MANAGEMENT DISCUSSION SECTION

Operator: Please stand by, we are about to begin. Good day and welcome to the Texas Instruments Third Quarter 2010 Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Ron Slaymaker. Please go ahead, sir.

Ron Slaymaker, Vice President, Investor Relations

Good afternoon, and thank you for joining our Third Quarter 2010 Earnings Conference Call. As usual, Kevin March, TI's CFO, is with me today. For any of you who missed the release, you can find it on our website at ti.com/ir. This call is being broadcast live over the web and can be accessed through TI's website. A replay will be available through the web.

This call will include forward-looking statements that involve risks and uncertainties that could cause TI's results to differ materially from management's current expectations. We encourage you to review the Safe Harbor Statement contained in the earnings release published today, as well as TI's most recent SEC filings for a more complete description.

Our mid-quarter update to our outlook is scheduled this quarter for December 7. We expect to narrow or adjust the revenue and earnings guidance ranges as appropriate with this update.

In today's call we'll describe how TI's strategic position in our core businesses of Analog, Embedded Processing and smartphone chips continues to strengthen. We'll discuss our manufacturing strategy and recent additions that we have made to our analog capacity. We'll also provide our perspective of the near-term demand environment.

Revenue in the third quarter generally tracked closely with our initial expectations in the quarter. In July, the middle of our guidance range projected about 6% sequential revenue growth. We held that level with our September update, and in the end we delivered 7% growth. Although our results are good, demand is a bit of a mixed bag. The industrial market was strong for us in the third quarter as it continued a cyclical recovery. We believe this market has now recovered, and therefore, we expect industrial growth will be somewhat less robust in the fourth quarter. In communications, wireless infrastructure was strong as operators continued to expand capacity to support increased data traffic. Accordingly, demand for chips that we sell into smartphones was also strong in the quarter.

As we said at our September update, we saw a notable slowing in demand for products that we ship into the PC market during third quarter. We expect demand from our PC customers to remain subdued in the fourth quarter. Similarly, some of the consumer-related markets, such as televisions also slowed in the third quarter, and we expect these trends to continue through the current quarter.

The increase in TI revenue was driven by growth across all of our segments. Analog revenue grew 5% sequentially and 35% from a year ago. Sequentially, Analog revenue was up most in High Performance Analog where we have higher industrial exposure. High-Volume Analog and Logic and Power Management products both grew although to a lesser extent with their exposure to the computing and consumer markets. From a year ago, all three product areas contributed to growth about the same and all contributed to TI's market share expansion in Analog.

Embedded Processing grew rapidly again this quarter. This partly reflects its exposure to markets that performed well, including industrial and communications infrastructure. It also reflects continued market share gains for TI, and the strategic importance of Embedded Processing to our company. Sequentially, Embedded Processing grew 12% with both communications infrastructure and catalog products contributing about equally to this growth. Catalog products include both digit signal processors and microcontrollers. From a year ago Embedded Processing grew 47%, with catalog products being the biggest factor in the growth.

Wireless revenue grew 6% sequentially, and 11% from a year ago. Collectively, products targeting the smartphone market, those being connectivity products and OMAP applications processors, grew 6% sequentially and 37% from a year ago. These are the prop Wireless products that we're investing in for growth. We've had tremendous design-in success, especially with our latest generations of OMAP application processors, across a range of smartphones and tablets, and we look forward to solid growth as our customers' new products transition into volume production.

Baseband product revenue was $438 million in the quarter, and grew 5% sequentially, and declined 3% from a year ago. Our Other segment revenue grew 10% sequentially driven by custom ASIC products, DLP products, and calculators. From a year ago this revenue was up 29% with growth from DLP products and custom ASIC products being the biggest factors.

Distribution resales were up 8% sequentially in the quarter, about the same as TI revenue overall. We were able to help distributors build a few days of inventory in the third quarter. We're comfortable that their inventory is appropriate relative to current levels of demand and to historical metrics.

Now Kevin will review profitability and our outlook.

Kevin March, Senior Vice President and Chief Financial Officer

Thanks, Ron, and good afternoon, everyone. Our financial performance this quarter underscores the benefit of our transformation to a company focused on analog and embedded processing.

Gross profit increased 8% sequentially, and our gross margin moved up another 30 basis points to 54.5% of revenue. The combination of R&D and SG&A increased 38 million from the second quarter, with most of the increase in R&D, especially for our core businesses.

Operating profit for the quarter was $1.23 billion, an increase of 11% from last quarter as we once again pushed the bar higher from last quarter's record high. Operating margin in the third quarter was 32.8% of revenue. Net income in the third quarter was $859 million, or $0.71 per share.

In the EPS calculation, please note that accounting rules require that we allocate a portion of net income to any unvested restricted stock units that receive dividends. In the third quarter, the amount of net income excluded from the EPS calculation was 13 million. If you don't make this adjustment, you'll likely calculate EPS to be a penny higher than we have reported.

I'll leave most of the cash flow and balance sheet items for you to review in the release, however, let me make just a few comments. Cash flow from operations was $1.32 billion. This was up 756 million from the last quarter, and up 484 million from a year ago. Capital expenditures increased to $396 million in the quarter, and include additions to our assembly and test capacity, as well as our analog wafer fab capacity.

In July, we announced that we had purchased additional 200-millimeter equipment and an operational – 200-millimeter fab and 300-millimeter equipment as part of Spansion Japan's bankruptcy proceeding. This purchase closed on schedule at the end of August, and we're now porting TI's analog process technology into that fab.

Earlier this month, we announced that we also acquired our first wafer fab in China. This 200-millimeter operational fab was also purchased at a substantial discount and will support our growth strategy for analog in the years ahead. With these acquisitions, we believe we are very well-positioned with wafer fab capacity to support our intermediate-term growth plans. Return on invested capital in the quarter moved up to 34%. Our strategy is to drive significant growth while also generating high returns on our investments. Having purchased manufacturing assets that have long productive lives and purchasing those assets opportunistically at low prices is an important part of the strategy.

We used $600 million in the quarter to repurchase 24 million shares of TI common stock, and paid dividends of $143 million in the quarter. We increased our inventory by $75 million in the quarter, while lowering inventory days by one day to 75. Our lead times have continued to decline as we bring additional manufacturing capacity online and get better positioned with inventory. Orders in the quarter declined to $3.43 billion. TI's book-to-bill ratio was 0.92 in the quarter.

Turning to our outlook, we expect TI revenue in the range of $3.36 billion to $3.64 billion in the fourth quarter, or down 10% to down 3% sequentially. Part of the decline will be associated with the normal seasonal decline in calculators following back to school, as well as seasonality in semiconductors. Depending on where we land in this range, revenue could come in a little below normal seasonality due to the impact of continued subdued demand from our computing and consumer customers. We expect earnings per share to be in the range of $0.59 to $0.67. Our estimate for 2010 R&D now rounds up to $1.6 billion. Our estimates for 2010 depreciation, capital expenditures, and the annual tax rate are unchanged.

In summary, we continue to execute on a strategy that is focused on significant expansion of our market position in the analog and embedded processing markets, as well as the strong growth resulting from the increasing demand for smartphone chips. These are all large, diverse markets that provide us an excellent opportunity for long-term growth. Combining the financial returns of these markets with growth that is significantly above market rates will deliver an earnings model that we believe will be attractive long-term to shareholders.

We're also maintaining a strong discipline on capital and spending levels. If we find great opportunities for investments, we have a strong balance sheet and a resolve to move aggressively to pursue them, such as you've seen us do with the manufacturing assets that we've purchased over the past year. If we're generating cash beyond the needs of the business, we're proud to return it to our shareholders through share buybacks and increased dividends.

For example, since the end of 2004, we've lowered our shares outstanding by 32%. This means that, all else being equal, our shareholders are now getting 47% more earnings per share than they would have had we not done these repurchases. And in September, we announced that our board authorized an additional $7.5 billion in repurchases or about 25% of our recent market capitalization and another dividend increase.

We are confident that continuing to tune our business to generate higher growth and earnings while also maintaining a capital model that lowers our shares outstanding will be a good combination in the years ahead.

With that, let me turn it back to Ron.

Ron Slaymaker, Vice President, Investor Relations

Thanks, Kevin. Operator, you can now open the lines up for questions. In order to provide as many of you as possible an opportunity to ask your questions please limit yourself to a single question. After our response, we'll provide you an opportunity for an additional follow-up. Operator?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Chris Danely of J.P. Morgan.

<Q – Christopher Danely>: Thanks, guys. Just to clarify, you continue to expect the lead times to normalize by the end of this quarter?

<A – Kevin March>: Chris, lead times did come in, in the third quarter and we expect them to continue to come in, in fourth quarter, and if all goes well then as we enter next year we should have lead times back to normal.

<Q – Christopher Danely>: Great. And then as my follow-up, it seems like the PC, and the consumer end markets are below normal. Is everything else roughly normal? Or is anything above normal.

<A – Ron Slaymaker>: Chris, I would say probably – is this a fourth-quarter question?

Okay. I guess what I would say is, you're right. Those are the areas that would be below normal run rates. Probably the one area I would say that continues to be strong is comms infrastructure. Handsets, since we have only one customer there, really, I don't want to provide any specific commentary. Industrial, I would say probably the best description there is that it is normalizing. It's going from – transitioning from third quarter, which is really an extension of the first three quarters of this year where it has been growing pretty rapidly due to that cyclical recovery, but I would say fourth quarter would represent more normalizing to probably a more typical seasonal pattern from Industrial. So, you did identify really the two areas that we would call out as being weaker, those being computing and parts of the consumer market.

All right, Chris, thank you for your questions, and we'll move to the next caller.

Operator: Our next question comes from Glen Yeung of Citi.

<Q – Glen Yeung>: Thanks. Ron or Kevin, it just doesn't feel like this cycle is as dramatic as maybe we've seen other cycles in the past. At least that's my perception. I wonder, one, if you agree with that? Two, when do you think the inventory issue might be over, and what are the clues that you have that suggest that, if that's, in fact, what you see?

<A – Kevin March>: Glen, I think that your perception probably is shared by us. That is that the adjustment that we're seeing under way or starting now is probably more focused and not broad-based and is probably generally pretty mild. If you look in the past, when you look at book-to-bills, typically, we get four, five, six quarters of positive book-to-bills and followed by a couple of quarters of negative or near one book-to-bills and we'd typically suggest we'd have maybe a couple of quarters from an adjustment phase before we have a resumption of demand in the PC and consumer space. As we discussed here we saw demand softening up in that quarter, so we're probably halfway through our first quarter on that. And so if we take a look out, it would be from our view, reasonable to assume that we get through this adjustment process over the next quarter or two, and then we see a resumption of overall end market demand.

<A – Ron Slaymaker>: Do you have a follow-on, Glen?

<Q – Glen Yeung>: Yeah, there's a press release just a little while ago about ZTE spending a bit of money. You guys were named as one of the people with whom they'd be spending. I wonder if you can just shed any light on that particular announcement, and help us to understand whether or not this is something that's new with these guys with ZTE and that there are any material elements of the contract we should know about?

<A – Ron Slaymaker>: Glen, I probably don't have a lot to say. I would refer you to ZTE in terms of anything they may want to offer. We've had a strong presence in China overall, and we've had a relationship specifically with ZTE for many years. So, I think this is just an extension of a lot of good things that have been happening for TI for some time and our growing momentum in that market, which is one that we see is going to be especially important for TI in the years to come. But beyond that, I really don't have anything specific to say about that one specifically.

Okay, Glen, thank you for your questions and we'll move to the next caller.

Operator: Our next question comes from Tristan Gerra of Robert Baird.

<Q – Tristan Gerra>: Hi. Good afternoon. The ramping capacity you're putting in place implies a lot of market share gains over the next couple of years. What's your pricing outlook for Analog with regards to that strategy and also, in view of the current weakness that we're seeing in some end markets notably at the low end?

<A – Kevin March>: Tristan, I don't think that the capacity that we're adding necessarily has any bearing on the pricing outlook per se. That capacity, you may recall that we began over a year ago with the acquisition of equipment from Qimonda who was in bankruptcy at the time to begin to put 300-millimeter equipment into our RFAB, our Richardson fab. We went through a second phase on that with another location they had in Dresden where we purchased equipment to complete phase two in RFAB. In addition, last quarter we announced acquiring Spansion of Japan out of bankruptcy. And this past month we announced our first manufacturing acquisition or manufacturing plant in China.

To put it into perspective where we're at in those acquisitions right now, the RFAB qualified its first product this quarter and we do expect to ship our first revenue-generating wafers out of that factory this quarter. It will ramp up consistent with demand. As Spansion is concerned, the one we acquired in Japan, we expect to have our first wafers out of that factory by the end of this quarter as we ported one of our processes into that factory. And with the Chengdu factory in China, in fact, we had been already been using that factory as a foundry for some of our HVAL products. And we will be porting additional products into that factory over the next couple of quarters.

So we would expect those factories to ramp up fairly slowly on our products consistent with whatever we see in demand. In the meantime, those two factories, the one in Japan, and the one in China, in both cases we have transitional service agreements with the sellers whereby we are selling them some product out of those factories that to a large extent will offset our operating costs as we bring up our own process technologies in those factories.

<A – Ron Slaymaker>: Tristan, I guess the only thing I would add is, if you think about what Kevin said, I mean, even with RFAB where we're moving into production this quarter, as of now, we have one product qualified and moving into production. So, really if you think about the timing of that, as well as the other two factories and you compare that to what Kevin said previously about this period of market weakness, our view is it is going to be relatively short-lived and mild. Those factories ramping really are probably coming on more online on the other side of this period of weakness as opposed to while the market weaknesses is underway.

Do you have a follow-on, Tristan?

<Q – Tristan Gerra>: Thanks for that one. How do you expect re-sales to disty to track in Q4 versus sell-in? You mention that your inventory level in the channel level were at normal levels. So, is it fair to assume that you don't expect any type of adjustments for this coming quarter?

<A – Ron Slaymaker>: Tristan, I probably – I guess I'll stick with our normal practice, which is we don't try to forecast re-sales in the out quarter. Probably the best I can do is point out that if you look in the prior quarter, the third quarter, re-sales generally track very closely with TI's own revenue trends, but I don't have a specific projection for you on re-sales in Q4.

Okay, let's move to the next caller. Thank you, Tristan.

Operator: Our next question comes from Edward Snyder of Charter Equity Research.

<Q – Ed Snyder>: Thank you very much. Ron, thinking about 300-millimeter here, and where we are in this thing, kind of in the whole cycle, you've got things moderating a bit. Industrial seems like it has peaked out, and am I taking you correctly in saying that it's not necessarily slowing down, it's just not going to grow as fast as we have seen over the last several quarters or so?

<A – Ron Slaymaker>: I think you have it right. It is slowing down, but the comparison is to a cyclical recovery. It's moving more to seasonal patterns. It's not expected to go through a – at this point, we don't see a correction, per se. We see it moving to a more normalized seasonal pattern.

<Q – Ed Snyder>: If we've got things returning to normal, you are bringing up 300-millimeter. It sounds like pricing remains firm. You've had a nice ramp of margin improvement here. Why shouldn't we expect, say, through next year that margins will continue to improve as your cost basis drives down? It doesn't sound like we're in a downward cycle with demand, and yet your costs have got to be starting to drop, especially if you're bringing up these new fabs close to operating costs in terms of the agreements that you're doing with the people you're buying them from?

<A – Kevin March>: Edward, clearly bringing on these factories at these kind of cost profiles certainly is a favorable outlook for our overall margins. Importantly, as analog and embedded processing become a bigger portion of our overall portfolio, that also will give us more tailwind on our margins.

The fact of the matter is we are not really focusing on trying to improve our margins so much as we are focused a lot more on trying to improve our top-line growth. You've heard us talking for a number of quarters now about having a growth objective, whereby we are considerably outgrowing our markets and gaining market share from our customers. And that's really where all our energy and focus is at.

That doesn't mean we that we will not let margins fall through as they produce themselves, but that's not what we're aiming at, and that is not the purpose of the acquisition of those factories. The purpose of the acquisition of those factories is really to support that top-line growth, and happily those factories came to us at very inexpensive cost.

<A – Ron Slaymaker>: Okay. Do you have follow-on, Ed?

<Q – Ed Snyder>: Yes, just as a clarification then, if it comes down between you not getting the top-line growth that you're after and your margins are at record levels, we would be reasonable to assume that the margins will be tapped and maybe have a little more aggressive pricing profiles so that you can grow the top-line?

<A – Kevin March>: Yeah, I don't think I'd make any assumptions Edward. I think that the – we don't set the prices, the market sets the prices and we can't anticipate how competitors will respond to customer demands. What we're really focused on is making sure we have adequate capacity to grow as rapidly as we can as our customers will accept our products. But to infer that that would lead us to a pricing decision would be an incorrect conclusion because frankly, prices are set competitively, not unilaterally in our space.

<A – Ron Slaymaker>: Yeah, and as you've heard us say for some period, but for the broader audience, you know especially in analog, pricing is determined, more based on the quality of the product, the specifications of the product, the performance levels of the product, and you know you have to be competitive on pricing, but that's not how you win business. You win business based upon the quality and performance levels of the product, and so even in a weaker market environment or if growth is not producing the levels that we expect, you don't change that fundamental dynamic by changing your prices. Changing prices or lowering prices below market just leaves the money on the table. It does not result in incremental revenue for the vast majority of our product line.

There's a small part of our product line that represents less than 5% of our revenue that would be considered commodity-type products that is price elastic, but again, that's a nit relative to I think the broader product portfolio.

Okay, Ed, thanks for your questions and we'll move to the next caller.

Operator: And our next question comes from Ramesh Misra of Brigantine Advisors.

<Q – Ramesh Misra>: Hi, good afternoon, guys. My first question is in regard to your capital spending; you've been very opportunistic over the last 12 to 18 months, but it sounds like you're still looking for opportunities here and if you found an inexpensive fab you'd still be expanding capacity. So, at what point would that stop?

<A – Kevin March>: Ramesh, what I've indicated to you in my opening remarks was that we believe we have acquired enough capacity to meet our intermediate-term growth term objectives so we're pretty satisfied with what we've got so far. Now, that's not to say that if we continue to find some of these factories at price points that, frankly, are unheard of in our time in this industry, that we may not consider them for acquisition, but our focus now is on bringing these factories up that we have and bringing products up into production and getting them ready for what we believe will be a resumption of growth in the industry in the next couple of quarters.

<A – Ron Slaymaker>: And I think Kevin was just saying in general we look for investment opportunities that make sense for our business. That could be smaller acquisitions or that could be the capital equipment that you've seen us, but probably the former would be the priority.

Okay. Do you have a follow-on, Ramesh?

<Q – Ramesh Misra>: Okay. Just a very quick one, in your Other segment did you see weakness in the consumer-oriented part of it as well, such as calculators? In other words, was your strength in the Other segment driven predominantly by your custom ASICs?

<A – Ron Slaymaker>: It wasn't – I don't know I'd say predominantly, we actually saw calculators increase sequentially from second to third quarter, but that's just seasonal. Back to school usually peaks in the third quarter for us and third quarter typically increases somewhat beyond second quarter.

The biggest area of sequential strength in that Other segment wasn't custom ASIC. I would probably note a couple of areas inside of that. One is, we do have a significant part of our custom ASIC business that goes into communications infrastructure, both wireless base stations, as well as the enterprise side and both increased sequentially in the quarter.

And then we also sell custom ASIC products. This is kind of more one-off, but for touch-screen controllers going into smartphones that also did nicely for us in the quarter. That's a little bit of insight into the custom ASIC.

The other area that we mentioned was DLP. DLP is still being dominated in terms of that revenue base by front projector business and continues to be a nice business and has even shown some recent growth for us, so no real change on that front though.

Okay, Ramesh, thank you for your questions, and we'll move to the next caller.

Operator: And our next question comes from Uche Orji of UBS.

<Q – Uche Orji>: Thank you very much. Ron, can I just ask you within the HVAL business you talked about weakness in computing and consumer products. How is that stabilizing now in terms of booking strength? And within that also can you talk about whether you have any position in the tablet markets, and what all it means for TI?

<A – Ron Slaymaker>: Okay, I think if you look at HVAL, you are right. There's – probably there the computing tie is more through products that go into hard disk drives. Our Power product line in Analog also sells into PC'-s via some of the power management products, but HVAL's probably more through hard disk drives than storage products. It – and I think your description of that – well, I'll just say, we expect that it will continue to be what I said before. Demand will continue – kind of the current trends that we saw in third quarter slowing going into fourth quarter as well.

HVAL also sells into a range of other products, such as smartphones, some of the power management areas in smartphones. They sell into some video gaming on the consumer side. And even though we've said consumer televisions were weak, there were other areas, such as video gaming on the consumer side that actually did reasonably well for us in the third quarter.

And I'm trying to think if there are – I'm trying to think if there are other areas of notable to mention. Those are probably the ones I would tie. Maybe a final one would just be infrastructure. It sells into some of that communications and wireless infrastructure as well. And of course, almost anything that's touching infrastructure for us and that would be I guess on both the HVAL side, but then also some of the HPA products tie into comms infrastructure as well. And as I said, anything that we have selling into infrastructure, whether it was the ASIC products I mentioned, the embedded processing products or some of these analog products have done well and we would expect to continue doing well into the fourth quarter.

Okay, Uche, do you have a follow-on?

<Q – Uche Orji>: Yes, just we've talked about tablets. We've seen some strength in tablet markets. And my question here is, how does that impact TI across the board? One would obviously expect gains for the OMAP business, but I would quite like to get a sense of your focus there, and your positioning in some of the upcoming tablets? And then how that cuts across other segments of your business through, you talked about HDD, obviously tablets are going to kind of be like the PC. What will be the impact of that on TI? Or do you have a commensurate gain also on tablets offset any weakness there? And so any comments you can make as to what this means for TI across your OMAP business would be helpful.

<A – Ron Slaymaker>: Okay, so I would say we sell a lot of – I guess I would describe it as principally various analog products, for example, power products that go into tablets. We saw strength in those areas, as you might guess, in the third quarter. That strength was not, even though it's a nice growing business and offset some of the weakness that we saw on the PC front or the notebook front, it wasn't the PC exposure these days just because of the relative size of that market, of course, is higher for us. We'll see how that changes over time. But those tend to be some of the more – those type of products tend to be a little less visible, I guess you might say. I know I see all the various tear-downs, and they try to describe who has this processor or that processor. Products like power tend to run under the radar.

A couple of other areas I would mention would be audio amplifier, some of the connectivity products. Certainly, there's opportunity in tablets. And then, as I previously mentioned, clearly OMAP as the main processor to handle some of both the applications, the graphics, et cetera, certainly is a great opportunity. But the opportunity goes well beyond OMAP, and we're already benefiting even in third quarter from the growth of tablets, and we expect that to just broaden as products like OMAP transition into production in that space.

Okay, Uche, thank you for your question, and we'll move to the next caller.

Operator: Our next question comes from Shawn Webster of Macquarie Capital.

<Q – Shawn Webster>: Yeah, thank you. On the factories, is what you're spending for the factories in China and Japan part of your capital expenditure budget? And then, can you add some color on – you said you were getting some revenues from some of these factory agreements. Can you quantify that, and how much that's contributing going into Q4?

<A – Kevin March>: Yeah, Shawn, the factories, some portion of those acquisitions are in capital and some portions of those acquisitions are being accounted for as an acquisition of a business. In fact, you can see that on the cash flow statement with our earnings release.

For example, on the Japan acquisition, we used a net of about $130 million acquiring all of those assets, and about 59 million of that is for an acquisition of a business, and the balance of it goes through CapEx. With the acquisition Chengdu, we'll initially use about $140 million in acquiring that asset, and most of that will probably go through acquisition of the business. The remaining $35 million or so will be earned out on that acquisition over the course of the next year. So, it's a bit of a mix. Some of it is going through CapEx and some of it is acquisition of a business.

As far as the revenue that we expect, we anticipate that the revenue that we'll get through those transition service agreements will be less than 1% of TI's revenue. And by and large, what that will wind up doing is absorbing the cost of those factories during the period that we are bringing up our own process technology inside those factories.

<A – Ron Slaymaker>: So transitionally, I guess, the other way we tend to look at this, yes, there will be a little bit of benefit as we have some of that revenue in Q4 that we did not have in Q3, but at the same time, I'll remind you that we also are selling our cable modem business, and we expect that transaction to close in Q4. And for the most part, what we lose in Q4 transitionally on cable modem will be about the same amount that we'll gain through some of these transitional supply agreements.

Okay, Shawn, do you have a follow-up question?

<Q – Shawn Webster>: Yeah, maybe just on gross margins and utilization rates. Can you give us, I guess, your view on the puts and takes for gross margins going into Q4, and maybe into the first half? And also, can you share with us what your utilization rate trends were in terms of are they higher in Q3, lower and your expectations for Q4? Thanks.

<A – Kevin March>: Yeah, Shawn. We have not publicized our utilization rates in a while, but I will just leave it to say that they were relatively flat the last couple of quarters. And with the increase in capacity coming online, and our expectation of declining revenues going into fourth quarter, we expect our utilization probably to drop a little bit. But I don't think there is going to be a material impact there, especially given the cost of the capacity we brought online. We don't give a GPM forecast. We just give a revenue and earnings per share forecast, and I think I'll leave it at that for now.

<A – Ron Slaymaker>: Okay, Shawn, thank you for your questions, and we'll move to the next caller.

Operator: Our next question comes from Srini Pajjuri of CLSA.

<Q – Srini Pajjuri>: Thank you. Ron, on the disty – distributors growing inventory a little bit, I'm just wondering, given that demand is weakening on the margin and also, you're heading into a seasonally weaker period, why would the distys be building inventory? Is it because there were some pockets of strength? Or is it because in some regions needed more inventory? If you could just clarify that?

<A – Ron Slaymaker>: I think it was because they needed more inventory in certain product lines and certain areas. And keep in mind, lead times have been extended and supply has been constrained for some period. And even though we've made progress, lead times are still, as Kevin pointed out earlier, extended beyond where we really want them as of right now. And so I think as things have loosened up a little bit, we, and the distributors took advantage of that in the third quarter to put in place some inventory that they really had been trying to get in place for some time.

Do you have a follow-on, Srini?

<Q – Srini Pajjuri>: Yes, for Kevin. Kevin, on the gross margin, I was just wondering about as we head into the first half, which is seasonally somewhat softer, should we expect, besides the utilization coming down maybe a bit, should we expect any incremental depreciation from some of the new acquisitions? Thank you.

<A – Kevin March>: Srini, there will be some incremental depreciation, in fact, with the qualification of RFAB this quarter. We expect to see depreciation going up a little bit in the fourth quarter, but I would remind you also that there's a natural roll-off that goes on. So, while depreciation may be up for a couple of quarters, I expect it'll come back down as we move into next year. In fact, if you just kind of step back and take a look at the broader picture, you may recall that we depreciate on a five-year straight-line basis. If you go back to 2005 and look at our capital expenditures back then, it was about 1.330 billion, if I recall. And that's beginning to roll off, and will roll off over the next couple of quarters.

Our CapEx forecast for this year is 1.2 billion. And I mentioned earlier that some of those acquisitions are going through acquisition of a business. So, you add it all together, and we're probably talking about 1.4 billion, or so of assets that we are acquiring this year that will be depreciated. So, to a large extent, what's rolling off will be replaced with the acquisitions that we've made in 2000 – or plan to make here in 2010. And so year-over-year, we don't expect our depreciation to change all that much. We'll be able to give a more precise outlook on that after we close the fourth quarter, but for some early planning, and for trying to figure out what depreciation might do for GPM, that may help frame that for you a little bit.

<A – Ron Slaymaker>: So Kevin, I would just add on as a question, so fixed costs are relatively stable. But what about some of the variable costs then associated with the new factories we're bringing on?

<A – Kevin March>: The variable costs of RFAB will scale with revenue. So, clearly staffing and material costs, and so on are highly variable, and will be brought on only as revenue pulls demand through that factory. And then the variable costs associated, again, with the acquisitions in Japan and China, by and large, are being offset by the transition services agreement as we bring up our new processes there. So, we expect a fairly smooth transition as those transition services agreements begin to shift downward, and that cost is left behind, that should happen at about the same time that we're bringing up our own production inside those factories, and we can absorb that into revenue generating wafers.

<A – Ron Slaymaker>: All right. Thank you, Kevin, and Srini, thank you for your questions. We'll move to the next caller.

Operator: Our next question is from Stacy Rasgon of Sanford Bernstein.

<Q – Stacy Rasgon>: Hi, guys. Thanks for taking my question. Very quickly in the Wireless business, so you had all pieces up, but we had OMAP application processors that were up evidently a little less in connectivity. And I actually found that a little bit surprising. Was there any way you can talk a little bit about what you think is driving the larger upside that you're seeing particularly in connectivity in terms of end market or products? And if you could comment a little bit on how you see market share in application processors, particularly as that market is growing very strongly, and you have competitors like Qualcomm and some of the other guys that are also making their pushes in there as well?

<A – Ron Slaymaker>: Sure. Stacy, I guess I would just say that what's designing – what's driving growth in connectivity are just a series of design wins that we've accomplished over the last several years. I believe we have the most integrated connectivity solution that's out there centered up on our Wi-Fi solution. And even if you look at where connectivity has been over the last few years, and where it's going, clearly there's a trend toward integration, and a lot of the players that kind of were single technology players just don't have the capability to integrate and do it as quickly as TI has, where we've played across historically Wi-Fi, Bluetooth, GPS, FM radio, and so we – it's quite natural for us to have the capability to roll that all together into an integrated solution. So, the trend toward integration in the connectivity market has positioned – has just favorably worked to TI's benefit. We've won a lot of designs as a result, and you're seeing that in terms of revenue growth.

Now before you take that and extrapolate it too far, as I said in the prepared remarks, we've also had tremendous success in designing in OMAP 3 and OMAP 4 product generations as well. And so I think you'll see that even though, for the last few quarters, connectivity has probably been the fastest growing, that could rapidly change and go through a period of time where OMAP is growing fast. So, I think you'll see both of those areas grow, but it will kind of happen in fits and starts, based on as new generations of product roll out and as design wins move into production.

Do you have a follow-on, Stacy?

<Q – Stacy Rasgon>: Yeah. I think part of my first question was also on application processors if you could address that. But my follow-up would be one more on gross margins, just really briefly. I'd like to see if you could give me any color on for next quarter, do you anticipate any sort of impact, either the positive or the negative, from the 300-milimeter as you start to ramp that to volume, and is there any sort of measurable impact on the gross margin front from the foundry arrangements from Spansion and from Chengdu?

<A – Ron Slaymaker>: Stacy, I think we hit the apps processors in the first discussion, so we'll just go ahead and move on to let Kevin answer the gross margin question.

<A – Kevin March>: Stacy, I think that the short answer is no on the impact of GPM. I did mention earlier that we will see depreciation go up a bit in fourth quarter, because we have now qualified most of the equipment in RFAB. So, clearly that will be there, but I don't think it will actually move the needle that much from an overall GPM standpoint.

<A – Ron Slaymaker>: Okay, Stacy. Thanks for your question. We will move to the next caller.

Operator: Our next question comes from Ambrish Srivastava of BMO Capital Markets.

<A – Ron Slaymaker>: Hello, Ambrish.

<Q – Ambrish Srivastava>: Hi, thank you. Kevin, question on – excuse me, my voice is really hoarse from rooting on the Giants.

[Laughter]

<A – Kevin March>: Good luck with that.

<Q – Ambrish Srivastava>: Yeah, I know, I was going to say, on the TI call. My question on the ROI, Kevin, you do give out the number every quarter. I'm just going back looking historically. I don't think you guys have been this high, and now you're bumping up against that other analog company that's only slightly more profitable than you. Is there a target that you're managing the business to, Kevin? And then I had a quick follow-up as well.

<A – Kevin March>: No, on the return of invested capital, you're right. It's pretty high this quarter. We're about 34.2%, by my math there. I wouldn't say that there is a model per se, other than that we're mindful of the fact that profitable enterprises have to return on their capital in excess of what their cost of capital is. So, clearly as long as we are above that, we believe we are adding value to our shareholders and clearly, we are well above that right now.

One of the things that high ROIC does do for us, is it allows us to generate healthy levels of cash. And as we have seen here, certainly for an extended period of time, cash in excess of what we need to actually grow and operate our business on a day-to-day and quarter-to-quarter basis, which allows us to be pretty aggressive on buying back shares and also, over time, returning cash to shareholders in the form of dividends as well.

<Q – Ambrish Srivastava>: And a quick follow-up, Kevin?

<A – Kevin March>: Sure.

<Q – Ambrish Srivastava>: And actually maybe Ron could answer it as well. What is the normal seasonality for the OMAP, and the connectivity business for Q4? Or given the design win momentum you have, is it not relevant in the coming quarter?

<A – Ron Slaymaker>: Ambrish, I would probably agree with the latter. I think in general, what we're seeing there are secular trends that go well beyond any kind of normal seasonality that might apply in the wireless market, so – I guess I would agree with your conclusion there that, that doesn't matter.

Okay. So, with that, we will move on to the next caller. Ambrish, thank you for your questions. I note you mentioned you were cheering on the Giants and not the Yankees, but that would be a distraction, so we'll move to the next caller, please.

Operator: Our next question comes from Chris Caso of Susquehanna Financial Group.

<Q – Chris Caso>: Thank you. I'm not sure, Ron, if you directed that at me, but you'll notice I'm a Yankee fan and my voice sounds just fine.

<A – Rich Templeton>: You didn't have anything to cheer for. Go ahead, Chris.

[Laughter]

<Q – Chris Caso>: There you go. Well, I wondered if you could talk a bit about the strategy going forward, on adding new capacity, and there's obviously been a lot of talk from some of us on the analyst side, some of your competitors, about where the low-hanging fruit is for you guys. What do we see as we go through the next year in terms of where you guys would expect the most growth as a result, from this new capacity?

<A – Kevin March>: Chris, the capacity we're putting in place is aimed directly at our Analog portfolio. If you take a look from a 300-millimeter standpoint clearly the higher volume parts, such as those parts by – that are developed in our HVAL business, as well as some of our higher volume Power parts and certain other parts would be prime candidates to go through that factory.

I also mentioned earlier that the factory in Chengdu, China, was already manufacturing some parts for us for our HVAL business, and they'll continue to do that as we port our processes in there. We expect to put our power MOSFET business into that factory as we go into 2011. And then, as it relates to our factory in Japan, the process we are porting there will be initially ideal to suit the High Performance Analog business portfolio. So, each of those factories will be able to support all three elements of our Analog, but again, are really aimed at the Analog portfolio.

As we look into 2011 with the fab capacity brought on-line we'll be continuing to pay attention to our assembly and test capacity to make sure that we keep that ahead of the output from those wafer fabs.

<A – Ron Slaymaker>: So Chris, the only thing else that I would add is – and I'll even just respond to this in reading various sell-side notes from visits to various competitors. It seems like the common denominator is that each competitor feels 300-milimeter is directed at somebody besides them. And what I would say is 300-milimeter is going to go across the board in Analog and that means HVAL, it means Power, and it means High-Performance Analog.

And we won't delve off too deeply here, but 300-milimeter we have a lot more flexibility given the automation systems in that factory to take a 300-millimeter lot of wafers and subdivide it down into two wafers of product A and four wafers of product B. That lot does not have to all be the same product. So, therefore, the argument that somehow 300-millimeter scale doesn't apply to certain areas, such as High-Performance Analog, makes no sense to us. I think you will see us move forward accordingly.

Do you have a follow on, Chris?

<Q – Chris Caso>: I do. Thanks. And I guess you guys have stopped breaking out baseband within the Wireless. If you could give us just a bit more color, however, on where we are in the transition away from the baseband business relative to what you told us in the past?

<A – Ron Slaymaker>: Chris, actually we do break it out. I gave it in my prepared remarks and if I can find my data real quick, I'll give it to you. It was $438 million in the quarter. So, that grew, it looks like, about 5% sequentially, and it was down 3% from a year ago. I'm sorry, was that the question or was there...?

<A – Kevin March>: The profile.

<A – Ron Slaymaker>: Oh, the profile. Okay. So, again, probably nothing really has changed. I think what we've described before is that if you basically just straight-line it from here to zero by the end of 2012, you will have quarters as you have seen, some quarters that are above that line, some quarters that are below that line. And so really it's probably no different in terms of guidance from us. It will be a bit noisy, but that's probably about the best that we could recommend. No change in terms of when we expect that revenue, basically, to be essentially to zero by the time we go into the year 2013.

Okay, Chris. Thank you for your questions. And we'll move to the next caller.

Operator: Our next question comes from Adam Benjamin of Jefferies.

<Q – Adam Benjamin>: Thanks, guys. You commented the fact that you thought this was going to be sort of a shallow problem here in terms of demand. And I was just curious what gives you confidence that, that's going to be the case, and why? based on the orders you are seeing or just some customer feedback? That would be helpful. Thanks.

<A – Kevin March>: Adam, I think a lot of times in the past when we've seen what are typically described as inventory corrections in the semiconductor market it's brought on by usually an excess of inventory in the channel or more often an excess of capacity driving that excess of material. And in fact, we appear to see just the opposite. Channel inventories remains fairly lean, at least from indications from our products that we can get from – information from our customers for our products.

And broadly speaking if you look across the whole industry, I have seen numerous reports that indicate that total installed capacity for wafer fabs from a start standpoint globally is still down significantly from its high point in third quarter '08. The most recent stats I've seen suggest that it's still running around 15, 14, 15% below where it was back then. So, we don't have excess capacity driving excess production.

Generally speaking, we do not see much evidence of any excess components of ours up in the channel. What we do seem to be seeing is, after the cyclical snapback last year and a half in many of these channels, we are seeing growth rates now that have begun to mirror much more to what's happening in the global economy from overall demand.

So from that standpoint and just from the history of these kinds of adjustments, we'd expect to see a couple of quarters of relatively mild adjustment and a resumption of growth. We're not making a prediction as to what that growth looks like when it resumes, but we expect it will be a resumption of growth after a few quarters of pause.

<A – Ron Slaymaker>: And I guess, just to add to that, Adam, if we talk about order trends, our orders, and of course, in third quarter were a step down from what we saw in second quarter, but we also didn't see orders spiral down as we moved through the quarter month by month. They actually stepped down in July and held at that level relatively stable through August and September. So, that's just another data point, I guess you might say, as to what is driving those comments from us.

Do you have a follow-on, Adam?

<Q – Adam Benjamin>: I do. On the connectivity business, I was curious how committed you are to that business going forward? Obviously you have some significant customer concentration and you've done pretty well in terms of the portfolio and ahead of many of your peers. But I'm just looking out longer term, I know you're not going to tell us, you're going to shut it down or sell it tomorrow, but I'm just curious how committed you are in terms of R&D investment going forward, given that you're not in the baseband market going forward?

<A – Kevin March>: Adam, I'll go ahead and answer that for you. I think that the R&D investment is probably a good intro to an answer on that. Over the last year we have pretty much removed all of our investment in the baseband as we've talked about for multiple quarters now, and directed that over to the non-baseband portion of our Wireless portfolio, which is both connectivity, as well as the apps processor, and clearly, the apps processor is getting a large share of that R&D investment.

I would add that connectivity is also, as we're finding different markets for those products to be sold into, but clearly the lion's share of the R&D is going into the apps processor space. That is a space that is ripe for growth not only in cell phones, but in tablets and other applications, as well as, such as personal navigation devices, infotainment systems on-board cars, a number of different spaces where those kinds of products can be used.

<A – Ron Slaymaker>: Adam, I guess the only other thing that I would say is, I know there is all this ongoing relentless debate about integrated solutions with baseband and connectivity products with baseband and applications processors, but if you just look at it, our connectivity and OMAP revenue is up over 50% year-to-date. And so it's a great growth business. And that's up 50% while – it's clear we're getting out of the – we're pulling back on baseband and exiting that marketplace. So, again I think the data and evidence increasingly proves, that can be a very good growth business for TI even without being in the baseband business. So, we'll keep riding that one hard. We like it.

Okay, Adam, let's – that was your follow-on, let's go to the next caller, please. Thank you for your questions.

Operator: Our next question comes from Tore Svanberg of Stifel Nicolaus.

<Q – Tore Svanberg>: Yes. Thank you. First of all, it looks like your embedded processor business saw a pretty nice increase in its operating margin. And I was just wondering what that came from? And I know it grew sequentially, but it was a pretty steep increase in operating margin. Just wondering where that came from?

<A – Kevin March>: Yeah, Tore. That was – that's really just getting leverage from the revenue growth that you saw there. The overall operating expenditures are – we increased those. You might recall back in first quarter, we moved quite a few resources from our Other segment into the EP segment, into the Embedded Processing segment, which temporarily depressed operating margins there. And now as we're seeing the revenue growing very strongly there, we're just simply getting a great deal of leverage off that.

<A – Ron Slaymaker>: Do you have a follow-on, Tore?

<Q – Tore Svanberg>: Yeah, the follow-up is on CapEx. I think CapEx hit more than 10% of revenue, that's the first time in a long while. Let's take Q4 '09 out of the equation here, but it's above 10%. I'm just wondering is it – are we getting to peak there? Are we going to start to see it trend back down sort of to the 5% to 7% level again?

<A – Kevin March>: Yeah. Tore, our goal remains to be in 5% to 8% level. And as we have indicated, that should be what you see us doing over time. We won't let that artificially prevent us from going after very attractive opportunities, such as you've seen us move on here recently. But in fact, for purposes of the modeling you should continue to expect us to operate at 5% to 8% and consider what has occurred here recently as an opportunist aberration.

<A – Ron Slaymaker>: And clearly, I think you've heard us quantify how much revenue we can generate off of the capacity that we have purchased. Clearly, that's multiple years of capacity needs, so probably if anything, you could even see us moving to the lower end of that range in the near term.

Okay, Tore, thank you for your questions. And, Operator, I believe we have time for one additional questioner.

Operator: All right. And we'll take our next question from Jim Covello of Goldman Sachs.

<Q – Jim Covello>: Thanks, guys. I can see the strategy this year is to stuff all the Yankees fans at the end of the call to add further insult to injury, but thanks for fitting me in.

<A – Ron Slaymaker>: I wouldn't have fit you in had I known you were a Yankees fan, but go ahead.

[Laughter]

<Q – Jim Covello>: I understand your comments about fourth quarter disty inventory you didn't want to make a comment on that, but how about tax and zone inventory for the fourth quarter? Would you expect it to – flat, up or down?

<A – Kevin March>: Yeah, Jim. I'll comment on that. We grew inventory in dollar terms in third quarter and yet our days dropped by another day on us. And in fact, we would like to continue to try to grow some especially in those areas where we have lead times that are beyond what our customers expect of us. So, we will continue to operate the factories focused on those areas where we're still short on overall capacity and given the fact that we would expect revenue in the fourth quarter below our third quarter that should have some impact on our days of inventory as long as we go into the fourth quarter.

<A – Ron Slaymaker>: Okay. Do you have follow-on Jim?

<Q – Jim Covello>: Yeah. Please. The buyback you guys announced is terrific. As you guys talked about a quarter of the market cap is the authorization. There's not, your cash flow generation is terrific, but even you guys don't have that much cash on the balance sheet. Would you ever be willing to think about taking on some leverage in order to fulfill that buyback or should we just think about the buyback coming in as the cash flow growth continues?

<A – Kevin March>: I think it's the latter, Jim. You should look at us using our free operating cash flow for purpose of that buyback. We have no intention of doing an accelerated buyback.

Ron Slaymaker, Vice President, Investor Relations

Okay, Jim. Thank you for your questions. And let me before we leave, apologize if I offended or embarrassed any Yankees fans. I realize your team had already done that for you and to you. And San Francisco guys, you are next. In general, thank you for joining us. The replay of this call is available on our website. Good evening.

Operator: And this does conclude today's conference call. We thank you for your participation. And have a wonderful day.