

## — MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Texas Instruments Fourth Quarter and Year-End 2010 Earnings Conference Call. As a reminder, today's conference is being recorded. At this time, I'd 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 Fourth Quarter and Year 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](http://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 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 describe our views on the demand environment, where we are in the correction, and our near-term outlook. We'll also talk about the financial impact of the three new factories that we have now brought online and the opportunity for growth that these factories provide. Finally, we'll provide a retrospective view of the year and our expectations for the years ahead.

I'll start with the demand environment. As a reminder, from the second quarter of 2009 through the third quarter of 2010, the SC industry had six quarters of strong growth. Our own revenue in the third quarter of 2010 was up 79% from the first quarter 2009 trough. In the summer of 2010, the industry began to slow, and then declined in the fourth quarter. During our October and December calls, we said that we believed the slowdown would be both short and shallow. We were in an environment where lead times were shortening and inventories were being quickly reduced. At this point, we believe the correction is mostly complete. TI's lead times have now completed an orderly reduction and are back to normal, as we had projected in our last call. During the fourth quarter, we were able to replenish our inventory levels, which will help us keep lead times normal during 2011.

Regarding customer and channel inventory, while there are some customer-specific examples where inventories are higher than they desire, we see some of the important end markets, like PCs and LCD TVs, having largely completed their inventory correction. In the PC market, TI revenue from battery management products bottomed early in the fourth quarter and grew through the remainder of the quarter. In the LCD TV market, our customers tell us that their excess inventory was significantly cleared in the fourth quarter and to expect higher demand in the current quarter. As a result, even though new orders for the quarter were down again from the third quarter, after very weak month of October, net orders were appreciably higher during the months of November and December.

Let me translate all of this to our outlook. Historically, the first quarter for TI would be down about 5% compared with the fourth quarter. The middle of our current first quarter guidance range is a little better than seasonal. In addition, our backlog coverage as we entered the current first quarter was higher than recent years of history for our first quarter. To summarize the demand environment, we believe the slowdown that started in the summer of 2010 is mostly complete.

Turning to our fourth quarter results, revenue in the fourth quarter was slightly better than the middle of our range of expectations. Revenue declined 6% sequentially and was up 17% from a year ago.

Analog revenue declined 4% sequentially and grew 20% from a year ago. The sequential decline was primarily due to power management products, given their higher exposure to the PC market. High-volume analog and logic products and high-performance analog products declined to a lesser extent. The 20% increase in Analog revenue from a year ago was mostly due to strength in high-performance analog products, although HVAL and power management both had double-digit growth.

In Embedded Processing, revenue declined 7% sequentially and grew 31% from a year ago. The sequential decline was due to lower catalog product revenue, with revenue from products sold into communications infrastructure and automotive applications about even. The 31% increase from a year ago was primarily due to catalog products. Communications infrastructure revenue also grew and, in fact, its growth rate exceeded 30%. Growth from products sold into automotive applications was lower, although still double digit.

Total Wireless revenue was about even sequentially and from a year ago. Baseband revenue was \$435 million in the quarter, down slightly from \$438 million in the prior quarter and down from \$465 million a year ago. Sequential growth in OMAP applications processor revenue was offset by lower connectivity revenue and a slightly lower baseband revenue. From a year ago, higher connectivity and applications processor revenue was offset by the lower baseband revenue.

In our Other segment, revenue declined 14% sequentially, and grew 23% from a year ago. Most of the sequential decline was the result of the seasonal decline in calculators. DLP revenues declined by about the same amount as revenue from our transitional supply agreements increased. As a reminder, when we recently acquired our Aizu, Japan, and Chengdu, China, fabs we agreed to continue to supply Spansion and SMIC with product from those factories on a transitional basis while we ramp our own production in those facilities. The financial impact of these agreements should largely offset any carrying costs associated with those new factories and will be reflected as part of our Other segment. The 23% growth in the Other segment from a year ago was due to a combination of these transitional supply agreements, higher custom ASIC revenue, and higher DLP product revenue. I should also note that the gain on our sale of a product line is included in the results of the Other segment.

Distribution resales declined 4% compared with the prior quarter, not much different than our overall semiconductor revenue trend. We were able to help distributors replenish a few days of inventory in the quarter, helping to position them for expected growth.

Shifting briefly to our full-year 2010 results. TI revenue grew 34% in total. Each of our core businesses contributed strongly to this growth, with each area growing in excess of 40%. Analog revenue grew 42%, with strong growth in HVAL, power management, and HPA. Embedded Processing grew 41%, led by especially strong growth in catalog products.

In both Analog and Embedded Processing, we continue to benefit from the breadth and depth of our product portfolio, combined with the significant scale advantage that our field sales and applications force provides us. This means we have the ability to call on more customers, and engage with them more deeply compared with our competitors. We believe the share gains we earned in 2010 were largely a result of this.

In Wireless, the combination of applications processors and connectivity products grew slightly more than 40%. Wireless baseband revenue was \$1.7 billion in 2010, essentially unchanged from

2009. As a percent of total TI revenue, baseband declined from 17% of TI in 2009 to 12% of revenue in 2010.

We continue to be encouraged by our strong design position and momentum in OMAP applications processors. With our dual-core OMAP 4 applications processor generation, we have a combination of low power and high performance that we believe is unmatched in the industry. We are now in volume production of our first OMAP 4 device. We are deeply engaged and collaborating with multiple customers on tablet programs that reach across TI product lines, including OMAP 4 applications processors; single chip wireless connectivity solutions that integrate 4 radio technologies: Wi-Fi, GPS, Bluetooth and FM; and analog power management technologies that optimize overall power distribution and consumption within the tablet. There are a host of other examples of OMAP's broadening design-in success, including e-readers, personal navigation devices, portable data terminals, and many other devices that can leverage OMAP's combination of high performance and low power.

Now Kevin will review profitability and our outlook.

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**Kevin March, Senior Vice President and Chief Financial Officer**

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Thanks, Ron, and good afternoon, everyone.

Our financial performance this quarter again illustrates the benefit of our transformation to a company focused on analog and embedded processing, and our associated manufacturing strategy. We've discussed for some time that the additional manufacturing assets that we've acquired over the past 15 months would have minimal negative impact on TI's financials because of the low prices that we paid for this equipment.

In the fourth quarter, we ramped production of three new factories: RFAB, our 300-millimeter analog fab located in Richardson, Texas; the Aizu, Japan, fab that we acquired from Spansion Japan; and the Chengdu, China, fab that was previously operated by SMIC. As a result, this was the first all-in quarter from a financial perspective, and we are now depreciating all these acquired assets. While we're now carrying the full weight of this depreciation, loadings of TI products at these factories are still low given the early stages of our production ramp. These factories provide us with tremendous headroom for growth, more than \$4.5 billion in total additional revenue. As we load them with TI analog products, the profit potential is significant.

As you might expect, TI factory utilization was down in the fourth quarter, impacting gross margin. This was only partly the result of new capacity additions. It was also due to our lowering of production loadings in our other factories in response to the weaker demand environment. In other words, we had three variables influencing gross margin in the quarter. On the negative side, we had higher costs from the new factories, and we had lower utilization in our existing factories as the market slowed. On the positive side, we were able to make nice strides replenishing inventory for those products whose lead times had been extended for much of the past year, largely returning those products to normal lead times. Given these cross-currents, we're pleased at how our gross margin performed in the quarter. In total, gross profit fell 8% sequentially, and our gross margin declined 150 basis points to 53% of revenue.

Turning to our other financials, the combination of R&D and SG&A decreased \$26 million in the third quarter. We had a gain on the sale of a product line of \$144 million in the quarter. Operating profit for the quarter was \$1.23 billion or 34.9% of revenue. Without the gain on sale, operating margin was 30.8% of revenue. Net income in the fourth quarter was \$942 million or \$0.78 per share. In the earnings-per-share calculation, please note that accounting rules require that we allocate a portion of net income to any unvested restricted stock units on which we pay dividend

equivalents. In the fourth quarter, the amount of net income excluded from the EPS calculation was \$14 million. If you don't make this adjustment, you'll likely calculate EPS to be a penny higher than we have reported. As you'll note in the release, earnings per share included \$0.14 from the combination of the gain on the sale of a product line and a tax benefit that was primarily associated with the reinstatement of the federal R&D tax credit that was retroactive back to the beginning of 2010.

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 \$1.23 billion. This was down \$88 million from the last quarter and up \$230 million from a year ago. Capital expenditures declined to \$301 million in the quarter and included additions to our assembly and test capacity, as well as our analog wafer fab capacity. We used \$600 million in the fourth quarter to repurchase 19.5 million shares of TI common stock and paid dividends of \$153 million. We increased our inventory by \$96 million in the quarter and inventory days to 83. With this inventory position, we have returned lead times to normal levels. Orders in the quarter declined to \$3.13 billion. TI's book-to-bill ratio was 0.89 in the quarter. Orders bottomed in the month of October, with November and December orders appreciably above that level.

Turning to our outlook, we expect TI revenue in the range of \$3.27 billion to \$3.55 billion in the first quarter, or down 7% to up 1% sequentially. We expect earnings per share to be in the range of \$0.54 to \$0.62. Our estimate for 2011 R&D is \$1.7 billion. 2011 capital expenditures and depreciation are expected to be about \$900 million each. Our estimate for our 2011 effective tax rate is 30%.

Please note that our estimates for 2011 depreciation is approximately the same as we had in 2010. As I described in October, the additional depreciation associated with our acquired manufacturing assets will be mostly offset by the roll-off of depreciation from capital expenditures five years ago. Needless to say, even though our fixed costs in the form of depreciation will be essentially unchanged, our ability to grow and to respond to customer demand will be much higher.

Before I wrap up, let me make some brief comments about 2010 overall. It was a good year for TI and our shareholders, with strong 34% revenue growth, gross margins that expanded 570 basis points to 53.6% of revenue, and operating margins that moved up 1,320 basis points to 32.3% of revenue. We didn't just ride a rising tide of a growing semiconductor market. We believe we also gained significant market share overall, as well as in each of our core businesses.

We've described to you for some time the potential that we believe exists in a transformed TI, and I believe 2010 provided a glimpse into that potential. Our challenge going forward is to demonstrate that 2010 wasn't a one-off year. We must prove that we can continue to grow our Analog and Embedded Processing revenue significantly faster than those markets. We need to expand our Wireless connectivity and applications processor positions in the smartphone market, as well as in tablets. And we need to continue to manage our baseband business for maximum cash flow while it continues to become a smaller part of our company. If we do these things right, our shareholders should also continue to benefit.

For example, in 2010 alone, our return on invested capital was 30.7%, and we generated \$3.82 billion of cash from operations. This allowed us to repurchase \$2.5 billion of our stock and pay dividends of almost \$600 million. Combined, these cash returns to our shareholders amounted to about 10% of our initial market capitalization when we entered the year. Key to all this is that our Analog and Embedded Processing products are highly differentiated and not dependent upon the latest manufacturing technologies. Therefore, our capital requirements are relatively low. High differentiation and low capital requirements allow us to be more profitable, and we don't have to channel all of our profits back into the manufacturing operations. As a result, we expect to continue to be able to provide significant returns to our shareholders in the years ahead.

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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] We'll go first to Tore Svanberg with Stifel Nicolaus.

**<Q – Tore Svanberg>**: You talked a little bit about the bookings trends in November and December. Could you just talk a little bit about what you've seen so far this quarter, please? Thank you.

**<A – Ron Slaymaker>**: Well, I won't break it down week by week, Tore, but I will say that everything that we've seen both on the order front, as well as shipments or revenue, has been strong thus far in the quarter. So we've seen nothing thus far that would discourage us at all from the outlook that we've provided.

Do you have a follow-on?

**<A – Kevin March>**: Well, let me just add to that if I can.

**<A – Ron Slaymaker>**: Sure.

**<A – Kevin March>**: Our backlog coverage coming into the quarter was actually higher than we've seen for first quarter over the last few years, which gives further confidence to the outlook that we're providing.

**<Q – Tore Svanberg>**: That's very good. And I realize you were able to build a little bit of inventory in Q4. What's your inventory plan for the March quarter?

**<A – Kevin March>**: Tore, we won't get specifically into inventory plans per se, but we do expect to continue to build inventory. And on those parts that have high demand, we want to keep short lead times on. And clearly the shape of the Q2 demand will dictate just how much inventory we try to position as we go through the quarter.

**<A – Ron Slaymaker>**: But keep in mind, Tore, the other factor, even though we have a plan to build inventory, depending upon where we land in that revenue range, that could impact our inventory expectations or actuals as well.

Okay, Tore. Thank you for your questions. We'll move to the next caller.

Operator: We'll go next to Uche Orji with UBS.

**<Q – Uche Orji>**: Thank you very much. Let me just start off by asking in terms of where you're seeing bookings improvements. Okay, so you called out notebooks, you also talked about LCD TV. I just want to understand whether you're also seeing that from distributors as well. And so if you are able to kind of walk through by end market, however you can, just get a sense of where bookings improvement is coming from?

**<A – Ron Slaymaker>**: Uche, I guess I would say it is reasonably broad-based. Now, again, the overall trend was down, but we specifically called out what we were seeing in PCs and some of the HD TV space because those were areas that in prior calls we had noted that there was inventory correction under way, and those areas were particularly weak.

To hit on distribution, I think I said in the prepared remarks that our distribution resales were down about 4% sequentially. I think I noted that we were able to help distributors build a few days of inventory, but I would say their inventory levels are at very comfortable levels. From an absolute standpoint, they're just over six weeks of inventory currently. And if you look at historical levels,

we've seen them generally in the eight to nine weeks. Now, you probably need to adjust that for the 30% of our distribution revenue that we now support with consignments. But even with that adjustment, certainly inventories are at very – I'd call, normal or typical levels compared to history and at a comfortable level based upon what the distributors are expecting in terms of their future resale demand.

Do you have a follow-on, Uche?

**<Q – Uche Orji>**: Yes, I do. Can I ask you about OMAP 4? You've talked about the prospect of your dual-core OMAP 4. But one wouldn't help but notice that your OMAP 3 was designed out from one of your large customers. So I just want to kind of get a sense of how we should be confident about the prospects of OMAP 4, especially as you see more and more competition there, with companies like NVIDIA getting more active in the tablet space. So any comments you can make there, and also just use that to clarify your stance on the tablet market with OMAP 4. Thank you.

**<A – Ron Slaymaker>**: Okay, I'm sorry. Did you mention a specific competitor in the tablet space?

**<Q – Uche Orji>**: That's right. Well, we've seen one of them, NVIDIA's Tegra to get very aggressive. I mean, we've heard comments about how much share they've gained within the tablet market. So – and that's been the , probably the one dual-core product from ARM – that is, one of the ARM partners that is shipping now as far as tablets that we know. So I just want to see how – what makes you comfortable about OMAP 4's prospects in the light of all the competition we're seeing in the apps processor?

**<A – Ron Slaymaker>**: Okay, thank you for the clarification. What makes us comfortable are the design programs we have under way, and design programs that are specifically slated to go into production within a – let me just say these are not long-term development programs. These are programs that are going to result in relatively near-term revenue. The competitor you referred to, NVIDIA, to their credit, was the first out with a dual-core applications processor. I believe they had a – oh, a couple months, maybe a quarter, lead on our OMAP 4 product. OMAP 4 began sampling fourth quarter a year ago.

So we've had that product in customers' hands for over a year at this point. We're well along in development programs. And again, them being first, for customers that are trying to get out with tablet programs right away, especially some that are based upon the Android operating system, they were the first player out, so there's a natural alignment there. But I guess what I would say is we fully are comfortable that we will be there as these programs hit stride and ramp into real volume.

I think I mentioned in my prepared remarks, we are in volume production now with OMAP 4, and we're not just in production to put those products in inventory. In fact, we're shipping to a customer that plans to ramp their tablet production based on OMAP 4. So again, I think we've acknowledged for a long time the tablet market, as is the smartphone market, will be a competitive market. But I think you're going to find that translates to great opportunity for TI across a variety of product areas.

Okay, Uche. Thank you for your questions. And let's move to the next caller.

Operator: We'll go next to Jim Covello with Goldman Sachs.

**<Q – Jim Covello>**: Hey, thanks so much for taking the questions. First question. This quarter's a little bit unusual from the standpoint of your competitors are saying different things about their own lead times. Some say they're all the way back down to normal, consistent with what you're saying. Others are suggesting their own lead times are still elevated. Do you have any sense that you could

give us for sort of industry average with a combination of some competitors still being extended and other being all the way back down?

**<A – Ron Slaymaker>**: Don't, Jim. And I agree completely with what you're describing, that I actually think different competitors are at different points. I know even last week I was listening to a call where a competitor, very credible competitor, was talking about their lead times have progressed but they still remain extended, will take more time. I think the best thing I can say about our own situation is I believe we got on top of the situation earlier in terms of capacity investments, and we've brought that capacity online. And that's what's translated to lead time reductions for us.

I think you can always have demand fix your lead times if it turns down enough. I think if anything for us, this respite in demand we've had over the last couple of quarters really just allowed us to get the capacity investments that we had been making, get it online, get some inventory in place, and get our lead times back to normal.

I think the other thing that's going to be important is, depending upon what happens with growth in our industry in 2011, I think we feel completely comfortable with the headroom that we have on our capacity now that will allow us to grow quite aggressively if that's what the market wants to do, and at the same time, maintain our lead times where we and our customers want them to be. I think you'll find if we get into some heavy growth in 2011, a lot of our competitors that have not made capacity investments – and maybe lead times have adjusted maybe more recently because of slower demand environment over the last quarter – I suspect you'll find them in a different situation with their lead time trends in that kind of environment.

Do you have a follow-on, Jim?

**<Q – Jim Covello>**: Yeah. If I could ask specifically about how you guys feel that you're positioned within power management in the tablet space? I know another one of your competitors had referenced the fact that they'd lost the socket, the power management socket, in a tablet, and I know everybody's trying to figure out who potentially gained that socket. And I wondered how well positioned you guys think you are in that space?

**<A – Ron Slaymaker>**: There's a broad question, and then there's an implied question. Let me answer the broad question, which is, I think we are very well positioned in the tablet with our power management. And you know well, we're well positioned overall in the marketplace with power management, but certainly tablets are a targeted area for us across a number of product lines, just because that's a new emerging space with a lot of opportunity. In fact, maybe I can even diverge for a second and talk about that opportunity overall, but let me just – I'll stay away from the implied question, which was, were we the player that picked up their lost socket? But I will say we're well positioned, and we think there's a lot of opportunity.

Let me maybe just kind of walk through a little bit of our view of the tablet opportunity for TI. And I know there's a lot of dialogue amongst analysts and investors on how big is that opportunity and how does it compare to a PC? For us, we believe there's over \$30 of content opportunity in a tablet. And that goes across analog, OMAP, and wireless connectivity. And kind of the breakout of that is the analog content alone is over \$10. The OMAP content or the apps processor opportunity is in the \$15 range. And then there's probably an additional \$3 to \$5 of content opportunity for connectivity. By no means do we have all of that in each system. In some cases, we're playing on the analog and maybe not on OMAP. But certainly that's the opportunity.

If I compare that opportunity to a PC for TI, I'd say the biggest difference is that in a PC, the processor, as well as most of the connectivity value, really is dominated by a single player. And that's not opportunity for TI. Of course, unlike a tablet, a PC includes a hard disk drive where we would have probably \$1 to \$2 of content per system on average. But the net difference between



that PC opportunity and a tablet really represents a very significant opportunity for TI. The breadth of our portfolio across analog, OMAP, and connectivity, I'll just say gives us a tremendous opportunity to carve out what could be a very, very significant piece of this important emerging market. And we plan to make the most of it.

All right. Jim. Thanks for your questions, and we'll move to the next caller.

Operator: We'll go next to Shawn Webster with Macquarie.

**<Q – Shawn Webster>**: Great. Yeah, thank you. On the gross margins, can you give us a flavor of the moving parts as we go into Q1 and Q2 as it relates to your business? And more particularly, your utilization rates – do you expect them to decline again in Q1? And I have a follow-up.

**<A – Kevin March>**: Shawn, in the first quarter I already mentioned that we felt the full effect of bringing three new factories online. And so that clearly had an impact on us. The utilization in the fourth quarter was actually down quite a few points. And that wasn't all just attributable to the new factories. We consciously slowed down production in our remaining factories with the exception of those products where we had extended lead times. We continued to build inventory on those products alone in order to get lead times back to normal. So really bringing on the new factories and the declining overall utilization weighed on our margins in the fourth quarter.

Going into first quarter, we expect utilization may be up another point or two. Not significantly, but up a little bit. And really will be a function of both how demand shapes up in the first quarter and, more importantly, how our outlook begins to shape up for second quarter and beyond so we can have inventory ready on time to maintain the achievement we've had on bringing lead times in.

**<A – Ron Slaymaker>**: And then just to ask and clarify, Kevin, so the new factories that were being already accounted for in fourth quarter, for the most part, all the assets that we had previously acquired from Qimonda, Spansion, and the China fab, that was all in? There's not another chunk to come along in first quarter, correct?

**<A – Kevin March>**: There's not another chunk to come along. It is all in. In fact, one of the best ways that you can see that is look on our cash flow statement and look at the depreciation line. You'll see it stepped up from third quarter to fourth quarter. And if you just multiply that times four, it's consistent with our \$900 million depreciation outlook that we have for 2011.

**<A – Ron Slaymaker>**: So fourth quarter was already at the 2011 depreciation run rate?

**<A – Kevin March>**: Correct.

**<A – Ron Slaymaker>**: Okay. Thank you.

Shawn, do you have follow-on questions?

**<Q – Shawn Webster>**: Yeah, thanks. So on lead times, are there any areas where your product lead times are still the tightest or are actually going out in Q1? And you mentioned your end markets that were good. Are there any specific end markets that are still soft? Or you expect the weakest sequential growth in Q1? Thank you.

**<A – Kevin March>**: On lead times, the overwhelming majority of the products are back to a normal lead time. There are still some exceptions, but there always is in a normal industry cycle anyway. There are some parts where we prefer to have shorter lead times. Some customers would prefer that also, but that's now the minority of parts as opposed to the majority. But most of the rest are just fine. We expect now that we've gotten lead times largely caught up, we'll continue to use

the relatively seasonal down period in the first quarter to make sure that we've got much more attractive lead times in event that 2011 becomes a stronger year, as Ron was talking about earlier, so we can maintain what we've gotten there.

<A – Ron Slaymaker>: Okay. Shawn, thank you. And we'll move on to the next caller, please.

Operator: We'll go next to Chris Danely with J.P. Morgan.

<Q – Christopher Danely>: Thanks, guys. So you mentioned that the inventory correction looks to be over in certain parts, but maybe not over in other parts. Can you just talk about the various end markets and what stages you see them being at vis-à-vis any sort of inventory issue? And I guess maybe throw in your expectations for the end markets this quarter and the rest of the year.

<A – Ron Slaymaker>: Chris, let me take a stab at it, and then Kevin may have a few comments to make. And we're not going to be able to walk through market by market.

But I think what we have tried to do is identify in the few areas that we specifically had previously noted, the inventory correction was the most significant, we've tried to provide some guidance or perspective that we think that inventory correction is largely complete. If you go more broadly, there are some customers that probably are totally clean. There are other customers that would not be in a similar situation or still have more to go in terms of cleaning up inventory. And that'll vary customer by customer, maybe somewhat market by market, but probably more customer by customer. I don't know that we're really going to do us a lot of benefit to walk through each of those other than what you may gain from listening and talking to those customers directly as they report their own results.

Kevin, do you have anything to add?

<A – Kevin March>: No, I think that's right. Just to re-emphasize what Ron opened with, though, in the PC space, we saw – at least for our battery management products – bottomed in the beginning of the fourth quarter and grew steadily for the balance of the quarter. The TV space seemed to bottom out in the quarter and indications from our customers are that their inventory is largely cleared, and we can expect a resumption of orders in first quarter.

We talked about the communications infrastructure continuing to be solid in the quarter, automotive being reasonably solid. Smartphones were actually quite strong, and with the adoption rates at the consumer level around the world, one would expect that that would probably be – continue to be quite strong going into 2011. And then the industrial space, we had talked about, 90 days ago, that industrial had been enjoying quite a few quarters of very strong growth, led by inventory replenishment, as well as just end-demand growth, and that we expected that that growth rate would probably slow down in the fourth quarter. And in fact it did. It slowed down to just an end-demand kind of growth. And we expect that to be the norm going forward.

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

<Q – Christopher Danely>: Yes. So in 2010, your Analog, Embedded, and Other businesses all grew roughly the same, within a few points of each other. Can you give us your sense of, relative to your overall TI revenue growth, where you would expect those three product regions to grow?

<A – Kevin March>: Chris, I'd just remind you that our objective that we talked about is growing those core areas at faster than their respective markets. And in fact they did that this past year. They've done it now for a couple years, if you take a look at them. The total company grew at 34%. And the core areas grew at 40-plus percent. A little over 40% for the non-baseband Wireless. About

42% for Embedded Processing and 43% for Analog. So clearly very strong growth rates and a lot of momentum.

Given the scale of the sales force and the scale of portfolio, plus more recently the scale of our manufacturing capabilities, our ability to outgrow our competitors certainly seems to be more highly probable today than you might have thought a couple years ago. Especially in light of the observation that Ron made earlier, and that is we did take action in 2008, late '09, and especially '10 to increase our manufacturing capacity, which allowed us to begin bringing in our lead times, in many cases before quite a few of our competitors could. Many of our competitors did not necessarily take similar action, and should we have a resumption of growth as we go into second quarter and beyond, it could be difficult for some of them to respond to the customer demands, which increases the probability, again, that we will outgrow our marketplace in 2011.

**<A – Ron Slaymaker>**: And Chris, just – as I know you're well aware, but just as a reminder for the broader audience – there is baseband revenue that will decline over the next couple of years. And that's 12% of our revenue, both fourth quarter, as well as for the year. I found it interesting that even though it didn't contribute to company growth at an absolute level, it held – those dollars, baseband dollars, held relatively stable from '09 to 2010. Yet as a percentage of our revenue it continues to decline. It continues to – oh, I would say it as be less important to us and less impactful to us. So that will continue to wind down and certainly not provide the growth contribution that the core areas will.

And just to give you a set of – a refresh on the numbers: The baseband revenue is over 90% 3G at this point. If you compare that to a year ago, it was 66% 3G. So what you've seen is, both as the non-3G market has not shown a lot of growth, and to some degree as our customers brought on alternative suppliers in the non-3G technologies, that is now a minimal part of our revenue base. Sometime this year, they'll have a supplier for 3G on baseband. And you can expect at that time then an incursion into – or a degradation in that 3G revenue for TI. But just stay in tune with their alternative suppliers and what that customer says as to the timing of when that will be. It's not right now, is what I would say.

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

Operator: We'll go next to Glen Yeung with Citi.

**<Q – Glen Yeung>**: Thanks. Ron or Ken, maybe just a clarification from an earlier question, but in a circumstance where we're kind of an average growth year – call it a 5% to 10%, for the industry – do you feel that the capacity you've added is going be a competitive advantage? Or another way of asking that same question is, do you think that the industry, absent your capacity, is going be relatively tight, and really by adding capacity the way you have, you can therefore take market share? And that's sort of in an average growth curve.

**<A – Kevin March>**: Sure. I guess, Glen, if we just kind of take a look again at the capacity that is in the industry, you're well aware that with the onset of the downturn after the third quarter of '08, something on the order of 17% of available capacity was taken offline, and pretty much permanently offline. Well, since then there's been some capacity added. But the last reports I saw suggested that total industry capacity – and I'm not including memory in that statement – is somewhere around 90% of where it was third quarter of '08. I would just say that we're still under-capacitized given the demand, if you will, because the total market is now back above where it was in third quarter '08.

So even if you just have an average kind of growth rate like you're describing, it would certainly seem that the market is going to be very stressed on capacity – or the industry's going to be very stressed on capacity going into 2011. And competitors who have not thought ahead to put capacity

in place may find that rather difficult to deal with. What we find particularly attractive, again, is that the capacity that we have brought online has been at price points, cost points, that we simply had not seen in the past. So if it turns out to be a slow-growth year, it's not going to have much impact to us financially on a negative standpoint. If it turns out to be an average or a strong-growth year, we should be able to convert that into very profitable revenue at a rate beyond what our competitors can manage.

**<A – Ron Slaymaker>**: And, Glen, I'll just note rhetorically, when was the last time our industry has grown at an average growth rate?

**<Q – Glen Yeung>**: Yeah.

**<A – Ron Slaymaker>**: Usually it's very aggressive or we're in decline. So you know that as well as any of us.

Do you have a follow-on, Glen?

**<Q – Glen Yeung>**: Yeah, I do. You talk about OMAP 4 which is a dual-core solution today. Can you talk about your plans, if you have any, for a quad-core solution? And as part of that, can you address whether or not you think that's even a relevant architecture to have in today's market?

**<A – Ron Slaymaker>**: I don't know. I think if you look at the one – call it the next generation core, I don't think we specifically announced that we're using it for OMAP, but then again maybe we did – is we've licensed – in fact, I think we were the initial licensee – from ARM for their Eagle core. So I don't know that necessarily we go a, keep layering on additional parallel cores as maybe move to higher-performance directions such as Eagle. But I guess we always have that flexibility.

All right, Glen. Thanks for your questions, and we'll move to next caller.

Operator: We'll go next to Steve Smigie with Raymond James.

**<Q – J. Steven Smigie>**: Great. Thank you. I'm not sure if you discussed this, but could you talk about if your mix of Analog between high volume, power, and high performance has remained roughly the same, percentage-wise, as you've sort of discussed in the past?

**<A – Ron Slaymaker>**: Steve, it actually has. When we looked at how 2010 landed overall versus 2009 – you might recall in 2009 we described that breakout 40% HVAL and then 30% each high-performance analog and power. And the good news is – and, frankly, what we had tried to set as expectations was we thought we were at a point where we would have HVAL contributing at about the same pace as those others, so that mix – and in fact that happened – and the mix did not change 2010 compared to 2009. So again, further reinforcement that a lot of the work that we had done to have HVAL become a major contributor to our growth in fact has fallen through to reality.

Do you have a follow-on, Steve?

**<Q – J. Steven Smigie>**: Sure. With regard to HVAL, as you mentioned you put a lot of work into that. I know you have a number of wins. You've taken some technology, transferred it to other areas. Does that suggest that as we go through 2011, HVAL will now perhaps outgrow the other categories?

**<A – Ron Slaymaker>**: I don't know that we would expect it to outgrow the other categories. I think our expectation – and this is not a 2011 statement, it's a longer-term statement – our expectation is that the opportunity and our growth should be pretty well balanced across power, HPA, and HVAL. So that's probably as specific as I'd like to be at this point.

Okay, Steve. Thanks for your questions. And we'll move to the next caller.

Operator: We'll go next to Ross Seymore with Deutsche Bank.

**<Q – Ross Seymore>**: Hi, guys. Kind of a question that followed on from Chris's question earlier. Rather than by end market, if you talked about your better-than-seasonal guide by the four product segments you have, are there any big outliers in what's being better than seasonal, worse than seasonal, or right at seasonal?

**<A – Kevin March>**: Ross, I don't think there's anything really specifically to point at. Part of it is that we had a slightly below-seasonal fourth quarter. And so from that standpoint, just to be – the math works the other way when you go into first quarter. But again, beyond that, what we had dragging on us was the PC and consumer space, and with the TV space in fourth quarter, and as we indicated, we now are seeing PC begin to pick back up. And the indications from our TV customers is that – the TV people that we supply – is that we should expect to see a resumption of orders in the first quarter. Beyond that, there's not any one place that I would add additional color.

**<A – Ron Slaymaker>**: And, Ross, as you understand, probably, we try not to take our forecast or outlook and break it down by individual segments or product lines. So we probably will – probably serve us well to stay with that approach.

Do you have follow-on, Ross?

**<Q – Ross Seymore>**: Yeah. One clarification and a follow-up, if I might. The TV and PC together, what that represents as a percentage of sales? And then the real follow-up is, on OpEx, it dropped nicely in the fourth quarter. I know you give full-year guidance to R&D, but what are the puts and takes for OpEx in the first quarter specifically? And then I'll be done. Thanks.

**<A – Ron Slaymaker>**: Okay. Kevin, you want to go ahead and talk about OpEx puts and takes?

**<A – Kevin March>**: Yeah. Ross, the OpEx was down in fourth quarter. And that's fairly typical where we see people taking more vacation time and so on. That's why you'll tend to see OpEx decline, which it did nicely. We would expect in first quarter OpEx to increase. And a good parallel to that is go back and look at last year. Last year's first quarter over fourth quarter, our OpEx was up around \$30 million quarter over quarter. And that was a direct effect of the increase in pay and benefits, which are typically put into place in the first quarter, as well as just far fewer vacation days expected to take here in the quarter.

So again, we'd expect to see a similar up on a quarter-over-quarter basis to what we saw a year ago. In addition to that, you might note that I did give our R&D guidance as being up a little bit over what we spent this past year. And that will start immediately in the first quarter. So I would expect to be up, OpEx in first quarter, at a faster growth rate than what we saw last quarter – excuse me, a year-ago quarter, again, on the function of pay and benefit increases, fewer vacation days, and stepped-up spending on R&D.

**<A – Ron Slaymaker>**: Okay. Ross, and for your question, it's the mix of revenue that is TV and PCs. You're going to get a bonus answer, and I'm going to break out our revenue overall by market. And this is for 2010 as a whole. Communications was 42% of revenue. And that's down a few points from 2009. And I'll also note the biggest piece inside of communications is communications infrastructure. Computer was 22% of 2010 revenue, down a point from '09.

And let me break that 22% out, because it goes across several different areas. PCs, actually was about 9%. And that's what we sell directly into PC manufacturers. Beyond that, we also sell into



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storage manufacturers, both in terms of hard disk drives, as well as optical. That's about 6% of revenue. Servers is 1%. Monitors are 4%. And really think of that as DLP front projector revenue. And then printers are 2%.

So then continuing at the TI level. Industrial is 14% of revenue, or was 14% last year. And that's up a few points from 2009. Consumer was 11%, and that's unchanged from '09. And inside of that, Ross, is the TV number. But I don't have a specific breakout for television. Automotive last year was 8%, up a couple points from '09. And then education, which is really our calculator product, was 3% in 2010, down 1 point from 2009.

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

Operator: We'll go next to Tim Luke with Barclays Capital.

**<Q – Tim Luke>**: Thanks so much. Just as a clarification. Maybe from the fourth quarter and as you look at the first calendar quarter guidance, could you give us, Kevin, any feel for the contribution from the revenue associated with the factory service deals that you have in China and Japan? And separately, rather in the vein of Ross's question on the OpEx side, in seeing a somewhat lower gross margin in the calendar fourth quarter, could you give us some feel for what some of the puts and takes might be in what appears to be a slightly lower gross margin also for the first quarter? Thank you.

**<A – Kevin March>**: Yeah, Tim, on the revenue from the transitional service agreements, we've spoken in the past and still hold to the forecast; that is that we expect those revenues to be less than 1% of our 2011 overall revenues. And that's – we won't break it down any more than that or by quarters any more than that, because it'll fluctuate a little bit. I would just, to put a little bit more color on that, remind you that with the Chengdu fab, as we disclosed, that transition service agreement will run for three or four quarters before it winds down. And with the Spansion fab, that transition services agreement will run for up to two years, and winding down during the course of that period. But overall, revenue expected to be less than 1% of our 2011 revenue.

**<Q – Tim Luke>**: Is the contribution, Kevin, fairly similar in the fourth quarter and the first quarter? Or is that helping to some extent with the slightly better-than-seasonal guidance?

**<A – Kevin March>**: It'll be fairly similar quarter over quarter because fourth quarter was the first all-in quarter for all three of those factories – specifically those two that we're doing the transition services agreement on. So first quarter should be about the same.

**<Q – Tim Luke>**: Thanks.

**<A – Kevin March>**: And your second question, Tim, on OpEx -

**<Q – Tim Luke>**: It was more on the gross margin puts and takes as we begin the year?

**<A – Kevin March>**: Yeah, I'm not sure -okay, that's right, because you indicated that you thought maybe gross margin might be a little different in first quarter. I would remind you that we do expect utilization to be up a bit little bit from first quarter. I'm not quite sure how you're putting that into your model. But do make sure that you've got the OpEx properly accounted for on 4Q going into 1Q. That is, it was up \$30 million in that same period a year ago. It should be up more than that this quarter, because we're stepping up our R&D. Also, don't forget to – that restricted stock dividend equivalent adjustment that we have to make to our earnings per share. You need to make a similar adjustment when you do your model so you get back to what you think is a target GPM percent for us.

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<A – Ron Slaymaker>: Okay, great. All right, Tim. Thank you for your questions. And, operator, let's move to the next caller.

Operator: We'll go next to Stacy Rasgon of Sanford Bernstein.

<Q – Stacy Rasgon>: Hi, guys. Thanks for taking my question. I just want to clarify one thing. The orders down 9% this quarter, revenue guidance down about 3%. Is that mismatch strictly because of the order linearity in the quarter? And can you give me some feeling – I guess if October orders had been a little more normal, might those two numbers, orders and revenue guidance, been more closely matched?

<A – Kevin March>: I'll comment on that and then let Ron go ahead and add some more color to it. But what we're really seeing there, Stacy, is that as lead times came in, as they started coming in the third quarter, we already began to see our book-to-bill fall below 1, which is really quite normal. So customers who may have been putting six months of backlog on us, as we began to move the lead time in, didn't have to give us backlog orders as far out in time. So, frankly, they could go for a few weeks or even a couple of months without putting any new orders on and still have the backlog coverage that they want. So we saw that sort of phenomenon going on in third quarter and in the fourth quarter, and it's quite normal and was quite expected.

The other thing that we did see that gives us, again, reassurance as to the outlook that we provided for first quarter is that we had a backlog coverage going into first quarter that frankly was higher than we've seen for a number of years. And that's consistent, I think, with what we've been talking about on the markets, those major markets of PC and TVs that we talked about, pretty much cleared their inventory in the fourth quarter. And we're beginning to see kind of a normal order pattern beginning to show up as we came into late fourth quarter and currently as we're moving into first quarter as well.

<A – Ron Slaymaker>: So I would add maybe two other things, Stacy. Again, it's not new, but just reiterating what we said. Our views of the corrections and adjustments to customer inventories and where they are in that progress, is part of the reason. Another reason is – and maybe the last reason – would be that just what we've seen quarter to date in terms of strength, both in terms of orders and revenues play into that confidence as well.

Do you have a follow-on, Stacy?

<Q – Stacy Rasgon>: Yes, I do. Just regarding the R&D guidance, can you give us some feeling for where you're investing the incremental spend in terms of specific types of projects or areas?

<A – Kevin March>: It's going to be across the core areas, Stacy, of Analog, Embedded Processing, and the non-baseband portion of Wireless. But I would say that just given its size, Analog will get most of those dollars. And then you'll get a distribution of that into the Embedded Processing next, and the remainder of the growth will be into the non-baseband portion of Wireless. But it's all in the core product areas. It is not in other areas.

<A – Ron Slaymaker>: Okay, thank you, Stacy. And, operator, I think we have time for one final caller.

Operator: And we'll take our final question from John Pitzer with Credit Suisse.

<Q – John Pitzer>: Hey, Ron, thanks for getting me in here. Just a follow-up to an earlier question. On the \$435 million which is baseband, how do we think we should model that? It sounds like no incremental suppliers to your big customer until mid-year, and so flattish first half and then a decline? Or how should we think about that?

**<A – Ron Slaymaker>**: You know, John, you've heard us say before that if you straight-line from where we are today down to zero in first quarter '13, the only thing we can tell you is that'll be wrong. You'll have some quarters above; you'll have some quarters below. I know qualitatively I've tried to describe that most of that revenue's 3G. And until they have a 3G player ready to start supplying them, that revenue will – I won't say it's stable, but it'll move with our customer's own business levels. But we've kind of given up forecasting when they're going have a specific alternative supplier onboard. I'm going to shift that risk to you as the analyst now. But you at least know our mix of 3G to be able to base that on.

Do you have a follow-on, John?

**<Q – John Pitzer>**: Yeah, on the follow-up, if you look out over the last decade, you guys have always done a good job growing R&D slower than you grow revenue. And I know you're not going to allow me to easily back into a revenue guidance for the year, but when you look at R&D guidance, up over 8% for the year, is there something unusual about this year, that's a structurally high investment year? Or when we think about the core business, ex baseband, is that leverage that you guys have been able to show in the past still applicable?

**<A – Kevin March>**: Yeah, I don't know what your revenue assumption is, John, but it sounds pessimistic. You're saying R&D up – you said -

**<Q – John Pitzer>**: I guess my question is, is there anything that you see in the R&D for this year specifically which would drive R&D growth faster than revenue growth?

**<A – Kevin March>**: No.

**<Q – John Pitzer>**: That was my question.

**<A – Kevin March>**: Okay.

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**Ron Slaymaker, Vice President, Investor Relations**


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All right. John, thank you. And overall, thank you. As we wrap up, thank you for joining us. A replay of this call is available on our website. And good evening.

Operator: And again, that does conclude today's call. We do appreciate everyone's participation.

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