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Richard Kramer *Arete Research - Analyst*

PRESENTATION

Operator

Welcome everyone to HTC's 2014 fourth-quarter results conference call and webcast in English. Today with us we have CFO and President of Global Sales, Mr. Chialin Chang; AVP of Finance, Mr. Edward Wang; and Manager of Investor Relations, Ms. Christine Chi; Ms. Kelly Hsu; and Ms. Sally Kuo.

(Operator Instructions) For your information, this conference call is now being broadcasted live over the Internet. Webcast replay and English transcript will be available within an hour after the conference is finished, and Chinese translated transcript will be available within a week after the call is finished.

Please visit www.htc.com under the investors section. And now I would like to introduce Ms. Christine Chi, Manager of Investor Relations. Ms. Chi, you may begin.

Christine Chi - HTC Corp - Manager, IR

Thank you. Good morning, good afternoon, and good evening, ladies and gentlemen. Welcome to HTC's 2014 (corrected by company after the call) fourth quarter analysts call. This is Christine Chi, HTC's IR manager. The event is now being broadcasted live via HTC's website at www.htc.com. If you are joining us through the dial-in line, your call is now being placed on mute.

As this conference is being broadcasted by investor around the world, we will conduct this call in English only. The format for today's call will be as follows; first I will help to summarize our operations for fourth-quarter 2014 followed by our guidance for the first-quarter 2015.

After, our CFO and President of Global Sales Chialin Chang and AVP of Finance Edward Wang will lead the Q&A session.

Before we begin, I would like to draw your attention to the disclaimer statement on page 2 of the presentation slides. Please note that this presentation contains forward-looking statements. These statements are based on our current expectations.

Actual result may differ materially from our expectations, and the Company undertakes no obligation to update these forward-looking statement going forward. If you have no questions, I may begin the overview of fourth-quarter 2014.

Please turn to page 3. Page 3, fourth quarter financial highlights. Revenue for fourth quarter is TWD47 billion with gross margin of 20.4% and operating margin of 0.4%. Net profit after tax was TWD0.5 billion, and EPS is TWD0.57 per share.

Fourth quarter overview; HTC maintained profitability in the last quarter of 2014. Revenue up 12% year on year, 14% quarter on quarter on back of the ability to offer tailored product mix in suitable price points which enable us to closely address the need of specific markets.

We embarked a diversification strategy in fourth quarter to extend the mobile lifestyle and broaden consumer reach. HTC entered into the first of several strategy partnerships aimed at facilitating the new product categories.

Collaboration with Under Armour announced at the CES show in Las Vegas early this year aimed at bringing a line of connected health and fitness-related devices to market that helps the athletes of all levels.

The HTC RE camera was launched in fourth quarter of 2014, and took considerable acclaims from lifestyle and consumer media. This remarkable little point-of-view camera redefine lifestyle photography, enabling people to step out from behind the viewfinder and capture the moment.

The award received in 2014 (corrected by company after the call) fourth quarter spanned multiple media types as HTC products extend their appeal beyond the mainstream tech and gadgets media segment.

The HTC One (M8) won another host of award including the "Best Android Phone You Can Buy" by Business Insider; "Best All-Round Smartphone" by PC World; "Best Smartphone of 2014" by TechCentral; and Smartphone of the year by T3, and also by Travel and Leisure, a lifestyle publication in North America.

This also -- it also won numerous award in China from Tencent, E-fashion and News Press Daily among others. In addition to M8 award, the innovative DotView casing also was named the "Wireless Handsets Accessories Honoree" by CES Innovation Awards, while the RE camera won the gold medal for Design by Spark Awards.

Page 4; page 4 gives an overview on revenue and operating profit. Revenue for fourth quarter came in at TWD47.9 billion, operating profit at TWD0.2 billion.

Page 5; page 5 gives an overview of gross margin and operating margin. Gross margin for fourth quarter was 20.4% and operating margin for fourth quarter was 0.4%.

Page 6 and 7 for the financial overview for income statement and balance sheet.

Page 8, guidance for the first quarter of 2015. Revenue is expected to be at a range of TWD41.5 billion to TWD45 billion. Gross profit margin is expected to be 19.5% to 20%. EPS expected to be in the range of TWD0.08 to TWD0.47 per share.

This draw out the content of our presentation. And now I would like to turn the podium to HTC CFO and President of Global Sales, Mr. Chialin Chang. Chialin? Moderator (technical difficulty) -- any question.

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions)

Chialin Chang - HTC Corp - President of Global Sales & CFO

Hi everyone, this is Chialin. Before we take question, I just have a few points to make -- to share with everybody. So to get a quick state of business where we are at HTC.

First of all, our revenue was up in Q4 last year. It was up sequentially quarter over quarter. It was up on year-over-year comparison basis. One thing I want to highlight is that actually quarter four last year is the quarter we have highest number of smartphone shipments in the last I will say probably quite a few quarters, starting in 2014, possible in 2013 as well.

Getting the number of shipment with the right price positioning to us it's important. We're seeing the momentum going into 2015. Obviously this is a market that's very competitive, but we feel positive about where we can capture the market share in places we could improve and places that we need improvement is number one.

Number two, Peter, our CEO, has been working, meeting, and driving business beyond smartphone. And he -- what you see here, he has been doing that actually since 2013. So it's quite a lot of quarters already.

We're seeing some early fruits that's been announced. I think the RE camera is one thing aiming for lifestyle recent. You see that we launched in Q4 last year.

Under Armour announcement you heard connecting in the fitness and healthcare -- in the fitness and connected health area that we're going to have exciting parts to come later in the year. We'll have more exciting emerging opportunities that we'll welcome everybody on this call to stay tuned in the coming months for further announcement we feel quite exciting in areas beyond the smartphone as well.

So in the end what you see, we want to have a balanced growth, both the smartphone, the tablets, as well as the emerging opportunities that we talked about. And we have quite a few areas in emerging opportunity we are quite excited about.

So I'll just pause here and answer any question.

QUESTIONS AND ANSWERS

Operator

Thank you Mr. Chang.

Arthur Hsieh, UBS.

Arthur Hsieh - UBS - Analyst

And -- well, I think it was great to see that you are returning to growth. I have three questions. First is that when you mentioned about the tailored products mix at the suitable price points, would you be a little bit more specific about what are the sweet spots that you found that you could potentially extend the initial success and further expand your current position? So that's the first question.

I think together -- along with the first question especially about the areas beyond the smartphones, I think RE is an interesting product. But to the management, how would you assess the success or not of that product? Could you also comment on that?

Chialin Chang - HTC Corp - President of Global Sales & CFO

Yes, thanks Arthur. The -- to answer your first question in terms of what we meant by having a suitable product, the world is very diverse, and in major country including developed countries as well as emerging market, there are different stage of wireless development and infrastructure.

And different country and region have different GDP per capita. So it's important to have a portfolio even for the same price point a different product tailored into the need of consumers.

I'll give you the examples. The -- you have developed countries in US, UK, Germany. They are operator-driven and the need for that is actually different from the need in China even though China is pretty much -- a big majority is migrating to 4G.

That is also further different from the areas like India and Middle East, it could be a mix. If you look at Dubai, it's different from the other places. So you're seeing a very diverse world.



So how do we leverage our capacity and capability with internal-external resources to capitalize that? That's something we're working on. That's what I meant.

The second question on RE on how do we measure the success. At the end of the day, the success of business obviously is the revenue and profitability and the return to shareholders. I think RE is one thing little -- we call it a little remarkable camera that actually for everybody who is aware and using it, they are all quite excited about it including my -- the friends, associate in my circle as well.

The success for us in the beginning is people feel like it's very nice and handy lifestyle-connected device. I will call it connected self, which to us is very important. In the further development in wireless world and mobile world, how do we see a different category of connected world and domain to us is important.

So this is, as I said, beginning, it's just a start. The kind of brand impact also important for HTC to be seen, not just a smartphone brand, the high-end smartphone brand or mid to high-end smartphone brand, but in seeing as very cool our lifestyle brand including smartphone and other connected devices that for us is important.

So that will be my response to your question for second one.

Arthur Hsieh - UBS - Analyst

Thank you. Would you be able to provide the contribution in terms of sales and earnings from RE?

Chialin Chang - HTC Corp - President of Global Sales & CFO

No, I don't think we are able to comment on that. I think in a quarter or two, we should be able to comment on that. We start getting traction in major region. We haven't really do -- to be honest, haven't really done the whole entire global launch. We're going to do one by one.

The way we do it here is actually different from the -- a smartphone brand. Just give you an example, you can go in Hong Kong, it's actually the number one lifestyle camera is RE camera. You can go and ask and check the data. So we want to do one by one in major countries. So that's the area we're aiming for.

Arthur Hsieh - UBS - Analyst

Sure. Thank you. And the second question is with regard to the (inaudible). I think the mid-point of your sales suggest around close to 10% sequential decline. I think it's already well-circulated there could be a potential constrain of key component. That's actually affecting many players in the industry.

So I think the question is about whether your current guidance already discounted any kind of potential impact coming from -- the component I'm referring to is a flagship chipset supplying by one of your strategic supplier.

So how robust is the guidance in you responding to this potential component supply issues? Now that's the second question.

Chialin Chang - HTC Corp - President of Global Sales & CFO

I -- first of all, the guidance we're providing obviously taking into account a lot of uncertainties, okay? There's all sorts of different uncertainties we combined there. It's very hard in the smartphone world to guide -- sort of like we're trying to be as transparent as possible based on the outlook we see.



I can only tell you qualitatively we feel good in terms of momentum in some of the product lines there in certain markets, but given the -- a lot of uncertainty here, we just can't comment further on that. And I want to comment on something you referred to in terms supplier, and I will be explicit on your comment.

I think you mentioned Qualcomm. I want to comment on Qualcomm there. I think HTC has historically working very well with Qualcomm, and in the vast majority of instances, actually HTC is the one pioneering Qualcomm's flagship chipset.

And I think the -- we're very excited about working with Qualcomm and leveraging their high-end flagship chipset solution. So we've been working well with Qualcomm. And now there's odd news and rumors circulating around here. I don't want to comment on those.

I only want to comment that HTC feel very comfortable working with Qualcomm and in terms of their kind of historical relationship, and we feel very positive going forward as well.

Arthur Hsieh - UBS - Analyst

Well, thank you for the feedback. And the last question, I think it's with regard to the recent partnership between several handset OEMs with the Internet companies, and also increasing push into this online distribution channel. So how do you see this change in the landscape in terms of a lot of these Internet companies getting more aggressive, getting into these power products? And also how is the current status of your online business?

Chialin Chang - HTC Corp - President of Global Sales & CFO

I think the -- thanks Arthur, for the -- we notice the news going on and then we play in the industry, so we are aware of some sort of alliance in that regard. What I will comment on is all our e-commerce is always going to be quite important part of the sales channel.

In China, it's seen very strong. In India as well. And some people using it in terms of getting the buzz out and then to help selling it in the offline. I think to us we just want to have a balanced and healthy approach. You also saw the -- we opened our e-commerce store in Taiwan. We had a pretty healthy business in the last two or three days. So we want to have a balanced approach.

With that said, the physical storage channel is actually quite important to us. So that's something we cares too much. So we feel like we need to have a balanced growth in that regard in channel distribution.

Arthur Hsieh - UBS - Analyst

Well, allow me to ask the question in a different way. Well, first of all, do you feel the need to find some partner in this Internet world and do you need to invest more, try to expand your overall sales distribution through this online channels?

Chialin Chang - HTC Corp - President of Global Sales & CFO

I think what you meant by that -- find partner means finding a partner having some sort of equity investment or joint venture.

Arthur Hsieh - UBS - Analyst

Yes. Well, it could be either, yes.



Chialin Chang - HTC Corp - President of Global Sales & CFO

At this stage -- I can tell you at this stage here we have not thought about that. That's what I can comment. In terms of working business-wise with all these big online players, that's actually happening in terms of daily activity.

Arthur Hsieh - UBS - Analyst

Right. So does that mean that actually the overall handset sales volume through the Internet channels is increasing and you need to expand the related investments in this area?

Chialin Chang - HTC Corp - President of Global Sales & CFO

We already have the infrastructure, online infrastructure in terms of e-commerce both the -- in our internal e-commerce. You can see the eStore in China and eStore in Taiwan. We're going to open up other eStore in other region when it's ready. We are also working well with the partners in terms of big eStore guys in China and also in India, but as I said we need to have that balanced approach.

Arthur Hsieh - UBS - Analyst

All right. Thank you. Enjoy the party tonight.

Chialin Chang - HTC Corp - President of Global Sales & CFO

Thank you. Thank you, Arthur.

Operator

(Operator Instructions) Richard Kramer, Arete Research.

Richard Kramer - Arete Research - Analyst

Several questions if I may. First one, and very simple one, when you look at wearable with Under Armour, with RE, with the tablet, putting all this together, will this be a material part of sales in your guidance for first quarter or 2015, or is this something that we should look at as being good for the brand overall rather than a separate business in its own right?

Chialin Chang - HTC Corp - President of Global Sales & CFO

I think the -- I can tell you the -- in our (technical difficulty) the material part of it for Q1 guidance, certainly we hope that these are going to be material in the second half and even more material obviously is a very fuzzy and quality definition of material.

We certainly hope that it start becoming more -- I would say the start becoming more meaningful in the second half and become more material in the financial world terms into the 2016 and beyond.

Richard Kramer - Arete Research - Analyst

Okay. I'd also like to ask about the cost structure of the business and how you see HTC moving to being sustainably profitable. I mean, this is the year where you seem to be settling into a pattern where marketing costs are fairly flat with a spike in second quarter around the flagship launch.



And we also saw G&A get cut by more than a third sequentially to the lowest level since, I think, second-quarter 2010. So how do you think about beneath a 20% gross margin which seems to be an industry level right now moving the Company towards being sustainably profitable more than a third of a plus-minus few percentage points operating margin?

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

I think to answer your question, to us profitability is important. I think to us growth with profitability is quite important. You need the growth, you need the volumes so to make sure that there's a healthy flow in the channel. That's important from the channel partners' perspective. Profitability to us obviously very important.

To answer your question on the OpEx front, I don't think we -- just to be -- to give you more color I think we didn't really cut G&A. The G&A has historically being lean on HTC.

What you see the number of reduction, it's just the legal expense reduction. There's some settlements in there, that's why there's a legal expense reduction. So legal expenses, that's a bit uncertain, depends on the situation. But outside legal, G&A has always been lean. It's always been that case. We didn't cut anything to be very candid with you.

On the marketing expenses as we talk about it and as we're going to repeat again here, we want to make sure that the -- you balance that, the awareness and preference in terms of marketing spend so you balance the efficiency and effectiveness there. And in certain places when you work with partners, especially in the operators, the spending may be high in certain places when you work on distribution.

When your brand is strong that the -- then the spending could be even more efficient in that regard. So we're constantly balancing that.

Richard Kramer - *Arete Research - Analyst*

And I guess the last question just to understand this rising level of shipments in Q4 and how you see it going forward, can you give us a sort of regional breakdown of where you are seeing the volume increases?

And especially I think there's a lot of concern in China and in Southeast Asia markets generally about just how cutthroat the competition is and how many players there are and what limited margins they are operating on. So can you give us a sense of where are the volumes ramping for you, in which sort of price tiers, and where do you see that continuing in --?

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

I can give you a couple of the indication there. I think the -- we're getting -- we become stronger in the US given the portfolio we adapted, we talked about earlier. I think we're also seeing a good recovery in our UK business.

Our UK last year overall [form] is actually quite good. We're seeing a pretty substantial in India and I think we maintain in China, like you said the -- we want to be taking a very careful approach not to get into that kind of bloodbath, but we have different way we think we can continue to improve in terms of getting the growth in China business in the area which we get the right brand attraction.

Southeast Asia, we're historical not there yet compared to other regions there. I don't think we're seeing a meaningful outcome until probably middle of the year to the second-half of the year in Southeast Asia. So the impact on the HTC business is not material, but we do have ambition to grow there given the size there.

Taiwan, you saw Taiwan I think we have ambition to further grow market share. We're going to cater into different price tier. So that's a different color for you. I think Middle East we're also seeing growth. If I understand correct here, our market share in Dubai actually is quite good.



Richard Kramer - *Arete Research - Analyst*

Okay. And maybe just the last thing on that, you've traditionally had sort of one big flagship launch of the year, but it seems now your success is coming more from taking that flagship and translating it to lower price points.

Will that change the sort of cadence of products and the approach to the portfolio this year, or should we expect very much the same thing we've seen over the last four or five years from HTC?

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

You said this changed the last four or five years. I think the -- I would answer in a slightly different way.

First of all, I can tell you M7 is the best-selling product in the entire calendar 2013 and made HTC One -- I shouldn't say M8, I should just be careful in the wording that HTC One (M8) is the best-selling product in terms of volume. It's the highest shipping units to be precise of HTC product portfolio in 2014 calendar year.

And we expect HTC One, the new flagship product in 2015, will be -- continue to be the highest selling sort of single product unit in that regard. That's all we aim for.

We want to use that to create the halo effect to get it into the different -- the Desire line and also the rest of product in HTC One. What I want to say differently here is it's not just getting into different, let's say, low-price product there. Entry-level LTE is just one bucket of things.

We're actually getting into -- if you look at our market share, if I've read the data correctly, our market share in December in India for example is around 5%. And that 5% is in the domain where India below INR10,000 around 70%, don't quote me exact number, but just roughly 70% is below INR10,000.

And the -- so we complete basically in that remaining 30% while we still have close to 5% market share. It shows we have to go into the low price.

In my view personally, the low-price tier not necessarily is less competitive. In my view, it's actually more competitive. In area where HTC have brand traction and pull, actually that's where we think we can get to that sweet spot. And we notice that in a lot of emerging markets.

Richard Kramer - *Arete Research - Analyst*

Okay. Thanks very much.

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Thank you.

Operator

(Operator Instructions) Arthur Hsieh, UBS.



Arthur Hsieh - UBS - Analyst

Just a follow-up; as Chialin just commented about the legal expense reduction in the fourth quarter, it seems to be about TWD300 million to TWD400 million -- I think it's about TWD300 million to TWD400 million in the administrative expense compared with the previous quarter.

So I'm wondering whether that is just one quarter event or it's -- going forward your administrative expense is likely to stay at below TWD1 billion? That's the first question.

Chialin Chang - HTC Corp - President of Global Sales & CFO

I can tell you that, Arthur, I know it's not going to be a good answer for you to model your financial model there. And the expense on legal side really depends on, one, number of cases there; and second, at what stage in a legal lawsuit in terms of core, discovery, et cetera, on those -- I'm not expert on those.

And the way we treat the accounting, just to be more explicit, the way we treated accounting is basically the expense as it occurred during that quarter. Not like waiting for the bill, but expense as it occurred in that quarter just to follow a more -- the right -- in my view the right accounting treatment.

In terms whether this thing going to be below in terms the -- below TWD1 billion, I don't know if that's the case. But certainly we want to be more efficient in the legal side as I told our general counsel. So we're working in that regard. But it's going to be quarterly fluctuations, so I can't say for certain.

Arthur Hsieh - UBS - Analyst

All right, thank you. And the second question is with regard to this -- the volatile global currency environment between the emerging countries. But I think you did well in the fourth quarter. So how did you manage the risk? And then whether this is something that you need to take extra action to prevent the potential negative impact such as depreciation in the many emerging market currencies?

Chialin Chang - HTC Corp - President of Global Sales & CFO

Yes, I think the -- this is a very difficult question. I wouldn't say we managed well. We're just facing that pressure. So we don't do speculative -- we don't do speculative hedging. So that to me is a oxymoron anyway.

We only do hedging when we ship out the products. So we do a currency hedging there. If there is a secular decline or depreciation in currency, we're going to bear the pain because we just want to do hedging only on the business side. We don't do anything speculative.

So that create a lot of issues. With the currency we have today now in a lot of the emerging marketplaces here in Europe, we're seeing that currency. We're watching very carefully although.

And then the question is operation-wise how are you going to react? You want to stay with the same price or you're going to have to raise it? That's the constant battle we have had to face every day.

Arthur Hsieh - UBS - Analyst

Okay, thank you.

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Thank you.

Operator

(Operator Instructions) Richard Kramer, Arete Research.

Richard Kramer - *Arete Research - Analyst*

Just one other question. You've had -- you brought us very similar capital structure now for a long time and I'm just wondering if sitting on a lot of cash on the balance sheet which is effectively capital not employed, the -- is working capital somewhat this quarter, but it's been relatively stable.

What are you going to do and what's sort of the point to having TWD55 billion on the balance sheet? Do you see any way for you to use that cash productively in the business? And if not, would you consider making more dividends, buybacks, what have you? It just seems as if you're running a strange capital structure given how high a level of cash relative to the market value of the stock.

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Well, I don't see it that way. I see it -- first of all, we do have a very exciting and strategic need of the cash. So -- and I think the cash is going to be deployed very productively to further grow the business.

With the growth of business, hopefully our stock price will follow and that ratio between cash to market cap will be different. That's how I see it.

Richard Kramer - *Arete Research - Analyst*

And can you be a little more specific about how you might deploy the cash again? Working capital is -- yes, it's far below that.

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Okay, so -- I think the -- just to answer your question there, first of all, we have been as you can see in the last few quarter pretty efficient in terms of managing the working capital and just not the cash. In the further growth, hopefully revenue will grow and then the -- you will see more regular use of working capital in terms of cash.

Second, we do see the cash for a strategic need for the coming years for HTC. So if you ask me, I can be more explicit. We have no intention to do a share buyback or that sort of things we envisage. We do see things that deploying that cash in a strategic way in the coming years is going to reward shareholder even more.

Richard Kramer - *Arete Research - Analyst*

And I guess the other question related to that and cost structure, do you see any prospect over time that we would deviate from the sort of 20% gross margin that you've had in your guidance for the year and going forward? Is this just settling into the pattern that is now the norm for the industry and there's no prospect to return to for yourselves or others -- no one seems to be guiding this sort of higher gross margin levels we saw a few years ago?



Chialin Chang - *HTC Corp - President of Global Sales & CFO*

I think the -- obviously you know this industry very competitive, and we expect there could be further consolidation in the coming two years in my personal opinion. Maintaining the right P&L with the right growth to us is important.

I watch gross margin carefully. But that to me is the reference point. I care more about how you sell in various countries in terms of flagship product and also the rest portfolio there. And so we want to make sure that the -- at the end of the competitive period here we stay strong and then stronger.

And I do see that -- beyond the smartphone into the other lifestyle devices I do see hopefully that we can extend that kind of gross margin, but that depends on what area we get into and the -- what volume we have. So I won't be able to comment at this point.

Richard Kramer - *Arete Research - Analyst*

And given you just made a very provocative comment about further consolidation, but you also answered to Arthur that you're not looking to partner with an Internet company, can you elaborate a little bit on that? I mean you have seen a couple of landmark deals with Lenovo, Motorola, et cetera, in over this last year. I mean, what sort of role do you envision HTC playing in this consolidation?

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Yes, see the thing is that the way I see it -- the way I -- maybe that may not be the right -- the way I interpret consolidation may be different from what you guys read as consolidation. I don't necessarily mean consolidation means the merger or combination.

Consolidation in the industry in my view now is it will be after a year or two the leading tier and the lagging tier will be further deteriorating. So that to me is that, what I meant by consolidation. We'll see hopefully the leaders getting stronger and laggards will be further declined. Whether they will be leading to any of the combination or exit, that I cannot comment. I don't know either. So that's not --

Richard Kramer - *Arete Research - Analyst*

Okay. Thanks very much. Yes, thanks.

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Thank you.

Operator

(Operator Instructions) There is currently no question in line. I will pass the call back to CFO and President of Global Sales, Mr. Chialin Chang, for closing remarks. Mr. Chang?

Chialin Chang - *HTC Corp - President of Global Sales & CFO*

Yes, thank you very much for you guys on the call. Appreciate you got the time. And for those whose (inaudible) the Chinese New Year, Happy New Year to you guys. Hopefully see you guys soon. Thank you.



Operator

Thank you for your participation in HTC's conference. There will be a webcast replay within an hour. Please visit www.htc.com under the investors' section. You may now disconnect. Goodbye.

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