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Webcast (English and Mandarin)

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Rich Kramer *Arete Research - Analyst*

Robert Yen *Goldman Sachs - Analyst*

Jasmine Lu *Morgan Stanley - Analyst*

Julia Tai *UBS - Analyst*

Sean Louie *JJ - Analyst*

PRESENTATION

Operator

Welcome everyone to HTC's 2012 Q3 results conference call and webcast. Today with us we have CFO, Mr. Chialin Chang and IR Director, Mr. Joey Cheng.

All lines have been placed on mute to prevent background noise. After presentation, there will be a question-and-answer session for investor and analysts. Please follow the instructions given at the time if you would like to ask a question.

For your information, this conference call is now being broadcasted live over the Internet. A webcast replay and English transcript will be available within an hour after the conference is finished. Please visit www.htc.com under the Investor section.

Now I would like to introduce Mr. Joey Cheng, the IR Director. Mr. Cheng, you may begin.

Joey Cheng - HTC Corporation - IR

Debbie, thank you. Good afternoon, ladies and gentlemen. Welcome again for joining HTC 2012 third quarter analyst call. In the presentation we are going to --- we're about going through has been sent out 10-15 minutes ago. You may also download it from our website or participate through webcast.

And if you do not have the presentation material, please let us know now and your line will be cut off -- will be put on mute when we are presenting. And if you are cut off, please dial back in or call Sally Kuo at 886-960-761-958 for assistance.

And also we will conduct our later Q&A session in both English and Mandarin since we are combining previously a separate Mandarin and English conference call into only one call we are doing at the moment.

And before we start, I would like to draw your attention to the disclaimer statement on page 2. And please note that this presentation contains forward-looking statements and these statements are based on our current expectation. Actual result may differ materially from our expectations and the Company undertake no obligation to update these forward-looking statement going forward.



And I'll go over our third quarter business review in English, but we have both English and Chinese slides on which you guy can choose proper version to refer while I am presenting.

Now please go to page 3 on our presentation.

First of all, third quarter financial highlights. During the quarter, our revenue was TWD70.2 billion, and the gross margin and operating margin were at 25% and 7%, respectively. Net income was TWD3.9 billion.

A quick business update for the quarter. Number one, China remain a key growth driver, and continuing to further increase local brand awareness, retail presence, and operator partnerships.

Number two, US was pretty much inline with our earlier expectation and the flagship product were well-received.

Number three, Japan had initial success with the HTC J and we have also launched HTC J Butterfly to continue the momentum.

Number four, EMEA region focused on enhancing brand consideration in both developed and emerging countries. In the end, South Asia continued its efforts to build distribution channel as well as local presence.

Page 4. First, investment recap. During the quarter, we have \$35 million strategic investment for a 17% stake in Magnet Systems, the creator of a next-generation software platform for mobile enterprise market. Number two, we also recognized a \$40 million investment impairment for OnLive.

A recent new product we have launched so far, HTC One X+, that's an enhanced version of the HTC One X, operates on the new HTC Sense 4+ with faster speed, longer battery life and expanded internal storage.

HTC One SC, SU and ST, that's a well-sculpted dual-core 4.3 inch tailor-made for the Chinese market with a improved camera capability and Beats Audio effect. A Windows Phone 8X and 8S by HTC, those are considered the Windows Phone hero product by Microsoft. It's perfectly sculpted, three-dimensional pure uni-body design and with ultra-wide-angle front-facing camera.

HTC Desire X, that's an affordable smartphone with a dual-core 1 gig processor, featuring a 4 inch super LCD, state-of-the-art camera, including VideoPic and Continuous Shooting, and authentic sound.

HTC J Butterfly, together introduced with KDDI, that's the first quad-core smartphone with 5 inch Full HD super LCD 3 display having a 440ppi resolution and being built in a 9.1 millimeter slim design and with a eye catching color.

Page 5 and 6 give you a quick reference of quarterly trend on our quarterly revenue, operating profit, gross margin and operating margin. And page 7 and 8 are our simplified consolidated P&L and balance sheet statement for your quick reference. And page 9, 4Q business outlook. For coming quarter, fourth quarter, we expect our revenue to be around TWD60 billion and gross margin is expected to be around 23% with operating margin expected to be around 1%.

This wraps our presentation. Debbie, we can start Q&A now.

QUESTIONS AND ANSWERS

Operator

We will now begin the question-and-answer session. Kindly leave the time to investor and analysts. For media, please contact the HTC PR team after the call if you have any questions.



(Operator Instructions)

[Annie Choi], Credit Suisse. Annie, please begin.

Arthur Hsieh, UBS.

Arthur Hsieh - UBS - Analyst

Hi, can you hear me?

Chialin Chang - HTC Corporation - CFO

Yes.

Arthur Hsieh - UBS - Analyst

I think the guidance is a bit low than the market expectation. Could you give us a bit more color in terms of what's changed? Is it because the Company is taking more aggressive pricing strategy or is there any specific reasons that both sales and the margins are kind of low? Thank you. That's the first question.

Chialin Chang - HTC Corporation - CFO

Thank you, Arthur. Before answering your question, let me make a few points here. In part, it's going to be answering your question. First of all, welcome everybody on a call here especially for those who're dialing from North America or a different time zone, making it difficult. I appreciate you dialing in on our call here.

We're trying to combine both English and Chinese into one session, primary for the purposes so everybody only have to do it once without missing the other call and missing potential other information. So we consolidate the call information in there. As a result, we can find time so hopefully most of people can dial in. And because of that, our format will need to be combined into the English and then Chinese. So we're trying to make it work. We appreciate your feedback on that.

Next I will make two statement and part of it is to answer your question, Arthur. First of all, I will talk about the --- in terms the --- the trend, our revenue trend and the second point I will talk about the overall in the third quarter in terms of different regions there. So people can --- I think this is probably going to be most commonly asked question.

First of all, talk about the revenue on a third quarter trend. Actually you can see our third quarter trend from July, August and September. September month in revenue is, I will say, from capital market perspective or the investor perspective here lower than initially anticipated part due to two reasons. One, there is some lumpiness in the monthly sales in the third quarter. Second, there is some anticipation or expectation in the market in terms our new product launches.

So as a result, what you're going to see here is the September quarter is lower than the July and August month. Based on our guidance here, I can also just give you more granularity in terms the fourth quarter trend in terms of monthly sales. What we're seeing here is you're going to see October sales are going to be lower than the September sales and before it coming back up for November sales, we're expecting November sales will be higher than the September sales and hopefully can carry the momentum into the December quarter based on what's seen here today.

The reason for the December quarter, i.e. the fourth quarter to be lower than you just said your expectation primarily is due to the following reason. Our -- almost all the majority, I will say the vast majority our new product launches -- not the launches, the shipment actually going to come in in



November probably somewhere in the --- around the second or mid-November timeframe to be available on the shelf. So you're going to see the decline in October revenue before picking up in November and hopefully will carry the momentum into December. So that's basically the trend we are seeing today.

In terms of margin, basically what we're seeing the gross margin around 23% partly due to mix and partly actually we make some reserve to -- it's needed to clean some of the channel inventories, some of our older product, if needed, on that basis. So when we're guiding the market here, it's about 23%.

In terms the operating margin about 1%. A lot of the analysts and investors also ask me in terms the -- where we're seeing the operating expense, so I'll make it more clear on that. Because the guidance on the revenue side is TWD60 billion, because that scale, some of this was [business] nature of operating expense resulting in a higher operating expense ratio as a percentage of sales. However, one thing I need to emphasize here that we did not decrease our sales and marketing budget and expenses because we think it's important.

For both one, new -- introducing new product launches in December quarter and also it's important to continue to promote the HTC brand. We all understand this is the market, the combination of product and also the brand is going to be very important. So we make a very conscious decision to continue to invest because we think this is a better for HTC's future. As a result of that, you will see the --- when we guided the operating margin to be around 1%.

So hopefully that answers you first questions here. I don't know, Joe, you want to just say in Chinese or I'll say in Chinese -- why don't I just say in Chinese here. (Spoken in Chinese).

Arthur Hsieh - UBS - Analyst

Yes. (Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

Let me answer this question here, and I'm just going to do it in English one by one and then -- your question, then I guess start in Chinese, and hopefully we'll try to get the format to work. Arthur, first question basically saying that typically your shipments start in October, is any specific reasons for that this year starting.

There's a combination of different things here. The channel readiness, partner readiness, the platform readiness, I think there's no specific particular reason which are causing the delay. It's the planning. Actually, it is all being planning according to our schedule here, so there's not particular reason to that.

Our product gross margin, how do we -- sort of the product gross margin, how much we make reserve here. I probably will not be able to tell you a very specific number, if it's just regarding some of our tactical decision here. I'm only here for six months, so I can't comment on in the past how we do it here. But you see, we want to make sure our product -- overall product gross margin is higher than this. Slightly higher than this, I wouldn't say a lot higher than this here, so probably due to mix on that. But we did reserve, yes, to clean some of the inventory in that.

So the third question Arthur is asking about the -- in terms -- I think you look at some of the slides here, it says the days payable outstanding 127 days, seems to be quite high. I will make the following statement here. Frankly, I kind of -- personally I do not want to put these numbers. It sometimes maybe a bit misleading here because that's not -- first of all, just to clarify, Arthur, this is not the channel inventory, it's inventory in house. And then days payable outstanding combined as a mature payable versus other payable.

And then you could take out only material payable, actually the days is actually much, much lower than this thing here, but just not to complicate things so we just follow the format, so we need to study this how to make it more sensible.



So I'll just stop here, anymore questions?

Arthur Hsieh - UBS - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). So want I just talked to Arthur is that -- his question is what are the area we're focusing most of our time there. I told Arthur here is that first of all, yes, we appreciate the market; it's very competitive. We're also watching the dynamics quite closely and there is quite a few lesson learned in last nine months here. There's one thing we focus quite clearly is continue to promote HTC brand and also having the right sales and marketing, the execution and also the right marketing message.

As the Smartphone continue to migrate, it has become very quickly a lifestyle product. So how to promote HTC brand, how to get the right marketing message, how to get the corresponding marketing and execution to us is a key priority and, Peter, our CEO, is also personally driving down this as well. So this is one area we focus a lot of time on it.

Arthur Hsieh - UBS - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Operator

CK Cheng, CLSA.

CK Cheng - CLSA - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). I'll quickly summarize in English here that, what we're seeing here, China market continue the momentum on our new Desire series. There will be a new successor for the new Desire series and we have a new China product called the One X, product in China [jargon] when retail call it -- it's called 528, because our new Desire series is called 328, so they go walking in there, they're buying the 528, the current momentum we're very encouraged by the initial momentum.

The US is performing in line with expectation. Some of the flagship product is well received here. What we need to focus on is in the European markets here both, developed markets and also the emerging markets and Europe, which we believe there's still room to improve.

Fundamentally, what we need to focus on is on the brand preference and consideration. On the awareness side, there is some piece and there is room to improve, but we think it's even more that important, or imminent is on the consideration and preference side.



In Japan market, we have a good success -- initial success on HTC J with KDDI and hopefully the new HTC Butterfly will continue that momentum. Some of the markets in Asia Pacific is also not up to what we expected. We understand some of the markets here especially some emerging markets here. We will continue to increase the distribution channel and also the local presence. I'll pause here.

CK Cheng - CLSA - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

CK Cheng - CLSA - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). Basically, what I just clarified a question here as -- what I said here is our quarter four sales and marketing expense budget allocation will be higher than quarter three and primary because of new product, not just because of that, we'll continue to invest because this is important for our future.

And in terms of whether this is including the employee bonus, all the number we included is all -- is all in cost in that regard.

Basically, the question about dividend policy will be more clear around the end of quarter or maybe our first quarter earning call. We're trying to migrate toward a direction which people can predict likely will be a certain payout ratio but that number we cannot finalize it yet until the first quarter next year, but yes, we are discussing internally.

CK Cheng - CLSA - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Operator

Rich Kramer, Arete Research.

Rich Kramer - Arete Research - Analyst

Couple of questions, I guess the first one, if we step back and look over the past couple of years, HTC has made efforts in content with watch and listen in Beats and now you're investing in enterprise.



Just from your perspective over the past six months, do you think HTC has the right management team in place and skill sets to provide services that are not related to the hardware or is the DNA of the Company as you see it going forward just to continually put out a stream of products and push them in from a sales and marketing perspective?

Chialin Chang - HTC Corporation - CFO

I think from our perspective here, I'll answer your question in a different way here is what we're focusing on is you can say, you call it a service. What we're focusing on more is at the end of the day how do we decide what the best consumer or customer or the end-user experience. That experience is important and with that you call it content, you call it service, we call it overall the package, overall offering, need to provide the right experience in that.

And that will require not just the -- and you say internal management expertise here than providing that, that requires a lot of internal expertise, hardware, software, UI, content or you call it the user experience service, all in one package and sometimes you make alliance with other partners here. Sometimes the partner require investment in there. Some times you don't. So it's overall package we are looking at it.

In terms of Magnet here, I don't think this is in conflict in terms the -- our investment strategy here. The enterprise mobility market, I think a lot of people are talking about it as well. It's going to be quite important as people access the information through the mobile platform, so which we think is a good important market. So we make the investment in a team. We believe have a track record and also a good cultural fit. Both teams already started working on it and will hopefully sometime next year will we have more information to report to everybody.

Rich Kramer - Arete Research - Analyst

Okay. And a couple of thoughts -- quick follow-up questions on the financial. First of all, can you walk us through the decline in overall cash and maybe comment a little bit about the cash flow and also what was the TWD1 billion difference between the operating profit and the pretax profit, was it just the write-down of OnLive or were there other factors in there?

Chialin Chang - HTC Corporation - CFO

The \$1 billion difference?

Rich Kramer - Arete Research - Analyst

The TWD1 billion difference between operating profit of TWD4.9 billion and pretax profit of TWD3.9 billion.

Chialin Chang - HTC Corporation - CFO

Okay. Let me (technical difficulty) and I'll just say -- answer your question just for the benefit of other listeners especially, some of our retail investor in Taiwan in Chinese.

First of all on the -- in terms of the cash flow, just roughly speaking, I'll give you a very quick sense here. At the end of second quarter, we had about TWD81 billion cash and in third quarter we did a few things. One, we pay out cash dividend, which is about TWD33 billion. We actually lent to Beat, as reported last time about the TWD6.7 billion or so, which is going to be due in one year. And we also pay out employee bonus and that actually is in the long-term incentive. So it's going to be spread out into the coming year but the whole package is putting the trust. So it is out of balance sheet as well in that. And we make an investment in there.

As a result of that, the cash level will be lower than what we have today, so the first item is our income for third quarter. Some of the amortization there is non-cash -- the non-cash item we added back here. And also we make a very good effort in terms, on the AR side here, so we'd get more



cash back here. So as a result, we had about the TWD50 billion. So more detail you can work the team here but basically that's the [high about] here.

And answering second question here on the -- between the difference of EPS or net income versus the operating income here. The two primary difference, one due to the OnLive write-off here was about \$40 million. That's the minus side. On the plus side, there is some tax benefit that we're not going to detail. Basically we have the deferred tax asset and as you know going forward in Taiwan the minimum tax is going to be increasing from 10% to 12%. So we evaluate the deferred tax as we request the content and we need to then realize that benefit, the product benefit in the third quarter. So that's only one time, as a combined of that. That's the result.

Rich Kramer - Arete Research - Analyst

Okay, thanks and maybe my final question. Just going back to the discussion we had in the last conference call. We asked last call about inventory and you said there was really no issue and now you're talking about reserves that you are taking on to clear the channel.

Are these reserves on relatively new products and what does that mean in terms of the clock speed of a Company and the shelf life of the products if you're having to take reserves on products that you really would have only shipped in the past few months or really would have been a very new fairly refreshed portfolio?

Chialin Chang - HTC Corporation - CFO

Actually to answer your question just to clarify here is -- when we talk about in the second quarter result and also back in the probably early June the call here, the reserve -- the write-off -- the impairment at that time is for the product shipped in December in fourth quarter last year here. And here when I provided guidance for the fourth quarter this year is a precautionary reserve we want to put aside just in case during the quarter we want to clean out some of the stuff here. So they're not in conflict, they're not actually related I would say. You can say clean inventory, it's the same thing but if there's two different time period products here in that regard.

And for us we, want to just going forward to on that front you are taking a more prudent approach. We're will gradually migrate toward the -- in that part here. But I wouldn't say -- I would just say this is part of that. I would say in a normal course that the inventory management in terms of channel, what we plan to do.

Rich Kramer - Arete Research - Analyst

Okay, thanks.

Operator

Robert Yen, Goldman Sachs.

Robert Yen - Goldman Sachs - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).



Robert Yen - *Goldman Sachs - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese).

Robert Yen - *Goldman Sachs - Analyst*

(Spoken in Chinese). The fourth quarter revenue guidance was down 15% quarter on quarter and you also mentioned fourth quarters product mix is actually improving. So, that means the shipment is actually down more than 15% quarter on quarter. Can I confirm that?

And my second question is, right now the fourth quarter is -- the revenue is actually lower than the first quarter's level. That means right now the situation is actually even worse than what having first quarter which was originally a very challenging quarter. And right now the new product only has like three months away life shelf space before supposedly you launched the new product in Barcelona, of course you will be the in February of next year. How do you manage your new product cycles for the next two quarters in order not to confuse the consumers again?

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese). So I'll just answer your question here. The second part of it was the, Robert, your question here is we believe the product announcement and ready on the shelf the new products starting in the fourth quarter this year, hopefully the momentum will continue into quarter one. And yes indeed every year we will have our flagship, sort of the hero product coming out. We believe from the variety on the type and also the price perspective here, it should be a good smooth transition into next year. So that to answers your first --- the second question. What's your first question, I even forgot already?

Robert Yen - *Goldman Sachs - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese). So let me answer your question here. In terms of China momentum here, I specifically said Robert, don't interpret that, because the China momentum, so China momentum means the revenue will be higher. That's why the rest of region in the world will be lower. So I do not want the mis-communicate that way. When I say momentum, it's overall momentum. China is also going through the product transition here. As I said, we have at the new Desire series, which we're going to have at the continued momentum with the new product here. We are also shipping a might the -- number call the One X specific tailor-made for China product, which actually is called 528. In China's jargon here, they're called 528 here.

If I may just add on one more here, in China we have very good plan and very strong -- the partnership with channels and also with the operators. We have good brand awareness and good consideration. We need to go from that basis here and the -- although what we're trying to do here is migrating people from the new Desire series, continuing that new Desire series or the successive product, the momentum and also migrating people up, because that's kind of the whole line to us in point. Not just for the brand, not just for the product, for revenue also for the brand in China.



Robert Yen - *Goldman Sachs - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese). Sales and marketing trend, this is optimal that took a resource allocation among regional activity, that's something we care. The second question here is, the efficiency in sales and marketing, also we care. And also the effectiveness in sales and marketing we care. So those three things we care. We recognize this is not area that we have done the best job here and we have a lot of room to improve and that we focus on and answered Arthur's question early on as well. This is the area we spend a lot of time internally.

Robert Yen - *Goldman Sachs - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese).

Operator

(Operator Instructions) Jasmine Lu, Morgan Stanley.

Jasmine Lu - *Morgan Stanley - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese).

Jasmine Lu - *Morgan Stanley - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese). So my question here it's just for the transcript, English transcript purpose here is. As I said, here October revenue, lower than September and November revenue would be based on what we're seeing today, it will be higher than September. And hopefully will carry through the momentum into the December. That's what we guided the TWD60 billion here.

And Jasmine asking in terms the inventory in house, this is part of the supply chain issue here. We're trying not to put a lot of materials in-house. Some of it actually is still open order here. So we wanted to -- this part of supply chain management perspective here. And maybe partially that explain our October revenue here but I wouldn't sort of read too much into it for our overall December quarter, so December quarter number is what we've guided early on.



Jasmine Lu - *Morgan Stanley - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese). So I just said a couple this here is; one, yes, we do see a bit lumpiness in the monthly sales here and therefore a kind of revenue scale we have today, that may be more invisible in terms of monthly lumpiness.

Second thing here is that the product cycle due to competition or any other reason here, we do see the product cycle is not longer than we'd want it to be, and that's why it's very important for us to continue to extend the OnLive product, that's basically we need to continue investment in brand, because important not just promoting the product spec, the product features, it's also the overall HTC brand. We want the consumer to feel like whatever product HTC product they buy, they have the kind of sense of coolness, which we think is very important.

Going into the provision for the potential channel inventory, I would encourage people not to read too much into it here. We think that's just a prudent way of doing things. In terms -- making sure that we have -- we are more prepared in terms of managing the new product and also product into the channel, we have better management, that's all.

Jasmine Lu - *Morgan Stanley - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese). So my question to Jasmine here is that the, when you're looking at sales and marketing on overall absolute amount or just looking at ratio of percentage of revenue, you look at both facets here. But it's important in the December quarter, not just for new product launches, not just for the competition, also we need to have a continuing brand building in terms of our voice being heard by consumer over the world here. So that going into 2013 to us is important.

So we're continuing to make that investment because the brand equity needs to be accumulated. With that said, yes, given the fluctuation in quarterly sales, do we look at the ratio? Yes we do look at but we need to make a conscious decision combine those two factors here and decide what we need to do and then that's what we decided for December quarter.

Jasmine Lu - *Morgan Stanley - Analyst*

(Spoken in Chinese).

Chialin Chang - *HTC Corporation - CFO*

(Spoken in Chinese).

Jasmine Lu - *Morgan Stanley - Analyst*

(Spoken in Chinese).



Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Jasmine Lu - Morgan Stanley - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Jasmine Lu - Morgan Stanley - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

So what I just said to Jasmine here is that she said that can we expect the operating expense to between TWD10 billion to TWD14 billion. Obviously this is pretty big range in that. And I basically explained to her that we'll continue to invest this is very important for not just competition not just the new product here and also continue our brand building and momentum into 2013, so we make the conscious decision into December.

For the range TWD10 billion to TWD14 billion operating expense that's the range relatively big here, but that's the range we probably -- you can expect in coming quarters in that year.

Operator

[Julia Tai], UBS.

Julia Tai - UBS - Analyst

Hi. Thank you for taking the question. (Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). I did not -- I also mentioned in US market as well, say US market in third quarter in my expectation here we have some new product going into US market as well and we will hopefully will continue that momentum.

Julia Tai - UBS - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). I did not say what you said here, I said the guidance about 23% I guess part of which -- overall product mix issue, overall product gross margins is higher than 23% and I stop at that point.



Yes, we indeed have some provision for potential channel inventory and we will continue to take that similar approach in a prudent way here and that's how our comments just here.

Julia Tai - UBS - Analyst

I see. And then how much would that amount of provision be in Q4, if you can share with us?

Chialin Chang - HTC Corporation - CFO

I cannot share with you unfortunately, I mentioned that, I apologize that.

Julia Tai - UBS - Analyst

Okay, and lastly this is actually maybe a hopefully a answer for me. HTC J Butterfly seems to be a very good product and available only in Japan. I was just wondering when are you going to make it available internationally including Taiwan.

Chialin Chang - HTC Corporation - CFO

It's our Company policy that we would not comment on the potential future product that's not yet announced and well, I would only say that the we care our Taiwan customers here and then the HTC always -- this our home market so this is the market we care very much.

Julia Tai - UBS - Analyst

Thank you.

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Julia Tai - UBS - Analyst

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Operator

(Inaudible), Infinity Capital.

Unidentified Participant

(Spoken in Chinese).



Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). To answer to your question here is we've recognize that, it will probably not proper for us to compare HTC product with competitors product in the market. What I would say here is the we recognize the smartphone has become a lifestyle product here so it's very important not just to have very compelling and competitive product but also carry through with your strong marketing message and marketing execution.

The overall package to us is very important we recognize that we'll continue to optimize our overall infrastructure message and team spirit and also to improve from that.

Unidentified Participant

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).

Unidentified Participant

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). So I'll just say that -- yes, in terms of some of the select people leaving or departing HTC I'd just make a few comments. One, I say I would just not make specific comment on individual person, for the person who has actually left the Company here, we respect their career planning. And we also thank them for their contribution to HTC.

Second comment I make here is, yes we're facing challenge, we recognize the challenge, we recognize the competitive dynamics here, but I would not look too much into that and to magnify the individual situation to paint a overall situation in the HTC especially when we're facing the challenge the people like to have a different, looking this as to paint a different picture HTC. But my understanding HTC and I'd just be candid, when I stay in a company during the day here tend to be really long, what I see my peers, my direct staff and the team here, the people are very motivated. And to us HTC is open entity, we learn, yes, we have challenges we make mistake, we learn our lessons here. But we are very motivated, we want to go through the challenge and hopefully get into the next level a better level for us.

Unidentified Participant

(Spoken in Chinese).

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese).



Operator

(Operator Instructions) [Sean Louie, JJ].

Sean Louie - JJ - Analyst

The question I want to ask is on the R&D side of things. You've talked about your OpEx wanting to keep that between TWD10 billion and TWD14 billion going forward. So R&D is a portion as a percentage of your sales. What do you expect that to remain over the course of FY '13 looking forward?

Chialin Chang - HTC Corporation - CFO

R&D level here, I think I would say R&D level you can, I don't expect big changes there are some changes sometimes due to some pilot. There is some pilot tests here we're put in part of R&D. There's some project expenses some time maybe on and off depends on number of projects we do for the upcoming quarter or two quarters, but overall R&D level I will say in the coming year will be roughly around similar level I will say.

I won't say specifically a number in that, but I wouldn't see really big changes in the R&D. One second, our IR just wants to show me something. What are you trying to tell me?

I wouldn't comment on the percentage what I'd just comment on is on the absolute number. I don't see a big fluctuation in the absolute numbers. There may be changes due to some project expenses maybe on [pile] around that a little bit there, but the overall R&D I think is stabilizing.

Sean Louie - JJ - Analyst

Do you want to translate that or shall I follow-up with the second question.

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). Okay, go ahead.

Sean Louie - JJ - Analyst

Okay, I've listened to what you said about OpEx costs and looking at your -- the trend of your GPM, here is my question. For next year, I mean I see that we are going to have a 1% OPM level for Q4. If you're going to keep your OpEx at TWD10 billion to TWD14 billion, that's assuming that your revenue run rate has got to remain somewhere above the TWD60 billion mark, somewhere around that.

And looking into next year Q4 is obviously an uptick because it's a good quarter. So TWD60 billion for Q4 let's assume that. Looking forward Q1, Q2, Q3 of next year if you don't have successful product launches that revenue could actually drop below that, which would mean that you're going to go into a loss making scenario.

So listening to what you're saying about the fact HTC is a lifestyle product or smartphones are a lifestyle product et cetera and you want to appeal to your customer et cetera and I am one of them. Then what are you going to do to make sure that you don't become a loss making company and that cash pile of TWD50 billion that you have now isn't going to halve again same time next year? I apologize for just asking for the question.

Chialin Chang - *HTC Corporation - CFO*

No, problem, then I apologize I won't be able to answer in kind of granular manner I think you desired here. What I was saying here is obviously it's probably not proper for me getting to that speculation, but I will say the following here. Profitability to us is important. But continue to invest for the future is also very important here.

We are going to expect our revenue next year to be something like this and that's not obviously what we want to expect, we want to expect that. We believe into the fourth quarter this year, into the next year we're pretty confident about our products, what we need to make sure is would the product -- do we offer the right marketing message and execution that too us we need to get it right here.

So we obviously -- our current infrastructure is a design for us to be a higher revenue run rate in that and either on the overall fixed infrastructure or on the sales and marketing budget in that regards. That's how we plan for it.

In your scenario here we will adjust accordingly here. So in that scenario profitability to us is important, but I want to emphasize here obviously we don't want to get into that scenario. We think with this thing here we think we should have a better outlook into next year. So did I answer your question not directly here, but I think touched on the main points.

Sean Louie - *JJ - Analyst*

Yes, I think I understand that that effectively what you're saying is that you're implying that next year's revenue must remain at above Q3, Q4 levels that we're seeing in the second half of this year?

Chialin Chang - *HTC Corporation - CFO*

No, what I --- yes to some extent that's what I say here. I said our infrastructure either fixed infrastructure or flexible infrastructure is designed to have a higher revenue run rate here. So it's probably not appropriate for me to get into the scenario as you speculate here, but if the scenario like that happened to us profitability is important. So I will just make that that two comment.

Sean Louie - *JJ - Analyst*

Yes, thanks very much and let me just say one final thing then I'll leave. In those circumstances could we potentially expect some write-down on the OpEx side, so for staff or for some write-down in terms of your assets because it could very well be that, is there a possibility that we could expect some write-down that hasn't quite come yet in order to bring your OpEx down?

Chialin Chang - *HTC Corporation - CFO*

The OpEx, you mean write-down, what does that mean write-down of staff, you mean the cost-cutting?

Sean Louie - *JJ - Analyst*

Yes, sorry cost cuttings is all I mean, yes.

Chialin Chang - *HTC Corporation - CFO*

And then write-down because I want to clarify when you say write-down of asset means impairment or what?

Sean Louie - *JJ - Analyst*

Talking about impairment of assets, provision for employee pay that you would have to make it if you it's -- cost associated with cutting. So for example in the US or Europe or even in China for example?

Chialin Chang - *HTC Corporation - CFO*

Yes, so let me answer your question here that and I'll say --

Sean Louie - *JJ - Analyst*

Sorry, that's my last question.

Chialin Chang - *HTC Corporation - CFO*

I'll phrase in different words here. I'll phrase in a different way here. Our operating expense and all people ask me a question without going into any specific detail I'll just qualitative saying the following. Our operating expense, yes, contains both the flexible infrastructure and also the relatively fixed cost in that regard. The flexible part of it is actually it's a pretty big part of it, it's not like (Inaudible) (1:22:03) operating expense is actually fixed nature. So we have flexibility in that regard.

And again I do not want a whole --- certainly hope we do not get into that scenario you've depict here. But when this scenario happens here we hopefully not. By if happen possibly to us is --- I'll stop here, but again our infrastructure and our investment are continued investment is actually done in anticipation to a budget outlook into 2013.

Sean Louie - *JJ - Analyst*

Okay. Thank you very much, Chialin.

Operator

(Operator Instructions).

Rich Kramer, Arete Research.

Rich Kramer - *Arete Research - Analyst*

Thank you very much. Just to add one question. If we're looking out into 2013, HTC has been trying to preserve this mid or high 20s gross margin for some time and it's clear that there is a very vast low-end smartphone market developing.

How do you think about the trade-off between accepting lower gross margins but looking for a larger top line, which would support the sales and marketing expense that everyone has asked about already. I know there is some members of the management team and team philosophically oppose to going down market but others of the team to think it's necessary but what's your view on accepting for example to try to get an extra TWD10 billion or TWD20 billion of sales, 20% or a lower percent gross margin on those products. Thanks.



Chialin Chang - HTC Corporation - CFO

Right, I know -- thanks, Richard. I know your question here then I will say the following way here. The way we see internally here obviously the overall shipment and revenue growth is not in exactly direct conflict with the overall gross margin or the overall gross profit.

Obviously, part of it is due to your product mix. Our current view here is we want to grow the shipment and we want a grow the revenue here. At the same time hopefully we'll also grow our overall gross profit maintain a healthy gross margin in that regard.

When you say that low end there's always the definition about what exactly is a low end or an affordable and in that regard. To us we have a product lineup from the [flat] all way down to our (inaudible) notes the four product coming out of HTC, we call it the Desire C in that regard.

To us there is a overall growth potential issue and then also there is a brand building issue here. We think it's very important that you at the different price segment from the coming from the top hero end and to one step down, two step down, and three step down into the Desire C, that you will have the market share you should get.

And then from that we grow from that. Can we expand broader into a broader price bank, yes, potentially, but it's very important when you think about that. Have you actually maximized your potential in each price band you currently are. So those are the two issue we do get -- we talk about it.

We're not necessary got stuck or hung up on say we're not going to specific price bank period. We actually ask two questions not just the question you asked and also for each price plan, and have you really maximize our potential in market share which we have. So relatively we consider here.

In the end, hopefully what we see here is that you get the growth on the revenue and also total shipments here. Your gross margin and resulting gross profit will not be too far from that.

Rich Kramer - Arete Research - Analyst

Okay, thanks very much.

Operator

(Spoken in Chinese). There are currently no questions in line. I will pass the call back to CFO, Mr. Chialin Chang for closing remarks. Mr. Chang please begin.

Chialin Chang - HTC Corporation - CFO

(Spoken in Chinese). And I guess we know we are going to end this analyst call. And thank you for all your participation and we look forward to see you probably in three months again. Thank you.

Joey Cheng - HTC Corporation - IR

Thank you everyone.

Operator

(Spoken in Chinese). Thank you for your participation in HTC's conference call. There will be a webcast replay within an hour. Please visit www.htc.com under the investor session you may now disconnect. Good bye.

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