Thomson StreetEvents℠

ARM.L - Q4 2009 ARM Holdings plc Earnings Conference Call

Event Date/Time: Feb. 02. 2010 / 9:30AM GMT

CORPORATE PARTICIPANTS

Warren East
ARM Holdings plc - CEO

Tim Score
ARM Holdings plc - CFO

CONFERENCE CALL PARTICIPANTS

Gareth Jenkins
UBS - Analyst

Gunnar Plagge
Nomura - Analyst

Nick Hyslop
RBC Capital Markets - Analyst

Jerome Ramel
Exane BNP Paribas - Analyst

Janardan Menon
Liberum Capital - Analyst

Didier Scemama
RBS - Analyst

Simon Schafer
Goldman Sachs - Analyst

Brett Simpson
Arete Research - Analyst

Arun George
Noble - Clear Capital - Analyst

Paul Morland
Astaire Securities - Analyst

PRESENTATION

Warren East *- ARM Holdings plc - CEO*

Well, Good morning ladies and gentlemen. It's 9.30 so we'll start away; and welcome to our results presentation. I'm going to talk for a little while and give you an update on the business, and then Tim will give a slightly more detailed update on the numbers. Then we'll hand over to Q&A in the usual way.

So to start with 2009; we're reporting this morning 2009 and Q4 results. 2009 for the semiconductor industry was a pretty horrible year, particularly in the first half. And so we're very pleased to be standing here this morning talking about a year with our revenues down about 10%, versus an industry down about 20%.

To see that continued outperformance of the semiconductor industry at large is very encouraging. And we're doing that through continuing to gain share in end markets and gain penetration in markets where we're already established. And there are trends happening in Smartphones, mobile computing, micro controllers and consumer electronics that are helping us on our way there. And we've had a very successful year for selling licenses, more on that later.

Our physical IP strategy is in good shape from both the licensing point of view and some very pleasing royalty numbers coming through from that part of the business.

We exit the year with our backlog at record level, up substantially, sequentially and also substantially year-on-year. So that's a good position to be moving forward on.

And the way in which we've managed the business during 2009 obviously, as I say, it was a difficult year and so with revenues coming down, as was the inevitable, we had to be fairly disciplined about where we made our investments during the year. We need in our sort of business obviously to continue with investing in major technology developments. And so I think 2009 has been a pretty good year in terms of managing that financial discipline. That's translated into by the end of the year Q4, margins at record levels and record cash generation.

The slide is exactly the same format as the last couple of years of results presentations. So, very much we're going to be talking about how we're concentrating on executing this strategy, which has not changed for some time, and will demonstrate how we're achieving growth in non-mobile applications; how we're increasing the value of ARM in products where we're already present; and how we're extending the IPs that we're outsourcing to our customers.

So industry as a whole probably the worst year for semiconductors for getting on for a decade and for ARM a year of resilient execution closing with several records, and we'll talk some more about those I'm sure.

So now, I'll delve into a bit of the detail hopefully. Processor Licensing, this is obviously an engine for ARM's future growth. Licensing is all about equipping the ARM semiconductor partners with technology that drives future business. And given the wider economic conditions in the first half, it was a very good year for building our licensing base. You can see our licensing base grown to over 660 licenses. The second half in particular strong for the number of licenses sold and our exit rate of $36 million in the quarter in Q4 is an encouraging place to be.

Now behind those numbers, there was some quite meaningful public announcements from some of our licensees. So the Infineon architecture license for security is clearly a meaningful announcement for ARM, breaking into a new area with a leading player in that area. We saw some encouraging licensing in the quarter as well for the Cortex licenses and for Mali. And this morning we're starting to talk about the fact that one of those Mali licenses was with Samsung whose obviously a leader in the industry, and an opinion former in the industry as well. So that's very encouraging for our graphics licensing.

When you look at the pie chart at the bottom, which again we've shown in several of these presentations, the picture is as it has been for some time with licensing driven by both mobile and non-mobile. And we're very encouraged by continuation of the non-mobile licensing. And within mobile, we're increasingly seeing ARM processors used in peripheral controllers in the phone away from the traditional just the baseband modem, just the applications processor. So we're talking connectivity, cameras, power control, touch screen and those sorts of applications.

Now I'll just look at the licensing in a slightly different way. And again, the left hand slide of this slide is a chart with which I hope you'll be familiar. It's the traditional format where we show the base of licenses that are out there to generate future royalties. And the numbers in parenthesis are what's been added to those licenses during 2009.

And now I showed a very similar slide this time last year, where on the right hand side of the slide we talked about three new processors that we were intending to launch or deliver during 2009. Well, we did absolutely deliver those products in 2009 and we've sold licenses.

And so now here's a look ahead to 2010 where we have another three new microprocessors lined up for launch and/or delivery in 2010. And as shown on the slide, we've been signing up lead licenses for each one of those processors. And you can see the Eagle processor; this is the high end applications processor targeted at the top end application processor market. We've got some real core aimed at real time applications and we've got a new addition to our micro controller product range as well. So

those we're all coming to market in 2010. And so that's the look forward to what's happening there. A similar slide to the one we looked at 12 months ago.

One of the things -- little details you might notice here down the right hand side of the slide though, is that with the growth particularly of the microcontroller product portfolio we have updated some of our market size numbers. And in the complete slide pack in the appendices, you'll notice that Ian has updated the charts again; charts which I hope most of you are familiar with. And you will see that the total market that we're aiming at has grown a little.

So, I've just accidentally moved forward there by another slide. So our licensing is all about driving future royalty and it's happening in a variety of ways. But the numbers across the bottom are showing our licensing aimed at semiconductor partners, aimed very specifically at growing our market going forward, in the mobile space, but also in some new areas. And outside in the demonstration area, we have ST today. Some of you will have seen the demonstration there. They're showing off their digital set top box and I already mentioned the Infineon design. The numbers down the bottom indicate, where is ARM in these markets today and where is ARM going forward?

If I switch now to royalties, then our Q4 royalties up sequentially and well ahead of the industry. It was a record number of (inaudible) chip by our partners in the relevant quarter which, of course, calendar Q3. And that's driven by serious increases in microcontrollers, serious increases in smartcards, and the traditional areas in mobile phones, consumer products and enterprise.

And the pie chart at the bottom of the slide is again a familiar pie chart. You should see that the proportion of mobile/non-mobile it's switched around slightly. And I think that's primarily driven by the growth in the embedded areas, the little yellow wedge on the slide. And we should also note at this point that the Cortex products have grown very strongly in the last quarter as well, and we're now up to 2% of the total being driven by the Cortex product.

So in the year as a whole, where did these volumes come from? The thing to note here, I've had lots of pictures of electronic products into which ARM has designed over the years.

I think a key thing here is the proportion of telephones that are there. And this is just more than telephones and it's adding some color I hope to the royalties picture and noting as well, although in the 3.9 billion microprocessors for the year, it was a record 1.3 billion in Q4. And this breadth of different products into which the processor is designed, it's what's enabling the continued out performance, where we're outperforming the industry.

And in the chart on the left hand side, again this is an update of a familiar chart where you can see the ARM growth line consistently a gap above the industry growth rate. And obviously over the years that's cumulative that consistent gap builds up and that's really what's driving our continued outperformance of the industry as ARM grows its market share.

If we look at the numbers for the year as a whole then the units were down arithmetically, but that must be put in the context of industry shipments, excluding memory industry shipments at large are down about 20%. And there we've broken down some of the key markets sectors where those shipments have happened and how ARM is performing relative to those key markets sectors. So ARM shipments generally outperforming the industry at large right across the application space.

Now a little bit of detail on that, another metric that we're tracking on an ongoing basis, and we've shown charts like this over the years, looking specifically now at the mobile space. The increasing amount of value per ARM powered product, if you recall the first slide that I started off with, the strategy about growing our market share into new areas, but also increasing the value of ARM per consumer product that gets shipped.

In phones, the number of ARM processors per phone average 2.1 for the year up from 1.9. And for the last quarter that we're just reporting it's a record 2.4 ARM microprocessors per handset. And the sort of things that are driving that are the phone market dynamics themselves, more high end Smartphones getting smarter. And the second thing is ARM being designed into a wider range of functions within the phones.

So the phones are now coming out with functionality like touch screen. People are paying attention to have more sophisticated power controlled schemes within their handsets and you need a microprocessor to do those things and that's where ARM is getting designed in. And that's helping drive up this average number of ARM micro processors per handset.

And those two factors translate, if we move to the bottom half of this slide, into royalty revenue as a proportion of handset ASP. The chart on the bottom shows that that has consistently increased year-on-year, and is actually up about 70% since 2004, so over the five year view. And we believe that that trend is likely to continue. And ARM11 A-class processors do get designed into higher value chips, and so we'll see that trend continuing.

And if we move to the bottom of the slide and think beyond Smartphones about mobile computers and mobile computing generally, well we like to think of those as, if you like, Smartphones on speed where we'll have even higher value chips and an even higher proportion. So, that's phones.

Now, it isn't just phones, it's the wider gamet of consumer electronic products. I was at the Consumer Electronics Show the first week in January, and it was very impressive to see the number of exhibitor stands there with ARM technology on their stands. We did a little survey and it produced very high number. And it was encouraging to see ARM being designed into an ever wider range of consumer products.

Translating that into numbers and some of the sectors which we track in things like set top boxes and digital TVs, already ARM is sat on a market share of about 30%. That's what we're measuring from what's coming out in 2009. And more significantly in 2009, we've had some announcements of design wins. Again, I'll refer to the ST demonstration outside. Design wins which at the moment is a licensing activity and a design win activity, but which will translate into shipment royalties and increased market share in future. So we're already gaining market share and that market share gain is set to continue.

And it isn't just with the generic ARM general purpose micro processors, it's things like the specialist processors, the Mali graphics [core] as well, finding their way into those products. I'd encourage you to go an look at the demonstration to see what that Mali graphics processor can really do.

Moving to mobile computing, there's been a lot of noise about mobile computing over the last 12 months in the press. And as I say, there's a huge range of different form factors out there. We've got some of them in the demonstration area outside. There has been a lot of noise.

At the moment, it's at the stage where there's a lot of semiconductor partner design wins that have been announced, and some early products. What we're really interested in is not the number of net books sold in 2010, but just how this whole mobile computing market space is expected to grow over the next several years.

And with that I'll set that in context of the wider number of Internet connected devices that we see. This is what's really exciting us about the opportunity facing ARM over the next several years. You'll have a huge range of different form factors. I can't tell you what they're going to be.

Some companies have -- or different companies have different terminology to describe this. Some companies talk about the three screen strategy. We have rather more than three screens on the bottom of the slide, because we can't really tell how big these screens are going to be from here. But what we can tell is that OEMs who are designing these products like a choice of suppliers, the ARM business model gives them the choice of suppliers and the ARM technology is used for a range of different functions within these electronic products.

And what we're spending a lot of time and effort on at the moment is developing the software eco system and the development environment, so that this architecture is ideally placed to gain a lion's share of the market as it develops over the next five years or so. And an indication of that is shown on that slide.

Stepping back a little about market share and market gain, I wanted to summarize and we had a slide a little earlier in the presentation about how our licensing I was targeted at some growth areas, how does that play out once you get from licensing into design win? I think different sectors we're at different stages. And that's what this slide is meant to show.

On the right hand side of the slide in the mobile phone space, it's all about innovation. And this is one of the reasons we're also very keen on mobile computing, because it's a place where a lot of innovation is taking place and we've always said the mobile space is a great place to design your product because it's a very demanding environment technically and economically. And if you can develop things, which are successful in this space then they can be applied into other application sectors.

Backing off into the enterprise space, the key factors are a little bit different, it's about multi-sourcing and having common architecture, re-use of software, re-use of tools and so on, and our share is growing there. It's obviously not as developed yet in that space as it is in the mobile space.

In the consumer electronic space represented by Digital TVs and Set-Top-Boxes, it's about growing the eco system and the development environment. But it's also about market making semiconductor companies switching to ARM generally to reduce their total cost of ownership and cost of dealing with these markets. And the share is less well developed today, but is clearly on that trajectory moving towards the right-hand side of the slide.

And then in 2009 we also saw some activity in microcontrollers and smartcards. We saw very strong growth in volume shipments there. But actually if you look at the total market our share in this market at the moment, in spite of that very strong growth, is very small.

And what I'm hoping to demonstrate here is the huge potential growth opportunity in this sector of the market as we move from the position where we are on the left-hand side of the slide more towards the position on the right-hand side of the slide. Tremendous opportunity there, we've been bringing new products to market. We've been bringing new tools to market. Our semiconductors partners have been launching ranges of products. And so, the future for microcontrollers is bright.

Switching gears now and look at our Physical IP business. Physical IP business has performed resiliently in 2009. We've sold three new platform licenses in the fourth quarter, which if you look at the number of platform licenses we typically sell in a year this is a very good result for a quarter. And there's a span there of technology as well with the Globalfoundries deal at the very leading edge and that's key for signing up the semiconductor companies and giving them something to work with. But other semiconductor companies and big ones in some parts of their portfolio make use of older technology and it's instructive to note that we're still able to sell platform licenses for new physical IP products on older geometry.

Most of the royalty today comes from older technology, but since 2007 when we had advanced nodes you'll now see that nine platforms are delivering royalty, nine of the new platforms are delivering royalty. We've pushed the leading edge, and I'll talk more about that in a moment or two. We've pushed the leading edge and we're expecting to see royalties per 32 nanometers before the end of 2010.

If I switch to royalties for a moment just talk specifically about that, Q4 was a very pleasing quarter with underlying Physical IP royalty, that's excluding catch up, up significantly year-on-year. And the chart at the top shows Foundry revenues and if you actually extract from the diagram, which I admit is quite difficult, but basically Foundry revenues declined by about 5%. You need to look at the Q3 '08 bar and the Q3 '09 bar and that corresponds to the royalties that we record in Q4 and look at those bars and you'll see our royalties up. The Foundry space is down and that's indicative of increasing penetration there -- more continued increasing penetration, so it was a record underlying royalty and indicative of gaming penetration.

With that those games are going to come from in future, a bit like our processor business where the licensing activity is equipping semiconductor partners with our technology to drive future business, so it is with our physical IP business where selling physical IP platforms is equipping Foundries with the appropriate technology so that we can then get design wins and then go on and generate future business.

And the chart is a snapshot of where we are today in terms of the platforms that we have out there spanning the full range from 250 nanometers right down to 28 nanometers. And you can see some of the data there. And we're typically growing that by, as we say, about eight different platforms per year.

Now today only about half of the total are delivering royalties, so there is royalty potential building up in future and you can see the new royalty payers coming out in 2009, that's a trend that we're going to see continuing. Actually, the leading edge that I referred to the 65 nanometers and below that's now contributing about 10% of our Physical IP royalties. So most of it, 90%, is still driven off the older technology, which again illustrates the tremendous potential for future royalty growth in this physical IP part of our business, as well as in the processor part of our business. And we also note that an increasing number of the top 20 semi players are users of our physical IP today.

One of the interesting things to note is what's been going on inside in the operational aspects of our Physical IP business. There we've been, as you know, doing a lot of investments over the last several years and that investment has and continues to transform the business. It has transformed the business into where it is now a leading supplier of physical IP.

We've had investment in technology, and more on that in a moment, we've also had investment in the development process and the internal environment that's used to create these products. And what that has done, that leads us to be able to build better microprocessors and we have achieved some processor design wins utilizing our physical IP, which delivers better power performance characteristics.

And that investment is also transforming the operations of the business and that helps to improve the productivity internally. And those two factors together mean that as we move forward our Physical IP profitability we expect to improve, because licensing and royalties are driven by the delivery of new technology into the marketplace. And at the same time as that licensing and royalty grows the costs actually grow more slower because we're now more efficient at creating the product. And so, with better productivity we have better profitability.

Snapshot update, a slide that we've shown for the last several times and the three bubbles on the right-hand side of the slide is where the updates have taken place since we last showed this six months ago. Since six months ago the top right-hand bubble there where we're talking about optimized Cortex processor products, we'll be licensing 32 nanometers during 2010. Back in -- at the very beginning of Q4 we licensed Globalfoundries and we've also delivered 32 nanometer physical IP product to the marketplace; so progress in terms of deploying the technology, progress in terms of engaging with the marketplace and progress in terms of delivering new products.

One of the key ways in which that physical IP progress translates, and this is the last slide I'm going to show, is building better microprocessors, it's a key result area for us. How our microprocessors perform is important. And our optimized physical IP keeps our microprocessors at the bleeding edge of competitiveness.

So last year I showed a slide a bit like this, which was how we intended to improve the performance and our characteristics of the Cortex-A9 and the way in which we expected to extract from the physical IP those improvements. This year I'm showing you the results of that. And this shows that with -- if you go for a high performance we can get the Cortex-A9 on a 40 nanometer-G process to 2 gigahertz. If you optimize for power consumption instead you can take the Cortex-A9 and run it at the same 800 megahertz but actually reduce the power consumption to 500 watts. So that was the activity in 2009.

In 2010 we're taking this activity forward and what we've done on 40-G we'll be doing on 32 nanometers. And when we go to 32 nanometers then we expect to improve the power characteristics. When the thing is running we expect to improve the power characteristics meaningful by between 10% and 20%. We expect to improve the standby power by at least an order of magnitude and, therefore, improve battery life. And if we optimize for high performance then we expect to be able to deliver the 2 gigahertz part with about a 30% improvement in power consumption.

So we laid out our plans last year. That's the result for 2009. That's what we're aiming at in 2010. And that's what physical IP is doing to our microprocessors improving the competitiveness. With that I'll hand over to Tim to talk about how this is translated into business.

Tim Score - *ARM Holdings plc - CFO*

Morning everyone, the usual quarterly change of the microphone position.

The good news is I've got five slides on the financials. There's a lot of detail in the release. There's a lot of detail in the slides and the detail -- I think the format of that most of you will recognize. So I'm just going to spend a little bit of time briefly summarizing, but also talking about some of the things that you'll be probably be thinking about as you look at your models for 2010. And that's really going to be the focus.

And a bit similar to last year, we came into last year quite a difficult year to call actually. When we were standing here this time last year I think the general sense was the industry was probably heading down about 30%; certainly 20% to 30%. And that's actually quite a different context to manage a business.

So a year on, as Warren said, we're using the word resilient quite a lot today, but I think it's actually an appropriate term for the way ARM has performed during a year. We have outperformed the industry in line with previous years. Licensing I think has held up fairly well. Royalties, gains in market share, and that's enabled us to maintain an operating margin north of 30% for the year. And I think that was by no means a given coming in, so that's very encouraging.

And we have continued to manage headcount carefully, as Warren said. And in fact, we end 2009 about 30 people less than we started. And in fact, the end 2009 headcount is actually below the end 2007 headcount too. So we really have been balancing this quite carefully, but absolutely maintained investment in the key projects, and I'll touch on that a little bit more in a minute.

We had a pay freeze in, as you know I think, which stayed in for most of -- or throughout 2009. I'm going to talk about OpEx and OpEx guidance in a minute, but we have -- there has been an annual pay rise effective January '10 and we'll touch on that.

And from a balance sheet capital structure it's been a strong year for cash conversion and cash generation, we started the year just under GBP80 million and we're ending it just over GBP140 million; and in Q4 net cash generation over GBP30 million, very, very strong performance.

Looking at Q4 in particular, again I'm going to go through this pretty quickly because we've covered most of it. It was a strong licensing quarter and we saw the pick up in licensing in I think in Q3 number of licenses. Q4 strong both in terms of the number of licenses, and I think we talked last time about the broad mix of models that we have. We're doing more term and more per use, so the number of licenses is higher, but the absolute value of bookings in Q4 was very strong, which has obviously driven the backlog at the end of the quarter.

And part of that, of course, is the substantial long-term deals that you see up there, the renewal of the STMicro subscription and the Infineon deal that Warren referred to and the Globalfoundries deal. These are not deals that are going to yield step changes in license revenue in the first half of 2010, because the revenue recognition here is longer-term. But these are certainly deals that underpin future licensing revenue for a long time, which combined with a technology portfolio of more mature cores that yield revenue recognition immediately, that's quite an attractive mix as we come into 2010. And as I said, their backlog very high.

Royalties as we've said for a long time are gradually increasing as a proportion of total revenue. In most periods royalties are going to go faster than licensing. And of course, the impact on that over time is to drive up our margins both at the gross level and at the operating level. I'll touch on that in a second and I am going to talk about OpEx.

OpEx in Q4 a little bit above consensus, two things there really; one is gross margin was considerably above consensus, so there's a little bit of reclassification there particularly around the PIPD engineering time between OpEx and cost of sales. But also with a very strong revenue performance in Q4 and very strong bookings and, therefore, sales commission performance in Q4, the accruals or the charges for those payments in Q4 is higher than run rate and they would drop back down in Q1. So when you look at the combination of that dropping down and inflation for the pay rise coming in you get to a broadly flat picture.

So let's just talk a little about gross margin because we started -- well, in 2008 the gross margin was just over 89%, in 2009 it's just over 92% and in Q4 is just over 94%. So the sales side guys are sitting here thinking what's the gross margin going to be in 2010? I think that's a fair question. So the way to look at this, I mean obviously revenue is a huge impact on this, but let's focus in on the cost pieces.

And you can see from that chart that there are really three elements to our cost of sales. One is the engineering -- the time of the service guys when they're generating service revenue. There is the product cost of some of the development system products. And then there is the engineering time from the Physical IP division that is spent not generic technology development, but on customization technology to yield revenue.

And you can see that the first two of those are fairly stable and they would very much track services and development in system revenue. The variable tends to be the Physical IP, which is why you can see in Q1 of 2009 the gross margin was lower at 90% and that was a quarter where the PIPD engineering charge into cost of sales was higher.

So I think my message is that number will vary depending on what we're doing. But I think we are probably -- it's probably fair to say that a gross margin base now of around 92% is the way to think about it rather than the 89% or what we saw in the first half of the year. I think consensus before today's results for 2010 gross margin was about 91.5%, but it does look as though somewhere around 92% is going to be the base looking forward. And as I say, over time that grows as royalties grow as a proportion of the total revenue.

We've talked a bit about balance, let's just discuss how we are looking at this at the moment. Throughout the last couple of years where we've managed our headcount very carefully we've continued to be completely focused on the technology roadmap development that drives this business forward.

What we expect to happen in 2010 is a gradual increase in headcount subject to the market panning out in the way that we all currently think it's going to. And therefore, for Q1 as I said before probably going to be fairly flat with Q4, incentive accruals lower, wage inflation in there. And then if we do increase headcount then obviously there could be a gradual increase in that number.

So I would expect consensus OpEx to rise a little bit from where it is. I would expect gross margin to rise a bit. I would expect consensus OpEx to rise a bit.

And where it is in the GBP48 million to GBP50 million range, FX translation is clearly a big issue. Half of our costs are in dollars. What's the translation rate going to be in Q1? We don't know. What's the mark-to-market FX impact going to be at the end of Q1? That's going to depend on what the rate is at the end of the quarter. So there are variables that you can't be specific, but it feels as though it's going to be broadly flat against Q4.

But I'd just reiterate that our more longer-term guidance about we expect to grow our cost base about the half the rate of revenues very much stays in place and that is a function, again, of the royalty growth over time. And that's the thing that drives this business to a sustainable margin of 40% and above, which we've been talking about now for some time. And you can see that we've been making some good progress towards that in the last couple of quarters.

So what are we actually saying today, what we're saying is we see here and read what everyone thinks is going to happen to the semiconductor industry in 2010. We read all the reports. We talk to our customers. And I think it's fair to say we don't have

8

THOMSON REUTERS

any information available that says that's not going to happen. But what we are saying is we don't have a crystal ball into the second half of the year either and, therefore, we are not going to be declaring victory on a big up year for semiconductors, but we completely understand why the current estimates are the way they are. But we'll put a qualifier on that.

What we do know, because of our licensing portfolio and because of design wins we know we've had, this business comes in 2010 very well placed in the sense [to] continue to outperform whatever the market throws at us. So we are confident about that and, therefore, what we're saying today is reflecting on the industry improvement expectation that is out there and reflecting on the position that we have in the marketplace, the backlog that we have going in to 2010 we would expect our full-year revenues in 2010 to be at least in line with what's currently out there in the market. And just to stem off the question, coming into these results it's about $555 million consensus revenue for 2010 as of this morning.

Now with that before we get into Q&A. I think Warren is going to come back and make a couple of summary and longer-term comments.

Warren East - *ARM Holdings plc - CEO*

Thanks. Yes, thanks Tim. So summary 2009, I think we've summarized it to death really. It's very resilient execution but our balance there about building the platform for the future. In 2009 we knew it was going to be difficult, but we kept our investment going in new products. And as I said a little while ago, that enabled us to deliver new products and enabled us to have new products for release and delivery in 2010.

So we did that at the same time as outperforming the industry at large. The new products came in the form of new microprocessors, new tools, new physical IP and that takes us into new markets. We're positioned with a record number of new licenses as well, and they're the basis for future growth going forward.

So, we do expect ARM to accelerate its gains in market share, particularly as we're exposed to areas of long-term structural growth. So, in mobile phones we're seeing 2.4 microprocessors per phone, and we see that continuing to increase.

In mobile computing we see a new range of products with all sorts of different form factors. We're seeing some significant customer announcements with digital TVs. In disk drives we're seeing increases in market share. We're seeing key announcements of market making semiconductor companies in areas like smartcards, in areas like microcontrollers where we're also growing the portfolio of products. And we're gaining traction in things like graphics, and outperforming the market in Physical IP as well.

Now, that was all about where we are and the trajectory, and we did want to step back at this point and just sort of set that in the context of the longer term picture for ARM.

In 2010, in November 2010, we'll be celebrating our twentieth birthday in this business and as we look at the industry for the next decade we can see people struggling with technology and the need for technology which delivers low power, which is key to a huge range of electronic products. We see people are struggling with managing costs, and we put both of those together, and say ARM has a business model, which enables outsourcing, and ARM has technology which addresses these longer-term technology challenges that our customers face.

And we're putting effort into supplying an ecosystem, which allows those customers to use our technology, take advantage of it in the growth markets that they see coming forward. Mainly today, a snapshot of those markets would be characterized by more electronic functionality, more software functionality in products, more of things like connectivity, Internet, clouds and so on.

So, over the next 10 years we think we're pretty well positioned to take advantage of this. As we sit here today we know that are semiconductor partners have shipped over 18 billion products, 18 billion microprocessors. So, over the next couple of

months, in our twentieth year we'll go through 20 billion microprocessors and the ecosystem is well established with huge numbers of engineers.

So, these customers, faced with this burgeoning electronic market place, can use ARM technology, whether they're building products for entertainment, productivity, making people better, saving energy, you name it all these companies have different drivers of their business. But the common factor is ARM is uniquely positioned to enable and take advantage of that growth market, if you take that slightly longer-term view.

So, with that, we'll hand over to Q&A.

QUESTIONS AND ANSWERS

Gareth Jenkins - *UBS - Analyst*

Thanks; it's Gareth Jenkins from UBS, a couple of quick ones, if I could.

Just on the headcount increases. Tim, I wondered whether you could talk to where those headcount increases will go to and what the strategic priorities are in terms of R&D over the next two years or so.

And then, secondly, I just wondered whether we can talk about [Intel's] competition during the course of the latter stages of this year into next, and what your assumptions are in terms of the Smartphone market share going forwards? Thanks.

Tim Score - *ARM Holdings plc - CFO*

Yes, from a strategic priority standpoint, the headcount investment will be largely within the Process division, and within the Media Processing division. I think we've said here, recently, that our expectation in the Physical IP division, if anything, over the next few years is, actually, going to have the headcount gradually reduced, as we move out of this phase of catch up of technology, and we move in to more productivity and efficiency within that division.

And so -- but we do see significant opportunities in the Processor division for further technology development to grasp the opportunities that Warren described. And also, of course, the multi-media processor is a much younger business, that has a very attractive prospect in front of it.

So in terms of those two would be the key, in terms of the support functions, the overheads, these will all be very, very carefully controlled, and the thrust is going to be in those areas.

Warren East - *ARM Holdings plc - CEO*

With regard to the question about Intel, then absolutely we see Intel as a very serious competitor for us in this marketplace. Clearly, the largest semiconductor company in the world has got to be a serious competitor.

Actually, the ARM world is also a serious scale, with approximately the same amount of ARM microprocessor revenue per annum as Intel microprocessor revenue per annum funding those two development activities. We absolutely would expect Intel to make some progress at improving the -- how appropriate their products are for embedded applications, and things like mobile phones.

Similarly, ARM is making progress in its ecosystem developments, in its range of standard application software that's out there, and in terms of position within, perhaps, markets that are a bit more traditionally viewed as Intel markets. We had some pictures

in the presentation about Smartbooks, and Netbooks, and those sorts of things. So ARM is making progress in that area. And one of the messages I hope you got out of the presentations that we both gave, is investment in future technology.

So, right now, ARM technology is a long way ahead of Intel technology in terms of appropriateness for these types of market. Intel is making progress. ARM is also making progress and ARM is also investing to open up that gap going forward with some of the improvements that I talked about.

Gunnar Plagge - *Nomura - Analyst*

It's Gunnar Plagge from Nomura. The 4.9% or the 9% sequential decline in the average royalties per unit; you had previously, I think, talked about that you reached about $0.05 royalties per unit when you reached about a billion of micro-controllers. So was there any seasonality in that, or was the decline actually slightly stronger than you expected?

Tim Score - *ARM Holdings plc - CFO*

You're right; it is about the product mix. I wouldn't say it was necessarily unexpected; it's what pops out of the arithmetic. The fact is that microcontrollers have just grown on top of a large number by 60%, and smartcards have grown by 100%, and modeling is never completely accurate, and the result which pops out can move in both directions, depending on the product mix. So, not particularly surprised and not particularly concerned.

We'd point out that actually the royalty in the quarter, in revenue terms, exceeded our expectations and that of others by about GBP3 billion -- GBP3 million; wish it was GBP3 billion -- $3 million. And also the volume exceeded our expectations, by a couple of hundred million units as well, so it's just one of those things. You have higher volumes. You, typically, have a lower price per chip.

Gunnar Plagge - *Nomura - Analyst*

A similar question on mobiles, 2.4 cost per unit. Can you give us maybe an idea where you see that at the end of the year, the run rate?

Warren East - *ARM Holdings plc - CEO*

Hard to call the end of the year, because really it is about [calling] both the proportion of Smartphones, but also the increased smartness of simpler phones. And the message that we tried to get across in the presentation is that this is not just about having more Smartphones with an applications processor, as well as a baseband modem; it's about ARM technology being used in a range of functions within the handset. So, we absolutely expect to see that number increase. Whether it goes 2.6 or 2.7, I couldn't tell you.

Nick Hyslop - *RBC Capital Markets - Analyst*

Hi, it's Nick Hyslop from RBC. You mentioned, obviously, Samsung as a new customer for the Mali graphics processor. I wonder if you could give us an idea of what some of the drivers were that led Samsung to select Mali, and that having won a Tier 1 manufacturer, whether you would have increased confidence in other Tier 1 manufacturers taking Mali more seriously than they have so far.

Warren East - *ARM Holdings plc - CEO*

Well, first of all, on Samsung specifically. We've talked about it as much as we're going to talk it in these results. Samsung will be having their own product announcements, when they announce the product, and then they'll be talking all about where it's going, and the whys and wherefores. So, that's for them.

In terms of other companies like Samsung, well, I would count companies like ST as pretty serious leading edge companies, and we're happy to have them with us today. We're happy to have Mediatech in the fold, announced before. And so I think it's a matter of time, and I'm confident that some other large players will shift in due course.

Nick Hyslop - *RBC Capital Markets - Analyst*

One second question. On your guidance of $555 million, if you look at the industry guidance for 2010 and semi's is something -- say, 10% to 15%, you're looking at 10% or 11% that you're saying you're comfortable with, and yet your historical ability has been to outperform that by some margin. What are you basing your comments and your comfort on, in terms of what you think the industry will do?

Tim Score - *ARM Holdings plc - CFO*

I mean, so what we're saying is that $555 million, which is about 13%, right, is probably lower, I think, than most people's expectations for 2010. What we're saying is it's most people's expectations, which is for more than that comes to pass, then we would expect to do at least as well as $555 million, because, you're right, we're struggling to find a year where we haven't outperformed the overall industry.

Our only qualification in our guidance today is we can't call the industry. What we can say is that we expect to outperform the industry and, therefore, if the industry grows, in line with consensus, then we kind of know what that means for the expectation of ARM revenue. But, without that qualification, we're here gazing into a crystal ball into the second half that no one knows anything about. And there's sufficient uncertainty in the macro world to not be standing here, or sitting here, in early February high five-ing that it's all glorious and it's all 20% up for the industry; too early to say. But whatever the number is we would be very disappointed if we're not ahead of it.

Nick Hyslop - *RBC Capital Markets - Analyst*

Thank you.

Unidentified Audience Member

Couple of questions. Clearly, you've licensed the Mali quite extensively now. How should we be look -- have the royalties on the Mali started coming in already? How should we be looking at the Mali royalties versus the processor royalties? Is it a percentage of the chip ASP, given that those chips may already have your processor on it, for instance?

And, secondly, there are going to be multiple processors, multiple chips selling out there for the Smartphone market, which integrate the application processor functionality with the baseband functionality, so maybe dual core ARM processors how will that impact the ST's in this Smartphone cycle?

And then, finally, Tim, one question for you on the overall guidance. When we look at some of these -- when we look at what you've said in the past; for instance, ARM has a model of growing 15% CAGR over -- on the revenue terms and OpEx growing at much lower rates than half that revenue level, why haven't you stuck to -- clearly, you're giving market -- what [today] the

THOMSON REUTERS

market is. Are you trying to say that you're on model at this point, ahead of model, or are you not willing to say any further or are you not willing to make a call on the industry?

Tim Score - *ARM Holdings plc - CFO*

Thank you for directing your other five questions to Warren, I appreciate that, because I was trying to unravel those.

But, no, I mean we -- look, this is a bit like last year. We sit here at the beginning of February; no-one really knows what's going to happen in the full year. Consensus was 455. It drifted up through the year. We're usually slightly ahead of it, and we ended up at 490.

As regards the -- what does ARM grow in the medium-term, yes, we do see this business as a 10% to 15% grower through cycles, but we've been through some pretty interesting years. Two years ago our royalties grew 28%, last year they're down a few points, because of what's going -- so I think it's very -- so what we're saying is, medium to long-term this business outgrows the industry. This business has a business model that's driving operating leverage to the margins that we think are sustainably north of 40%.

For this particular year we can only really comment in reference to what we see around us, which is an expectation for the market of around 15% 16% growth; some are higher, few a little bit lower. That will be a great outcome and we would expect to outperform it.

Warren East - *ARM Holdings plc - CEO*

The questions about Mali and royalties, typically, we've said that from licensing microprocessing to core to generating meaningful royalties is a time delay of about four years. Now, obviously, some companies get there faster than that and some take longer, but it's about four years. And it's exactly the same with the Mali core as it is, where the general purpose ARM core, [and] it's the same process designing a system on chip device.

So, we started our Mali activity around about the end of 2006, effectively the beginning of 2007. And you're right, we've licensed the core extensively over the three calendar years since then. And we have, actually, seen our very first Mali royalties coming through, but it's not very meaningful at the moment, because of that four year lag.

How does it work? It's very similar to a generic general purpose ARM microprocessor core; it's a percentage of the chip price, typically. And, if you integrate a Mali core on the same chip as another ARM microprocessor, then it's similar to integrating two ARM microprocessors on the core. Typically both cores command a royalty, and the second one has a discount. And, perhaps, because of the special purpose functionality in the Mali core, the discount is probably not as great as it would be for a second general purpose ARM microprocessor. So, you can think of it as an incremental royalty.

And, whether there is an application processor or a baseband, and exactly how many cores are integrated, the principle's exactly the same; multiple cores commend multiple royalties with discount for integrating multiple things on the same chip. In some instances we win out of that integration, in some instances the semiconductor companies win out of that integration. And there are all sorts of schools of thought about which is the best way to integrate.

Jerome Ramel - *Exane BNP Paribas - Analyst*

Jerome Ramel, Exane BNP Paribas. I got a question concerning your backlog. It seems to me that it is in the hands of a couple of customers, so I'd like to understand if you are seeing the Tier 2 customers coming back, or if it's just the Tier 1 so far? And, if we could assume the backlog will stay where it is today going forward in Q1?

And, second question, is there any reason why you haven't gained any market share in the automotive?

Tim Score - *ARM Holdings plc - CFO*

Yes, I think what we're saying today is that, if you look at -- quite a spike in the backlog actually. What we're really saying is that most of that uplift has been generated by the sort of longer-term deals.

With regards to the general health of the licensing and the Tier 2's and all that, I don't think they are back up to full speed, by any means, and I think we would expect to see that situation further improve. It's quite sort of regional, I think, in terms of that.

But -- so I think the backlog is a couple of things; it's pretty healthy licensing generally towards the back end of the year and it's significant long-term deals. And it's that latter point that I'm saying, don't expect the spike in license revenue in Q1 and Q2 just because of that backlog. It's helpful and it contributes, but the opportunity pipeline for Q1 and Q2 deals of more mature processors, which generate revenue recognitions immediately, is in a sense more important than the take from backlog.

But the backlog contribution to first half revenue is still pretty healthy by historical standards; I just wouldn't want you to map it proportionately against the increase in backlog in the fourth quarter.

Warren East - *ARM Holdings plc - CEO*

Okay, and the question on automotive; where are we in automotive at the moment? Included in the packs you'll find we've updated the segment slides on slides 31 through 33. But referring specifically to automotive, we're on about two ARM microprocessors per car at the moment.

Automotive is a very slow market to adopt our sort of technology. It's very conservative. There are some established players out there with 32-bit processors in engine management systems. Engine management is a relatively low volume application for us, and it's not one that we have historically concentrated on. And as ARM make progress in general purpose microcontrollers, then I think you'll see some more progress in automotive. As we make progress in the multimedia areas, navigation and those sorts of things, you will see us making progress in some of those in automotive.

And, to be honest, the analysis on the slides 31 through 33 is probably not perfect. And some of the automotive navigations could well be coming through in some of the other areas, as well as in the Automotive line. So we might, actually, be a little bit ahead of the number on the automotive line at the moment.

Janardan Menon - *Liberum Capital - Analyst*

Hi, it's Janardan Menon from Liberum Capital. I'll try and slip in a few questions here.

One is on the commission and bonus payments that you've paid in the last quarter. How should we think about that? Is that something that's more likely to pop up in Q4 every year? Or, if you do have a good licensing quarter in any quarter of the year, can they pop up here and there?

Second question is, you finished the catch up phase of your Physical IP business, and now you are licensing 32/28 nanometer Physical IP. So, does that give you a lift in terms of licensing revenue on the PIP division from the $9 million/$9.5 million that you're running at or is this it? Is it pretty much at the run rate that you think is going to be there in the long-term?

And three, there's been a lot of talk about the Netbook market and the -- and how ARM is penetrating there. Do you need an additional product there above the A-class processors, especially if in the future Microsoft comes to ARM processors, etc. and

you have a chance of getting into the laptop market as well? Is the Smartphone application processor-orientated product enough for that market or do you need something which can run at 2 gigahertz/3 gigahertz and compete with the best that Intel can throw at you?

And a fourth if I can throw it in is, on the microcontroller -- 32-bit microcontroller market alone just on the 32-bit part, do you have an estimate of what your market share was at the end of last quarter? Thank you.

Tim Score - *ARM Holdings plc - CFO*

Can I volunteer for the first one? You all right on the other three Warren? Delegation; upward delegation's a good idea.

I think you need to look at sales commissions and bonus payments separately, okay. The -- when I talk about the bonus this is the corporate-wide bonus plan that is tied into annual revenues and profits. And what you're trying to do with that, of course, is trying to accrue through the year, so that when you get to the end you've accrued the full amount.

So, therefore, in a fourth --- it could happen in any quarter, you could have a spike, but in the fourth quarter you can see from expectations that the outcome was a bit better than we would have accrued for in October. So there was a little bit of truing up. So you got accruals in Q1, Q2, Q3, which needed to be topped up.

Sales commission is something that is essentially paid following the previous quarter's performance, and you're obviously accruing for it based on what's actually happened in the quarter. Therefore, in any quarter, where there is a significant bookings quarter, you will get a higher commission. To be honest, quite often in our business it is the fourth quarter.

And I think we all know, because we talked about it before, in the third quarter that's quite a challenging quarter for licensing, because it's quite a short quarter. And quite often, fourth quarter budgets, people's mindset about getting deals done by year-end, that sort of thing, does -- this is not unusual that ARM's had a strong Q4 for bookings than we have in most other quarters. So, two slightly different reasons but, as I say, ordinarily you would expect that number to drop into Q1.

Warren East - *ARM Holdings plc - CEO*

Okay, let me deal with the other three questions. The first one was about Physical IP licensing and the fact that we now have our products available at 32 nanometers and what we're going to see in terms of how that translates to license revenue. I don't think you're going to see explosive growth in our physical IP license revenue. But I think you will see steady growth, not necessarily every quarter increasing. But we have spent time and effort getting this product portfolio in place. It is in place. It is being adopted by leading foundries and the products are being taken up by leading players.

So, I wouldn't expect to see it necessarily grow as rapidly as Physical IP royalty, which is, of course, cumulative compared with the licensing. And, as I said in the presentation, is driven off a whole lot of platforms, whereas we tend to be licensing probably more at the leading edge. So, you'll see growth, but modest.

Netbooks, PCs, high-end that question; I don't think we need a product which is specifically different. I think if you look at the top end of our application processor roadmap at the moment, we have Cortex-A9, which is not really in any end product as they exist today. If you go and buy a state-of-the-art mobile computing product, it's probably got a Cortex-A8 in it today, a single core Cortex-A8 running at somewhere between 600 megahertz and 1gigahertz. Cortex-A9 will comfortably run at those sorts of frequencies and, indeed, with physical IP optimization, we demonstrated can scale up to 2 gigahertz today on 40-G processors.

The other Cortex-A9 has a lot more headroom to go, it's a multi-processor design, so you can have quad-core -- or up to quad-core implementation. And one of the products that I had on the to be delivered flash released this year is Eagle, which takes our

---

application processor products onto yet another level of high performance. And obviously we'll talk about the details on that when we launch the product. Sorry, we're not launching it today.

So, I think we are addressing that market with the products we have and with the new products in the roadmap.

On 32-bit MCUs, have to confess we don't break that data out separately. We don't do that separately because we regard the 8-bit MCU market as fair game for our microcontrollers. And very much, I don't see it winning in 32-bit microcontrollers and just defining the market as that space as being winning. Winning is winning in microcontrollers where today the bulk of the volume is actually 8-bit microcontrollers and that's why we call that the market.

Didier Scemama - *RBS - Analyst*

Hi there, Didier Scemama, RBS. I would like to ask a couple of questions, if I may.

First of all, talking about, I think, your ambitions because I'm not sure they were targets were ambitions of market share in things like portable computing, e-readers, tablets, Netbooks. [I think, Warren,] could you refresh our memory as to where you think you could be this year.

Also, related to portable computing, should we assume that the royalties of PIPD will really take off when this portable computing opportunity really materialize? And I've got just two quick follow-up on licensing.

Warren East - *ARM Holdings plc - CEO*

Okay, I'll refresh your memory. I think what we said in June 2009 was that we have an internal target for 2010, to be in 20% of the Netbook. We actually missed that target by a long way; there are no appreciable ARM-based real Netbook products out there that you can go and buy today. There are many design wins, but I think the dynamics in 2010 have been held up by a couple of factors.

First of all, the economy and the industry at large was not a good environment for exploring new products. Secondly, there's been a lot of uncertainty over which Linux desktop operating system should be released and we had, in particular, a couple of switches around of which the favorite would be; so, a number of reasons.

But internal target we kind of missed. But I think as I said probably a year go, we're talking of 5 million or 6 million units here, when we're talking about these products. So let's put that in the context of the 3.9 billion ARM microprocessors shipped when we talk about the opportunity.

Your question actually referred to is there's more than just Netbooks, however. And you talked about e-readers and tablets and those sorts of things. I think you'll find pretty much all, if not all, of the e-readers are ARM-based that are out there. The one that we've got out there on the demo area is an ARM11, and most of the others are ARM11 as well, at the moment; so a very strong share in that particular form factor.

Tablets, when at CES you can see a few tablets based on our microprocessors and we'll see. It depends on things like the operating systems and exactly how those tablets take off.

Didier Scemama - *RBS - Analyst*

[Did you mean] 2009 for your targets not 2010?

THOMSON REUTERS

Warren East - *ARM Holdings plc - CEO*

Sorry?

Didier Scemama - *RBS - Analyst*

You meant 2010 or 2009 when you said 20%?

Warren East - *ARM Holdings plc - CEO*

Yes, by the end of 2010. It was, you're right.

Tim Score - *ARM Holdings plc - CFO*

I think he's declared failure a bit early.

Didier Scemama - *RBS - Analyst*

Yes, that's what I thought.

Warren East - *ARM Holdings plc - CEO*

Just pointed out I got my years messed up.

Didier Scemama - *RBS - Analyst*

Okay. And just a quick one on licensing, you announced Cortex-A5 as a replacement to the ARM926 for baseband. Can you talk about maybe licensing output for that part? What sort of feedback you get from your clients. And also, if you could give us an idea of [what] you're looking in the roadmap at the ARMv8, so the next processor core. What sort of performance are we looking at in terms of gigahertz/power consumption?

Warren East - *ARM Holdings plc - CEO*

All right. Cortex-A5 we've had a little bit of licensing of Cortex-A5. We've not particularly separated it out in these numbers. We would expect that part to license quite strongly into the user base for ARM926, ARM1176-type products. This is for people who are building an application processor, but perhaps one that's perhaps going to sell at a slightly lower price point than a Cortex-A8 or a Cortex-A9. So, we see that going forward.

Your last question, I'm afraid --

Didier Scemama - *RBS - Analyst*

I was just wondering if you could give us a flavor of the ARMv8, what [features] we're looking at here?

Warren East - *ARM Holdings plc - CEO*

Well, as I said, in answer to the previous question, we're not ready to talk about future products in detail today, unfortunately. That comes at product announcements not earnings announcements, sorry.

Didier Scemama - *RBS - Analyst*

No problem. Thank you.

Simon Schafer - *Goldman Sachs - Analyst*

Thanks. Simon Schafer, Goldman Sachs. I want to ask a follow-up question on Janardan's point on PIPD? Should we take the statement that licensing revenue in PIPD is perhaps growing moderately? And if we look at last year, your cost base was almost twice the run rate of your sales level. I know perhaps on a reported basis, net's not quite the same as you think about it.

But in that context, if licensing's really growing at a moderate pace, as you say, it'll take you a good three years to get that business to breakeven on a stand-alone basis, unless costs are falling. So should we assume costs are falling very substantially, or does it just mean that we're looking at a significant loss run rate for an additional two years?

Tim Score - *ARM Holdings plc - CFO*

Don't forget when you look at those, the segment analysis, you have to allocate all of, in a sense, the fixed costs of the business across the revenue earnings streams, okay. So, incremental PIPD revenue makes a big difference in terms of the contribution it generates on top of the fixed. So if you look at here's PIPD revenue, here's PIPD direct costs, that is what we're going to see in improving profitability. So, yes, you're right, you need to look at a direct and contribution level versus covering fixed costs.

Simon Schafer - *Goldman Sachs - Analyst*

Yes, I'm not sure I understand. Does that mean that cost is being reduced for that standalone business or it'll take three years to be profitable or breakeven on a standalone basis? I understand the difference in allocations but --

---

Tim Score - *ARM Holdings plc - CFO*

Yes, I don't we're prepared to sit here and say costs in that division will fall over the coming years. But what we are prepared to say is that costs will rise much more slowly than revenue. And I'd point you -- and the reason that we included on the slide the productivity increase, that's how we're driving the increased revenue, more products coming out of there.

The investment has not just been about developing new products. It's about investing in developing the new product development process, which enables us to be much more efficient and enables us to grow the business without really growing the cost line very much at all.

Brett Simpson - *Arete Research - Analyst*

Thanks, it's Brett Simpson, Arete. I've a couple of questions, maybe first for Warren. At lot of the mobile chip makers have started to report fourth quarter numbers and suggesting down revenues sequentially, and they're warning about pricing for next year being a much tougher environment. So, I'm just -- you put a chart up showing the value, the ARM royalty per handset it continues to go up. It's been a consistent theme over the last four or five years. In the face of chip ASP declines for the chip makers, and Smartphone ASP declines, how do you see -- how sustainable is rising value -- royalty value per handset and mobile?

THOMSON REUTERS

Warren East - *ARM Holdings plc - CEO*

Well of course, the answer that pops out is the result of how quickly does the number of our microprocessors per handset increase compared with the ASP of those that are there decline. And if one declines -- if the one declines faster than the other one increases, then you won't see that chart continuing to increase.

But I would say that price pressure and price erosion is a feature of our industry, has always been a feature of our industry, and applied just as well in 2004 when we started doing those charts, as it does today. And so, history doesn't necessarily guarantee the future, but it's a pretty good indicator and so I think we'll see that chart continuing to increase.

Brett Simpson - *Arete Research - Analyst*

(Inaudible) for Tim. Can you maybe just confirm where the order cover for PD licensing is for 2010? Normally, it's around the 50% level as you enter the year, is that still the case this year?

Tim Score - *ARM Holdings plc - CFO*

I would say historically it's been more round the 40%, which is what we said and I would say it's at the right side of that coming into 2010.

Arun George - *Noble - Clear Capital - Analyst*

Arun George from Noble. Just one question for you Tim. In terms of the long-term operating margin target of 40%, what's your underlying assumptions for the margins of PD and PIPD?

Tim Score - *ARM Holdings plc - CFO*

We don't go into that level of details in terms of margin, and the reason for that is that this business has many elements. The costs base of this business are unified and one. And so I think the key point is operating leverage in this business is not just about the process of royalties growing faster than the cost base.

[Simon], I appreciate that wasn't a very coherent answer, but PIPD and the sort of things that Warren was talking about is a very -- is going to be a very meaningful contributor to the increase in the overall Group margin. Because a revenue line that's growing modestly on licensing and probably better than modestly on royalty, with a cost base that's much flatter than the rest of the Group, the increase in contribution from that division to cover the fixed overhead of the wider ARM business is going to be really quite meaningful.

But we don't any more break down, sort of artificially recreate, for the external audience the margin by division, because we don't really manage the business quite like that.

Arun George - *Noble - Clear Capital - Analyst*

Thank you.

Didier Scemama - *RBS - Analyst*

I've got a follow-up question. We are seeing some of your customer referring to 32-bit controller at $0.65 today. Do you think it could be a trigger for the industry to accelerate the migration to the 32-bit and to keep the 16-bit actually.

Warren East - *ARM Holdings plc - CEO*

By the way, I think we'd better have only one more question after this if there is one, because time is marching on. We'll be here to talk after the event.

That's one factor, which could contribute. You would expect me to say this, but I'm a firm believer that the market is going to migrate from 8-bit to 32-bit and 16-bit is going to be a niche area. And I think it isn't just the cost that's enabling that. It's all the advantages of 32-bit and, in particular, the tremendous industry standard that ARM has become. And the knowledge base that's out there around the ARM architecture just makes it very compelling.

If you can do that with no cost increment, compared with an 8-bit controller then you can do it with no cost increment, compared to a 16-bit controller; 16-bit just doesn't win. So, I think it is going to happen, the cost is one of the factors.

I think this is the last question.

Paul Morland - *Astaire Securities - Analyst*

Hi, it's Paul Morland from Astaire Securities. Just -- my question's just on the cash actually. You've just come off your best six month cash conversion in the last six six-month periods. Can you just say what's behind that and what it might mean for cash conversion going forward?

Tim Score - *ARM Holdings plc - CFO*

Well, I think in absolute terms what you've actually seen in the second half is really quite a pick-up in revenues, and specifically royalties, at a time when the cost base has been managed really quite hard, pay freeze and everything else. So -- and I'd also say that royalties, which has been one of the key drivers, you tend to collect quicker because it's one quarter in arrears. When the reports come in the cash is either same time or shortly thereafter.

So, I think the prognosis for profitability, which as you can see translates into cash pretty quickly, is looking very positive. I think -- it's on an upward trend and that's what you're seeing in the six month conversions.

Warren East - *ARM Holdings plc - CEO*

Okay, with that thank you everybody for your support and we'll see you in July.

Feb. 02. 2010 / 9:30AM, ARM.L - Q4 2009 ARM Holdings plc Earnings Conference Call