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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to Texas Instruments' Fourth Quarter and 2009 Earnings Call. Just a reminder, this call is being recorded. At this time I'd like to turn the call over to Mr. Ron Slaymaker. Please go ahead, sir

Ron Slaymaker, Vice President, Investor Relations

Good afternoon and thank you for joining our fourth quarter and year 2009 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 risk factors 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 complete description.

Our mid-quarter update to our outlook is scheduled this quarter for March 8. We expect to narrow or adjust the revenue and earnings guidance ranges as appropriate with this update. In today's call, we'll address growth, what's driving it and is it sustainable? We'll also address inventories and provide our perspective on where they stand today in the supply chain. Finally, we'll discuss actions that we're taking today to support continued growth in the future.

Revenue in the fourth quarter was near the high end of our range of expectations. Earnings exceeded the top end of our range of expectations. Sequential growth began in the second quarter of 2009 as our shipments normalized to customers' production levels following a sharp inventory correction. We believe growth is now being fueled by expanding production at our customers. Inventories, through TI's and our customers' supply chains are lean and growing end demand is stressing the entire supply chain.

Let's start with breaking down the fourth-quarter revenue trends. Overall revenue was up 4% sequentially or 21% from a year ago. Sequentially, our calculator revenue seasonally declined by $116 million. Our semiconductor revenue, therefore, grew about 9% sequentially. Our Analog, Embedded Processing and Wireless segments all contributed to sequential growth, while the Other segment declined due to the lower calculator revenue.

Analog revenue grew 9% sequentially and was up 27% from the year-ago quarter. Again, this quarter we had good contributions by all three of our major Analog product areas to this growth. I described last quarter our high expectations for the long-term opportunity that we have in the Power Management area of Analog. Power was the fastest growing part of Analog for TI this quarter, as we penetrated new opportunities, and gained share. Specifically, growth was strong in power supplies for computing applications, an area where our share is rapidly expanding in a strong market.

We also had strength in displays, specifically LCD TVs as higher frame rates, LED backlighting and power efficiency become more important. As we saw strength in notebooks and smart-phones and for TI these are products such as white LED drivers and battery gauges. In HVAL, automotive was the fastest growing area sequentially and in HPA, low power wireless products were the fastest growing.

Embedded Processing revenue grew 5% sequentially and was up 21% from a year ago. Catalog products were the biggest driver of this growth, followed by automotive. Embedded Processing should continue to benefit as the industrial market strengthens. Wireless revenue grew 8% sequentially and 13% from a year ago. Baseband revenue of $465 million grew 3% sequentially and was even with a year ago.

Most of the Wireless growth was driven by applications processors and connectivity products. These products collectively grew 19% sequentially, and grew 46% from a year ago. Other revenue declined by 9% sequentially due to the seasonal decline in calculator revenue and grew by 17% compared with a year ago. DLP was the biggest factor in this growth and more than offset a significant decline in RISC microprocessors from a year ago.

From a geographical perspective, while sequential growth was fastest in the U.S. and European markets, all regions grew. Compared with a year ago, all regions were up, except for the U.S. market.

Turning to distribution, re-sales or sales out of our distribution channel increased sequentially in the quarter, as well as from a year ago. Distributor inventory was about even in the quarter and remains lean compared with 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 gross profit continued to expand this quarter, as revenue grew and utilization increased. Gross margin increased 150 basis points sequentially, to 52.9% of revenue. Compared with the year ago quarter, gross margin increased 890 basis points.

Operating expenses were down slightly from the third quarter and declined $90 million from the year ago level. Operating expenses were 23% of revenue in the quarter, well within our planned operating model.

Restructuring charges in the fourth quarter were $12 million, about the same as the third quarter and down 242 million from a year ago. The distribution of these charges across our segments is included in our earnings release.

Operating profit for the quarter was 875 million, 15% higher than the third quarter, mostly due to higher gross profit. From the year ago quarter, operating profit was up $824 million, primarily due to higher gross profit as well as lower restructuring charges.

Operating margin in the quarter was 29.1% of revenue. The last time we approached this level of profitability was the fourth quarter of 2007, when TI's operating margin was 28% of revenue. It is noteworthy that revenue was 18% higher in that quarter. Today's improved performance reflects the potential of our business model that is now focused on Analog and Embedded Processing. We expect the benefits of this strategy to continue to accrue to TI and our shareholders in the years ahead.

Net income in the fourth quarter was $655 million, or $0.52 per share. Net income includes $16 million in benefits from discrete tax items. 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.

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All of the higher net income compared with last quarter fell through to higher cash flow from operation, which was $1 billion in the quarter. This strong cash flow allowed us to increase our investments in manufacturing capacity, pay a higher dividend and repurchase more stock all while increasing our cash and short-term investment balances.

Capital expenditures increased to $436 million in the quarter. This included our purchase of the Quimonda fab equipment as well as continued elevated expenditures to expand our assembly and test capacity. As we discussed before, the Qimonda equipment is going into our 300-millimeter analog factory called RFAB. We have the initial pilot line in place today and have begun to process initial wafers. We are on track to achieve full production qualification before the end of the year.

We used $351 million in the quarter to repurchase 14.8 million shares of TI common stock and paid dividends of $149 million in the quarter. We increased cash and short term investments to $2.92 billion in the quarter. Our balance sheet continues to be strong and remains a competitive advantage to TI in this environment.

We were able to increase inventory by $86 million in the quarter, almost all in finished goods, resulting in inventory days increasing to 76. This will allow us to continue to improve our customer service performance levels. Our delivery performance has been improving since mid-November. Even so our inventory remains lean in this strong demand environment. TI orders in the quarter were $3.26 billion, up 5% sequentially. TI's book-to-bill ratio was 1.08 in the quarter, the same as last quarter.

Turning to our outlook, we expect TI revenue in the range of 2.95 billion to 3.19 billion in the first quarter, or negative 2% to positive 6% sequential growth. This compares favorably with our more typically seasonal decline of about 5% in the first quarter. We expect earnings per share to be in the range of $0.44 to $0.52. This EPS estimate includes the negative impact of a higher annual effective tax rate which we estimate will be about 31% in 2010. The increase in tax rate includes our estimate for higher profits, as well as the impact of the expiration of the federal R&D tax credit at the end of 2009.

For 2010, our estimate for capital expenditures is about $900 million. We expect these expenditures to be weighted toward the first half of the year as we continue to expand our assembly and test capacity and install equipment in our 300-millimeter analog fab. Our estimate 2010 R&D is $1.5 billion, about even with our 2009 level. We estimate depreciation will be about 900 million this year, about the same level as 2009. In summary, as the recovery continues to develop we are seeing the results that we expected from our focus on analog and embedded processing.

We are investing to position TI for growth in these strategic areas as evidenced by our investments in the industry's first 300-millimeter analog fab and our assembly and test capacity expansion as well as our continued investment in deploying field sales and application resources into the regions and markets that we expect to grow the fastest. And we're well positioned in electronic markets that we expect to drive growth. For example, our position in base stations is strong and continued data traffic increases should drive accelerated deployments of wireless infrastructure.

Also, our products are well positioned in the industrial markets that are still in the early stages of recovery. And there's a lot of pent up demand for PC upgrades especially in emerging markets for which we'll benefit from well positioned products such as our Analog Power Management as well as products sold into hard disk drives and other peripherals. All of which gives us confidence that there is plenty of opportunity for TI and our shareholders ahead.

With that, let me turn it back to Ron.

Ron Slaymaker, Vice President, Investor Relations

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 yourselves to a single question. After our response, we will provide you an opportunity for an additional follow-up. Operator?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions]. Our first question comes from Uche Orji with UBS.

<Q – Uche Orji>: Ron, can you hear me?

<A – Ron Slaymaker>: I sure can, Uche.

<Q – Uche Orji>: My first question is on lead times. There has been some talk in the industry about lead times generally coming down. Can you give us some color as to what's happening to lead times across the various products that you have? Are there some areas of shortages or tightness? Any color there would be helpful. Thank you.

<A – Ron Slaymaker>: Okay. Uche, I can't break it out product by product but, what I would describe is that our operations have responded aggressively to meet, what's been some pretty strong increased demand across the last few quarters. But with that increased demand our lead times have generally moved out as that demand has outpaced our supply. I'd say it moved out fourth quarter overall relative to third quarter and that's very similar to how I described it back in the December update.

We're certainly investing in manufacturing equipment to relieve these operational bottlenecks especially in our assembly and test areas and to get the lead times pulled back again. But to this point, I would describe fourth quarter generally lead times moved out relative to third quarter. I will note what Kevin said in his prepared remarks; that our delivery performance has improved since the mid-November time period. But we're focused on getting delivery performance improved before we start pulling lead times back in. Do you have a follow-on Uche?

<Q – Uche Orji>: I do. Kevin, you made a point about gross margins and the fact that revenues are lower than the same levels that you saw the same level of gross margin in 2007. If I look through the rest of the year can you just kind of walk me through what will be the key drivers of gross margin? It will be utilization rates, demand, mix, any color you can give as to how to think about gross margins maybe for next quarter and also for the rest of the year if possible. Thank you.

<A – Kevin March>: Okay. Uche, actually what I mentioned was operating margins had reached a new high versus where we were at in late 2007. On the gross margins, we did turn in a solid quarter at about 52.9% and as we look forward, as we've discussed in prior calls, we would expect that trend to continue to work its way up, really as we move forward on a higher mix of Analog and Embedded Processing as a proportion of our total revenue.

From a utilization standpoint, we're getting back closer to more normalized utilization levels and so there's probably a little bit less to be expected on that front as we go forward. Really, it's going to be much more driven by a higher mix of Analog and Embedded Processing. I would add to that, that we'd expect to see some benefit also as we put in place low cost manufacturing. And a good example is the 300-millimeter analog fab that we just opened in Richardson.

<A – Ron Slaymaker>: Okay. Uche, thanks for your questions and let's move to the next caller please.

Operator: Next question will come from John Pitzer with Credit Suisse.

<Q – John Pitzer>: Yeah. Good afternoon, guys. Congratulations. A couple questions. First Ron, when you look Q4 above seasonal, your guidance for Q1 above seasonal, to what extent do you think this is true demand pull versus the supply chain trying to refresh some inventory in the March quarter? And I guess how comfortable are you that you can tell the difference?

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<A – Ron Slaymaker>: I don't know that we have great visibility into our customer and our customers and their supply chain. I think we commented that our view was if you go back to fourth quarter, and this is more anecdotal versus direct measurement, our view is that the supply chain truly all the way to end demand are lean on inventory. I think customers would have liked to have built inventory, but to this point, they're pretty much hand to mouth ramping their production to be able to support higher levels of end demand.

Where we can measure is our own distribution channels and, I'll just repeat what we said in the prepared remarks. Inventories there was pretty much unchanged from the third quarter on re-sales that were higher. So again, our distribution channel inventories are clearly lean by any historical metric. Do you have a follow-on, John?

<Q – John Pitzer>: Yeah. Ron, we're all hyper-focused on lead times and when they might come in and what that might signal. I guess when we look at the data, you guys have done a great job gaining market share despite pretty tight back end capacity. How would we think about your ability to gain share if you were able to grow back end capacity going into Q2? Or do you think you're leaving business on the table right now?

<A – Ron Slaymaker>: I think John if you look at most of our products, they're proprietary or they're differentiated products that, customers don't have a lot of fungibility across different suppliers.

You know, I know there are some suppliers especially in the Analog marketplace, that have been vocal and crowing about their short lead times. But I'll also note those are the same Analog suppliers that for the most part are not growing. And I think although some of the Analog competitors and suppliers are starting to show some sequential growth again, I don't think any of our major competitors in Analog has posted anywhere close to the 27% growth that our Analog business just did from a year ago.

So to the extent – and that is not a statement that says we are satisfied with our all aspects of delivery and customer service levels. You've heard us say we're doing a lot of investment to try to fix that. But I'll also note that to a large part, we were, especially when it comes to the Analog space, I'm not aware of too many suppliers that added capacity, both fab capacity as well as assembly test capacity all the way through the downturn the way TI did.

So I think what you're seeing in terms of lead times, from TI simply reflects the demand that customers have for our products and to the extent that there's anything left on the table, it really comes about because our customers may not be able to fully get everything they want in the near term that they would maybe desire from TI.

But again, I think if you look at the investments we're making, and generally the relationships we have with our customer base, it's pretty clear to us that they like where we're headed. They like where we're headed long term with the capacity investments we're making and they believe TI is the Analog firm with the capacity investments we're making and they believe TI is the Analog supplier they want to bet on for the long term.

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

Operator: Next is Tristan Gerra with Robert W. Baird.

<Q – Tristan Gerra>: Hi. Do you see the potential for higher wafer pricing at foundries this first half, and what is your strategy this year for in-sourcing versus outsourcing?

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<A – Kevin March>: Tristan our foundry agreements generally tend to be long term. So we don't see anything in the way of short-term price fluctuations on that front. As far as our foundry usage going forward, we'll really do more of the same that we've done in the past, and that is an increasing portion of our advanced CMOS, or advanced digital capacity will come from foundries. And we'll source pretty much the majority, if not almost all our capacity for Analog internally, with a bit of supplement from external.

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

<Q – Tristan Gerra>: Quick one, which is how would you characterize U.S. OEMs' ordering patterns post Christmas? Do you think we're back to normalized ordering patterns or do you see or get a sense that people are still pretty cautious in the way they're ordering?

<A – Kevin March>: I'd just offer up that our book-to-bill came in at 1.08 again. That's the second quarter in a row it was 1.08. It's been positive almost all year. So what we're seeing I think from OEMs in general, is that, again there's visibility into their orders a little bit further out in time. That backlog is extending and so that could suggest an increasing level of confidence that's given us a better ability to plan for their needs as well.

<A – Ron Slaymaker>: Tristan, one other thing that I would add, there are orders which, basically about 60% of our revenue that's supported by, and then separately we have consignment programs where those customers, they provide us visibility into their needs based on rolling forecasts from their MRP systems. So again, 40% of our revenue on consignment and for that revenue, basically order entry occurs at the same time as the revenue is recognized.

So from an investor standpoint or externally you see that as all kind of turns, what looks like turns business, because the order comes in inside the same quarter that we're shipping. But from a visibility perspective their forecasts provide us a more detailed visibility.

Okay, Tristan, thanks for your questions, and let's move to the next caller.

Operator: Next will be David Wu with GC Research.

<Q – David Wu>: Yes. Can you hear me?

<A – Ron Slaymaker>: We can

<Q – David Wu>: Okay. Can you, in terms of the very unusual first quarter, can you talk about what is – what will have sequential revenue increase in Q1? Are they the same kind of things that we saw in Q4 or are there other drivers for Q1 of 2010?

<A – Ron Slaymaker>: David, I think in Kevin's prepared remarks, he talked about some areas that we expect to be longer term drivers. But what I would say is that inside of Q1, we don't specifically try to break our forecast out, but we have some areas that typically are seasonally down, that we expect to be seasonally down in first quarter. And we have other areas that for example, industrial, I think you've heard from a lot of suppliers that industrial usually tends to be seasonally strong in first quarter. Industrial was an end market that came on later in terms of its recovery. And a lot of that strength is still ahead of us.

So I would say inside of that first quarter outlook, you have a range of some areas seasonally down and other areas that are still kind of ramping driven by recovery and there's going to be a range inside of there.

Do you have a follow-on?

<Q – David Wu>: Yes. Can you talk a little bit about the Wireless business? The baseband business I guess has been perplexingly robust or stable throughout calendar '09 and I was wondering what's your visibility into 2010? And can connectively and application processor increase in a seasonally-tough first quarter?

<A – Ron Slaymaker>: You're right that seasonally, Wireless is an area that is typically down in first quarter. So again, I'm not going to try to forecast specifics about that segment or product lines inside of that segment.

In terms of baseband, you're right. I think if you look at the trends there, you've seen sequential growth now three quarters in a row. And the reality is I think we have some competitors that are late relative to their original plans in bringing up their baseband product line. And until they do we are more than happy to continue to supply our customer with baseband products.

That being said, we have, as we've described before, stopped our investments in the baseband area. But again, we will continue to supply that product as long as the customer needs us to provide it.

That being said, even though the profile maybe has been a little bit surprising in terms of the sequential trends of late, we do expect that, or continue to expect that revenue basically to have ramped down by the end of 2012, such that we really have no remaining revenue in 2013.

So no real change in expectations on the end point although the last few quarters certainly have held up stronger than maybe we would have expected and I'm not going to try to forecast 2010 other than to say or suggest look at various baseband alternative suppliers and make your own assessment as to when you think they're going to be positioned to ramp. And especially I would say ramp on 3G product, as that's where the strong majority of our sales continue to be.

Okay...

<Q – David Wu>: Thank you.

<A – Ron Slaymaker>: Thank you, David. With that, we'll move to the next caller.

Operator: And the next caller will be Edward Snyder with Charter Equity Research.

<Q – Ed Snyder>: Thanks a lot. I mean, everybody's trying to get their arms around the difference between inventory replenishment, to recovering the economy and the market share gains. I know it's kind of difficult for you too given how widely diversified your Analog business is, but since that's the big grower here, maybe we can touch on that quickly. How do you determine whether or not, and we all talked about inventory, whether or not the channel's filling, we understand that. But how much of this is market share gain versus how much would you say is economic recovery? Or is it just post, did you just see as the quarter unveiled that you're posting better sales than you have expected and just go with it for as long as it lasts? I mean, can you give us some kind of feeling where all this strength is coming from?

<A – Kevin March>: Ed, I don't know that we can give a highly accurate answer, but I can give you some anecdotal observations. Back to what Ron indicated earlier. If we look at the majority of our Analog competitors, our Analog business has continually outgrown them sequentially and year-over-year for several quarters in a row now. So it would certainly suggest that one side of the, one answer to your question is that we're gaining some market share. But as to how much of it is, how much additional growth may be attributable to inventory replenishment or economic recovery, boy, that's pretty much an impossible answer for us to be able to give to you.

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<A – Ron Slaymaker>: One thing I would say, I know a lot of times it gets, the term inventory replenishment gets thrown around. But I'll just remind you that early in 2009, as the inventory, the economy had turned down and there was a very serious inventory correction underway, our shipments into, I'll just describe the channel overall, specifically our customers and their supply chain, was well – our shipments into that channel were well below what our customers were producing and what they were shipping out. And so certainly to a large, not necessarily still today, but as I said before for certainly second quarter and third quarter sequential growth, a lot of that was just our shipments normalizing back to their production levels.

So again, that's not inventory replenishment, but there was that normalization process taking place, whereas now we believe it's being driven by their increasing production levels.

Do you have a follow-on, Ed?

<Q – Ed Snyder>: Yeah, I'd like to do the same thing for Wireless side, which is a little bit easier to get your arms around because I know you've got fewer larger customers there. OMAP or the apps processors and the connectivity seem to be doing particularly well. Do you see that as a few big programs? I think everybody knows all the smart phones that you're on now, some of which are launching, some of which have launched and they're still selling well. Are you seeing share gains? Is the strength you're seeing in Wireless due to a lot of other folks signing up and starting to ship product or to a handful of very successful products that are still ramping?

<A – Ron Slaymaker>: Okay. It's share gains in the form of more customers that we're engaged with. And then it also ties to penetration of technology. For example, the various connectivity technologies into a broader range of handsets. So again share gain on both OMAP and connectivity. And then certainly, the number of smart phones and the size of that market, speed at which it's growing is a big factor on both ends. But then connectivity, the penetration rate or pervasion rate for technology such as GPS and Wi-Fi into a much richer set of handsets.

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

Operator: Moving on to John Barton with Cowen.

<Q – John Barton>: Thank you very much. In your prepared comments you talked about the expansion of field sales and field apps. Can you just touch on what that might mean to the SG&A line and kind of how you're approaching that? Is it just as guys become available that are good, you're picking them up or would you expect something more aggressive? You're regulating it based upon revenue expansion, etcetera?

<A – Kevin March>: John, we're focusing on growth in that area. And we have been actually throughout 2009 and we'll continue into 2010 in to markets that we think will give us a disproportionate growth. So right now that's really talking about China, India and certain parts of Eastern Europe. That, of course, will, as you point out, come through the SG&A line. But I don't think you'll see like a pop. What you'll see is a gradual change in that over time.

I would just take a moment to point out though that going into first quarter, embedded in our discussion about what our earnings range is, is that we do expect pay and benefit increases to occur in first quarter which often happens in the first quarter of the year. Did not occur last year of course because restructuring was underway, but we are resuming, giving increases this year. We also expect 2010 to be a more profitable year than 2009. And so other incentive type of compensations like profit sharing and so on would accrue at a higher rate going into next year, starting in the first quarter.

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So you will see some increases probably in the G&A line. And perhaps even in the R&D line as well as we transition into those higher accrual rates. But you'll also just see a steady increase in the Sales and Apps line as we go throughout 2010 and probably into 2011 as well.

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

<Q – John Pitzer>: Yeah. Specifically to the March quarter and the SG&A line, could you further quantify exactly what you might expect to see sequentially from that event?

<A – Kevin March>: I think at the highest level on the OpEx, the total OpEx for R&D and SG&A I wouldn't be surprised to see it increase up to 40 or $50 million kind of range.

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

Operator: Thank you. The next caller will be David Wong with Wells Fargo.

<Q – David Wong>: Thank you very much. Can you give us any feel as to who your biggest customers in application processors are, please?

<A – Ron Slaymaker>: David, I think if you look, we are across a lot of the traditional handset players. So, I'm trying to think what's been publicly announced. But I think clearly it's known that Nokia's a customer. Sony Ericsson has done announcements. Samsung has done announcements. Motorola in a lot of their new products, their Android-based Droid handsets are OMAP based.

Obviously there're a couple of players that are more positioned in the smart phone space, those being Apple and RIM, where we are not engaged with OMAP. Apple using their own proprietary architecture and then RIM using, for the most part, a legacy architecture that they've been engaged with for some time. And then there is one other player, Palm, that is focused primarily on the smart phone space that is OMAP-based as well. So hopefully that gives you a feel for where we are positioned.

What I would say also is OMAP3 has done very well for us. We expect we have something like 40 different program engagements that will be ramping into production over the next 12 to 18 months. That will be good for us in that space.

Do you have a follow on David?

<Q – David Wong>: Yes, one other. You sort of touched on it. Can you give us a feel which of your end markets are showing the strongest amount of recovery at the moment and are there any that appear to be not yet recovered?

<A – Ron Slaymaker>: I don't know that I would say there are any that not yet recovering. They've moved at different paces. I think, if you go back through 2009, late in the first quarter and into second quarter, you heard us talking more about high volume spaces. Products like computing, some of the handset areas, some of the consumer areas, that seemed to recover fastest. And then probably the last market that has been more recent in its recovery would be industrial. And I'm sure inside of those different markets you can find particular products that maybe are still lagging. But for the most part I would say with industrial now picking up, it looks like, all the major markets are now in recovery mode.

Okay, David. Thanks for your questions. We'll move to the next caller.

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Operator: Moving on to Ross Seymore with Deutsche Bank.

<Q – Ross Seymore>: Thanks, guys. Just a question on the margin side of things. The gross margin is a couple points off your long term target while the operating margin is actually pretty close to it. Can you hit the long term gross margin target of 55 if wireless basebands are still 15% of sales?

<A – Kevin March>: Ross, when we talked about that, that's really a function of increasing mix of the higher profitability products such as Analog and Embedded Processing. So inherently that's going to suggest that baseband will become less than 15% that it currently has reduced to over time. And as Ron mentioned earlier, we expect it to go to zero by the end of 2012.

So really just the growth alone of the Analog and Embedded Processing even with baseband in there at 15%, you're seeing margins come up pretty strong. And so I don't think you have to depend upon baseband to be gone in order for the margins to continue to improve. But that certainly would accelerate the arrival of higher margins?

<A – Ron Slaymaker>: And I would just add even with baseband in the mix, we're certainly not in any kind of hurry to push that out to enhance gross margins. Because with very little operating expense, it falls through nicely to operating profit and cash flow as well. So we will welcome that baseband business as long as our customer wants to purchase that product. And as long as we're continuing of course not to be making investment, which is our plan.

Do you have a follow-on, Ross?

<Q – Ross Seymore>: Yeah. Just, kind of, exactly what you were just talking about. You almost hit about a 25% operating margin in that Wireless business. How should we think about what sort of OpEx is necessary to keep the OMAP and connectivity side going as you're clearly doing a great job of milking the baseband side?

<A – Kevin March>: We won't go into specifics into how the P&L shapes up inside those segments other than just talk about the segment as a whole. But the overall economics of that business unit will be such that we should continue to see it delivering margins not too far off from where it's at, these kind of revenue levels. The mix of product will continue to change over time, as connectivity and OMAP become a bigger portion of the revenue inside that.

<A – Ron Slaymaker>: Yeah. It's safe to say, Ross, we're investing ahead in OMAP and connectivity. Both areas have gross margins above, for example, what baseband has. But, we certainly expect growth in OMAP and connectivity to exceed – revenue growth in those areas to exceed any additional operating expense for us in those areas.

Okay. Ross, thank you. And we'll move to the next caller.

Operator: Moving on to Jim Covello with Goldman Sachs.

<Q – Jim Covello>: Good evening, guys. Thanks so much for taking the question. Q2 inventories, do you have a goal for internal Q2 inventories?

<A – Ron Slaymaker>: Q2? We haven't even shared a goal...

<Q – Jim Covello>: I'm sorry. Q1?

<A – Ron Slaymaker>: Okay. Well I like that you think ahead, Jim, but the answer is that we don't have specific goals that we want to publicly share anyway on Q1 or Q2. And, as you've seen even the last few quarters, you know, a lot of what we achieve or what we don't achieve in repositioning of inventory will depend upon what happens with end demand as well as, what actions we might be taking to support quarter out demand expectations as well as what we're doing from a customer service metric positioning. But we don't publicly disclose those expectations.

Do you have a follow-on Jim?

<Q – Jim Covello>: Yeah. Could you let me know what would CapEx have been in the fourth quarter without the money spent toward the Qimonda assets?

<A – Kevin March>: Jim, I think it was the press there that we spent about $172 million on those assets.

<Q – Jim Covello>: Okay. So all that 172 million was recognized in the fourth quarter CapEx?

<A – Kevin March>: Right.

<Q – Jim Covello>: Terrific. Thanks so much.

<A – Ron Slaymaker>: Okay, Jim. Thank you. Next caller please.

Operator: And the next question comes from Stacy Rasgon of Sanford Bernstein.

<Q – Stacy Rasgon>: Hi, guys can you hear me?

<A – Ron Slaymaker>: We sure can, Stacy. Go ahead.

<Q – Stacy Rasgon>: Great. Thanks for taking my question. I just wanted to verify something. In terms of the upside, the little bit that you saw in Q4, it seems from your commentary and from the release that you don't feel like you saw restocking this quarter. It was really all due just to continued normalization. Upside in Q1, you actually expect to see that upside from some re-stocking activity. And I was wondering if you could give me any color on whether or not you expect that re-stocking activity to continue past Q1, and into, maybe into the first half or into the rest of the year?

<A – Ron Slaymaker>: Stacy, I agree with your characterization of Q4, that I think for the most part the supply chain was stretched, and even if there had been a desire to get some inventory position, for the most part the supply chain was not able to do that. Now, whether they are able to take an advantage of does end demand seasonally slow in Q1 and are they able to take advantage of that to be able to get some inventory position? I think a lot of customers and distributors down through their supply chain would like to do that. But again, the question is just going be are they able to do that in Q1? And, you know, I really don't have a forecast or perspective to be able to provide on that.

Do you have a follow-on, Stacy?

<Q – Stacy Rasgon>: Yeah, I do. Around the CapEx budget for 2010, the 900 million, can you give me some feeling for how that is going to split up from assembly and test versus maybe additional 300-millimeter investments to round out the process set versus additional 200-millimeter buys. Can you give me some feeling for how that might split?

<A – Kevin March>: Right now, Stacy, I would suggest that the majority of that will be going towards the assembly and test operations as our volumes continue to increase. We will put more into the 300-millimeter as we bring up incremental parts of that line. And we'll put more in 200-

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millimeter into the other factories as we did during the past quarter. But certainly the 2010 budget, the majority of that will be pointed towards the assembly test sites.

<A – Ron Slaymaker>: Okay. Stacy, thank you for your questions, and let's go to the next caller please.

Operator: Moving on to Srini Pajjuri with CLSA.

<Q – Srini Pajjuri>: Thank you. Just a couple of clarifications on the gross margin side. Kevin, just if I take the midpoint of your revenue guidance and plug in the assumptions, I'm getting gross margin to be about flattish. And based on what you're saying about Q1 and the history, I would expect the mix to improve and the revenue to start growing. So my question is, why wouldn't the gross margins go higher? Are there any outstanding factors here?

<A – Kevin March>: Yes, Srini, I think that – I'm not sure how you're building your assumptions in, but let me just be sure to share a couple points that might help understand how we're looking at the first quarter. We – if you look on the balance sheet you actually saw that we grew the inventory in the fourth quarter. And principally on the finished goods line, which is one of the things that will allow us to be able to continue to improve on our delivery commitments to customers in first quarter and help our revenue outlook in the first quarter. That also goes to say that we probably have enough wafers in flow to begin to deal with demand. And so therefore, we don't expect utilization of our factories, of our front-end wafer fabs to change that much in the first quarter.

I mentioned a few minutes ago that the outlook for the year is for higher profitability than what we had in 2009. And I also mentioned that we're resuming increases in base pay for people. Those two combined will increase not only our OpEx fourth quarter to first quarter, but will also have an increase on the cost of goods line, which will affect GPM a little bit. So those may be two things affecting the analysis you're trying to put together right now.

<Q – Srini Pajjuri>: Okay, great. And then if I look at the Analog business, Kevin, you know, some of the product share gains that you mentioned, looks like a majority of them were coming from the consumer side, like the PCs and LED TVs. My question is, how does that impact the gross margins for that particular segment, the Analog business going forward? I mean, do you see any impact at all, or do you expect to maintain that 65 to 70% gross margin that, that business typically has. Thank you.

<A – Kevin March>: Srini, that higher gross margin that you're talking about is typically on the High-Performance Analog products, and we actually don't see that being impacted by the demands that we're seeing from that part. Some of those other spaces that you were referring to actually was in the Power Products, where we're seeing a lot of success of new products going in there. And while the margins, the gross margins there may not be quite as high as the, as one might expect in High-Performance Analog, the operating margins are very similar.

So while there may be mix over time that causes bits and pieces to move it up, down a little bit as we pass through from quarter to quarter, we think overall the mix will continue to go up because the total Analog portfolio and Embedded Processing portfolio combined exceeds what we get from the rest of the portfolio. And in addition, they're growing faster than the rest of the portfolios, so they're becoming a bigger portion of the overall revenue mix.

<A – Ron Slaymaker>: And pretty much those same comments apply to HVAL, where the gross margins are a little lighter than – when compared to High-Performance Analog, the SG&A and R&D requirements are lower, and operating margin is very similar. So whether it's HVAL, whether it's HPA or whether it's Power, our objective and our expectation over the long term is to get all of them growing at about the same pace. But even if there are variations at the operating margin, it won't make much difference.

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

Operator: Moving on to Craig Berger with FBR Capital Markets.

<Q – Craig Berger>: Hey, guys. Thanks for taking my question. You know, just in talking to some of the investors, I mean the main concern is as lead times come down, you may see order volatility or you may see a little air pocket of demand. Do you think that there's enough inventory out there in the channel for that situation to arise? And can you also just talk about where fab lead times are and back end lead times are? Thank you.

<A – Ron Slaymaker>: Let me take part of it. And then I'll let Kevin add to it. I think, if lead times decline, might there be order volatility? Could be. But I'd also say we're not overly concerned with that. Like I said, there's a lot of means by which we have visibility into what demand is and orders are just part of that.

You know, to the extent – the second part of your question I think is totally pertinent, though, which is, is there enough inventory out there such that true demand from our customers would go volatile. And that's where, given how lean the supply chains are, I don't think it would make any difference. So again, if lead times pulled in today, customers may not feel the need to give us much – as much long-term visibility into their demand. But their take rate in terms of shipments, demand per shipment, likely wouldn't wiggle at all. But we'll see how that develops over time.

The second part of your question? I think, we're both – Kevin and I are both sitting here with – are you still there, Craig?

<Q – Craig Berger>: Yes. Lead times, front end, back end?

<A – Ron Slaymaker>: Okay, lead times. So you're saying manufacturing cycle time?

<Q – Craig Berger>: Meaning, what are your, what are your – generally, oh I'm sorry. The question was utilizations. Front end and back end. Where are they and where do you see them going?

<A – Kevin March>: On utilization, we don't actually call it out. I'd say we're back more to a normal kind of utilization environment. Unlike where we were a year ago of course when our utilization in first quarter dropped into the mid-30% kind of range. We're back into a more normal kind of utilization rate today. I mentioned a few minutes ago that we'd expect our utilization going into first quarter to be very flat to what it was in first quarter. That's on the, that's a reference to our front end or the wafer fabs. On the back end, we have been investing for a couple quarters now in expanding our capacity there especially on certain package types, and clearly our utilization is very, very high on certain of those lines. But that is, the equipment is getting into place now. And we're beginning to see our throughput increase. Again, you can see that if you look at our balance sheet, where our finished goods actually began to increase, actually for the first time since the second quarter of 2008.

<A – Ron Slaymaker>: Okay, Craig, thanks for your questions and let's move to the next caller.

Operator: Next will be Doug Freedman with Broadpoint.

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<Q – Doug Freedman>: Thanks for taking my question and congratulations on a strong quarter. If you could talk a little bit about where we are with the distributor conversions that are going on and how much that might have impacted revenues either this quarter or next?

<A – Kevin March>: Doug, right now we're probably about a quarter, let me just go to the highest level. There's probably about 30% of our revenue goes through the distribution channel. And of that, about a quarter of it is on consignment. We are slowly increasing that each quarter, the portion that's on consignment, with the idea that some time probably late next year, next year being 2011, we'll arrive at somewhere on the order of half of our total distribution inventory be on a consignment basis.

<Q – Doug Freedman>: And were you able to calculate what impact that had to revenue recognition this quarter?

<A – Kevin March>: Not precisely, Doug. I don't have that number with me so I can't, I just don't have the answer for you.

<A – Ron Slaymaker>: Right. Again you can, probably the way to think about it, Doug, is if you go back we started that consignment program with distributors in June of 2008. So, over the last, what, six quarters we've gotten 25% of that revenue converted over to consignment. You probably based on that, can go make some average, call it headwind calculations from that consignment program. But, the fact that we're doing a relatively slow deployment on that would say probably in any one quarter, it's kind of a slow, steady headwind on the timing of revenue. But again, it doesn't impact re-sales at all. It doesn't impact the end-demand, it just has the effect of moving it out a quarter as distributors rely more and more on that consignment program.

Do you have a follow-on, Doug?

<Q – Doug Freedman>: The guys have already commented on your operating margins coming in sort of above target this quarter. Can you give us an idea how many quarters you would run with your operating margins above your target before you think it might be appropriate to adjust some of the targets? If I look at the R&D and SG&A as a percentage of sales, I guess it might be a really good quarter to be at TI next quarter. Because you're going to have to increase spending a lot more than what you just guided to get it up to the 25% number.

<A – Kevin March>: Doug, I think that we still have not achieved the targets that we set for ourselves a couple years ago which is 55% gross and 30 operating. We didn't set those as ceiling we just set those as an objective the company should be able to operate at and ideally on a sustained basis. So we think it's important for us to be focusing on top-line growth right now and demonstrate that we can sustainably deliver those kinds of margins over a period of time.

<A – Ron Slaymaker>: And let's not celebrate yet. We're close to the margin goals but we're not there yet.

Okay, Doug, thank you for your questions. We'll move to the next caller.

Operator: Next will be Glen Yeung with Citi.

<Q – Glen Yeung>: Thank you. Can you guys talk about the pricing environment that you're seeing sort of generally across your products but specifically in some of the commodity products?

<A – Ron Slaymaker>: I'll start with commodity. But let me do the normal caveat of remember, it's only a few percent of our revenue. But, pricing in commodity is doing what you would expect in a

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situation where suppliers pretty much across the board are short relative to what the demand environment is. So pricing is moving up on commodities as you might expect.

Outside of commodities I would say, which again, is almost all of our revenue, pricing is pretty much following normal trends, so nothing really environmentally unusual there. Even in commodities, it's not unusual but it has moved up in this constrained environment.

Do you have a follow on, Glen?

<Q – Glen Yeung>: Yeah. If you look back at the 2003/2004 timeframe, really 2004 was the last time we had a material inventory problem. And I'm wondering if you can compare and contrast what you see today versus what you saw back then?

<A – Kevin March>: Glen, are you talking about coming out of the tech bubble?

<Q – Glen Yeung>: No. No. I'm really thinking about '04 when we had, what I would characterize more as an inventory issue, shorter term obviously. You can look at the tech bubble, too, where it was obviously a much bigger inventory issue but I think in both periods we had some problems.

<A – Ron Slaymaker>: Glen, I have a couple things I would observe and I suspect you've noted it also. I mean typically when you get into, call it the cycle rolling over again, you are coming from periods where inventory has been inflated. Usually as that inventory build is taking place, customers, suppliers, distributors convince themselves it's being done because the demand environment outlook is going be strong. And, then it results in some form of correction of that excess inventory level.

I think what's different between – and we all recognize when that inventory is being built. But again, we convince ourselves, and I'm talking the entire supply chain here, that it's appropriate relative to the demand outlook. I think what's different in this environment is pretty much if you look at TI, you look at our distributors, you look at our customers, you see inventory levels that are historically lean. And that's a big difference between, pretty much every other cycle that peaks out, rolls over, versus where we are today. We have demand today that is being driven, call it more macro level end demand increases.

And you have inventories that to date have remained very lean and well behaved. So, I think that Stacy asked the question earlier about replenishment and, whether that's an expectation. I think typically, at some point as demand continues to build and as suppliers get capacity online, you would expect at some point replenishment of inventory levels. But I would describe that as ahead of us as opposed to anything that we've seen to date.

Okay. Glen, thanks for your questions. And operator, I think we have time for one additional caller, please.

Operator: Certainly. That question comes from Chris Danely with JPMorgan.

<Q – Christopher Danely>: Hi, guys. Thanks for squeezing me in.

<A – Ron Slaymaker>: Didn't know it was you, Chris. No just kidding. Go ahead.

<Q – Christopher Danely>: I'm small enough to be able to easily squeeze into almost anything. On the Analog I know you talked about trying to get the HPA, HVAL and Power to grow equally. Can you just give us the relative growth rates between those three products in 2009?

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<A – Ron Slaymaker>: Chris, let me say first of all that, I think if you look at, when I say – I don't know that I intended to say it's our objective to try to get them to grow equally. Clearly historically, we've had really good growth in HPA and we've had outstanding growth in Power, but HVAL has been a laggard. And frankly it wasn't just a laggard relative to those other two product areas, it was a laggard relative to what our perception of the market was. So our view is there is no reason that all three of those areas shouldn't have growth that is relatively similar across them.

But, to some degree, you're going have variations that develop. I think if you look at, historically – like I said, I would just almost have to leave it at that. HPA and Power clearly have been the primary areas of growth in Analog over the last few years. HVAL lagged. HVAL lagged through even the first part of 2009. I would say mid-year, we bottomed out. Some of the fruits of our efforts over the last few years basically to – starting with, management changes and then organizational changes below that, end markets on which we were focused, all the things we've talked to you about in the past started to come to fruition. And, over the last couple quarters certainly, HVAL has pulled its weight as well.

But that's really what we're intending to say. And I think we're reasonably satisfied that we have good growth opportunities in all three and we're positioned to realize those growth opportunities. But, any quarter-by-quarter even year-by-year, you may have differences and that will be okay.

Do you have a follow-on, Chris?

<Q – Christopher Danely>: Yes. So just on the lead time thing. So lead times have been going up for a couple of quarters now, and I think you guys have said that it's mostly related to back end issues. So my question is, is when you guys first saw the lead times going out, why didn't you just ramp up your back end aggressively and squelch them? I mean, are you trying to sort of keep the lead times a little bit longer. I'm wondering about the machinations of that process.

<A – Kevin March>: Well, Chris, when you think back to when we began to see some of the challenges that were still on the way down. You know, how quickly we forget sort of thing. It wasn't that long ago when the bottom was falling out of demand across the board. And then when demand did start coming back in second quarter, it was all of us scratching our head trying to decide whether or not that was real. Certainly in retrospect, it was real. And once we acknowledged that, we began to step up capital spending. You saw it move up in the third quarter and you saw it move up again in the fourth quarter. And most of that money is going towards back end capacity to try to relieve those constraints.

So again kind of remembering the history that we came through is how we kind of got to where we're at. It certainly was not an intended outcome. The last thing we want to do is displease our customers in the manner in which we have in certain of these product lines. And it's our objective to get this fixed as quickly as possible, but experience also tells us that when we get behind like this, it usually takes us quite a few quarters to get caught back up.

<A – Ron Slaymaker>: And, Chris, just as a reminder, I mean don't forget second and third quarter, growth rates across that six-month period was higher than what we've ever seen before, at least in any of the history that Kevin or I could find. So you do your planning, you do the best you can, and sometimes it's not good enough. But nonetheless, we'd rather be in this situation where we have revenues rapidly growing than the alternative, certainly.

Ron Slaymaker, Vice President, Investor Relations

Okay. Chris. Thank you for your questions. And overall, thank you for joining us. A replay of this call is available on our website. Good evening.

Operator: And that does conclude today's conference. Thank you for your participation today.

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