 21x, as appropriate given multi-year WFE upcycle, secular tailwinds, and incremental AI data center investment.

Risks

Downside risks to the achievement of our target price include the following: 1) As fab utilization and capital equipment orders are closely linked to the stock price, any material differences to our supply/demand model (e.g. demand drops suddenly, or supply increases more rapidly than we predict) may cause our valuation methodology to be inaccurate. 2) As the market share leader in multiple sub-segments of semiconductor equipment, AMAT is uniquely positioned to capitalize on inflections as well as face tough competition from large peers in industry cycles.

KLA Corp

(KLAC.O; US$147.83; 1; 22 Oct 26; 16:00)

Valuation

We value KLAC at $290 using a 38x P/E multiple on 2028E earnings power. We view a 38x multiple or above 3-year average of 25x on multiple re-rating in the group due to growing AI WFE exposure.

Risks

The key upside/downside risks that could impede the stock from achieving our target price are: 1) lower/higher competition from competitors like AMAT/ASML; 2) foundry inventory correction risk on 10nm/7nm; and 3) fast/slow adoption of new Gen 4/5 and EUV products.

Lam Research Corp

(LRCX.O; US$230.15; 1; 22 Oct 26; 16:00)

Valuation

We value LRCX at $435 using ~33x P/E multiple on CY2028 earnings. We view a 33x multiple vs 3-yr average of 25x as appropriate given extended WFE cycle, secular AI tailwinds, higher services sales contribution, share gains, and rising equipment capital intensity.

Risks

The key downside risks to our investment thesis and target price on LRCX include: 1) increasing competition in deposition and etch; 2) weaker-than-expected overall semi market demand, especially memory; and 3) slower-than-expected demand in China due to US-China trade and IP tensions.

