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## CORPORATE PARTICIPANTS

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

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

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**Anne Lee** *Nomura - Analyst*

**Dennis Chan** *Citigroup - Analyst*

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

## PRESENTATION

### Operator

Welcome everyone to HTC's 2015 second-quarter results conference call and webcast in English. Today with us we have CFO and President of Global Sales, Mr. Chialin Chang, Vice President of Finance, Mr. Edward Wang, and Investor Relations, Ms. Kelly Hsu. (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](http://www.htc.com), under the Investors section.

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

Thank you. Good morning, good afternoon and good evening ladies and gentlemen. Welcome to HTC's 2015 second-quarter analyst 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 through the dial-in lines, your call is now being placed on mute. As the conference is being broadcast by investors around the world, we'll conduct this call in English only.

The format for today's call will be as follows. First, I have to summarize our operations for second quarter, followed by our guidance for the 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 two of the presentation slide. Please note that this presentation contains forward-looking statements. These statements are based on our current expectations. Actual results might differ materially from our expectations. And the Company undertakes no obligation to update these forward-looking statements going forward.

If you have no questions, let me begin to give the overview for second quarter. Please turn to page 3.

Page 3, financial results. Revenue for second quarter was TWD333b, with gross margin of 19.3%. Operating loss was TWD5.1b and operating margin of negative 15.6%. One-time charge for idled assets and prepaid expenses were TWD2.9b. Net loss after tax was TWD8b or loss per share of TWD9.7.

Key highlights for our second quarter. Weaker than expected demand at the high end, consistent with the current Android market, along with weak sales in China, lead to a year-on-year fall in the second quarter. Meanwhile, year-on-year shipment volume increases were seen in select key emerging markets.

HTC has begun to implement Company-wide efficiency measures to reduce operating costs across the organization and ensure resources are appropriately allocated to future growth.



HTC continues to invest in promising new product areas such as virtual reality where the Company is working with over a thousand developers on content creation over a wide spectrum of applications, including gaming, entertainment and education, to ensure a compelling ecosystem ahead of the highly anticipated launch of HTC Vive at the end yearend.

Page 4. Page 4 gives you an overview on revenue and operating profit. Revenue for the second quarter TWD33b and operating loss was TWD5.1b. Page 5. Page 5 is an overview on gross margin and operating margin. Gross margin for second quarter 19.3% and operating margin was negative 15.6%. Page 6 and page 7, our financial overview for income statement and balance sheet.

Page 8, guidance for the third quarter 2015. Revenue is expected to be in the range of TWD19b to TWD22b. Gross margin is expected to be 19% to 19.5%. EPS is expected to be negative TWD5.85 to negative TWD5.51 per share.

This wraps up the content of our presentation and now I would like to pass 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

Thank you. Ladies and gentlemen, we will now begin the question and answer session. Kindly leave the time to investors and analysts. For media, please contact HTC PR team after the call if any questions. (Operator Instructions). Anne Lee, Nomura.

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### Anne Lee - Nomura - Analyst

Hi Chialin and Kelly. This is Anne from Nomura. Just a very quick question regarding, how would you see what kind of strategy your Company will implement to help the Company to turn around or narrow the losses?

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

Thanks Anne for your question. To answer your question, let me start up with a sort of broader perspective what we intend to do and also our overall strategy and the initiatives we actually copy in with some of those as you actually read it on the press release.

First of all, let me explain what happened in Q2. In Q2 what happened is there's a softness in the high-end demand of smartphone, part of it due to the overall Android market, part due to our HTC-specific.

On the HTC-specific, our flagship phone, we call the classic, iconic One, we also recognized there was a group of people and consumers who prefer a more fashionable one with HTC DNA, which we're addressing and we'll talk a bit later. I think the second softness is because every time HTC rely on, quite heavily on the high-end smartphone and the halo effect created, so without the high-end carrying the load, creating the halo effect, there's some impact in there. And the third thing is the China softness. I think we're going to do a dramatic turnaround plan for China and we'll also address it a bit later. So those are three reasons we actually encounter in terms the -- on the smartphone side.

In terms the outlook for second half, especially for third quarter and the second half, I'll say the following and we'll talk about the overall strategy, what we intend to do and the initiatives, we'll talk about it. Third quarter, you can see the guidance. We're also guiding a sequentially down quarter, and also year over year down quarter in the third quarter guidance, because it's a transition period.

As I've said, in the high-end smartphone, as our Chairperson also mentioned, that we intended to create a, I would say for lack of better description, and we're not disclosing the product details in follow our tradition, more a fashionable, trendy design, while consistent with HTC DNA, for the



[Holiday Hero]. And during this transition period we are having a quarter that the contribution from the high-end smartphone is actually not as high.

And in the following quarter, in Q4, as well we are going to reposition a classic version of our flagship phone, tweaking some of the features there and positioning it even sweeter spot, hopefully to carry into the holiday, along with the trendy version. So that's our goal for Q4. And hopefully that will carry momentum into Q1. So that's the tactical side what we intend to do with the second half of the year.

And in light of the current challenging environment, we are doing a few things. First of all, we're actually rethinking about what's the right smartphone strategy. As you can see, a lot of vendors basically treat smartphone as the entry point for mobile internet. As you can see, a lot of vendors, whether private, public, powered by fundings, based on the funding from other areas or funding from capital markets, or funding from the private equity or venture funding. So to us, it's a game. Obviously people try to grab subscribers through the more volume of smartphone. So it becomes a very intensified competition.

And for HTC, we have a few advantages and in light of advantages we're going to have to play in terms according to our strengths. So we are going to address more premium segment. Premium doesn't necessarily mean just flagship-only. Especially in the retail environment, premium could be a couple of tiers below the flagship product tier. So we're going after profitability instead of -- we're going into the profit share and profitability instead of the volume share. That's something we think we're going to do it differently.

So, with that, we are going to actually streamline and optimize our portfolio. And we optimize according to that portfolio in terms of the product chain, technology platform, putting the ecosystem, as well as the operation. And to match the challenging environment there, we also would optimize our operating expenses, try to increase the efficiency also to reduce the costs.

So our goal is, from third quarter into Q4, with some of the tactical things we talked about, to sequentially increase the revenue and hopefully reduce the cost, reduce cost and as a result narrow the losses, and then eventually, hopefully, in the not-too-distant future there we are intending to breakeven in the smartphone area. What we intend to do is making sure we are competitive in the smartphone in terms of profitability instead of the going after volume share.

In the meantime, we're extending beyond the smartphone, primarily in two areas. One in the connected devices. We also have a strategy in terms of going after interconnected devices. We're going to do it slightly different what we do in the smartphone area. We are going to partner and then go to market together. As you can see in the personal well-being, fitness performance side, we're working with Under Armour. So that's a reflection of part of what we intend to do in the connected devices because we believe in the connected devices in different verticals there is opportunity in there.

And the second thing is in the virtual reality, which you read in some of the press, we published in some of the articles there. We think this is another big area. We actually feel that we have the early-mover advantage. We also have a good, robust offering, which we think we have quite a strong advantage in those.

So that's the overall, we talk about smartphone plus the expansion of that smartphone for the HTC in the upcoming strategy. We want to go after the profit share, so we want to reduce the losses quickly so we can turn profitability in the smartphone while we are addressing and then growing the other emerging areas. I'll just pause here.

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**Anne Lee - Nomura - Analyst**

Okay. Thank you. Regarding the cost cuts, what kind of magnitude you will expect could happen in the third quarter or even fourth quarter?

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

I think basically you have not seen the guidance for Q3 yet in terms of operating expense. It probably reduce a little bit. You'll see sequentially more reduction in the operating expenses in Q4. And I have been thinking about it that what exactly the number we're going to guide you, we're going to just say it's going to be material. So I decided not to disclose that in terms of specific number of expenditure in terms of operating expense cost down.

What I will highlight, however, I think majority of cost down are going to be reflected. You'll see that airing through a little bit in Q4. I won't be able to say it for now until next guidance. I think you're going to see a big chunk of it starting in Q1 that we're going to bring down quite significantly in terms of the operating expenses.

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**Anne Lee** - Nomura - Analyst

You also mentioned that Q4 you will have refreshed the high-end portfolio with more fashionable or trendy design, and then you in the same time you want to cut the cost. So how would you do the marketing or --

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

That would not impact how we campaign on high-end. So there's a different way of doing that. So I won't be able to disclose as it's still some time away. I don't intend to use the platform to disclose product details. But you will see -- that's part of the reason you won't see the whole result of the cost reduction in Q4. We're already making what's needed for the campaign because having a successful campaign is important. We don't want to get into the vicious cycle. We want to get into a positive cycle in that.

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**Anne Lee** - Nomura - Analyst

Okay.

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

But I will highlight, however, that the high-end smartphone, the trendy one, as I described it, I think it's well-received by both the channel partners and operator partners. So we believe this will be well-received by the consumers in the coming holidays and into next year.

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**Anne Lee** - Nomura - Analyst

And my second part of the question is regarding the new products beyond smartphone, such as virtual reality products and even some medical. Could you have more things to share with us?

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

I think for the virtual reality I can only comment what we said. I think the good thing is that we are on track and the good thing about, since the announcement and also secret activities, we are getting a lot of the enthusiasm in the development communities and also these early, we call it, gamers or adopters. What we intend to do is we're going to have some sort of a, quote/unquote, consumer meet, a roadshow in select places, to both promote this and also to enhance the brand HTC, and also hopefully having a carry-over effect into the perception and acceptance of our smartphone. So that we're doing well in terms of how we're tracking it.

In terms of the, I wouldn't specifically call it in terms of what vertical in there; I would just say the connected devices. I think the Under Armour partnership is one good stuff. We intend to, both sides, capitalize on that opportunity. We're very excited. We think we have a good offering. We're

starting briefings. Certainly we haven't officially unveiled in the press in terms of our product offering, but hopefully we're going to do that in the not too distant future. So far so good in terms of the connected devices.

As I said, through working with industry leader in the respective vertical on the media connected devices, also something we're going to be able to work out well for HTC. So hopefully when we have something more concrete we could report and disclose more.

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

Okay. Thank you. I have no more questions. Thank you.

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

Thank you.

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**Operator**

(Operator Instructions). Daniel Chan, Citigroup.

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**Dennis Chan** - *Citigroup - Analyst*

Hi Chialin. Hi Kelly. This is Dennis Chan from Citigroup. Most of my questions have been answered actually. Just have two quick questions. The first one is that in our third-quarter guidance do we expect any significant non-op or write-off?

The second question is when do we expect to see a more significant contribution from our non-handset products?

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

The answer to your first question is no.

Second question is you're going to start seeing that contribution in 2016.

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**Dennis Chan** - *Citigroup - Analyst*

Got you. Thank you.

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

Thank you.

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**Operator**

(Operator Instructions). Kylie Huang, Daiwa.



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

Hi Chialin. Thank you. Thanks for taking my question. I'm Kylie from Daiwa. I just have a quick -- your handset business, you mentioned you would more focus on trendy model and the premium model, so does that mean you will reduce your model number in the coming years or you have any other picture for your medium models?

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

I think when we say, when I said trendy, I'm just try to distinguish this from our HTC One M9. But when we say going after premium market, it's going to a market where we actually could have a good profitability on per-SKU basis or the geographic market. We are going to actually reduce our portfolio starting 2016 quite dramatically in light of that strategy that I talked about. And I think with that we're still going to have a mid-tier; it's just the lifecycle of mid-tier is going to be longer. So you're going to start seeing that more in the first half of 2016 when they start becoming more concrete. But that's basically what we intend to do.

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

Okay. Thanks.

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

Thanks.

**Operator**

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

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

Thank you for joining the call today. Have a nice day.

**Operator**

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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