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## CORPORATE PARTICIPANTS

**Kelly Hsu** *HTC Corporation - IR Manager*

**Chialin Chang** *HTC Corporation - CFO and President of Global Sales*

## CONFERENCE CALL PARTICIPANTS

**Richard Kramer** *Arete Research - Analyst*

**Anne Lee** *Nomura - Analyst*

## PRESENTATION

### Operator

Welcome everyone to HTC's 2015 third-quarter results conference call and webcast in English. Today, first we have CFO and President of Global Sales, Mr. Chialin Chang, and Vice President of Finance, Mr. Edward Wang, and Investor Relations, Ms. Kelly Hsu.

(Operator Instructions). After the presentation, there will be a question and answer session. (Operator Instructions). 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](http://www.htc.com) under the investor section. And now I would like to introduce Ms. Kelly Hsu from Investor Relations. Ms. Hsu, you may begin.

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### Kelly Hsu - HTC Corporation - IR Manager

Thank you. Good morning, good afternoon and good evening ladies and gentlemen. Welcome to HTC's 2015 third-quarter analysts call. This is Kelly Hsu, HTC's IR Manager.

The event is now being webcast live via HTC's website at [www.htc.com](http://www.htc.com). If you're joining us on the dialing lines, your call is now being placed on mute. As this conference is being broadcast by investors around the world, we will conduct this call in English only. The format for today's call will be as follows. First, I will summarize our operations for third quarter. Afterwards our CFO and President of Global Sales, Mr. Chialin Chang, and VP of Finance, Mr. 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. First, note that this presentation contains forward-looking statements. These statements are based on our current expectations. Actual results may differ materially from our expectations. And the Company undertakes no obligation to update these forward-looking statements going forward.

If you have no questions, I'll begin to give the overview for third quarter 2015. Please turn to page 3. Page 3, third-quarter financial highlights. Revenues of third quarter was TWD21.4b, with gross margin of 18%. Operating loss was TWD4.9b and operating margin a negative 23.1%. Net loss after tax was TWD4.5b or loss per share of TWD5.41 per share.

Key highlights for third quarter. While demand at the high-end remained soft, third-quarter results came in at the higher end of our expectations. HTC's comprehensive program of restructuring and streamlining continued in third quarter, resulting in significant reduction in operating expenditure across the organization and a sequential reduction in operating loss.

The HTC One A9 was unveiled in New York early this month to critical acclaim and it's been widely hailed as setting a new standard for premier Android phones. Already available in several territories, the HTC One A9 has been welcomed in major markets and places HTC in a commanding position in smartphone innovation going into the New Year.



Page 4. Page 4 gives you an overview on revenue and operating profit. Revenue for the third quarter came in at TWD21.4b and operating loss was TWD4.9b. Page 5. Page 5 gives you an overview on gross margin and operating margin. Gross margin for third quarter was 18% and operating margin was negative 23.1%. Page 6 and 7 were financial overviews for income statement and balance sheet.

This wraps up the content of our presentation and now I'd like to turn the podium to HTC's CFO and President of Global Sales, Mr. Chialin Chang. Moderator, please start the Q&A session.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Richard Kramer, Arete Research.

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### Richard Kramer - Arete Research - Analyst

Good morning guys. Good afternoon. A few questions to start with. First of all, we obviously are missing the guidance slide. It's a notable absence. Can you say anything about your fourth-quarter sales and profitability expectations? And why don't I take each one of these in turn, and then we'll -- so maybe we'll start with that one.

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### Chialin Chang - HTC Corporation - CFO and President of Global Sales

Richard, you want to go through your question list because that's the first thing I want to address, I want to personally address that. Your questions.

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### Richard Kramer - Arete Research - Analyst

Okay. The second one is where are we in the restructuring that you mentioned. That will obviously be reflected to some degree in the guidance, but obviously there were some costs for reducing headcount and so forth, and reducing marketing, and I'd like to know how much of these one-off costs you've worked through and how much more there is to come.

A third one is, you'd said, Chialin, earlier, I think in the first or second quarter call, that you expected some material contribution from non-smartphone products in 2016. You said 2015 would be too early. Is that something that's still on the agenda? And, if so, could you lay out the dimensions of that, whether it's Vive Re, the under armour or fitness tracker, which we've yet to see? What are the products and what's the realistic expectation for that?

And then maybe the last one is, obviously you've had quite a bit of cash outflow this year both at the operating and financing level. Where do you stand on further cash outflows? And is that something that should be -- will constrain your operations going forward given that you traditionally have a dividend payment coming up in the second quarter of next year? Thanks.

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### Chialin Chang - HTC Corporation - CFO and President of Global Sales

Thank you Richard. First of all, let me address this, not just a question; this is a statement from us in terms of answering your question and then I'll go through the rest of your questions here.

First of all, we would not be providing the financial forecast for Q4. And it's our intention that we will not be providing financial forecasts in the coming quarters. The reason is the following. Given the stage of HTC business and in light of contracted Taiwan regulations, as you can see, in the



last few quarters we have been providing not just a simple financial guidance, a very detailed line-by-line financial forecast. If you look at the income statement, it goes through the revenue, profit, every line of the P&L items there, and same thing for the other statement in that regard.

So that made that financial forecast, per se very difficult. We don't want to create a side effect given the uncertainty in forecasting some of the -- every one of the line items there. So that's the main reason, and given the dynamic nature of this business here we have decided not to provide that kind of detailed financial forecast. And we looked at the Taiwan context that fewer and fewer people, companies providing that. I don't have a detailed number for you, but happy to get you guys feedback in that regard. So those are two reasons. Primarily the first reason that we actually feel like it's actually difficult to have a detailed line-by-line financial forecast to suit the purpose we need.

With that said, in order to maintain an adequate amount of transparency and so-called guidance -- it may not be the right word, using a guidance, but we're not getting into the kind of financial forecast. In the spirit of complying with the local Taiwan regulation, I would say the following. We are expecting, we likely expect Q4 result, as compared to Q3 result, to see the incremental improvement on revenue and the net income. So that's all we say. I won't be able to elaborate further quantitatively or get into numbers in order to comply with the Taiwan regulation. So that's the statement, also an answer to your question number one.

Your question number two is regard to our cost structure, the restructuring status and where we are. I think we have gone through the first phase, especially a quick phase of financial restructuring. There is some one-time charge; in Taiwan there is not so-called a one-time charge, but booked into part of the operating expenses. It's going to be in Q4. And that first phase I think we have completed in terms of we're pretty sure we've improved the cost structure to an active level.

We're going to, in terms of the second phase or the final phase we're going to have to take a more streamlined, focused approach in terms of where to focus the resources and where people fit the resources, so we can complete the entire restructuring. I expect that to be completed hopefully by the end of first quarter. If not, definitely into the -- finish it by the second quarter. But it's our expectation to finish it by the end of first quarter here.

I wouldn't say that would be a cost-cutting. Hopefully that would result in more rationalized resources. That's probably the key given that we've diversified beyond the smartphones. And hopefully through that process it will be a cost optimization in that regard. So that's answer to your second question.

In terms your third question, I assuming in terms the contribution on the non-smartphone business, I did say that in, earlier in Q1 or Q2, I don't recall, I did say that in 2016 we're expecting a more meaningful contribution from the non-smartphone. Just to be more specific, non-smartphone, as you see, we've diversified into a related area in terms of the Internet-of-Things, if you call that a better description. And we expect in that area we will have a contribution in that regard.

We also expect to have a contribution coming out of the HTC Vive, the virtual reality part of it. I won't be able to give you a more specific or quantitative, but I would like -- it's my expectation that, given the visibility, very limited visibility, it's my expectation that we'd like to see a meaningful contribution for the entire 2016 as we roll out the product in both the wearable side and also on Vive side. So that's the question number three.

What's the question number four? Cash out.

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**Richard Kramer** - Arete Research - Analyst

Cash outflow.

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**Chialin Chang** - HTC Corporation - CFO and President of Global Sales

Cash outflow. Yes, the cash outflow, you see we believe we have a solid balance sheet. Because of cost restructuring, and some of it was due to our flagship product, we have some cash outflow. I think we still have a solid cash balance with no debt. If we were to monetize some of the assets



we have, including some of the real estate, we were to monetize here we would have even more cash in that regard, because we have not been able to see the need, in terms of operational need, for that need outside of our current cash level. That's why we haven't been able to wanted to monetize the things we have.

So overall, the answer to you here is that we believe we have adequate cash. We want to make sure our cash flow -- financial -- not just the financial performance, also on a cash flow element of the financial performance, coming to the adequate level. So it's going to more than two or three quarters to stabilize. Primarily, as you see, once the flagship level of smartphone not performing to your level of expectation, it takes a cycle time to change that. And also we need to getting the non-smartphone business to come in. So it's a combination of that.

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**Richard Kramer** - *Arete Research - Analyst*

Okay. Do you anticipate, given the cash outflows now and the restructuring, that you would be in a position to pay a dividend next year or is that something that you should just put off until you start to see the sales and profits grow again?

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**Chialin Chang** - *HTC Corporation - CFO and President of Global Sales*

I think because of Taiwan's regulation we would not be able to pay the cash dividend if we don't have the profitability. But in terms of the different way of rewarding shareholders, we look at various options here. The good thing about it, we do have a good cash level. So that's what we have.

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**Richard Kramer** - *Arete Research - Analyst*

Okay. Thanks.

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**Chialin Chang** - *HTC Corporation - CFO and President of Global Sales*

In light of the difficulty of doing that, I won't be able to comment at this stage.

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**Richard Kramer** - *Arete Research - Analyst*

Okay. Thanks very much.

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**Chialin Chang** - *HTC Corporation - CFO and President of Global Sales*

Thanks, Richard.

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**Operator**

Anne Lee, Nomura.

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**Anne Lee** - *Nomura - Analyst*

Hi, Chialin. This is Anne from Nomura. Just a quick question. Could you give us an update about your smartphone strategy? Because last quarter you highlighted some changes on the strategy, and given the dynamics in this industry so also want to get some updates from you this quarter.



**Chialin Chang** - HTC Corporation - CFO and President of Global Sales

So in terms of smartphone strategy, we know internally where we stand in terms of the brand perception, where the phone positioning should be, where we're strong, we're relatively weak in terms of various geographic markets. So we have gone through the internal exercise in terms of where we're going to focus our marketing, in terms of market priority. And we have a cost priority. We, as we said, we're going to streamline and refocus our product portfolio and also we're going to have the resource allocation according to that.

We, as we see some of the people are asking, we had a good launch and we had a pretty good feedback on the HTC One A9, and this is one of the examples here. Outside of the top-end flagship phones, we're able to provide a premium design, good performance, high-quality performance, a phone sitting at the premium end and carving out a space in that regard for both the industrial economy and also for the emerging market. This is one of the things we're going to do, that.

We will not go after volume and sacrifice the profitability. So we're going to have to find the right balance. Things like this, easier said than done, because in certain operator partners, for example, they want to have a portfolio concept. So that's something we also streamlined for that.

In certain areas we actually restructure the team. In certain areas we actually -- geographic area that we have a good team and good brand traction here, we are pumping up in terms of volume and also profitability. So that's something we're doing in terms of the strategic focus.

On the product side, as I talked about here, we're going to streamline the portfolio, really concentrated portfolio. As we'll start announcing these things, you probably will see that.

So, to summarize your question, we have a geographic market priority focus, we have a product priority focus, and we have, according to that, the resource allocation. Because we want to allocate some of our resources there given that streamlined focus, we can allocate some of the resources beyond smartphone, because one of the core strengths, as we said repeatedly, is the core engineering strength we're going to allocate to whether HTC Vive or the IoT side.

One lastly, but not the least, is that you'll see in the coming year we are going to how we have an integrated story, so not three independent. It will be diversified area independently doing well and prosper, but you will see an integrated story, how we tie in our, for example, smartphone with the Vive, and also with the IoT together. So that's the kind of integrated story our partners would like us to see, and that's something we're working on as well. That's our intention.

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**Anne Lee** - Nomura - Analyst

Okay. Thank you. My second question is, given that you have several like emerging business, I think the outlook for those new business looks promising given the market trend. Have you think about like doing some financial restructuring? For example, spin off those divisions as independent companies, something like that?

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**Chialin Chang** - HTC Corporation - CFO and President of Global Sales

So first of all I want to say something before I answer your question directly there. I think on the IoT and the diversify into the virtual reality area, you can see a lot of [DNA] about Powered by HTC. So IoT is a good example here, the Powered by HTC content, which is something which one of our core strategies, working with partner, go to market directly. Whether you go into B2B2C or B2B2B, that's something we're going to provide. We think this is one of our core thing we're going to say there. So I want to elaborate that, so make it more transparent to the community.

In terms where -- I think Richard Kramer was talking about dividend, return to shareholders. In terms of where to enhance the valuation as a value to shareholder, we're considering various way of doing that. I won't be able to comment on these things because once we comment on this they may be interpreted differently and getting pretty sensitive in that regard. But there's always different things we think about the value to shareholders. I won't be able to say beyond that.

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**Anne Lee** - Nomura - Analyst

Okay. Thank you.

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**Chialin Chang** - HTC Corporation - CFO and President of Global Sales

Thanks.

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**Operator**

(Operator Instructions). Richard Kramer, Arete Research.

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**Richard Kramer** - Arete Research - Analyst

Hi, Chialin. Just it seems like there few of us on the call. Just a couple of other quick ones from me. You mentioned multiple times on this call the phrase resource allocation. The business is down now at, over the last quarter now at a run rate of a couple of billion, TWD2.5b or so. Can you talk a little bit about the regional sales strategy?

I know HTC had tried in the past to address really a global platform. And now obviously you've launched the A9 One with at least some initial differential pricing in Europe and the US obviously, and it's an attempt in the short term to rebuild your US position. Are you still trying to be a global brand and a global company? Where should we look regionally for your progress? Obviously China is an extremely difficult market right now so if you could comment on whether you intend to keep at it in mainland China, but just some thoughts on your regional distribution would be great.

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**Chialin Chang** - HTC Corporation - CFO and President of Global Sales

Thank you. Richard, thanks for that. That is a good question. When I state resource allocation what I have in mind, both on the product engineering, also on the sales and marketing side, what I have in mind, more of the -- we want to allocate part of the engineering resources into Vive and also the IoT, as we talked about it. Because once we streamline our portfolio -- and our smartphone, what we will do here is, hopefully in the coming years we're still seeing HTC have a lot of innovation coming in. We're going to have a very focused innovation in that regard, for lack of a better description.

And we're going to allocate to those two areas that we talked about. Because we believe IoT then is a vastly expanding area, whether it's the consumers, also the different industry verticals. And Vive, as you see, the combination of virtual reality and augmented reality will be one of the key, I would say, computing paradigms. So that's something we actually want to put enough resources to make sure that will grow accordingly.

When your question comes to in terms how we align our regional resources in terms of sales and marketing, I would say the following. First of all, without any doubt, HTC would like to continue to be a global brand. It's very important for us. And in fact we're able to leverage multiple things to ensure we can sustain a global brand status.

One thing you can say, you can see the Vive, in a very short period of time -- we're going to have (inaudible) for you the information -- very short period of time our brand in terms of coming into a new cool thing and the same phase we can achieve, actually it's tremendous. Then we can leverage that brand into selling more other stuff, which we think is actually quite important.

Same thing on the Under Armour partnership and go-to market together in 2016, that we're able to marry the brands together in terms of the design, engineer, ITC, content, which is quite important in terms of the global awareness. Some of the things that you can see in the US. For example,



a few cities we have this Vive Truck. Actually it's a tremendous buzz they've created due to that. So those are the things we're doing to continue to enhance and sustain our global brand.

In terms where market focus on that, I want to clarify. A lot of people have that question so want to clarify it. In fact HTC One A9, the pricing to the partners and distributors basically globally, take out exchange rate fluctuations, it's basically the same.

So some of the people, they didn't see it differently here. For example, we have in Taiwan a promotion about TWD12,900. That's roughly about \$400 US. That's actually including tax. And that's a promotion for people who want to buy outright naked phones instead of going to tariff plan. They have the opportunity. We've used that also as an opportunity to create a buzz. And for the early birds, HTC loyalists, they want to get another phone without buying another tariff. So that's a very short period of time. You can say it's a flat sale; it's not necessarily in that spirit. It's more of the purpose I just described.

Same purpose for the US actually is before tax and it's basically the similar price and for people preorder. Because US, we're not going to be on the shelf until November 7, so for people who want to order and buying an outright phone with the more pure Google HTC experience without the operator approval in there, they can do that. So that's for that purpose. As you can see, in the US majority of sales is going to come out of the operator sales, similar to Taiwan, with the installment of various other ways of doing that. They have other ways of doing that. That's what we're doing in that regard.

In UK in fact the pricing to the operator, as operator knows, some of the channel partner, retail partner may know, that pricing basically the same level. But in UK, people don't know here is there's close to 20% VAT tax and all the things they're selling is afterward the retail price. So I want to clarify that. So that initial promotion's for the purpose described and in fact in terms of invoice price globally we have the price harmony. Otherwise, we can't even manage the price in terms of gray market issue.

So, that said, for different regions we're going to have a different focus in that. The region you talked about in terms of China, in terms of the US, UK, Germany Middle East, in terms of India, Australia, Taiwan is our home country, we're going to continue to be very focused. In the big geographic areas here, for example, South America, we're probably going to focus mostly probably going to be with Mexico or American Mobile. And we'll not be able to do broadly beyond that simply because our resource focused. So those are the things I talked about; we're not going to spread very thin.

And China, we're going to continue to be present in China. We just restructured the team. Hopefully our team restructuring will be done by the end of Q4. Starting selling product starting in December timeframe in China and then that will be a, hopefully a mixed hybrid model, which will be clear -- hopefully we'll report further in January. So that's how we see the market.

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**Richard Kramer** - Arete Research - Analyst

Right. And any comment on channel inventories at this stage?

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**Chialin Chang** - HTC Corporation - CFO and President of Global Sales

I don't think we have -- I can tell you the reason we have more depressed level on the revenue here is we are not selling more of the flagship model. So the entire basically flagship product on the M9 or M9+, basically by the time the next month, it's actually pretty healthy part of it. What we want to do is to sell more stuff out in terms of the premium product in that regard. So I don't think the channel inventory is to be something we concern about.

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**Richard Kramer** - Arete Research - Analyst

Okay. Thanks very much.



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**Operator**

(Operator Instructions).

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**Kelly Hsu - HTC Corporation - IR Manager**

So I saw some analysts on the line. I'm not sure if there's any following-up questions. If we don't have further questions, we'll wrap it up.

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**Operator**

Thank you, Kelly. If there's no questions in line, I will pass the call back to CFO and President of Global Sales, Mr. Chialin Chang, for closing remarks. Mr. Chang, please proceed.

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**Kelly Hsu - HTC Corporation - IR Manager**

Thanks everyone for joining the call today. The replay will be available in an hour on our website. So have a nice day. Thanks.

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**Operator**

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

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