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PRESENTATION

Jim Covello - *Goldman Sachs - Analyst*

Great. Thanks everyone. I'm Jim Covello from Goldman Sachs. And joining me today are Bruce Kiddoo and Matt Murphy from Maxim. Guys thanks so much for being here this morning.

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

Thank you.

Jim Covello - *Goldman Sachs - Analyst*

So we'll hop right into it. 2013 and 2014 were actually pretty similar years for Maxim in the sense that the automotive growth -- the growth in the automotive segment is great and the data center and comm growth was great, but there was obviously issues in the handset space -- the consumer space. So could you talk a little bit about that, and kind of how we break out of that pattern looking forward?

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

Sure. I mean I think 2011 and 2012, we had some very good years in mobility that candidly became too big of a part of our business, right. I think I've been around this business for a long time and we know when customer concentration gets to a certain point that can only -- than can end badly. Obviously, we went through that time period. Our largest customer went from 28% of revenue to today it's now around 15% of revenue.

We've had a very, kind of strong push to both differentiate what we do in that consumer market and to reduce where our investments in that market to only invest in those areas, which we think we have a differentiated product and which is sustainable over time.

In doing that, we think we've now kind of brought down our exposure, the volatility associated with that, and really to allow the businesses that we say (inaudible) business and automotive or communication, our business in industrial, which have been doing well combined with kind of the strong controls around spending and actually spending reduction, which is going to drive margin expansion, to let those really kind of come through and drive value for the Company.

Jim Covello - *Goldman Sachs - Analyst*

Hindsight is always 20/20 and it doesn't always do too much good to be on to a quarter back, but if you had to do it again, knowing what you know now, what would you do differently, it's tough from -- and is not big business that your customer wants to give you, but are the things that you could do differently if you -- if you had to do it all over again?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

I think we would have been much more aggressive on the diversification side and more aggressive on moving to more ASSP or standard product type. I think consumer at the right size, it not necessarily a bad thing. We make a lot of money there right, it's good profitability, it's outsourced manufacturing but when you get that customer concentration when you're doing semi-custom products, those are hard to amortize that across multiple suppliers, multiple vendors, and multiple platforms. So I think and as you say, right, when you're doing very well and you're going to continue to invest there but I think if we had done it differently, I think it would have been this much higher push both -- what we've done today as far as diversification around customers and technologies and platforms, I would have done that more aggressively sooner.

Jim Covello - *Goldman Sachs - Analyst*

And diversification within consumer or even more aggressively earlier in auto and comps?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

I think I do believe we were always investing in automotive. I mean if you think of automotive -- we started investing there really in 2004. But we kind of took current products and moved those over and it just -- that's a business that takes time and I think Matt can comment on that. I think I probably -- maybe we'd have looked at some of the investments where we thought innovation, what's going to allow us to differentiate like in MEMS. We thought there were things that we can do that other people couldn't and customers would pay for that. It turned out we were wrong, though in hindsight that would be one -- if I'd been able to see the future we would have lowered our R&D investment there.

Jim Covello - *Goldman Sachs - Analyst*

And you have done some restructuring within the consumer space in terms of markets that you're not investing in any more. Can you talk about how you see this playing out over the next 12 to 18 months?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

Yes, I mean I think when we look at the consumer space, certainly we've always talked about it's a profitable business and we're not going to chase revenue just for revenue. And so the decision to exit consumer MEMS, the decision to exit touch were both along that lines, right. These are -- our customers weren't willing to pay for differentiation, for kind of innovative technologies. And so I think that's the business that we decided to exit.

I think we're being very focused in where we invest; our investment is obviously lower than how it has been in the past. And we're very cognizant of really diversifying across the customers and not letting one customer become too large and so we're putting steps in place in the Company and really managing it through margin targets of not allowing one customer to become too large, that's about it, it drives the issues around concentration.

Jim Covello - *Goldman Sachs - Analyst*

And is the key really that you want to make sure that you're investing in areas that you can integrate with other pieces which insulates the pricing pressure in any of the discrete elements. I mean is that, at the end of the day, is that really the key because if you have standalone pieces, the customers are going to find ways to wave that away. But if you have, like your power management [IC] the things that you're integrating together tend to be more insulated from that heavy price pressure, is that a fair breakdown?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

I think to the extent that you have highly integrated products and solutions, I think customers clearly value that. I do think there's actually a balance though between high integration and -- let's call it kind of ASSPs or application specific standard products that you can sell to a broader base of customers, because generally when you do a high integration product there's times when maybe you're integrating in different functions that maybe -- that a functionality that only that customer wants.

So I do think you need to balance between the two, and I think again your earlier question on hindsight, I think we probably went too far to the, let's call it the semi-custom product, and less to the kind of the ASSP type products.

Jim Covello - *Goldman Sachs - Analyst*

I just want to do a couple more on consumer before we get in some of areas on automotive and comps. First the big picture one, if I look back over time in the analog space, there's been a pretty consistent track record of the different analog companies at different points in time, getting to a certain stage of growth or stage of scale and saying, jeez I better go, my core businesses isn't growing as fast, I'm going to go try to get some consumer business, and that was -- or I'm going to get bigger in consumer. And Texas Instruments did that and then they eventually unwound that, maybe Linear did that and they eventually unwound it. ADI is finishing unwinding that now.

You guys, I think, I'm not saying unwinding it but in the process -- maybe in the middle of the process of decreasing that as a percentage of the overall revenue. There's other companies that are just starting that process and maybe kind of -- they are where you were a couple of years ago, ramping getting the 10% 15% of revenue with a single customer today on the way up a lot higher.

Is that just something we're always going to live with an analog or do you think the industry is going to evolve and auto is going to grow fast enough that we're going to decrease the reliance on the consumer from time to time?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

Yes, I mean, I do think, to the extent that you can -- fast growth industries aren't necessarily back, right. Automotive is a great example, right, that's growing -- it's been growing 30%, 40% a year, right. So, I think to the extent that it's an area that has -- pays for differentiation, it has long product life cycles. I think that's good, I think that's obviously a great business to be in.

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

I think there are segments within consumer, if you look at our power management business. We had power management wins with our largest customer since 2008 through today, and so we've been able to maintain that. I think the key is in any portfolio, you don't want one element of that portfolio to become too large and especially in an area that has the cyclicality or the volatility of the consumer market can have.

So certainly from our point of view, we're reducing the size of that part of our business. We see kind of great opportunities in automotive, great opportunities in industrial and the communication space. And so from our -- we've always had our strategy of innovation, integration, and balance. I think we're kind of just continuing to manage that balance piece of our business.

Jim Covello - *Goldman Sachs - Analyst*

One final topic on the consumer side, then we'll go onto automotive. Wearables, how aggressive do you want to be in wearables given the lessons learned in [handsets]?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

So I think wearables is a good opportunity to really kind of apply in ASSP strategy, where you're not doing custom solutions, but you're doing a power management solution. That can go into multiple wearables. Alright, you're doing an analog front-end or sensor technology. You're doing a very low-power microcontroller that you can sell to multiple, multiple customers.

I think the key thing about wearables is it's a brand new market, no one knows. I mean if you look at medical wearable, there's probably 300 companies out there right now that's doing some sort or trying to get into the medical wearable business. In the end, there will be a successful medical wearable business. I think for us having a standard product, you know in ASSP that you can sell across that customer base. Same thing, whether it's on the consumer side as well. So I think that's the right way to approach wearables is that idea of the standard products.

Jim Covello - *Goldman Sachs - Analyst*

If we go into the automotive space, and this business has been a terrific business for you guys, I think you have the fastest growth in automotive of any of the analog companies over the past couple of years, albeit coming from a little bit of a lower base. What's driving the success in automotive and where do we go from here?

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

Sure. Thanks for the question. So [technical difficulty] automotive it's done well for us. I think it's some ways exceeded our expectations. Bruce mentioned, we made a decision to invest in that market seriously and about 2004 is when the efforts started. So the results that we're seeing now are after years of a lot of work, and then I think when everything finally hit, it hit bigger than we thought. So that's been good and I'd characterize it as -- what do you think of it?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

Jim, it's kind of two big pieces of that business. One is where we started off in automotive was taking the existing Maxim portfolio, and applying automotive grade quality to it in terms of the testing on the reliability. And so, you'll find in lot of cars now, huge number of individual Maxim components that are automotive qualified.

So, that drove the early growth in automotive, that's a big base of our business now, where we just kind of sold what we had, but we had to improve the quality on it. And in parallel, our R&D efforts really were around a number of different application-specific product line. And there is everything from lighting, USB port protectors, power management ICs, both kind of larger scale ones for power and processors, as well as high-performance single-function parts, RF (inaudible) battery.

In the last year and a half, as we've really seen our growth accelerated, really it's all of those product lines now starting to generate revenue, kind of almost all in parallel, and so there's been a nice compounding effect where the base is growing, new product lines are heading, and what's good about two is that, the diversity of that revenue stream is really both geographical in nature. So, it's coming from, at first it came from Europe and now we're seeing strength in Japan and Korea as well as traditional US.

And then we're seeing quite a breadth of customers also driving the growth. So, it's not a one trick pony, it's really a result of a lot of work for a lot of years. But, we're very happy, we've kind of built a nice franchise here. And last thing to answer your question from earlier, I don't think we've left anything on the table. We've really invested aggressively in automotive, I think the Company was good about keeping the investment high and even upping it over the last three years even though the revenue was trailing. And now I think we're seeing the result for that.

Jim Covello - *Goldman Sachs - Analyst*

So can you talk about the products that you're selling into the market. In terms of the, the areas that you're selling infotainment, powertrain, safety, what area represents the biggest opportunity in auto?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

So, today the bulk of the revenue growth we've achieved has come from infotainment (technical difficulty)

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

So it's clearly going to increase. I think part of the challenge will be how well does Matt grow his comm business or industrial business as well.

And so from that point of view, more absolute dollars then how does automotive do versus the others, but again it's a business that has been growing at 30%, 40%. We think that growth rate comes down, obviously it is now like you say, 12% of our revenue, but certainly for the next several years at least, right, we see that that's continuing to be a double-digit growth driver for us and our fastest growing business.

So it will increase where it gets too. I think it's more relative to -- I think I'll major him on absolute growth as opposed to relative growth within the Company.

Jim Covello - *Goldman Sachs - Analyst*

Fair enough. So I do want to get to the comm's business in a second, but one more question on automotive. In the fourth quarter of this year for the analog industry, most of the companies with a fair amount of analog exposure or auto exposure, took it on the chin. Some of your biggest competitors in auto had really bad fourth quarter (technical difficulty) in auto, there were some negative pre-announcements, almost everybody in auto guided down pretty significantly.

Now that seems to have been behind us for now. You guys powered through that, why were you --- was it a segment issue, was it a design win issue, why were you able to have good automotive growth in the fourth quarter and then guidance for the March quarter when almost everybody else in auto hit a speed bump?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

We'll take it well. I think the primary reason is that we are coming off a small base and our growth is being driven by expansion of new applications. So, we haven't necessarily been in the mode of -- some cases where we've taken share, we've won a socket that the other guy had. But, really we've been kind of in a mode where lot of the growth we're getting, because we've created a new segment or new application space.

And again relative to the size of the industry, I think we're still got a lot of room to grow. So, yes it was encouraging to see with your words we were sort of able to power through it, where we saw some puts and takes within the business, but overall we powered through, and this actually kind of set us up for a nice first half of calendar 2015, which is typically seasonally strongest period to be within our third and fourth fiscal quarters in the first two calendar quarter of any given here.

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

I mean it's just an indication of the momentum in the business. We did about seasonal in December, we had a good quarter. We've guided all of our businesses that from March, we guided automotive up strongly. This is the good period for us, obviously March and June. But, I think it's a business continues to exceed our expectations from a forecast point of view. And I think it just goes through the kind of the strength of the design wins and the momentum. And again across a lot of products and a lot of the OEMs.

Jim Covello - *Goldman Sachs - Analyst*

Let's move on to the comms business. What is the biggest driver going to be? I know you've talked about the back half of this year, potentially some of the hyperscale and (inaudible) company's driving a lot of growth. What are the biggest driver is going to be as we go through this year?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

So, I think a couple things, I think there at the end of the calendar year, I think we will see to your point some of the results of the progress we've made with some of the engagements with the cloud vendors, whether sort of taking control over the design of their data center and server architectures. I think we've got some exciting programs there.

Jim Covello - *Goldman Sachs - Analyst*

Can you touch on that when you say they've taken control of the design? How do you mean that?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

Well, I think if you go back -- the way we got a big in this market was we did the acquisition of Voltera, in October 2013 we closed that acquisition. And one of the things we said when we bought the company was that, they had done well in traditional server manufacturers, kind of blue chip companies there. There was an emerging trend that was talked about that the cloud leaders were starting to exert some more influence over their ODM partners with respect to how servers were designed, what efficiencies were required, and some unique ways of think about. Because they're actually building service for their own consumption. And so they have a different perspective than somebody who is not doing that. And so, on that front, we under kind of maximum umbrella, we were able to engage pretty quickly with the different people both in the US as well as even in China. And what we're finding is, there is a genuine interest there by these types of companies to take more control over their designs. They have a unique perspective of what they want and so we see a trend where some of them are now specifying the components that might go into their next generation than those. And we have a pretty compelling story with respect to our offerings there. And so some of those are now translating into engagements and wins and we expect that to be a growth driver for us. I'd say more in 2016 and 2017 but starting to see the bearing the fruit there.

A related note if you just talk about growth drivers, I think the other thing we are excited about again with the combination of Maxim and Volterra on power, because we had some very good technology too in the communications market that was the other reason why we wanted to do that is, we felt that the requirements in communications were going to be such that APEX and FPGAs we're going to have current requirements that starting to look like Intel processors just a few years back.

Volterra would be well suited there. They didn't have any penetration, they really couldn't get in. So, we've also been working hard on that effort and we expect that to also bear some fruit in the coming years.

Jim Covello - *Goldman Sachs - Analyst*

And then what about -- so the hyperscale customers a little bit back half of this year and more 2016, 2017. What about between now and the end of 2015, what's going to drive the comps business?

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

Yes. So I'll take a stab at the first part and I'll let Bruce answer the second. I think, one thing that is going to help us is seasonality definitely impacted us in the back half of calendar 2014. We had a weak calendar Q4 in comps, actually what we saw there was not unlike a lot of the big guys were more exposed to comps than we are so we felt that -- and we are driven by the...

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

And we are driven by the lumpiness in China LTE.

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

Primarily China LTE. So we do, we're not the barometer or the bellwether on this, but we tend to agree with the sentiment that's really what we look for out of the comm business.

Jim Covello - *Goldman Sachs - Analyst*

We've a couple minutes up, so I want to hit on gross margin, and then capital allocation. On the gross margin near 60-ish percent this quarter, I think the target model is between 61 and 64, what are the key drivers to get that into the midpoint, and then I'll open it up to the higher end of the gross margin model?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

So, I think there's two things, we've always talked about utilization. Our utilization dip down in December due to the challenges that we had in our consumer business. We expect that to get to mid-60s in March, and continue to improve consistent with revenue. So that will certainly be a tailwind for us.

The other one is restructuring. We announced the closure of a small development fab in San Jose, and that should add about 150 basis points to gross margin about a year from now. I mean, we'll start getting some of that benefit in the back half of 2015, but a year from now that by all else being equal that should add this $10 million a quarter or 150 bps worth of a benefit.

So, I think those are utilization increasing, reducing cost, will allow us to get where we believe comfortably until like you know the upper half of that 61% to 64% range.

Jim Covello - *Goldman Sachs - Analyst*

You have maintained about a 50:50 mix of internal and external fab capacity. And then there is some 200 millimeter some 300 millimeter manufacturing. As you de-emphasize certain areas of consumers, is there any reason that think about changing that mix, the split between internal and external fab capacity?

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

No, I don't think so, when we look at our capability certainly to the extent that industrial or some of our automotive does well, a lot of those were done internally. But, some of those are done externally as well, some of the RF and on the consumer side we've actually moved more to our next technology will be a 100% outsourced, right. So that's one of the reasons our CapEx is going to be at low end of our 3% to 5% kind of going forward. And so I think, so that's -- so that's going to put -- to the extent we still have a consumer business, right. More of that will be done externally.

Jim Covello - *Goldman Sachs - Analyst*

Texas Instruments had a call last week where they put even more emphasis on 300 millimeter manufacturing. Does that change your thought process around 300 millimeter at all? You've been one of the pioneers in 300 millimeter on the analog side as well, but any desire to get even more aggressive there to make sure you're keeping up with some of the competitors in the space?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

I mean we have that capability through a exclusive foundry partner where we have 300 millimeter. We will continue to have that capability as we move forward from a process technology. 300 millimeters makes sense in certain businesses, right. Usually your higher volume, higher integration where you have a larger die size, it doesn't make sense for a lot of businesses, say like in the industrial or automotive side where you have smaller die and lower volumes. So I think we have it, we have it in a very efficient way where we've had almost zero capital investment. And that capability exists but it's not one where we're forced to put parts into it that maybe don't naturally fit in that model.

Jim Covello - *Goldman Sachs - Analyst*

Just one minute left on capital allocation. You've been one of the pioneers in that -- and giving all the cash back to shareholders, pretty much 100% of the free cash flow plus dividend yields ands semi's. What's next on the capital allocation front?

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

I mean I think for us, we're driving very hard to drive our free cash flow margin, right. We used to be at about 25% free cash flow margin. This last quarter on trailing 12 months we are 28%. We're pushing to get that to 30% and that's a combination we've brought the CapEx down significantly from -- it was running at about 6% this year. It's going to run at about 3% of revenue. So we've seen that benefit. And then as we drive operating margin from where we're at today, 22% to 23% up to 30% that also will drive the cash flow from ops up.

So our whole focus is to drive free cash flow margin and then we have our commitment to return 80% of that to shareholders over time, we know where periods we've done over 90%. So to the extent that that cash is available. We're very comfortable and returning that to shareholders both through dividends, which will kind of follow free cash flow growth and buyback, which is more opportunistic.

Jim Covello - *Goldman Sachs - Analyst*

Bruce and Matt, thank you so much. I appreciate it and look forward to doing it again soon.

Bruce Kiddoo - *Maxim Integrated Products, Inc. - CFO*

Thanks Jim.

Matthew Murphy - *Maxim Integrated Products, Inc. - SVP*

Thanks Jim.
