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# EDITED TRANSCRIPT

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**Kylie Huang** *Daiwa-Cathay - Analyst*

## PRESENTATION

### Operator

Welcome everyone to HTC's 2013 Q3 conference -- results conference call and webcast in English. Today with us we have CFO, Mr. Chialin Chang, and IR Manager, Ms. Christine Chi. (Operator Instructions) After the presentation, there will be a question-and-answer session for investors and analysts.

(Operator Instructions) For your information, this conference call is now being broadcast live over the Internet. Webcast replay and English transcript will be available within an hour after the conference is finished and Chinese-translate transcript will be available within a week after the call is finished. Please visit [www.htc.com](http://www.htc.com) under the investors section.

Now I would like to introduce Ms. Christine Chi, IR Manager. Ms. Chi, you may begin.

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**Christine Chi** - *HTC Corporation - IR Manager*

Okay. Hi everyone. Good morning, good afternoon, and good evening, ladies and gentlemen. Welcome to HTC's 2013 third quarter analyst call. This is Christine Chi, HTC's IR Manager.

The event now is being broadcast live via HTC's webcast at [www.htc.com](http://www.htc.com). If you are joining us through the dial-in line your call is now being placed on mute. As the conference is being broadcasted by investors around the world, we will conduct this call in English only.

The format for today's call will be as follow. First I will help to summarize the operation for third quarter 2013, followed by our guidance for the fourth quarter. Afterwards, our CFO, Mr. Chialin Chang, will lead a Q&A section.

Before we begin I would like to draw your attention to the disclaimer statement on page 2 of the presentation slide. I just sent out the presentation slide three minutes ago. Please check your e-mail.

Please note that this presentation contains forward-looking statements. These statements are based on current expectations. Actual results may differ materially from our expectations, and the Company undertakes no obligation to update this forward-looking statement going forward.

If you have no question, I may begin to give the overview of third quarter 2013.

Please turn to page 3. Page 3, third quarter financial highlights; revenue for third quarter was TWD47 billion with gross margin of 20.4% and operating margin of negative 7.4%. Net loss was TWD3 billion and EPS was [minus] (Company corrected after the conference call) TWD3.58 per share.

Product innovation for this quarter; building on the success of award-winning HTC One, in the third quarter the Company introduced HTC One mini and HTC One max, delivering a family of device that offers something for everyone.

The launch of the new midrange Desire 601 and entry-level Desire300 further expanded HTC's portfolio enabling consumers to enjoy the premium experience at any price point.

Finally, HTC released a blue edition of the HTC One and a limited edition HTC Butterfly s Hello Kitty phone, bringing a fresh and unique approach to product design innovation.

Page 4; our new Here's To Change campaign affirm HTC's role as the change maker challenging the status quo since dawn of the mobile industry as well as our mission of continuing to bring change into hands of people around the world.

Awards and honors; the third quarter also celebrates the HTC One winning further from most of the influential consumer technology titles, including Phone of the Year in 2013 by T3 in addition to best European best European advanced smartphone 2013--2014 by European Imaging the Sound and Association (sic).

Furthermore, HTC Change campaign featuring Robert Downey Junior also significantly ramping up consumer's engagement and positive sentiment increasing advertisement awareness by 12% and brand momentum by 15% in the market that the campaign were aired.

Page 5, investment recaps; after 2 years of working together, HTC sold back the remaining 24.85% stake in Beats Audio for the total payment of \$415 million and focused on the development of its own proprietary sound technology, the HTC BoomSound which already is receiving positive industry feedback, seamlessly integrated hardware and software algorithm, delivering ultimate audio experience to consumers.

Additionally, HTC sold 100% of its stake in digital content provider Saffron Digital for \$47 million, retaining permanent royalty-free license to its own worldwide media services.

Page 6, regional update; during the third quarter HTC saw sustained momentum in EMEA region while maintaining number one market share in Taiwan. For the first time through the launch of new HTC One by Verizon, HTC became available across all four major carriers in the US, and in China the HTC One max is expected to be available as market's first wave TD-LTE products, marking another milestone for leadership in global 4G technology innovation.

Page 7; page 7 gives an overview of revenues and operating profit. Revenue for third quarter came in at TWD47 billion. Operating profit reported a loss of negative TWD3.5 billion.

Page 8; page 8 gives an overview of gross margin and operating margin. Gross margin for third quarter was 20.4% and operating margin for third quarter was negative 7.4%.

Page 9 and 10 were financial overview for income statement and balance sheet. And page 11 the guidance for fourth quarter of 2013. Revenue is expected to be in a range of TWD40 billion to TWD45 billion. Gross margin is expected to be 20% plus or minus 1%. EPS is expected to be in the range of TWD0.1 per share to TWD1.7 per share.

This wraps up the content of our presentation, and now I would like to turn the podium to our CFO, Chialin Chang. Moderator, please start the Q&A section.



## QUESTIONS AND ANSWERS

### Operator

Thank you. We will now begin our question-and-answer session (inaudible) to investors and analysts. For media please contact HTC PR team after the call if any question. (Operator Instructions) Arthur Hsieh, UBS.

### Arthur Hsieh - UBS - Analyst

I have a question about the operating expense target for the coming quarter and also in terms of the non-ops, is there any item in addition to the Beats disposal and what's the normalized operating expense that you foresee?

### Chialin Chang - HTC Corporation - CFO

Arthur, thanks for the question. I'll answer in two parts, first of all on the operating expense, we're trying to target in the quarter four will be, just to give you a specific number here, we're trying to aim for the TWD10 billion below. So we don't want to go above TWD10 billion. Obviously depends on the situation when it arrives. That's what we target in that. And in the coming quarter it depends on the run-rate, so some of the expenses variable part. We talked about in previous quarters. So it varies.

So it depends on the run-rate. And this is a guiding principle based on the current run-rate. Obviously we want to hopefully going up for a higher run-rate in the coming quarters there. That's where we are in the -- in quarter four.

Your second question is about the operating margin, how we see the coming quarters. If that's it, I already answered, but if not, the -- anything else you want to ask?

### Arthur Hsieh - UBS - Analyst

Sure. The question is in addition to the Beats disposal gain, is there any other non-recurring items that's foreseeable in the fourth quarter?

### Chialin Chang - HTC Corporation - CFO

As far as I know, the non-operating income part of it, yes, it's primarily coming the Beats. If there's some other thing, they're pretty small.

### Arthur Hsieh - UBS - Analyst

Okay. How about the tax?

### Chialin Chang - HTC Corporation - CFO

How about what?

### Arthur Hsieh - UBS - Analyst

Tax, is there any like tax credit or lower effective tax rate?



**Chialin Chang** - *HTC Corporation - CFO*

No, there's no tax benefit.

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**Arthur Hsieh** - *UBS - Analyst*

And on a separate subject, would you comment a little bit about the recent market chatter about the potential investment by, like, carriers? What's the management's attitude in terms of taking potential investors from the carriers?

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**Chialin Chang** - *HTC Corporation - CFO*

Potential investors by carriers, you mean like strategic investment?

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**Arthur Hsieh** - *UBS - Analyst*

Right, like -- the one that's being circulating is the China Mobile in a news report.

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**Chialin Chang** - *HTC Corporation - CFO*

I want to be very clear on that, and first of all, our policy is -- I can tell you two things; one, our policy is we obviously don't comment on the market speculation or rumors because it's going to cause -- it's going to exacerbate things. Second here, as far as we know we're not aware of any of those sort in nature.

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**Operator**

(Operator Instructions) Brad Erickson, Pacific Crest.

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**Brad Erickson** - *Pacific Crest - Analyst*

First off, just -- I'm trying to get a sense for looking out to the March quarter at all. Is it fair to assume a normal or somewhat normal seasonality in the March quarter given the step-down we seem to be taking in December?

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**Chialin Chang** - *HTC Corporation - CFO*

Obviously, it's probably not proper for me to comment beyond the December quarter given the regulation and given our past practice here. But obviously what I will say is the following here; every quarter beyond this coming quarter, even in the quarter now, there is always tactical things we can do on various things in pricing, on channels and everything, promotion, et cetera.

So our goal, as we stated in the very beginning, our goal is to see a sequential momentum, and that's what we aim for. But beyond that I won't be able to comment on anything specific.

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**Brad Erickson** - *Pacific Crest - Analyst*

Got it, no problem. That's helpful. And then just can you kind of give us a sense of the ASP trends you saw and any of the dynamics behind those in the fourth quarter as well as kind of how we should be thinking about ASPs going forward?



**Chialin Chang** - *HTC Corporation - CFO*

I think, to be very honest, I personally don't really track the ASP that much to the extent that the -- I'll just comment on the following; I personally track where we are in each different price band, what should we be in that price band, the market share or volume we should have. And ASP will be resulting the product mix in there.

For each specific product, market obviously dictated the final price and there is some sort of negotiation, the fluctuation among that. And largely as a average, the Company's ASP in my view will be largely coming from the product mix rather than the pricing. Every price band has always various degree of pricing pressure. In the lower end you're going to have a higher pricing pressure. In the higher end you're going to have less pricing pressure.

So you have individual nature of that, but as overall Company ASP is largely coming out of product mix in that. So that, I will say that. The reason I made this comment here is as we talked about it in the previous quarter that we do need to gain back our deserved market share in the mid-tier and affordable end.

If we gain more market share as a result of product mix, your ASP may look a bit lower than the ASP coming purely from the higher end, but that doesn't necessarily indicate a negative trend. So that's why I want to just make that kind of longwinded comment.

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**Brad Erickson** - *Pacific Crest - Analyst*

Got it. No, that's useful. And then on that front, so it sounds like you guys are getting a little bit more aggressive at the lower end in Q4. Is that kind of the direction we should expect going forward or is that just more like a Q4 phenomenon that you're speaking of?

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**Chialin Chang** - *HTC Corporation - CFO*

I want to clarify what you said here. We're not gearing toward the lower end of the product segment. As we said, if we forecast correct, we'll be ending, by the end of Q4, our Hero product will be selling better than our corresponding Hero product in 2012. That we said it last quarter, we'll continue to say that overall if you aggregate it for the entire 2013.

And looking forward, beyond providing specific comment here, we actually -- our internal goal is to continue to ride on the momentum, to aim for higher goal. In addition to that, what we aim for is to fill a few holes that were created as a result all sorts of reasons.

So we want to gain back, and I can tell you in the similar quarter last year or actually the entire last year, our mid-end market share is actually quite decent, and that's where we need to do. We got to go down to affordable end as well. So our product platform will be, hopefully, in the coming quarters broader, but doesn't necessarily mean in this quarter or in the coming quarter we are just going to tilt it toward the lower end. And obviously when we talk about this mid-tier affordable low end, we need to define very specifically what we mean by the different price band.

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**Brad Erickson** - *Pacific Crest - Analyst*

And then one last one if I could. You mentioned the OpEx levels for this quarter. It sounds like you've ratcheted things down pretty well. Is that kind of the new run-rate we should expect going forward or are there -- is there -- are there further efficiencies to be gained there going forward? And any color on how to think about that would be helpful.

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**Chialin Chang** - *HTC Corporation - CFO*

Yes, I'll just elaborate a little bit on that, and it's a combination of different things. Some of the folks asked a similar question here, is our tax as a percentage of revenue are still one of index that we look at it? Yes, we do monitor that. The actual OpEx level is also what we look at as well because -- simply because OpEx consists of both variable and a fixed part of the things.

Based on the current run-rate, as we guided for quarter four, we think it's appropriate to target TWD10 billion or below. And we believe that the resources are enough to support the current run-rate. As we said, we're aiming for higher revenue run-rate in the coming quarters and with that kind of momentum and then the operating expense would be adjusted according for that the -- for that reason.

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**Brad Erickson** - *Pacific Crest - Analyst*

Got it. And then one last one. Just on, obviously the Beats gain is clearly contributing to the overall profitability, but just any help on how we should be thinking about profitability in 2014 would be helpful. And that's my last question.

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**Chialin Chang** - *HTC Corporation - CFO*

Right, thank you. The Beats, as you said, so I won't comment further on that. In terms the -- we would -- we will comment on the following; a lot of people are asking the question, are we aiming for higher market share gain in terms of units or are we aiming for profitability. My answer is we are aiming for both. And it's my personal view that if you get higher market share your profit tend to optimized, I wouldn't say necessarily always maximized but will be optimized.

Your margin may vary from time to time, depends on various price band margin for individual products here. But what we aim for is only selling a product, we're not cleaning the end-of-life inventory. It's only selling product by -- in the normal course of business here we hope aim for a higher volume, and as a result of higher volume we think the profit, the product profit will be optimized and will not be too far from being maximized. That's my personal view.

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**Operator**

(Operator Instructions) Alban Cousin, Arete Research.

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**Alban Cousin** - *Arete Research - Analyst*

Could you just focus through how we should think about gross margins and what are the different positive and negative to expect in the next few quarters, and whether we getting out of this 19.5% or 20% range really depends on volumes or other actions you can take?

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**Chialin Chang** - *HTC Corporation - CFO*

If I may elaborate little bit more based on what I just said and also what I commented in the previous quarters, gross margin, the overall average gross margin of the Company is the result of product mix, and now typically, not always the case, I will highlight, but typically the higher-end product you have tend to have higher gross margin.

So if you measure a company's overall gross margin, it's a combination of one, the product mix, the gross margin of each product in a different price band and the resulting product mix and the result in the average gross margin.

And then going forward, in the coming quarter after we launch the product will be combination of price erosion and the ability to cost down so that we get the end gross margin.



And as we said in the earlier case, we're aiming for higher volume and we believe higher volume tend to give you a better profit. And I tend to use the word profit will be optimized, not necessarily always maximized, but I don't think it'd be too far from being maximized.

When the profit is maximized or optimized, your gross margin may vary from a trend line you target, but I personally don't believe will trend too far from where we are.

So that's something we aim for in 2014. We're not aiming for -- I personally don't believe that we would have -- in my view, we will have a huge volume, the margin tend to be a lot lower than what we have today. I don't think it should be too far from what we have today, if you have me look forward into the future, and that's how we monitor ourselves as well.

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**Alban Cousin** - *Arete Research - Analyst*

And then if I can just follow up, I mean how do we think about in some markets where you haven't been present today we'll see Lenovo, Intel's EMEA market or even the US. They're coming with very lower gross margins and arguably very good product design as well. How should we think about, how do you alleviate pricing pressure even on the high end?

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**Chialin Chang** - *HTC Corporation - CFO*

Yes, the -- I won't be able to comment specific name of competitors. And we obviously monitor each competitor, their footprint, where they're doing well, what product segment they're doing well, et cetera, and how they set the price migration.

So that would be monitoring and we are actually paying quite a lot of attention to that as well. That's number one without commenting on a specific name here.

Number two, the pricing pressure is always there. This is not new. And certain price segment when it gets into more mature, or some people would say getting commoditized, you may have even more severe pricing pressure.

To us, brand is important, price performance ratio is important, time to market is also very important. Pricing is one thing. The ability to get a faster time to market, this is one of the strengths of HTC, hopefully the thing we have is a combination of those.

In market where we believe we can do well, obviously channel strategy is also one part of it. We can do well with a combination of those things, determine how we price things, how we set the volume, how we get the profitability.

And different markets have different competitive nature as well. But I won't be able to generalize things, but what you say here is some of the vendor tend to lower the price in order to get into a certain price segment, yes, that happened all the time and make it more intense, especially on the lower end of the price segment, but that's what we're facing every day.

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**Alban Cousin** - *Arete Research - Analyst*

I suppose my question is just if you look over the last two years and the trend in gross margin, the competitive intensity in the market has only worsened. So I'm just trying to understand how we can prevent from gross margin going further down in fact.

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**Chialin Chang** - *HTC Corporation - CFO*

The combination of gross margin in simple terms is basically a balance of your cost structure as well as the pricing ability. And different price band you have, you can set a different pricing ability. And then I would not ignore the importance of time to market. For a -- I can give you a very specific example here.



For a very -- I will give you a very specific example here. For a RMB1,000 product, retail price, RMB1,000 to RMB1,500 product here, if you miss a window three months, then it doesn't really matter, your pricing, your margin, et cetera.

So that's because the shorter lifecycle of that product. So getting into the market early, that fit into the consumer need at that sweet time window, at that sweet price is more important.

But not necessary to say, okay, I -- they're getting lower, so we're getting no -- the hasn't matched the price. And if you get the right thing happen and if the market does not come out again very strong, it can last -- tend to be longer with a greater momentum because they're catching more attention.

So there's different factors into it. It's not simply a case, they're going price it lower, they're going to live with a 5% to 10% margin, what would you do? I think it's a combination of those.

As I said early on, to come back to my main point here is, we want to get better volume going forward to have a high revenue trend in the coming quarters here and we want to optimize or, you say, maximize the total profit, but the -- we want to just maintain, we hope, the gross margin not too far from where it has been -- not too far from where we are today.

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**Operator**

(Operator Instructions) Arthur Hsieh, UBS.

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**Arthur Hsieh - UBS - Analyst**

Just to follow up; usually in the fourth quarter it's a seasonal high quarter for the like Christmas shopping. So just wondering from management's point of view, how would you attribute to this sequential sales decline in the fourth quarter this year?

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**Chialin Chang - HTC Corporation - CFO**

There is a combination of different factors in terms of timing in introducing in the market and the shipment of the product. There is a different in terms the shipment in revenue, the revenue recognition shipment versus the so-called holiday season, the sell out in there.

What we've guided the market, there is a slight decline quarter over quarter from the third quarter. We recognize that. And I won't be able to comment specifically on, down to each product line in there, but as we said here, we're doing very tactical things here to gain the momentum beyond the quarter four.

And when you comment on the specific shopping season here, a lot of things, we want to focus on the sell out obviously. So you can have more sell out, you're going to have more sell-through and sell-in in that regard, not just for Christmas but also for -- we're planning for the Chinese New Year as well.

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**Arthur Hsieh - UBS - Analyst**

So if you compare with third quarter, is the decline more coming from the open channel or is it more coming from like wireless carriers?



**Chialin Chang** - HTC Corporation - CFO

I don't think they're specifically coming from more of the open channel or the operators or a mixture of this. And the -- I won't be able to -- there are some market performing better compared to the others. Due to competitive reasons here I won't comment on those specific markets in there, but I think it's probably not related to, tilted more into the carrier-subsidized market or the open-channel market. I won't attribute to that.

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**Arthur Hsieh** - UBS - Analyst

All right, in terms of the inventories, I think previously there were some excess inventory that the Company tried to work down. So that's, apparently that's not your inventory, that seems to be like your partner's inventories. So could you give us an update in terms of a latest market inventory situation?

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**Chialin Chang** - HTC Corporation - CFO

Right, we talk about inventory. We always -- we talk about there is a in-house material inventory, there is the inventory in a channel, and I assume what you meant is the inventory, the device we sold down in channel either in the warehouse or down at the retail outlets there.

In terms of channel inventory here, what I would say the following, it's it has improved quite materially from the last quarter when we reported our numbers and made that comment. Obviously this is something we track pretty continuously, not just on a weekly basis, it's sometimes a few times per week from various regions, and various countries, and various account.

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**Arthur Hsieh** - UBS - Analyst

That's good to know. Just the last question, in terms of the margin, obviously despite your overall sales could decline, but you still manage to maintain relatively stable that kind of gross margin and do you factor in any kind of a new product contribution that could help to lift the overall margin profile or is it more because of your really trying to reduce the cost structure or taking any activities trying to really manage the margin profile here?

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**Chialin Chang** - HTC Corporation - CFO

Arthur, do you mean the gross margin or operating margin?

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**Arthur Hsieh** - UBS - Analyst

Gross margin; I think we talked about operating previously, so could you also shed some light on this gross margin?

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**Chialin Chang** - HTC Corporation - CFO

Right, the gross margin, as I commented earlier, there to me is more the product mix. Obviously, for individual product it will be a combination of pricing at that given time versus the ability to cost down there.

I don't necessarily think that we have a similar gross margin as we had in 2000 -- in third quarter is because a contribution from a new product with better margin to make up for the shortfall of existing in-life product.

I don't think it's the case. I think it's pretty well balanced. For the in-life product, I think our margin, I did not see -- obviously take out the end-of-life, we're trying to clean up. For the in-life, in-force product here, I don't see a material deterioration in the margin overall without commenting on specific product.



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**Operator**

(Operator Instructions) [Abul Chen], [Infinity Capital].

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**Abul Chen - Infinity Capital - Analyst**

This is my first question. What do you think 4G will change smartphones? How do HTC think, the 4G change will be as big as what happened in 2G and 3G era, or 4G is just normal then an improvement of connections made?

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**Chialin Chang - HTC Corporation - CFO**

Yes, the, I would say -- I would answer your question -- thank you for your question, this obviously is pretty big question. I will first answer with starting try to paraphrase what our Chairman said.

She believes, we all truly believe we are still in the early stage of mobile revolution in there and 4G would greatly alter quite a lot of things. And in fact HTC back in November or October, I forget the -- we actually just had a 4G LTE forum in China and to promote the importance and upcoming the revolution due to the arrival of 4G.

HTC has been always at the forefront of technology revolution facilitating the adoption of consumers. We are the first -- we actually introduced the first 3G smartphone. We also introduced the world's first 4G smartphone. We enabled quite a few global carriers in the early part of the 4G adoption and the -- captured quite a lot of consumers.

We aim to do the same for China, also for the rest of the world. And as we said it in the -- I believe we have -- we indicated in some of the slides we sent out, we just introduced the first 4G TD-LTE product in China as well. So we aim to be at the forefront and we believe it would continue to encourage the consumer adoption and HTC definitely will be one to capture a big part of it.

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**Abul Chen - Infinity Capital - Analyst**

Okay. My next question is about the mid-end phone strategy. I think that HTC's strategy is to success in flagship form and then therefore reach this success to mid-end phone. But now it seems like this strategy doesn't work well, because smartphone industry -- because iPhone 5c sale is not good and HTC's new phone, mid-end phone this year dropped too. What do you think about this strategy right now, and what are your future strategy of mid-end phones?

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**Chialin Chang - HTC Corporation - CFO**

First of all, I want to clarify what you said here is HTC's strategy is not just focus on the high-end phone. We believe we are one of the very few smartphone vendors who can actually range our Hero devices in the broadest operators and channel partners possible worldwide. We are one of the very few.

Because of that, because of the partnership and because as a few years effort on the brand, we are able to range broadly our product at various price band. So we're going to compete quite actively in the mid-end and also we're going to compete quite effectively in the affordable end. We will not do in the very ultra low-end. A lot people asking we sort of tend to use the term quite loosely here, but without going into the detail, there is a definition of different price band. To me the price band is actually quite important.

So we will compete. If you say in the mid-end, I'll just clarify in your question here is somewhere around say \$150 to \$250 or slightly higher in that, we will compete quite aggressively. We aim to get the market share we deserve on the very high-end, and the mid to high-end, mid-end, and also affordable end.

And the strategy for doing that to us is pretty straightforward. Well, hopefully we have been seeing a premium brand in the high end. What we need to do is very important to have one, time to market; second, couple with the right brand; and third, the design and innovation.

I think even for people buying the mid-end product, the design innovation is quite important in addition to obviously the brand than is providing the right price-performance ratio product. These are the things -- the combination of those factors here determine the ultimate success.

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**Operator**

(Operator Instructions) Julie Tsai, UBS.

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**Julie Tsai - UBS - Analyst**

I actually have four. First question is actually regarding to the fourth quarter earnings guidance, it is a bit wide. Is there any kind of uncertainty on the non-operating side that's causing a wider range of the bottom line guidance? This is the first question.

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**Chialin Chang - HTC Corporation - CFO**

I believe the, Arthur asked that question, I think that below the operating line there is not much variation beyond the Beats contribution here. The reason if you go down from the very, the top line, there is a range in the top line, there is a range in the gross margin side here.

There's also a small range, not really a lot of range, depends on how you define small, in the operating expense line. As a result of (inaudible) range you come up with the EPS. We actually publish, we actually distribute a series of the documents including the October sales number as well as the more detailed guidance as a result of requirement due to regulation. You can look through it and hopefully that will provide you more color.

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**Julie Tsai - UBS - Analyst**

Just want to clarify, the guidance for the gross margin is 20% plus-minus 1% and also earlier you also indicate that you would like to have the operating expense to keep under TWD10 billion. So that translate into probably around operating expense of TWD22 billion to TWD25 billion. So I guess what you indicate is the variation over there or I'm seeing -- the way I'm seeing is actually at the non-core side.

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**Chialin Chang - HTC Corporation - CFO**

Okay, I'm not clear when you say operating expense TWD10 billion translate into operating expense TWD24 billion, TWD25 billion, I don't know what that means. But let me answer your question directly here. There is a range in the gross margin, there is a range in the revenue. So that would come out with a range of gross profit.

And when I indicated the operating expense we try to target TWD10 billion or below and then actually in our assessment there is a range in there, and there is a range in there as I've indicated because there's a calming out variable and the fixed cost part of things. So that's why you have the range in the operating side.

The biggest uncertainty, I would tell you that probably the -- there is not really much uncertainty below the operating line if it's something you tried to dig into. That's not the, that's not where the uncertainty we're trying to guide.



**Julie Tsai** - UBS - Analyst

And second question would be I think earlier as well you also gave us a bit of guidance towards 2014 where you would like to see HTC aiming for higher market share and also optimize profitability. For those two items, is it possible at all to give a bit of quantitative guidance at all?

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**Chialin Chang** - HTC Corporation - CFO

First of all, as I said here I need to be clear and clarify what we say. I did not provide guidance beyond quarter four and I will not provide guidance beyond quarter four.

What we aim for, to give you some color of what we're trying to do is we aim for better volume into 2014 and then we aim for, hopefully through that, a better profitability. Beyond that I won't be able to comment a little bit specifically.

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**Julie Tsai** - UBS - Analyst

Understand. And third question would be, is it possible, will you be able to share some insight to the investment coming from so-called the -- one of the media tycoon, Mr. Li? Will this just be a passive investment or is there a possibility that he could be involved in HTC in a more meaningful way?

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**Chialin Chang** - HTC Corporation - CFO

I think it's not proper for me to comment, but when I made the statement -- and I don't want to cause more speculation, so I will comment a little bit more to just the, hopefully to stop any potential speculation here.

First of all, in Taiwan, because the trading system, we're not able to know frankly specifically who are the investor in HTC. And second, we're not -- in terms -- I won't comment specifically, we're not aware they made an investment even before the report coming out of media here. We're not aware.

And I will just comment on this thing here. And obviously we want to, from HTC we want to work hard and providing the, deliver the, hopefully, better shareholder value for whoever investor into the HTC. And hopefully I make it clear to you for those three points.

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**Julie Tsai** - UBS - Analyst

And my last question will be will you be able to share with us some of the may be more recent upcoming product launch that's in maybe one or two quarter ahead?

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**Chialin Chang** - HTC Corporation - CFO

Yes, you probably know we won't be able to share.

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**Julie Tsai** - UBS - Analyst

Okay. Yes, thank you so much.

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**Chialin Chang** - HTC Corporation - CFO

I can only tell you to stay tuned for exciting moment in the coming quarters if I may give you a lighthearted comment.



**Julie Tsai** - UBS - Analyst

Okay. Will do so. Thank you.

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**Operator**

(Operator instructions) Kylie Huang, Daiwa-Cathay.

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**Kylie Huang** - Daiwa-Cathay - Analyst

I have two questions here. First is you mentioned about actually the timing to provide the products is very important, especially maybe the mid-range product line. I was wondering, does HTC consider to like outsource some project to ODM suppliers for like a mid-range or low-end market to like accelerate the design and the production time?

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**Chialin Chang** - HTC Corporation - CFO

I think this is a -- what I would comment is the following. This is a very fast-changing industry and even every month, every quarter things could change, change quite quickly here. So we need to change. We launched the slogan, a marketing campaign Here's To Change. So we're changing our mindset internally as well.

We're open to different ideas or possibility in order to do a few things; one, to come up with the best product with the HTC brand name to delight our consumer, that's the ultimate principle.

So from the cost perspective, from the resource perspective, from a better time to market perspective for making sure the deliver a quality product perspective here, but we're open to consider the various alternative in order to deliver the best product at the right time to delight our consumers.

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**Kylie Huang** - Daiwa-Cathay - Analyst

Sure. The second question is actually to follow up what you comment right now. In terms of if we are talking about the production, because market (inaudible) outsourcing to like EMS partner, do you think that's a possibility you will consider going forward and if that comes true, what kind of maybe margin contribution or overall supply chain management (inaudible) you think might be helpful for HTC?

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**Chialin Chang** - HTC Corporation - CFO

As I said, I think your second question seems to be similar to your first question. We're open to different alternative in order to deliver best product to our consumer here, either from a cost perspective, time-to-market perspective, resource perspective, delivering quality product perspective, we consider these options there.

You mentioned something about supply chain and outsourcing part here, yes. I think supply chain on a standalone basis will continue to optimize it and quite -- we had very -- a group of very capable team members working on that. That may be related to some of the things you said here, but on itself, even with or without those, the supply chain will continue to be optimized.

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**Operator**

Laura Chen, BNP Paribas.

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**Laura Chen** - *BNP Paribas - Analyst*

I have two questions. The first, probably you have mentioned that your OpEx will be under say like TWD10 billion in this quarter. I think it will be a historical low. Can you give us more color that how you will be able to cost down in the operating level? At the same time, you may continuously expand your marketing awareness and distribution and so on.

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**Chialin Chang** - *HTC Corporation - CFO*

As I indicated, on the operating expense side here, we try to target below TWD10 billion and I don't even recall this is historical low. It may be in the recent quarter. I don't remember in the previous years.

To us the operating expense comes on both a fixed nature of a cost and the variable part of it and part of it come from the efficiency. There is a better optimization on various things and various departments in there, and part of it come from the resource we have on the selling and the marketing side of things here.

To us getting a effective marketing resource and funding is important, but not necessary entirely just 100% correlated. The effective marketing coming from the alternative way of doing things, I think we -- our CMO must have communicated to the public quite a lot on those. That's something we focus quite a lot. And hopefully we'll begin to see more results in the coming quarters in there.

So what I'm trying to -- if I may elaborate a little bit more here, the traditional way of doing things may work, but there is always things to do it differently, to find alternative way. And then that may not sort of consume a bulk of your funding as you sort of spent in the past.

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**Laura Chen** - *BNP Paribas - Analyst*

Okay. Sorry, it's -- I mean it's quite a low since 2010 second half, let me correct that. And also I just wondering that based on your guidance of gross margin and OpEx, so your operating level could -- margin-wise could remain negative. Can you share with us how you may turn profitable in the near future? Do you have any more like color of your strategy and also all of your activity?

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**Chialin Chang** - *HTC Corporation - CFO*

As I say here, and I know obviously people want to see the future trend here, it's that future trend to us is very simple here. We're not going to be able to -- we're not really -- if you say, we're not really cutting cost per se, we're trying to optimize quite a lot of things here.

People tend to say what do you mean by optimize. We do optimize organizationally quite a few things, selling, marketing, different departments, all those.

But we're not -- you are not just going to be able to gain profitability by being more efficient. It's a big part of it. You still need to grow your top line, and top line starting from very simple, the very good product portfolio, very good marketing strategy, very good channel and operator partnership and strategies, and the overall market we focus on, geographic market and those.

So those are the things we look at quite carefully in addressing it. Again what we want to emphasize here, by growing volume hopefully we optimize the profitability as well which is -- to us it's important. We don't believe you can just go for a higher volume without getting any profit, but the top line and bottom line to us are equally important.

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**Operator**

Wanli Wang, CIMB.



**Wanli Wang** - *CIMB - Analyst*

A couple of years ago HTC built a factory in Taoyuan aiming to produce around 50 million units smartphone per year. But with the current shipment level, can we say that the factory utilization now is low? That's my first question.

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**Chialin Chang** - *HTC Corporation - CFO*

Your first question, I missed the very beginning part. Did you start by saying a couple of years ago we built a factory in Taoyuan aiming for 50 million annual run-rate?

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**Wanli Wang** - *CIMB - Analyst*

Yes. And then with the current shipment level, that right now the factory utilization is low?

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**Chialin Chang** - *HTC Corporation - CFO*

I won't comment on a factory utilization. Let me give you a little bit more color. The -- a bulk of that, I won't tell you a specific number here, but a bulk of the manufacturing cost is actually human labor related. In this industry the depreciation is not really a big, big part of the manufacturing cost. It's part of it, but it's not big part of it. We're not really capital intensive industry in that.

To us there is a short term, there is intermediate and a longer term planning. As we said earlier part, I said a few times, we aim for a higher run rate in the coming quarters in there. And how we optimize a lot of different factories we have and different -- the alternative ways of delivering the products here, that's something we always look at quite closely in there.

So I wouldn't comment here and say, okay, quarter four you have this, you're going to do the following, quarter one you have that, you're going to do the next thing, that's probably not a kind of the longer term or intermediate term planning we aim to do.

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**Wanli Wang** - *CIMB - Analyst*

Got it. But if we look at HTC's quarterly shipments or annual shipments for example, probably I would guess they won't be able to improve that much to the 50 million units level in the short term. So my follow-up question is that does your optimization plan include like dispose some of the factory, this capacity, or like take in some of this ODM orders for example to improve the utilization?

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**Chialin Chang** - *HTC Corporation - CFO*

When you say 50 million, we're not changing from that. What -- I don't understand your comment.

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**Wanli Wang** - *CIMB - Analyst*

I mean five-zero, because five-zero versus the currently HTC's shipment per year around 15 million to 20 million, that's a big gap.

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**Chialin Chang** - *HTC Corporation - CFO*

You're saying -- oh, you're not -- you're saying 50, five-zero, you're not saying 15?

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**Wanli Wang** - *CIMB - Analyst*

Five-zero, yes.

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**Chialin Chang** - *HTC Corporation - CFO*

I don't think the -- go ahead.

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**Wanli Wang** - *CIMB - Analyst*

I mean that previously --

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**Chialin Chang** - *HTC Corporation - CFO*

I don't think -- first of all, let me comment on this; as far as I'm aware I don't believe our current capacity in Taoyuan actually is existing set up for 50 million in Taoyuan factory alone. And I may be wrong. I think that's the -- I don't know how we got the numbers on those, the second thing in there.

And the second thing is, as I said, I think -- I -- more importantly it's important we're not, how do I say this, this is not a -- don't treat it as an industry in which saying we built this capacity, it's a heavy capital-intensive industry so we're going to have to fill the factories. As I said in the very beginning that the variable cost, a big part of it's human labor cost, is a big chunk of the manufacturing cost.

So that could be adjusted quite -- I wouldn't say quite flexibly, but a lot easier than compared to the other capital-intensive industry. So our goal is not to say we've built this thing, we're going to have to fill this thing here.

Our goal is find whatever internally -- you'll find different ways we talk about delivering the best product to consumers.

And with that said, manufacturing is a core part of the HTC. The important part of it, I wouldn't say you only talk about manufacturing alone, it's a whole design for manufacturing a linkage in there which is actually quite important.

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**Operator**

There is currently no question in line. I will pass the call back to Mr. Chialin Chang, CFO, for closing remarks. Mr. Chang, please proceed.

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**Chialin Chang** - *HTC Corporation - CFO*

Yes, thank you everyone for getting on our call. We appreciate getting on our call. You were passed quite a few slides including the guidance and the third quarter numbers, and we also passed our October number. You can refer to it in terms of October sales number. We also passed a little bit more detailed forecast for quarter four as a result of requirement from regulation in there.

If there are more questions, you can feel free to contact the IR team. I'll pass to Christine.

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**Christine Chi** - *HTC Corporation - IR Manager*

Okay. Thank you. And we'll end the call today. Thanks.

**Operator**

Thank you. Thank you for your participation in HTC's conference. There will be a webcast replay within an hour. Please visit [www.htc.com](http://www.htc.com) under the investor section. You may now disconnect. Goodbye.

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