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PRESENTATION

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Hello, everyone. This is Vivek Arya, Senior Semiconductor and Semi Cap Equipment Analyst at BofA Securities. Really delighted to have Brian White, Chief Financial Officer; and Kathy Ta, Vice President of Investor Relations from Maxim Integrated joining us this morning to share their insights about the company and this very interesting demand environment that we have in semiconductors. A really warm welcome to both. And what we will do logistics-wise is, I'll go through a set of Q&A. And if you have any questions, please use that Veracast window you have in front of you to just e-mail the question, and I'll be sure to weave it in my prepared questions.

QUESTIONS AND ANSWERS

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

So with that, maybe welcome, Brian, if maybe we could just kick this off with just state of the union. I imagine both the demand and the supply situations have been disrupted because of COVID. How are you seeing it from a Maxim perspective so far in the year?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Sure. I think that one of the main topics of discussion for the March quarter and then coming into the June quarter was disruptions in supply chain. And for Maxim specifically, we had some constraints within our Philippines test operations. Had staffing shortages related to COVID-19 that began in March and extended into the June quarter. And we adjusted our revenue guidance based on an expectation around a ramp back to normal operating levels. And I'm happy to report that we have successfully executed against that plan, and we've already returned to a normalized run rate. So the supply situation, although not completely without friction, we've managed to bring back to a normalized level of volume production. And I think the demand environment has remained solid. Obviously, we've seen some improvement with the resumption of activity in China. The rest of the world is beginning to follow. So improvements on the supply side, and I think a solid demand environment backdrop.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. So just to kind of close on the supply aspect of it, Brian, are you now kind of fully to the normalized run rate? Or there is still some more things that need to be done?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

No. I think at this point, it's really ringing out the efficiencies. Again, there's still a little bit of friction in terms of how we're able to run at a normalized rate. Then in terms of getting volumes through our back-end operations, we are now at prior normalized run rates. Obviously, we were not at that level for the entire quarter. We entered the quarter at a substantially reduced level. So our plan for the quarter was that we would ramp that and that we would exit the quarter at normal operations. And at this point, we've achieved that level.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Oh, that's good to know. And then in terms of the demand environment, could you give us some color by different end markets, where are you seeing kind of the best or worst in terms of a recovery from a demand perspective?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. I think some of the early recovery has been in the China region. We've seen a pickup in China as they've reopened their economy. This has helped our BMS business, which is it's highly indexed to China. China, obviously, has -- probably half the world's EVs are made by Chinese OEMs. So that's helping this business for us. So Automotive, I think, generally speaking, got very challenging in the COVID environment with factories being closed. That's beginning to improve on a region-by-region basis. But I'd have to say, it still remains soft, and there is certainly a way to go on the Automotive side. Industrial, we had guided up for the June quarter. Industrial remains -- we feel good. We're certainly seeing strong demand for products that make their way into medical applications. So a very, very strong medical business for us currently. We also -- seeing some recovery in control and automation. And Industrial is really an area where coming into the quarter we were -- is probably disproportionately impacted by supply disruptions. And so as we begin to alleviate that bottleneck, that's also helping as it relates to our Industrial business. Comms and Data Center continues to be solid. And in the data center, I think it's been an area that been very strong for a number of quarters. Our optical business continues to do well, both on the comms infrastructure and data center side. Consumer has been weak. Certainly, with the employment picture and consumer sentiment and related spending. That's an area that's been impacted. And so we're still looking for improvements in that end market.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. The U.S.-China trade tensions are kind of top of mind for investors. Could you give us a sense for how Maxim is potentially impacted by any recent trade restrictions or just a threat of more restrictions on Chinese customers? Maybe give us a sense for what your overall exposure is to domestic Chinese customers? And if you would be impacted in any way because of these new guidelines that are coming out from the Department of Commerce?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Sure. Maxim has a lower exposure to China design and base business than many of our peers. We put it in the mid-teens total company revenue on percentage terms. So the amount of consumer exposure within the domestic China OEM market is for that piece, low single digits of total company revenue. And our assessment of the latest trade restrictions indicate no material impacts to our business. So it's -- we're relatively low in our design and exposure and our valuation of any specific restrictions as of this point in time has resulted in no impacts to our business.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Then any sense of perhaps pull in by any Chinese customers ahead of some of these trade tensions? Did you see any abnormal inventory builds or double ordering or anything from Chinese customers? Or just because of COVID overall tensions?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. What -- overall, we've been running with very lean channel inventory. We finished last quarter with just 50 days, which was significantly below our 60-day target. Yes, we don't have perfect visibility to inventory beyond our channel partners, but we haven't seen anything unusual that would suggest significant pull-ins. We also implemented a policy of 45-day nonaccountable, nonreschedulable orders. We did that at the beginning of this quarter. And so I think that the visibility that we have to firm orders and those orders being real and the risk of double ordering, I think, is less as a result of those actions that we've taken. So it can never be completely immune to those dynamics. But we're not seeing anything that suggest there's an issue there at this time.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Maybe let's go through your different key end market segments starting with Automotive. That has been one of the more exciting growth markets for Maxim. Give us some color around what's going well for you in Automotive? I think you just referred to the BMS business when it comes to China. So what are the key things that can help you outgrow the Automotive market, both kind of from a near-term perspective? This year people are thinking units could go down 20%, 25%. So if that happens, how will Maxim fare in this environment? And then longer term, what helps drive your Automotive business?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Sure. Autonomous driving and electric vehicles are a couple of the megatrends behind our growth. Our primary product areas include serial links for high-speed data transmission and power battery, management systems for EVs and broader power management within the vehicles. So our Automotive business has been growing strongly for a decade up until the recent COVID-related challenges. And our design pipeline continues to be robust given the leverage of the high-growth areas of Automotive that we enjoy. Our Automotive business is a little bit newer than some other people that supply to automotives. And given that it doesn't go back multiple decades. Our content exposure is really heavily levered to the high-growth areas within Automotive. So we would expect to outperform the overall automotive market by about 10 points, is our model. Historically, this has been a high-growth area for us. And we expect it to return to high growth in the future. And during a soft environment, we think that will still outperform on a relative basis.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Brian, what's your gut on the longer-term Automotive unit trajectory? Because it feels like there is going to be some snap back in the back half. But do you think longer term, Automotive units can get back to even 2019 levels. And let's say, if that unit growth is not there. You still think the content growth aspect can help you drive this business right in a strong way over the longer term?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes, the content growth is what's going to allow us to outperform, independent of how the unit sales trends progress. I don't think that we have a unique perspective or any insight beyond the kind of market forecast that you may see out there for growth rates in the near term or the intermediate term. Our focus is to bring products to market that will differentiate us and allow us to outperform as we have been doing. So I think that we'll continue to do well regardless of how the unit sales turn out. I think that at some point, they -- we should get back on a normalized run rate, broadly speaking, from a SARs' perspective. But the timing of how that plays out over the course of the next couple of quarters or year, I don't think that we have any unique insight into that.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Maybe one last one on Automotive, just the competitive landscape. How would you size the competition from your traditional competitors? So for example, you have had NXP analog devices, Texas Instruments and others. Also talk about their BMS products. So how does Maxim differentiate from these traditional competitors? And then kind of the part B of that is, do you ever see some real competitors come up in China? Because I imagine that given all the R&D incentives that the government is putting in, at some point, they will want to have more domestic sourcing of some of the products that you are supplying. So any perspective on that would be really helpful.

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

We're not counting on having this market to ourselves. We haven't historically. There's been other suppliers. We take our fair share. And that share has been relatively stable for some time. And we don't really expect that to change a lot. So there are other suppliers out there. Each have their own unique characteristics and customer relationships that they've carved out. We tend to win on safety and -- safety ratings and performance. And we have a strong position, and we don't see that changing. As it relates to domestic Chinese suppliers, I think that there is always a risk out there, and that could apply to any end market, automotive or otherwise, that you could have new competitive entrants and particularly in China. But I don't think we see that as a near-term dynamic that would be impacting our business.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Then moving on to Industrial. I've been very positively surprised by how well your Industrial business is kind of held in for you as well as for the industry has actually done throughout this environment. Could you help us segment which parts of Industrial are doing better? And more importantly, is this sustainable? Or is this just kind of a temporary dynamic because of COVID? So which parts of your business in Industrial are actually sustainable as we go into the second half also?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes, kind of breakout our Industrial business. Nearly half is control and automation. And about 1/3 is driven by the verticals, medical, automated test equipment and financial terminals. Currently, COVID-19 is driving some unique strength in medical. Some of this is likely to be a spike tied to the current crisis. However, we saw medical as an attractive opportunity to focus area before COVID-19, and we continue to see it as a focus area for growth in the future. We're seeing a lot of demand for continuous patient monitoring type applications that we're addressing. So that's a big piece of what we're seeing in terms of near-term strength. I think additionally, we've also been very diligent in keeping our inventories lean in the channel, and we believe elsewhere in the supply chain. So we already went through an inventory correction in our Industrial business last year and had continued to run the channel tightly. And up to COVID-19, the Industrial business has been resilient, I think, broadly across the areas that we're exposed to. And supply constraints that we've had have disproportionately limited our ability to ship revenue into the market in the current environment with the COVID-19 disruptions. So I think we're exposed to the right areas. There's been a cleanup of the channel that's taken place -- channel and end customers has taken place over the course of the last year. We've had some disruptions. But as that supply comes back, it's matching up with demand. And so the Industrial business is looking very solid for us currently.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Moving on to Comms and Data Center. I think that's been another very interesting aspect of Maxim's business. I believe it's close to 20% of your sales now. How do you think about your business longer term? Do you think you have all the piece, parts? Is this a business you want to invest it from an inorganic perspective? Just longer term, how fast do you think your Comms and Data Center business can grow?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. Longer term, we would model our Comms Data Center business as a mid-single-digit annual growth opportunity. And that view incorporates our higher growth rates for optical and server power, which are expected to partially offset some of the slower growth in legacy products in comms infrastructure. As it relates to optical, we use a common technology to address a single lane of 25 gigabyte connection between the radio head and the base station of comms infrastructure. And we use that same common technology for 4 by 25 gig for a 100-gig optical in the data center. And the demand for optical products in both of these applications has been very strong for the past 2 quarters. We've also seen an uptick in our server power business in 12-volt cloud and in advanced computing platform. So when we combine some of the higher growth areas of optical and power in the data center with some of our legacy. Again, mid-single-digit grower long-term is our outlook.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. And then within the data center and the cloud business, where do you think, Brian, we are kind of in this 100-gig build-out? And do you think some of the strength that you saw in the optical business, can that sustain into the second half of the year?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. I mean I would avoid commenting on the second half of the year, whether it's optical or any other piece of our business because I think that there is still a fair amount of uncertainty out there. But in the near term, it continues to look very good. The vast -- we're shipping 100 gig for the data center. We'll continue to be shipping that for a long time. We're working on future generations of optical products at 200 and 400 gigabytes and our plan is to introduce those in the future. Those won't be very near-term things in the next quarter or 2. So those aren't second half events. The rest of this year will be dominated by 100 gig. And looks solid at the point, but I'm not going to make a call in the second half.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Just -- so without being Maxim specific, if you just look at cloud spending overall, there have been kind of 2 perspectives. One perspective is that, look, the cloud guys, right, especially the e-commerce companies or the streaming companies or gaming companies, have seen this work-from-home and stay-at-home dynamics, so they increased spending to perhaps unsustainable levels, and that surely must decelerate in the second half. The other perspective is the more optimistic one, which says that, look, COVID kind of accelerated a lot of things that were going to happen anyway. So what we are seeing here is a more secular rather than kind of a one-off dynamic. What's your sense of just the spending environment without being Maxim specific?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. I would fall into the second camp that this is a strong secular trend that's not unique to the COVID situation. I mean, it's possible that, that has driven some higher demand in the recent term. But I mean this has been a trend that's been in place for a long period of time, even well before, I mean, into the COVID-19 crisis. We've seen a lot of strength and positive trends in this area. So I don't think there's any reason to believe that this wouldn't continue moving forward. I mean maybe people are getting some slightly higher pop for a period of time. But I think that this is a trend, again, that's been established for a long time and is the one that's going to run for a long time into the future.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. On the telecom side, could you remind us what your exposure is to Huawei? And do you see any risk of them in-sourcing some of the products that you are supplying?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. We have basically no direct business with Huawei at this point. And that maybe a slight exaggeration. And it's -- we have, call it, broadly speaking, maybe a couple of million dollars a quarter as a company that we shipped to Huawei as a customer. That business, for us, rolled off a number of quarters ago. So we're at a very low base of existing business. And so we don't -- there's really not an opportunity for risk there moving forward.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. On the 5G side, how would you characterize Maxim's exposure to 5G? I recall a few years ago, Maxim rightly kind of deemphasized the whole base station and the wireless infrastructure market and you guys focused on auto and industrial, which were in hindsight the right decisions. But now that we are at the start of the whole 5G cycle, how is Maxim positioned? Is this an area of focus at all?

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Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes. Well, I think you described it well. There was a decision in the past to deemphasize the comm space and put more energy on Automotive and Industrial. And I think that's worked well for the company. If I look at, say, our base station related revenue, it's approximately 5% of total company. So it's not large. The primary driver of our 5G-related revenue over the past few quarters has been our 25-gigabyte single lane optical products for 5G fronthaul applications. So we ship the module makers who ship on into base station customers. And that has been a strong growth driver for us over the last few quarters. So we're happy to have that exposure. It's been good. But from a percent of total company basis, it's relatively low. And as you pointed out, the company is focused on some other areas beyond comms infrastructure.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. I got one investor question, which is -- I think you mentioned the direct exposure to Huawei is very small. Just a clarification, is there kind of indirect exposure through module makers or other means?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes, sure. That's a fair question. And I mean, the short answer to that is yes, of course, because Huawei is a consumer of optical products for comms infrastructure type applications, they're not a direct customer of ours as it relates to optical module makers would be. And so those optical modules are going to find their way into those comm infrastructure systems, the people that make those, including Huawei and the geographies that those are deployed. So we would have indirect exposure as it relates to that. I think that the follow-on question to that would probably be, okay, do you feel comfortable about being immune from restrictions and shipping products that indirectly make their ways potentially into Huawei products. And we spent a lot of time looking at that. And our view, based on everything that's come out to date is that we don't have restrictions that are impacting our ability to ship. So we're not seeing any material impact as it relates to indirect exposure to Huawei.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. And then finally, Consumer, at some point, there was a very heavy Consumer exposure, which has really come down significantly. What do you think is the right exposure to Consumer for Maxim? Are you there already? Does anything else need to be done? And are there parts of the Consumer market where you think could actually provide interesting growth opportunities in the future?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes, it's a mix. So yes, there are areas that provide growth opportunities. There's other areas that we're deemphasizing now. So we've really deemphasized the handset side of things. Our smartphone exposure is significantly lower than it was in the past. We have diversified into other applications, though to help offset some of the decline on the handset side. So our models for Consumer long term is really for a relatively flat revenue level. So revenue levels similar to what they are today. So given that the fact that we think we're going to grow, that segment will -- we would expect to slowly decline as a percent of Maxim's total revenue on kind of just a flat revenue base in consumer with growth in other parts of the company. So that's the way I would think about Consumer moving forward.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Gross margins have actually held up really strongly, 65% or so even at these -- despite all the macro headwinds to the top line, how do you make the journey towards the upper end of the long-term gross margin, the 67% to 70%? And the fact that Maxim has become relatively more asset light versus a number of your peers? Do you think that helps or hurts in terms of making that journey to the stronger gross margins?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Well, I think it helps, broadly speaking, right? I mean, the financial model that we have today is extremely resilient. And you're seeing that in much higher gross margins than the company would have been able to achieve in the past at the current revenue levels, which in the current environment are fairly significantly depressed versus where they were not long ago. So we're still putting up very respectable gross margins, mid-60s at the very depressed level of revenue. We do see a path to high-60s to 70%. I think we've fundamentally improved our cost structure over time, along with the resiliency that's come with a reduction in fixed costs and more of a variable cost model with outsourced manufacturing strategy. But that said, there is a dependency on revenue to get to the top end of that gross margin range. And so I would think about kind of the -- the key revenue level has been, let's call it, $600 million of revenue a quarter. We were there not too long ago. But we really need to get back that level of quarterly revenue. And then I think with that, combined with the really efficient manufacturing engine that we've put in place, I think that's going to be the key to supporting the high end of that gross margin target model.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. Have you seen any changes in pricing behavior or just competition via pricing given all the trade tensions and the desire for some customers to do more -- use more domestic suppliers? I realize the analog industry is perhaps more protected from that. But just over the last 1.5 years when we have seen the kind of the brunt of these trade tensions, have you seen the pricing dynamic change in any way?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

No. We haven't. And I think that the industry, and particularly in the analog space, but even more broadly speaking, pricing is a lot less volatile these days than it used to be. And I think it's a function of a number of dynamics. One, there's been a lot of consolidation that's taken place over time. And two, companies have moved away from these big fixed cost manufacturing structures that were highly dependent upon fab loadings to support gross margins, like Maxim has done. We're very light from a manufacturing footprint standpoint. We have a lot of companies out there today, just generally speaking, semiconductors that are completely outsourced, for example. And so we're all collectively sharing a pool of manufacturing assets and infrastructure, if you will, through foundry partners, which creates a tremendous amount of efficiency and it alleviates some of those motivations to try to fill factories and try to initiate pricing actions to facilitate that. So that -- I think you have that backdrop of changes that have occurred in the industry and just a lot more discipline in terms of how people manage their businesses. And then in the short term, which was really your question, are we seeing changes in pricing behavior? The answer is no, we're not seeing that.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Got it. To the last question, Brian, in terms of channel inventory, when do you see them getting back to normal levels and you reaching your longer-term targets? And will anything need to change in terms of utilization to get there? Just how are you thinking about channel inventory overall?

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Yes, it's going to depend on a couple of factors. Number one, how quickly we're able to draw down on our backlog delinquency. That will be a factor in that equation. And then resales, which are notoriously difficult to forecast, would be the other piece of that puzzle. But I'd say our objective is to get it up to 60 days. We think that, that is the right level of inventory for us to run with as a business. And so we'll work to make that happen sooner than later. But we have to be able to free up the supply to make that happen. And as I mentioned earlier in the call, we have been very successful in returning test operations to more normalized levels of activity. So I would expect that we will begin making progress toward that higher level of channel inventory in the near future.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Great. I think with that, we are at the end of our time. Really appreciate Brian and Kathy, your participation in our conference and sharing your insights. And thanks to the audience for joining. If you have any follow-up questions, please feel free to call. All right. But with that, let's close the call. Thanks again, Brian and Kathy.

Brian C. White - *Maxim Integrated Products, Inc. - CFO, CAO & Senior VP*

Thank you, it's always a pleasure.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Likewise.

Kathy Ta - *Maxim Integrated Products, Inc. - VP of IR*

Thanks, Vivek.

Vivek Arya - *BofA Merrill Lynch, Research Division - Director*

Thank you. Bye.
