

# FINAL TRANSCRIPT

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**ARM.L - Q1 2011 ARM Holdings PLC Earnings Conference Call**

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## PRESENTATION

**Operator**

Thank you for standing by, and welcome to the analyst conference call. (Operator Instructions). I must advise you that this conference is being recorded today, Wednesday April 27, 2011. And I would now like to hand the conference over to your first speaker today, Mr. Ian Thornton, Head of Investor Relations at ARM Holdings. Please go ahead, sir.



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**Ian Thornton** - ARM Holdings plc - Head of IR

Thank you very much indeed. Well, good morning, everybody. This is Ian Thornton, Vice President of Investor Relations at ARM.

On today's Q1 results conference call we have with me Warren East, the Chief Executive Officer, and Tim Score, Chief Financial Officer. On today's call Warren and Tim will take us through the highlights and comments from the quarter's results and then we'll open it up to a Q&A session. As a reminder, the presentation and press release can be found on the ARM investor relations website at [www.arm.com/ir](http://www.arm.com/ir).

Before I hand it over to them, I just have to read out a few words with respect to the conference call and what we're about to discuss. The contents of this conference call are being directed only to those of you who have professional experience in matters related to investments and information communicated on this call is being made available only to the investment specialists. Any persons present on this call who does not have professional experience in matters relating to investments should not act or rely on the contents of this call.

The following conference call will contain forward-looking statements which are other than statements of historical facts. The Company's actual results in future periods may differ materially from these statements as they are based on current expectations and are subject to a number of risks and uncertainties.

And on this note I'll hand over to Warren.

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**Warren East** - ARM Holdings plc - CEO

Thank you, Ian. Good morning, everyone. And thank you for joining us this morning. I'll go through the business highlights and then hand over to Tim to provide some more detail. And, as usual, we expect that we'll cover most of the contents during the question and answers.

So 2010 was an excellent year for ARM. And this morning we're pleased to announce that that momentum has continued through into the first quarter of 2011. And, as we look forward, we can see further healthy indicators for our growing strength in the medium and longer term. We came into the year with a record backlog. We had several new products scheduled for launch during the year and a strong competitive position as we're making further gains in these long-term structural growth markets.

And what's happened is that we continue to outperform the semiconductor industry, with strong growth both in licensing and royalties. We're benefiting from electronics companies developing products enabling a more pervasive consumer-oriented Internet. And that's the main driver of licensing, with 39 processor licenses sold during the quarter. Shipments of ARM-based chips used in these sorts of products grew 32% year on year. And that's about 3 times the rate of overall semiconductor industry growth, which drove those ARM royalties.

The revenue growth is enabling us to continue to invest further in R&D whilst at the same time growing earnings by 34% and delivering near-record levels of cash generation. We are looking forward therefore to the rest of the year. We anticipate normal seasonality for royalty revenues that we tend to see during the second quarter. And Tim will comment on that in a few moments.

There is some economic uncertainty as we're all looking for clarity on the medium-term impact of the Japanese earthquake and its aftermath. But nevertheless, we expect Group dollar revenues for the full year to be at least in line with market expectations.

Now I'll just discuss drivers for revenue and the different parts of the business in more detail and we'll start with the Processor division. We signed 39 licenses in the quarter; that's actually our highest number ever in terms of number of licenses. Most of them were as a result of current trends for increased Internet connectivity and also for smarter microcontrollers. There were

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eight licenses sold for Cortex-A family processors and seven Mali graphics processor licenses. 17 licenses in total were for Cortex-M family processors, and that's very good news, further increasing our penetration in microcontrollers and smartcards.

We're particularly pleased that several major companies who are developing chips for digital TVs and set-top boxes have decided to start using ARM processors in the future. This is a market we've been focusing on for a long time so it's excellent to see years of technology development, business management, marketing and design-in activity actually coming through and delivering some strategic wins.

Two major companies signed subscription licenses, Broadcom and LG Electronics. These subscription licenses are long-term commitments where a customer pays a fixed annual fee and then has access to a range of our processor portfolio. And companies who've signed that type of agreement are able to readily deploy ARM technology more quickly across multiple divisions. And so after a few years these sorts of companies often appear much higher up the table of royalty payers. So that's very encouraging news.

So switching to royalty, and I'll note royalty is reported one quarter in arrears so the Q1 number that we're just reporting is as a result of ARM-based devices sold during Q4 2010. But Processor royalty revenue was up 32% overall. The total volume was a record, at 1.85b units. And that was driven by continued growth and increasing sophistication in smartphones and continued growth in microcontrollers. And there's a more complete breakdown of volume shipments provided in our earnings release and in the presentation which has gone up on the IR section of our website.

If we look at the individual segments then, there's continued gain in market share in non-mobile applications, which is very encouraging. We've seen a 55% increase in microcontroller shipments against a backdrop of an industry where microcontroller shipments are growing less than 20% overall. In DTVs and set-top boxes, we've seen a 15% rise in the number of ARM-based chips. And that's into an end market which has been broadly flat overall. So good news there in non-mobile.

In mobile, we are clearly benefiting from an increase in Cortex-A family chips used in smartphones and tablets and those sorts of products. Shipments of Cortex-A family are now up to 4% of ARM's total unit shipments; that was 3% last quarter and 4% now. And, as discussed back in February with our full-year 2010 results, we're often able to achieve higher royalty rates for Cortex-A-based chips as these A-based processes deliver more value to our semiconductor partners. And these chips also tend to be the more expensive devices and so we benefit from a higher royalty rate on a more expensive device.

And these factors contributed to the average royalty per chip increasing sequentially from [0.046] to [0.048] in spite of the strong growth in microcontrollers. And at the microcontroller end, the Cortex-M-based products are now accounting for 13% of the total volume. So Cortex overall is 17% of total volume.

So now I'll switch to our Physical IP division. In Physical IP, revenue was up 19% overall, \$23m. And that was helped by licensing growing strongly, 43% year on year. And much of that growth has been from the strategic agreements that we've signed over recent years with foundry companies to develop advanced physical IP at 28 nanometers and below. And as our engineering teams are developing and delivering that IP, so we're recognizing the revenue and that's coming through and driving that licensing growth.

We've continued to see demand for the processor optimization packages that we talked quite a bit about back in February. These enable our Cortex-A9 customers to readily achieve high performance and low power processor implementation using our processor-optimization packages. And for every chip that's implemented using one of those, let's refer to them as POPs, ARM receives royalty for both the processor that's in the chip and for the physical IP that's there.

So during the quarter we signed three more licenses for POPs. And, in addition, we also signed agreements to create new processor optimization packs for Cortex-A family processors at 28 nanometers and at 20 nanometers. So that's looking good for the future.



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Underlying Physical IP royalties were actually down 1% year on year. But that was in line with the foundry industry. And we're beginning to see benefits as high-volume production moves to the more advanced nodes of 45 nanometers and below. And so we look forward to that effect going forward.

If I just touch on a few other operational and marketing points, we've continued with our recruitment. We grew fairly heavily in number last year. And we've continued in the first quarter of this year. We've added 33 people in total. This is growing our engineering teams, working on advanced processes and graphics products. And that brings the total ARM headcount to 1,922. And we intend to continue to invest in the team during 2011.

The big marketing event during the first quarter was Mobile World Congress. And that was probably our best Mobile World Congress yet. We had many OEMs showing off new high-end smartphones and tablets, mostly based on dual core Cortex-A9 chips. And in addition several semiconductor partners showed off their next chips for future generations of mobile computers. And these included NVIDIA with a quad core Cortex-A9, STMicroelectronics and Texas Instruments both announcing Cortex-A15-based chips.

So, with that, I'll hand over to Tim to provide some further detail on the numbers.

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**Tim Score** - *ARM Holdings plc - CFO*

Thanks, Warren. Good morning. Yes, as Warren's given a fairly clear overview of the results, I will just provide a little color on some of the numbers and some of the outlook.

As you've read in the release, Q1 dollar revenues \$185.5m, above consensus, which was around \$174m, driven primarily by a very strong performance in license revenue, which is up 50% in the Processor division year on year and up over 40% in the Physical IP division.

At just over \$51m, PD license revenues were ahead of the normal range of \$40m to \$45m per quarter that I referred to at the full-year 2010 analyst presentation at the beginning of February. But prospects for licensing continue to look promising, with a high backlog and a strong opportunity pipeline. But we do not necessarily expect the number of licenses that we've seen in the last two quarters, i.e. 39 in this quarter and 35 last, to be the norm. And nor would we expect licensing revenues to be in excess of \$50m every quarter.

But in addition to the high number of licenses yielding short-term revenue in Q1, several partners have entered into longer-term commitments to use ARM technology where much of the revenue associated with these agreements will be recognized in future quarters. And, as a result, the Group backlog at the end of Q1 is up about 15% sequentially and is more than double the level that it was at this time last year.

The usual analysis of backlog in terms of maturity and composition is included in the slide set on the website that Warren referred to. And that shows that 24% of total backlog is expected to be recognizable as revenue over the next two quarters and approximately 50% of PD license revenue in Q1 was generated from the backlog.

Our Processor royalties also grew strongly in the quarter, up 32% year on year and up 7% sequentially to just under \$88m. Typically seasonality results in about a 5% to 10% sequential decline in ARM's royalty revenues for the second quarter based on Q1 shipments. This has been the pattern over the last four years. 2009 the sequential decline was more than that, about 18%, but that of course was a time when the industry was going into downturn. So I think 5% to 10% sequential decline in line with normal seasonality is the way to look at it.



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And based on the industry data that we've seen for the first quarter, which of course is the relevant period for our Q2 royalties, we would expect to see normal seasonality again this year. And when you look at your -- the models and compare Q2 '11 forecast royalties to Q2 2010, it's probably worth remembering that last year we had a \$9m catch-up in processor royalties.

Moving on to costs, normalized OpEx in the first quarter was GBP60.3m compared to the guidance given in February of GBP57m to GBP59m. As mentioned in the earnings release, the sequential increase to a level just above the top of the guidance range is largely due to the impact of a weaker dollar in Q1 on the accounting for derivative instruments, which has resulted in a net charge of just under GBP2m being included in G&A expenses in Q1.

As a result of a strong revenue performance, the Group is reporting normalized operating margins in excess of 42% with net cash generation in the first quarter well up on the same quarter last year. And this at the same time as we have been continuing to increase our investment in new technology by growing our R&D capability.

Looking into the next quarter, we expect normalized operating expenses, assuming effective exchange rates broadly similar to current levels, to be in the range of GBP58m to GBP60m.

And reiterating the outlook that Warren referred to, we do anticipate normal seasonality for royalty revenues in Q2. And notwithstanding the current uncertainty as to the economic impact of the earthquake in Japan on the semiconductor industry supply chain and end product markets later in the year, we expect that Group dollar revenues for 2011 full year will be at least in line with current market expectations of about \$730m.

With that, we'll throw it open to questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Your first question comes from Sandeep Deshpande from JPMorgan. Please ask your question now.

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### Sandeep Deshpande - JPMorgan - Analyst

Yes. Hi. Thanks for the question. Just a first question on PIPD. Despite the wins you're seeing in PIPD, PIPD revenues seem -- royalty revenues seem to be declining year on year despite an increase in the semiconductor industry. Is there an explanation for that?

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### Warren East - ARM Holdings plc - CEO

Well, Sandeep, I think there is a very small decline year on year. And when we look at how that's made up, it's mainly due to physical IP users switching from -- switching their production down to the 65-nanometer node. And if you go back and look at the licensing that we were doing a few years ago, then actually our physical IP at 65 nanometers is much less penetrated than at 90 nanometers and, indeed, at 45 nanometers and 32 and below.

So that's why I'm actually quite encouraged and said in the opening commentary -- encouraged to see 45 and more advanced nodes starting to get to production because we do have a little bit of a soft patch in 65 nanometers. And that's what's coming through and affecting royalty today.

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**Sandeep Deshpande** - JPMorgan - Analyst

So do you expect that to continue for a few quarters? Or the first 45 nanometers is more second-half-loaded in terms of shipments?

**Warren East** - ARM Holdings plc - CEO

Well, we'll have to see exactly which effect dominates. There will be downward pressure from 65 and upward pressure from 45. And it's quite hard to call exactly which is going to dominate over the next couple of quarters. But if we look through several quarters, we can actually see some more moving to 45 nanometers and below fairly quickly.

**Sandeep Deshpande** - JPMorgan - Analyst

Warren, would you also like to comment on what you're seeing in terms of the reported royalty rates on the Cortex processors at this point as opposed to what you're signing and negotiating, what the reported royalty rates are?

**Warren East** - ARM Holdings plc - CEO

Yes. Again, obviously we're not going to comment in specific cases. But the Cortex-A products, which are shipping at the moment, accounting for 4% of shipments, are commanding the higher royalty rates that we talked about back in February. And that combined with the typically higher ASPs is what has driven the sequential increase in absolute dollars and cents per chip in spite of obvious downward pressure from the strong growth in microcontrollers.

**Sandeep Deshpande** - JPMorgan - Analyst

But you're not commenting on what this actual -- is it a 2% or 2.5% or what?

**Warren East** - ARM Holdings plc - CEO

We won't really comment on particularly the percentage there, Sandeep. There's a range. And we've said by the time you get through to Cortex-A9s and Cortex-A15s then you're at the higher end of the 1% to 2% range. The reality of most of what's shipping today though, there's very few other than Cortex-A8 products. And that's a little bit earlier on in that journey.

**Sandeep Deshpande** - JPMorgan - Analyst

Thank you very much.

**Warren East** - ARM Holdings plc - CEO

Thank you.

**Operator**

Your next question comes from Gunnar Plagge from Nomura. Please ask your question now.

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**Gunnar Plagge** - *Nomura - Analyst*

Yes. Hello. I was wondering whether you could speak a little bit more about the Mali design wins. I think you also mentioned recently that, compared to your main competitor, the ecosystem here is not as developed and maybe you could talk a little bit what we can expect over the course of the year here.

And as a follow-up, just a quick comment on the stock-based compensation which seemed to have jumped quite substantially from Q4 to Q1. Thank you.

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**Warren East** - *ARM Holdings plc - CEO*

Okay. Well, I'll start on the Mali question and Tim will come in on the stock-based compensation in a few moments.

We were pleased to see seven Mali licenses during the quarter. That is for a mix of mobile computing design wins and DTV set-top box type design wins. So Mali is going into apps processors for both those end products. Obviously that's licensing activity. We'll have to see how that translates into shipments over the coming years.

In terms of what we expect for this year, we continue to expect, as we said in February, shipments of Mali-based products in the tens of millions this year. And that is going to be in a mixture of smartphones and in DTV-type products.

It's correct what we said in February about the maturity of the Mali ecosystem being less mature than the Imagination ecosystem, which is essentially the incumbent in the mobile space. But we expect to see an acceleration in the maturity of the Mali-based ecosystem as those products start shipping this year in, as I say, the tens of millions of units. So I think that's it on Mali.

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**Tim Score** - *ARM Holdings plc - CFO*

Yes. Gunnar, on share-based compensation, there are some accounting effects which are one quarter only in Q1 based on the very significant rise in the share price during the quarter. We ended the year at GBP4.23 and by the time we did our RSU grant in early February, we were at GBP5.75. By the end of the quarter we're a little bit higher than that.

So what I will expect to see happening in the subsequent quarters of this year is the share-based compensation quarterly charge will return to the levels that we saw in Q3 and Q4 last year.

I think the other point to note is that our grants to employees are broadly based on proportion of salary. And therefore what we are seeing is the number of shares that are granted to employees is going down as the share price goes up. So that means in terms of the overall forward dilution in terms of number of shares is going down.

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**Gunnar Plagge** - *Nomura - Analyst*

Thank you.

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**Operator**

Your next question comes from Francois Meunier from Morgan Stanley. Please ask your question now.

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**Francois Meunier** - Morgan Stanley - Analyst

Yes. It's Francois. Congratulations on the results again. I've got a question first on the deal signed with LG yesterday. It looks like it's a pretty broad type of licensing deal. I don't think LG has made chips before. It's a bit of a new thing. If you could please comment on this deal with LG and maybe if you expect more OEMs going forward to use this type of strategy, maybe I'm looking at Sony as well, in terms of their new gaming consoles type product. Thank you.

**Warren East** - ARM Holdings plc - CEO

Yes. Good. Well thanks, Francois. There's nothing particular to note about the LG deal. It's a subscription agreement, as noted. It's targeted at a range of products, including phones, potentially some mobile computing, also DTVs and set-top boxes. And it includes ARM -- normal ARM microprocessors and Mali graphics. So I think that's all there is to note on it from the time being.

ARM has worked with LG for some time. ARM processors have been designed into LG's DTVs for some time. And this is just an extension of that relationship.

**Francois Meunier** - Morgan Stanley - Analyst

Okay. Just -- yes, a second question I would have is about the ASPs which are continuing to trend upwards. That's very good. Obviously we've seen recent tablets being launched with die size much bigger than the ones which were launched last year. Obviously all or most tablets being launched this year are dual core. Shall we expect the ASP for ARM of those new tablets to be much higher than what they were last year?

**Warren East** - ARM Holdings plc - CEO

Yes. Well, I think you probably can. These are new tablets launched around new chips. And of course the phenomenon that we usually observe is that when a new applications processor is first launched, it's released at a higher price than the generation of chips that it's replacing. And then normal ASP decline takes over over a period of a couple of years.

And so yes, we do expect to see higher ASPs from those particular chips. But I'd like to caveat, before everybody runs away and revises their models upwards, caveat that with normal ASP decline over a couple of years and, in spite of it's great to see all these tablets being launched, don't forget we're still talking about a market of 40m to 60m tablets for the year and we just shipped nearly 2b ARM microprocessors in the first quarter. So you have to put that into perspective.

**Francois Meunier** - Morgan Stanley - Analyst

Thank you.

**Warren East** - ARM Holdings plc - CEO

Thanks.

**Operator**

Your next question comes from Didier Scemama from RBS. Please ask your question now.



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**Didier Scemama** - RBS - Analyst

Yes. Good morning, gents. Congratulations on the results. Couple of questions, if I may. Just on Francois's question, just wanted to add one more element. When you look at the die area of what's available on the Internet of tablet processors, roughly what we're seeing is that the CPUs, the core CPUs, takes about 20% to 25% of the die area. And if I do the math right, that would be anywhere between \$3 to \$4, if you want, of the cost of sales, which is materially above what you charge. So what I'm wondering is if in the longer term, I'm talking in the next five to 10 years, we could see the royalty that ARM collects on the CPU side for those processors going into PCs and so on, could trend towards those numbers. That's my first question.

And second question would be, and I apologize if you've been misquoted, but I can see a Bloomberg comment that was made earlier this morning saying that AMD could do a lot more with ARM in the future. So I was wondering if you could elaborate on that, please.

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**Warren East** - ARM Holdings plc - CEO

Okay. Well first question about the royalty rates for chips. As we said in February, if we are supplying more value to a semiconductor company then we are replacing work that that semiconductor company would otherwise have to do. We're replacing costs that that semiconductor company would otherwise have to incur. And therefore we are able to strike an agreement with the semiconductor company that, in exchange for additional value, we will take home a higher royalty rate. That trend continues.

We try very hard to steer away from discussions about silicon area when we're discussing royalty with semiconductor companies. The point of the ARM business model is that we supply the microprocessor and different semiconductor companies differentiate around that microprocessor in different ways. In some instances, that will mean a greater amount of silicon area is in the semiconductor partner's differentiation piece and in other cases there will be a lesser area in the differentiation piece.

And because of that it's a very difficult commercial discussion to have for both sides. And so what we tend to do is look at the value of the ARM microprocessor in terms of the functionality that it delivers rather than the area. So I think that's all we really need to say about the royalty rates and chip areas.

On AMD, what -- we were asked a question this morning about AMD. And we simply said that AMD's a semiconductor company. They're in the business of shipping microprocessors. We're in the business of licensing microprocessor designs. So it's perfectly normal course of business for ARM to be trying -- you would hope that we would be trying to sell microprocessor designs to AMD.

Clearly AMD has signaled that they're going through a bit of a rethink of their strategy at the moment and therefore that presents, as far as we're concerned -- standard commercial common sense will tell you that that presents a heightened opportunity. And at the moment they don't use ARM microprocessors. And as far as we can see, there's an opportunity there where they might use ARM microprocessors in future. And you've got to expect that we'll be trying to persuade them of that.

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**Didier Scemama** - RBS - Analyst

And one final follow up if I may. What we see from the OMAP 5 from TI is a dual A15, and some slave, I believe, Cortex R5 or R3, I'm sorry I forget exactly which. On those chips that have dual CPUs plus sort of slave CPUs how much higher would be the royalty rate on those, the sort of quantum of improvement relative to just the dual A9's say.

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**Warren East** - ARM Holdings plc - CEO

Well, as you know, I'm very sensitive to commenting on particular semiconductor companies. In the general case then, where there are multiple ARM microprocessors per chip, then each microprocessor is commanding a royalty in a sense. So the -- in

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the general case a dual A15 will command a certain level of royalty. Not because it's dual but because it's A15. And the M4 that's the -- in the OMAP device, will be commanding another royalty sort of for M4. And typically there's a discount for the second and subsequent cores. And that discount might be quite significant like about 50%.

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**Didier Scemama** - RBS - Analyst

Perfect. All right, thanks so much.

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**Warren East** - ARM Holdings plc - CEO

Thank you.

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**Operator**

Your next question comes from Gareth Jenkins from UBS. Please ask your question now.

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**Gareth Jenkins** - UBS - Analyst

Yes, thanks. A couple if I may. Just wanted to see -- I wondered what you make of Google's intentions to reduce fragmentation and also an update on Linaro from your side.

And then secondly, I just wondered whether there's anything that you've seen from Intel that's particularly surprising, the sort of acceleration of Tick-Tock 14 nanometers and how that positions you. And then finally just the timing on 64 bit please?

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**Warren East** - ARM Holdings plc - CEO

Okay, on Android there has been in the quarter some speculation about and discussion about Google's intention to standardize. I think really to talk about Google's intentions you have to talk to Google not ARM.

As far as we can see Android is an open-source platform. There are benefits in the standard, but because it's open-source customers are able to take the starting point and make modifications to suit their own product. And at one level, if those modifications are not done in a controlled way that can lead to fragmentation and you can end up with applications that are written for one particular end product.

For example, an end product that has a small screen, maybe a particular product that's got a large screen you'll get a different type of application performance on that.

It's very much down to how sophisticated is the modification performed by the OEM. And what this open standard does is enable Google's customers to differentiate. Exactly how well they do that differentiation is up to them. Exactly how much Google wants to control that differentiation is up to Google. We are keen to support Google and its customers in bringing a range of diverse products to market. And we'll continue to do that.

Efforts such as Linaro do help those OEM customers to work across multiple systems on chip devices. And multiple systems on chip devices based on the ARM architecture. That's why we started Linaro a year ago. And Linaro continues pretty much as planned. The number of engineers deployed across Linaro has continued to grow as planned. I think they're up to about 120 people at the moment. But you have to talk specifically with Linaro about that.



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ARM is now an ordinary member, represented on the Linaro Board. We no longer have a sort of controlling interest or steering role in Linaro that is unique anymore than any of the other ARM partners that's involved in it. So I think that's all I can really say on Android and Linaro.

On Intel accelerating Tick-Tock down to 14 nanometers, yes, Intel has been quite explicit about manufacturing technology being their key area of expertise. And we have yet to see how that develops.

The ARM partnership has access to leading edge foundry capability from the leading foundries. And our physical IP division we are striking agreements with leading edge foundries to collaborate to 14 nanometers and below as well.

So, you saw announcements from ARM and IBM. You saw announcements from ARM and TSMC at the TSMC event the other day as well. And so it's very much normal progress in the semiconductor industry.

And your last question was about 64 bit. And all we've said on 64 bit is that clearly it's something that's being done in the world of computing. Everything we've done so far in the ARM architecture is -- simply followed what's being done in the world of computing, and taking that and implementing it on a system on chip type scale.

And so, yes, people are talking about 64 bit versions of ARM. But we are not in a position to make product announcements. We will make the product announcements as and when we are ready to do that.

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**Gareth Jenkins** - UBS - Analyst

Thanks, Warren.

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**Warren East** - ARM Holdings plc - CEO

[That's it], thank you.

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**Operator**

Your next question comes from Kai Korschelt from Deutsche Bank. Please ask your question now.

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**Kai Korschelt** - Deutsche Bank - Analyst

Yes, good morning. I have two actually. The first one was on ASPs. They moved up a bit sequentially, and given this is the sort of strong Q4 holiday season that's reflected in there with higher smartphones and tablets percentage, should this continue -- sort of trend down in Q1, which is your Q2, again or should ASPs stay at around that level?

And my second question is if I could maybe be a bit more pushy on stock options. Clearly it's a large part of your OpEx base and if we treat it as an expense, your margins would be materially lower now. It's obviously a good thing to have employees participate in the success of the company. But I was wondering if, given your strong balance sheet and cash generation, are you planning to at least offset the dilution to the existing shareholders from this via a buyback, for example, at any stage? Thank you.

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**Warren East** - ARM Holdings plc - CEO

Okay I'll deal with the first one and Tim is going to answer the second question. On ASPs, yes, you're quite -- the upward pressure on ASPs has been driven by smartphones, mobile computers, DTVs these sorts of consumer-oriented products, which tend to be more seasonal.

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And as we look at the next quarter, typically, we'll see market sectors such as industrial which is much less seasonal. We'll see microcontrollers probably dominate more, and that could result in a flat ASP for the quarter or even a decline as we've got these two sort of offsetting forces, one pushing the average rate up, one pushing the average rate down.

As we've discussed many times this is simply the result. And a good result for ARM may well be a lower average number overall, because that will mean that growth in microcontrollers has been stronger and therefore a lower average number could actually be a good result for ARM and you shouldn't necessarily interpret that as a bad result for ARM.

Q2 we expect normal seasonality. We expect overall royalty revenues to be down 5% to 10% as we've said through normal seasonality. And if you look at the mix there we would expect smartphones and tablets and things to have less of an impact than microcontrollers.

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**Tim Score** - *ARM Holdings plc - CFO*

And Kai, yes, you raised two issues there, one of in a sense remuneration policy, particular reference to share-based remuneration, and you're touching on, if you like, the wider issue of capital structure management and balance sheet efficiency. And of course there is -- could potentially be linkage between them.

Our approach to share-based remuneration has been consistent over many years. As I said earlier on the call each of our employees get some proportion of their salary in share-based remuneration. What that means today is that we are issuing somewhere around 0.5% or 0.6% per annum of our share capital to employees. And, yes, that policy has been consistent.

As to whether we do share buybacks to specifically offset dilution or for wider balance sheet efficiency management is something that we will wait and see. We've obviously done that before. Between '05 and '08 we bought back about 16% of the shares, returning about GBP260m of cash.

Our current plan of record is progressive dividend. We've been growing the dividend through the cycles. And that remains our plan of record. But share buybacks remain an option. We have the authority to do buybacks up to 10%. And we routinely renew that, so it remains an option. But there's nothing to announce on that today.

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**Kai Korschelt** - *Deutsche Bank - Analyst*

Okay, thank you.

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**Operator**

Your next question comes from Raj Seth from Cowen and Company. Please ask your question now.

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**Simran Drar** - *Cowen and Company - Analyst*

Good morning, thank you. This is [Simran Drar] calling in for Raj Seth. My first question was for Warren, for Mali you continue to see strong momentum for the second quarter. I was wondering when do you expect revenues from Mali to become material for your model. And in terms of gaining share versus your dominant competitor, how much of a deterrent are switching costs for potential customers.



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**Warren East** - ARM Holdings plc - CEO

Yes, okay. We are pleased to see continued momentum in terms of licenses in the quarter. As far as license revenue is concerned then a Mali license is fairly similar to a generic ARM microprocessor. It's typically the price would be less than something like a Cortex-A9, but it's more like a high-end ARM 11 or something like that in terms of pricing. And so that's the sort of contribution that's been made from a licensing revenue perspective. And out of a total of 39 licenses in the quarter, seven of them were Mali licenses. So you can gauge the contribution to license revenue from that.

In terms of when it's going to become significant for royalty, well I think 2011, as I said on the call, we expect to see tens of millions of units of Mali. That's obviously a small contributor compared with the run rates on this quarter of 1.85b units in the quarter, tens of millions of units is relatively small.

But Mali does tend to go into the more expensive devices, sat alongside a high-end Cortex processor in an applications processor. And so really it should be compared with the Cortex-A product, which in the last quarter were about 4% of total shipments. So in terms of that comparison then tens of millions of units this year will look like a reasonable contribution.

And it's those shipments of units this year which make an impact to the switching cost, because at the moment the key issue about switching is that the maturity of the Mali Ecosystem is clearly less developed than that of the incumbent, which tends to imagine based devices. But with tens of millions of units shipping this year we would expect to see that maturity develop and start to develop quite rapidly. And that will bring down the switching cost. So that by the end of 2011 those switching costs will be a lot less substantial than it is today.

I think that's (multiple speakers).

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**Simran Drar** - Cowen and Company - Analyst

Oh, thank you. One more question for Tim if I may. In terms of your model, Tim, could you remind me what typical seasonality is for the processor royalty side of your business in the second half?

And assuming a constant exchange rate how should we think about expense growth in the second half of the year? Thank you.

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**Tim Score** - ARM Holdings plc - CFO

Well, if you typically look at the shape of processor royalties through the year, as we've been saying this morning, we tend to see a 5% to 10% decline in the second quarter versus the first based on Q1 shipments, and then what we tend to see then is an uplift in Q3 and then a bigger uplift in Q4.

And I think the reference today to the uncertainty around Japan I just think needs to be considered when looking at the forecast for royalties in the second half. I think it's too early and is very unclear as to what impact there may be on consumer behavior in Japan at the back end of the year. But we do expect some impact. But normal seasonality is for an uptick in Q3 and a bigger uptick in Q4.

Assuming that similar level of -- we've guided for the second quarter, we are hit on OpEx, we're in investment mode. We expect to see an increase in headcount in the second half and therefore, probably a gradual increase in OpEx. Consensus OpEx coming into these results is about GBP236m for the full year 2011. That may edge up a little bit, but I don't think substantially based on today's results and the guidance for Q2.

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**Simran Drar** - Cowen and Company - Analyst

Okay, thank you.

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**Operator**

Your next question comes from Jerome Ramel from Exane BNP Paribas. Please ask your question now.

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**Jerome Ramel** - Exane BNP Paribas - Analyst

Yes, good morning. Just to come back to the full year guidance where you say are -- you expect revenues to be at least in line with consensus. If I look at what ST Ericsson said on the wireless, Broadcom on the wireless, Nokia units, iPad units, it seemed that the wireless is a little weaker what people were expecting going forward. So if you feel confident with the consensus, I just want to check if actually you feel more confident on the licensing revenue rather than on the royalties for the full year.

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**Warren East** - ARM Holdings plc - CEO

You're right. I think, yes, the recent announcements I think of some of the semiconductor companies who are ARM licensees about their first quarter and our second quarter, I think, does underpin what we've been saying about normal seasonality although there are clearly mixed guidance out there. Some companies are flat to growing, others are in that range and some are below that range.

I think in terms of the full year our comment is looking at our overall revenues, we do expect to see growth in royalties in the second half. We're just noting the fact that Japan is likely to have an impact on the shape of that. We have a record order backlog that underpins licensing in the second half. And we have a strong opportunity pipeline. So our comments are really based on the business overall.

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**Jerome Ramel** - Exane BNP Paribas - Analyst

Okay, thank you. And on the backlog any idea of whether it should be flat or to continue to grow this quarter?

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**Warren East** - ARM Holdings plc - CEO

Yes, I think it is very difficult for us to call backlog on a quarter-by-quarter basis. When we looking into our opportunity pipeline for licensing there is the normal mix of deals between those that yield short-term revenue because they are for more mature technologies and licenses for technology currently under development or future technology, and indeed potential longer deal deals such as that we've seen through this quarter.

So, yes, it really depends which of the pipeline closes in the second quarter as to what the backlog is at June 30. But looking overall into that pipeline it does look pretty promising.

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**Jerome Ramel** - Exane BNP Paribas - Analyst

Okay, thank you very much.

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**Operator**

Your next question comes from Nick Hyslop from RBC Capital Markets. Please ask your question now.

**Nick Hyslop** - RBC Capital Markets - Analyst

Thank you. Good morning, guys. I think most questions have been asked. But I have a couple. Obviously in the light of what Broadcom has said overnight, when you look at the kind of royalty checks coming in does the comments from Broadcom on weakness in mobile suggest that they're maybe minus 5% to 10% might be closer to the minus 10%? Do you have any sympathy with what they've said?

**Warren East** - ARM Holdings plc - CEO

That one sounds like a cracked record, Nick. Yes, I do -- what we are seeing out there is a range of reported results for Q1 for our customers and indeed for their guidance. There are companies that have seen sequential growth. There are companies that are flat. And there are companies that are down more than 10%. I think in the round 5% to 10% I think is the range.

We have actually received a very small proportion of royalties to date. So I think to be more specific than that would be unwise at this particular point. But like you we note very carefully what all of our [shippers] are saying in their public result to the extent they're public.

**Nick Hyslop** - RBC Capital Markets - Analyst

Okay, that's fair enough. And then maybe just could you -- can you tell me what you're expecting for the full year amortization charge with intangibles? It just seems to be very low. I know it's not an important one, but I'd be keen to know for the model.

**Warren East** - ARM Holdings plc - CEO

I think the run rate will be rather consistent. What's actually been occurring is that the intangibles that arose on the acquisition of Artisan at the end of '04, is the great majority of them have now been fully amortized, so you're seeing a much lower run rate relating to largely more recent acquisitions.

**Nick Hyslop** - RBC Capital Markets - Analyst

And therefore for the full year that is now -- four times that number is the right number?

**Warren East** - ARM Holdings plc - CEO

That's a good way to think about it.

**Nick Hyslop** - RBC Capital Markets - Analyst

Okay. That's great, thank you.

**Operator**

Your next question comes from Nick James from Numis. Please ask your question now.

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**Nick James** - Numis - Analyst

Morning. I just had a question on the physical IP POPs. I wondered if you could remind us when you started selling these. And how many of your customers have adopted them so far? And also the timeframe within the chip development cycle when people license the POP's and in terms of how long the delay is until you start to see royalty revenues from these products.

**Warren East** - ARM Holdings plc - CEO

Yes. So we started selling these as products at the very back end of 2009. And so far we've sold 13 POPs. If we analyze where those are going then people are using them for Cortex-A9. Rough, very roughly the sort of attach rate of a POP to Cortex-A9 is about 50%. So you can look at our A9 licensing, very roughly half of those licenses POPs have been licensed.

Exactly the extent to which the POPs are used in the chip implementations of course we don't know at the moment. But people are paying good money for them, and so we anticipate they are being used as part of the chip design process.

It's -- the length of time to develop the device is no different from sort of normal. We are not seeing a lot of people licensing a POP after they've licensed an A9, a long time afterwards. So we'd say typically about four years to meaningful royalties. And we started effectively at the beginning of 2010.

You might see, because people who are buying A9, typically they'll be sort of fairly experienced chip designers. You might see a little bit of an improvement on the four years. So initial royalty we'd expect to see probably more like three years. But any appreciable volume that you'll actually notice in terms of royalty revenue then I expect that to be about four years.

**Nick James** - Numis - Analyst

Great that's very helpful, thank you.

**Warren East** - ARM Holdings plc - CEO

Thank you.

**Operator**

Your next question comes from Brett Simpson from Arete. Please ask your question now.

**Brett Simpson** - Arete - Analyst

Yes, thanks very much. I have some questions on the PD licensing business. Revenue growth in this area clearly coming through much faster than historically has been the case, last few quarters up 50% year on year. And you've had record license intake in each of the last three quarters.

Warren, you've spoken in the past about the relationship between the licensing activity and the semiconductor design cycle where we see peaks and troughs in license activity, which has probably been lumpy in the past. Is this dynamic becoming less relevant in your view? And to what extent is this level of license intake sustainable over the next 12 months or so?



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**Warren East** - ARM Holdings plc - CEO

Okay. The answer is, yes, as ARM's market becomes much bigger and much broader then the lumpiness that is associated with licensing does tend to be smoothed out. However, we have said back in February and we are sort of repeating it today the licensing revenue that we would expect for a quarter, run rate we would expect to be in the sort of \$40m to \$45m. We don't want people to think that north of \$50m is the norm.

We are seeing a period of strong licensing at the moment as people are licensing Cortex-A9s. Cortex-A15s are not really sort of contributing in any way to license revenue at the moment. That's a brand new product. But we are in the sort of sweet spot of A9 licensing at the moment. You would expect, therefore, it to be a little bit product-cycle related, and that's why even though we've just reported two quarters of north of \$50m of licensing, we are still saying \$40m to \$45m is the normal range.

That doesn't mean that there won't be another quarter of \$50m plus. There might be. But if there's something more like 20 to 30 licensing in a quarter instead of 40 licenses in a quarter, and license revenue in the \$40m to \$45m range that's perfectly normal as well.

So you're right there's a little bit of lumpiness, but it's probably a lot less lumpy than it used to be, simply law of bigger numbers instead of law of small numbers.

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**Brett Simpson** - Arete - Analyst

Sure. And just to follow up, Warren, if I may, in the presentation pack it says you have signed cumulatively 68 licenses for Cortex-A. But can you talk about specifically how many licensees that translates to, specifically for multicore Cortex-A?

And I'd like to know how many chip makers are developing these types of application processors, as there's concern that only a small number of chip makers are actually scaling up in this area, particularly with Apple taking a disproportionate share at this stage.

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**Warren East** - ARM Holdings plc - CEO

Yes. It's true that the Cortex-A9 on the chart refers to A15s, A5s, A9s etc., etc. If you look at it from a number of semiconductor companies point of view there's about 30 of them in that -- involved in that activity.

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**Brett Simpson** - Arete - Analyst

30. Okay, great.

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**Warren East** - ARM Holdings plc - CEO

Yes.

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**Brett Simpson** - Arete - Analyst

And how many do you think, when you look at the total addressable market, how many chip makers do you think can -- the ecosystem they can sustain, this sort of development, given the growth outlook here?

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**Warren East** - *ARM Holdings plc - CEO*

Well, it's true that the general rule is bigger investment means that fewer companies are able to make those big investments. However, we have been talking at these sort of conference calls and meetings about the decline of ARM's licensing opportunity in terms of number of customers who are going to buy licenses. We've been talking about that for the last decade, as long as I've been doing this job. And in that time the number of licenses has consistently grown. The number of licensees has consistently grown. And indeed in the last quarter we had 10 new licensees, including a couple coming to the party for the first time with Cortex-A based products.

And so, yes, that general trend must be out there, common sense tells you that it must be out there. But actually we are continuing to find new customers that are ready to buy into the ARM architecture and existing customers who are ready to broaden their relationship and continue to invest in Cortex-A based products. So I don't want to sort of forecast the demise of this trend too early.

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**Brett Simpson** - *Arete - Analyst*

Sure. Okay, thanks very much.

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**Warren East** - *ARM Holdings plc - CEO*

Thank you.

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**Operator**

Your next question comes from Aalok Shah from Davidson. Please ask your question now.

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**Aalok Shah** - *DA Davidson - Analyst*

Good morning. One if I could, just a clarification on your opening comment about LG and Broadcom, the licenses there. You mentioned that Broadcom and LG were licensing for set-top box and digital TV. Is that true for Broadcom as well or were you referring just to LG at that point?

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**Warren East** - *ARM Holdings plc - CEO*

In the answer to the question I was referring to LG specifically. The subscription licenses signed by both companies are broad licenses for a broad range of products. And Broadcom will make their intentions clear when they're ready to do so, and it's not for us to comment.

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**Aalok Shah** - *DA Davidson - Analyst*

Okay, thank you.

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**Ian Thornton** - *ARM Holdings plc - Head of IR*

Operator, can we go for one more question please?

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**Operator**

We can do. Your next question comes from Andrew Gardiner from Barclays Capital. Please ask your question now.

**Andrew Gardiner** - Barclays Capital - Analyst

Thanks very much. Just a very quick one, just another clarification on the POPs within Physical IP, can you give us any sense as to how significant they are from a revenue point of view, in terms of licensing relative to perhaps sort of the norm?

**Warren East** - ARM Holdings plc - CEO

Yes, these are low value licenses of typically a few hundred K dollars apiece. So our intention with the POPs is to enable semiconductor companies who've invested in a Cortex-A9 or above type product to be able to bring that product to market quickly and accelerate time to royalty.

The purpose of the POPs is not really to generate lots and lots of revenue out of licensing them. But we do like people to make a commitment. And that's why it's at about that level.

**Andrew Gardiner** - Barclays Capital - Analyst

I see. And also I presume most of it at the moment is high-end smartphone mobile computing related, but is there any likelihood that you could expand this into other areas as well?

**Warren East** - ARM Holdings plc - CEO

Well, it's for Cortex-A9s at the moment, and actually they are selling to people who are building apps processes for DTVs and set-top boxes as well as for smartphones and mobile computing type applications.

It's literally just a way of getting a deterministic result out of your Cortex-A9 or A15 implementation. And in that way you're sort of -- that's one problem in the design process out of the way and you can get your chip to market faster.

**Andrew Gardiner** - Barclays Capital - Analyst

Very clear. Thanks very much.

**Warren East** - ARM Holdings plc - CEO

Okay, so with that we'll conclude. Thank you very much for dialing in and taking part. We are enjoying a good start to the year, a healthy pipeline looking forward, and we look forward to talking with you again in July when we come back with our half-year results. Thanks.

**Operator**

That does conclude our conference for today. Thank you all for participating. You may all disconnect.

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