SYNAPTICS – THIRD QUARTER, FISCAL 2019 CONFERENCE CALL SCRIPT

CALL IS ON THURSDAY, MAY 9, 2019 AT 2:00 PT

Good afternoon and thank you for joining us today on Synaptics' third quarter, fiscal 2019 conference call. My name is Jason Tsai and I am the head of Investor Relations at Synaptics. With me on today's call are Kermit Nolan, our Interim CFO and Chief Accounting Officer, and Saleel Awsare, Senior Vice President and General Manager, of our IoT Division, Corporate Marketing & Investor Relations. This call is also being broadcast live over the web and can be accessed from the investor relations section of the company's website at synaptics.com.

In addition to a supplemental slide presentation, we have also posted a copy of these prepared remarks on our investor relations website. The supplementary slides have also been furnished as an exhibit to our current report on form 8-K filed with the SEC earlier today and add additional color on our financial results.

In addition to the Company's GAAP results, management will also provide supplementary results on a non-GAAP basis, which excludes share-based compensation, acquisition related costs, and certain other non-cash or recurring or non-recurring items. Please refer to the press release issued after market close today for a detailed reconciliation of GAAP and non-GAAP results.

Additionally, we would like to remind you that during the course of this conference call Synaptics will make forward-looking statements. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance and business. Although Synaptics believes our estimates and assumptions to be reasonable, they are subject to a number of risks and uncertainties beyond our control and may prove to be inaccurate. Synaptics cautions that actual results may differ materially from any future performance suggested in the Company's forward-looking statements. We refer you to the Company's current and periodic reports filed with the SEC, including the Synaptics Form 10-K for the fiscal year ended June 30, 2018, for important risk factors that could cause actual results to differ materially from those contained in any forward-looking statement. Synaptics expressly disclaims any obligation to update this forward-looking information.

I will now turn the call over to Saleel Awsare. Saleel?

SALEEL: INTRODUCTORY REMARKS

Thanks, Jason, and I'd like to welcome everyone to today's call. I'm happy to be speaking to you today on behalf of the Board and our Executive Leadership Committee. I will first discuss the opportunities that lie ahead for Synaptics and update you on our business and then I will turn the call over to Kermit to discuss our financial results and outlook.

Synaptics is undergoing a corporate transformation, focused on driving innovation, unlocking the untapped potential within our extensive portfolio of technologies and expertise, and aligning the business towards better profitability longer-term. Our Board and executive leadership committee is committed to improving shareholder returns by carefully evaluating the opportunities ahead in the markets we serve, and making the right investment choices to further improve our gross margins. We are thoroughly reviewing our product portfolio to better leverage our best-in-class solutions with an eye toward positioning the company for higher gross margins and profitability longer-term. We are moving quickly to strengthen our performance and address the challenges we face.

With that said, let me now share a few product and customer highlights.

For our IoT division, Synaptics is laser focused on innovating at the Smart Edge, and we are very pleased to share that our new AS3-hundred family of SoCs, announced at CES earlier this year, has already begun shipping millions of units to a major customer, a full quarter ahead of schedule. The AS3-hundred family is at the heart of our Smart Edge AI AudioSmart solution, the world's first commercially available, fully integrated SoCs that incorporate machine learning neural network acceleration, a proprietary wake word engine, and highly-advanced far-field voice processing. This is also our first shipping design in 22nm, enabling a broad variety of voice-enabled Smart Home devices including hubs, Wi-Fi repeaters, speakers and appliances.

We are the leading solutions provider for intelligence at the edge, and we expect to capitalize and extend this lead. Smart Edge requires innovative technologies and integrated platforms that support the full range of consumer needs. Synaptics is building on its legacy as the leader in human interface technology to deliver a broad range of differentiated integrated solutions that encapsulate voice and audio, video and display, AI, as well as security and consumer privacy.

The market and adoption for these solutions are still in their infancy, and our differentiated portfolio will deliver best-in-class capabilities to the entire ecosystem and drive meaningful growth for our business over the next several years. We will continue to leverage our industry-leading technology and will launch some very exciting new products later this year that will drive further integration of our human interface portfolio.

In the mobile space, we continue to win major OEM's smartphone designs for both LCD and OLED displays. In LCD, we are enabling more infinity displays with our Full-HD TDDI COF solutions, including two new designs from Huawei and additional wins with other large OEMs. Our low power Full-HD TDDI solution also has flagship design wins at OPPO and Vivo. In OLED, we continue to win share in the high-end segment of the market and expect to see upcoming flagship devices from leading handset OEMs continue to be supported by our best-in-class OLED discrete DDICs and touch sensors. While OLED solutions will continue to be a strong growth driver for our mobile business, we anticipate that LCD-based smartphones will remain a vital part of our customers' portfolio for the next few years. We are seeing ongoing development with our largest customers for LCD-based handsets for their next-generation flagship and mainstream smartphones. We are excited by the progress we are making and are dedicated to supporting all of our large handset OEM customers as they ready their next-generation devices that will launch later this year, whether it be for LCD or OLED.

Smartphone headsets are transitioning from analog to digital, and we continue to leverage our best-in-class digital audio SoCs for this rapidly emerging USB-C headsets market. With that, we are pleased to announce a new USB-C headset design win with an additional top-three smartphone OEM for their upcoming flagship smartphone that will be included in every box worldwide. We will ship a few million units in the current quarter for this new design win, and it is expected to grow throughout the rest of the year. This follows our previously announced digital audio headset and dongle solutions shipping in the box with Google Pixel 3, and with multiple Huawei phones. The market for digital audio is growing very quickly, and our technology leadership in this space has enabled us to capture meaningful wins at the world's largest OEMs. We are very pleased with our progress and expect to see the wearables segment grow strongly for us as digital audio and active noise cancellation adoption for smartphones continue to expand.

On the topic of wearables, at the recent HP Reinvent World Partner Forum, HP unveiled its cutting-edge Virtual Reality headsets featuring Synaptics' ultra-high-resolution VR display technology. Our industry-first breakthrough display technology supporting higher resolution per eye has enabled OEMs to design a new generation of VR headsets with meaningfully better visual capabilities, bringing users a more immersive and better experience than ever before. Other VR headset makers that recently announced products using our display technology include the Pico G2 4H headset, and Acer with its ConceptD OJO. Worth noting is that Synaptics is the only company delivering an end-to-end (GPU to Display Pixel) solution by leveraging our VR bridge.

Just a quick note on our Automotive business. We are pleased to have secured many design wins with our TDDI and Fingerprint-based solutions, both of which position us well as these cars begin to roll off assembly lines over the coming years.

We continue to execute on our long history of delivering best-in-class human interface innovation to the worlds' leading technology companies, and we are excited by our strong pipeline of new products and design wins that will ramp later this year across all of our different products.

Lastly, I want to provide an update on our search for new executive leadership for Synaptics. The Board has engaged an executive search firm, and interviews for the CEO position are already underway. The priority is to fill this role before resuming the search for our next CFO. Given Synaptics' proven track record of technology innovation and market leadership, we expect to attract world-class talent and will update you as quickly as possible on our progress.

With that, Kermit will now discuss our results and outlook.

KERMIT: FINANCIAL RESULTS AND OUTLOOK

Thank you Saleel, and hello, everyone.

Synaptics posted third quarter results with revenue of $334 million, down 22% sequentially and slightly below our guidance range. Weakness in the quarter was primarily attributed to softness in the smartphone market, particularly in China, as well as the temporary impact of product transitions within our IoT business, partially offset by continuing stability in our PC products.

As reflected in the presentation materials released in advance of this call, revenue from Mobile, IoT and PC products was approximately 61%, 19%, and 20%, respectively.

During the quarter we had three customers above 10% of revenue, at 17%, 16% and 10%.

For the March quarter, our GAAP gross margin was 34.7%, which includes $15.2 million of intangible asset amortization, and $700,000 of share-based compensation costs.

GAAP operating expenses in the March quarter were $119.8 million, which includes share-based compensation of $15.1 million, acquisition related costs of $3.3 million, consisting primarily of intangibles amortization, and some transitory compensation program costs.

Our year-to-date GAAP tax rate was a negative 49%.

In the March quarter we had GAAP net income of $6.7 million, or $0.19 per diluted share.

On a non-GAAP basis, our March quarter non-GAAP gross margin of 39.5% was above our guidance range and primarily reflects an overall positive product mix. This was our seventh consecutive quarter of non-GAAP gross margin improvements.

March quarter non-GAAP operating expenses were $99.2 million, which was lower than expected primarily reflecting a reversal of variable compensation accruals from the first half of fiscal 2019.

Our year-to-date non-GAAP tax rate was 12%.

Non-GAAP net income for the March quarter was $29.0 million, or $0.83 per diluted share - a 10% decline year-over-year compared with $32.4 million, or $0.92 per diluted share, in the March quarter of last year.

Turning to our balance sheet, we ended the quarter with $324 million of cash, an increase of $41 million from the preceding quarter, which reflects approximately $47 million of cash flow from operations net of $7 million used for capital expenditures during the quarter. Depreciation for the quarter was $8 million.

Receivables at the end of March were $267 million and DSOs were 72 days, reflecting a back-end loaded quarter. Inventories were $153 million and inventory turns were 5.3.

Further, while we did not repurchase shares in the third quarter, we do have $148 million remaining in our share repurchase authorization and intend to opportunistically repurchase shares.

Now I will make a few comments regarding our quarterly outlook.

Based on our backlog of approximately $210 million entering the June quarter, subsequent bookings, customer forecasts, product sell-in and sell-through timing patterns, as well as expected product mix, we anticipate revenue for the June quarter to be in the range of $300 million to $320 million.

For the June quarter, by product, we expect our IoT revenue to grow sequentially; we expect that our mobile revenue will decline sequentially as a customer works through inventory in their supply chain; and our PC revenue is expected to be stable. Revenue mix in the June quarter from mobile, IoT, and PC products is expected to be approximately 55%, 25% and 20%, respectively.

During the second half of the calendar year, we expect growth in IoT and mobile revenue, while PC revenue is expected to remain stable.

We have taken a cautious approach to our guidance, considering the impact of existing supply chain inventory levels. We anticipate that the level of product currently in the supply chain will be sufficient to meet the reduced demand for certain of our high-end display driver products from a leading smartphone OEM, which we believe will clear in the first quarter of fiscal 2020.

I will now provide GAAP outlook data for our June quarter, and will follow with non-GAAP outlook data:

We anticipate the stock-based compensation charge in the fourth quarter to be in the range of $16 to $17 million.

In addition, June quarter GAAP expenses, will include non-cash charges of approximately $18 million related to intangibles amortization, of which approximately $15 million will be reflected in cost of sales.

I will now provide non-GAAP outlook data for our June quarter:

Based on our overall revenue mix, we expect non-GAAP gross margin in the June quarter to be between 37.5 and 38.5%. Gross margin is expected to decrease slightly sequentially due to product mix within mobile.

We expect non-GAAP operating expenses in the June quarter to be in the range of $102 million to $106 million. Our OPEX is expected to be stable sequentially if you exclude the one-time reversal of compensation accruals in the March quarter.

We anticipate our non-GAAP long-term tax rate for fiscal 2019 to be in the range of 11% to 13%.

Non-GAAP net income per diluted share for the June quarter is anticipated to be in the range of $0.20 to $0.45 per share.

Let me finish with some commentary around what Saleel addressed. As we look to transform the company, we are reviewing options to drive profitability, align costs and increase cash flow as we manage through short-term challenges. We will evaluate each of our product offerings carefully and look at opportunities with a much greater focus on profitability to drive investment choices. As we complete the process, our goal is to emerge with a business that will drive our overall corporate gross margins into the 40s percentage range, while aligning spending to improve operating margins and drive our business towards greater long-term profitability.

With that, I'll hand it back over to Saleel.

SALEEL:

Thanks, Kermit.

While we continue to work through some residual supply chain issues that are impacting our short-term financial results, we remain keenly focused on executing on our strengths and delivering on the untapped potential of our product platforms. This will entail an even more pronounced effort to reshape our portfolio towards higher margin products, with the goal of achieving meaningfully better gross margins longer-term. We already have the building blocks and customer wins in place to execute across our IoT platform, where we expect a return to growth and to drive even greater momentum across the portfolio.

We will couple this with smart, targeted investments in key products and market opportunities, as well as a focus on spending alignment to conform with the product areas that we choose to focus on over time. We are intent on delivering consistent, improved profitability for Synaptics over the long-term. We are in the initial phases of this process to directionally improve our long-term profitability and plan to keep you updated on our progress regularly. I am confident that we are making the necessary changes and focused on the right priorities to accelerate Synaptics into a stronger future.

Finally, we are participating in a few key trade events this month where we will demonstrate our latest innovations. This includes Display Week, which is next week in San Jose, and Computex in Taipei at the end of the month. If you are attending, we welcome you to stop by for a demo.

With that, I'll now turn the call over to the operator to start the Q&A session.