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CRUS - Cirrus Logic Inc at NASDAQ OMX Investor Program

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CONFERENCE CALL PARTICIPANTS

Operator

PRESENTATION

Unidentified Participant

Our next presentation is from Cirrus Logic, Cirrus Logic is a premier supplier of high-precision analog and mixed-signal integrated circuits for a broad range of innovative customers. The presenter today is Jason Rhode. Jason is President and Chief Executive Officer. Please welcome, Jason Rhode.

Jason Rhode - *Cirrus Logic, Inc. - President and CEO*

Thanks. Good morning thank you for coming. So just before we get started, the obligatory Safe Harbor. I'd like to draw your attention to that and point you to the risk factors that we also post in all of our filings. Now these are the kinds of things we spend a lot of time making sure don't happen, but they are real risks in our industry and we certainly want people to be mindful of them.

With that out of the way, I'll give you a little bit of history of the Company. Cirrus was founded in 1984. We're a well established fab, fabless supplier of mixed signal semiconductors. So we have a wide range of audio products, it's really spanning from the microphone, all the way to the speaker amplifier and centered on what we believe will be a growing trend of smart codecs in between those two things. But really a whole gamut of audio products across the board. Really largely differentiated in part by signal processing, which is really what our core vision is centered around.

So we recently acquired Wolfson Microelectronics that acquisition closed at the end of August. So just to put it in perspective, the combined companies in 2013 shipped over 850 million units in the audio markets. So that certainly makes us one of the largest suppliers to that market and as a combined entity we feel like we're spending more R&D dollars in that direction than anyone else out there as well.

So again, our core competency is analog and digital signal processing whether that's in the form of a chip or in firmware that runs on our chip, but what we monetize is selling products for non-IP provider per se.

We think that our reputation as an outstanding execution engine is really what's gotten us to where we are today. We developed very complicated products on time and help our customers succeed. So we've been and like I say a fabless supplier for long times. We're very, very good at supply chain management, which as you can imagine targeting the kinds of markets like portable audio, which are very rapid ramps is something that is also a differentiator for us.

So we're partnered with some of the best customers in the industry. We think we've got an outstanding suite of IP to build our products around. We like to partner closely with customers that can really move the needle are number one or number two in the market and we also like to have a broad suite of both custom and general market products that we can leverage across multiple customers as well.

If we're able to participate in that cycle directly, successfully rather so is typically easier to grow your business with your existing customers than it is to go get new ones. So while we're heavily engaged in diversifying our business through new customers, merging companies shipping mobile phones in China for example, great new opportunity for us. But we're also very focused on expanding our business with our existing customers either growing our share of those accounts or adding new functions and new features to our devices so that we can either preserve or increase our ASPs over time.

You don't get to do that every year. Obviously, you got to take care of business and help your customers drive their cost down over time. But over time, we've been very successful over the years of increasing our ASPs and we see continued opportunity to do that going forward. So we're very fortunate as I said to work with some of the best customers in the industry. I think it's a pretty non-principle if you can't get the attention of number one or number two in the markets that you're serving then you're probably barking up the wrong tree. We're very well-positioned in that regard across the whole tier of the industries we serve, particularly in mobile phones where we ship to five of the top ten brands today and we see opportunity to both increase our share at those five and increase to a higher number of the top 10 over time.

It's really a remarkable thing in phones, the transition that's happened where a number of years ago there were very few customers that were innovating around audio in phones or even able to do so. They were very beholden to some of the chipset suppliers to do a lot of their engineering for them.

But as the markets matured people looked for more and more ways to differentiate their products and audio has become a real central theme to the way that companies, even some of the smaller guys in China are wanting to differentiate based on the user experience and audio is a really good way to do that. So we see a lot of opportunity to continue to grow the business with the customers that have gotten us here as well as expand and there's some exciting new opportunities in China and elsewhere. Obviously the acquisition of the Wolfson brand.

While, we had some customer overlap, we actually had quite a complementary set of customers across the board. So, that's enabled us to broaden our customer base out as well as expand our engineering capabilities to go target customers or increase our content with customers we are already working with.

One of the things that really make Cirrus unique is our focus on our corporate culture. The kind of engineering we do takes years to develop the skills to do it. It's a real shame if people leave just when they get good at it. So we target having a very, very low turnover rate. We've been very successful at that. We've been recognized as one of the best places to work in the country in the US for a number of years in a row. We're looking forward to expanding that to the UK through the Wolfson acquisition. We think that for people to be successful in the kind of feel that we're in, needs to be something that they're passionate about that they're excited about and they are lot more likely to do that if they're in an environment where they really like what they're working on and like what they're doing like how they're treated and we've made great progress on that front. We're well recognized for having success there. It really has proven to be a tremendous advantage both in retention of existing employees as well as recruitment of new ones, almost every new employee I talk to about how did -- why did you decide to join us? The fact that we've been recognized as a great place to work factored into their decision. So a quick overview of the products.

Our largest market that we serve is portable audio obviously dominated by mobile phones, there is a lot of talk about that market saturating, maybe the growth in smartphones has slowed.

So you can have, I'm sure everybody has got their opinion on exactly what's going on there. But the neat trend for us is just the explosive growth of voice and audio features within the phones. So a few years back, it didn't seem like very many if any more than one customers out there were really focused on audio and voice differentiation. And today it's almost every customer we talk to that wants to find a way to add more functionality especially in the voice capabilities either through noise suppression or noise cancellation, voice wake, some of these features were the phone is always listing.

I'll talk a bit more about that in a minute, but these are functions that a few years ago there were only one or two customers that would even really have a vision of what they wanted to do. And today it's every customer you talk to that wants to add these features and they're all, there's no such thing as low enough power, they all wanted to be lower than you could possibly achieve. And the great thing about the market in mobile phones is we can perfect a lot of these same technologies in mobile phones and then leverage them in other applications such as wearable and automotive and other types of devices.

So following the Wolfson acquisition we're the only semiconductor supplier that spans the entire audio signal chain from microphones to speaker amplifiers. So we had some overlap in the middle of this slide prior to the acquisition, but Wolfson brought the microphones to the product line and Cirrus had the standalone amplifiers. So that really gives us an opportunity to leverage the whole chipset, expand our content with existing customers and really knit all these functions together within extensive suite of software that goes with them.

So I'll talk a little bit more about the kinds of functions that we provide in firmware. It's great when we can develop a custom product for a customer, but if you think about 55-nanometer where we're doing the bulk of our development today, developing a new chip can be a \$10 million, \$15 million expense. So there's not that many sockets out there where you're going to have the confidence and the customer relationship where you're going to go do a custom product for that customer. But again, like I said, these customers want to differentiate their products anyway. And one way to do that for a much wider range of customers is through some of these signal processing algorithms that then run on our smart codecs.

So between the two companies, we've really got a full array of software technology that runs on our chips either our own. We also have tools that let our customer report their code to our DSP as well as enable third-parties to run their software on our DSP and typically a customer that we're heavily engaged with on software will do some combination of those three.

So for our own technology, we've got voice capabilities such as multi-mic noise reduction, beamforming, other types of functions, echo cancellation, of course we would all like our phones to be much better smart -- much better speaker phones. So things like speaker protection, signal boost, so you get a lot more volume. And we did a press release about the LG G3 model earlier this year. The thing is just, is very, very loud and that's enabled in part by the amplifier that we provide. Other things such as the multi-microphone record functions, that control is really getting a lot of attention now, because it again requires the phone to be always listening. So these are functions where you can say, even though the device is laying on the table, not doing anything, you can wake it up by saying a catchphrase and it hears you.

So for the microphone to be always on, for an A to D converter to be recording sound from that microphone and making decisions like, is there a noise? Okay, was that noise a voice? Okay, was that voice saying the controlled command or the specific command and then kind of waking the system up in phases is something that requires an incredible amount of signal processing that's really only enabled now by the fact that we're able to do make mixed signal devices in advanced geometries like 55 nanometer.

So that is something that's really expanded the market and it's made it a more difficult type of function to achieve, because it needs to be on for such a long portion of the day. Obviously, anything in a cell phone needs to be relatively low power, but if it's going to be something that is literally on for the life of the phone then it gets an extra level of scrutiny. So there's a lot of these features that we've been shipping for some time and we need to continue to enhance those to make them lower power, to enable our customers to implement them across a broader array of their product line. So these are things like noise suppression, some level of beamforming, but then there are these newer functions and features such as the Always On and voice command that expand the market and enable us to add new functionality through our newer devices such as 55 nanometer smart codecs.

So I think there is a little bit of a misperception about the transition period that Cirrus has been in. Prior to, in the 2010 to 2012 timeframe, Cirrus expanded our content in the mobile space pretty significantly. Our -- the last two years really have not been a huge period in new product introduction for Cirrus as we've been migrating a significant portion of our portfolio from 180-nanometer to 55 nanometer. So I think where maybe the misperception comes in is from the digital world when you migrate a product down in process, you typically are able to make the device more significantly lower cost.

But in a mixed-signal world, where the devices half analog and half digital, if you simply took that same device and migrate it down to 55 nanometer, you'll make it much more expensive, because the analog typically doesn't shrink at anywhere near the rate that the digital does. So for us to migrate a product to 55 nanometer, it's got to be because we're adding content, we're adding signal processing capability, we're adding memory. So for us to migrate to 55 nanometer is not at all about making the devices lower cost, it's about making them add a lot more content, a lot more value.

So a good example of this chart is kind of a little bit of a summary of the kinds of things we've done for the general market. And this is really more a depiction of the former Wolfson product line. But in the 2010-2012 time frame, well, in particular in 2010, you're really selling a codec, it might have an integrated speaker amp for the earpiece, obviously some headphone amplifiers and things like that, but you're talking about a device that was on the order of \$1. And over the past four years or five years, that's really expanded to include a little bit more signal processing power, each generation. And then the device that, that we and Wolfson were shipping earlier this year, starting earlier this year in very high volume is a 65-nanometer device. This is a part with 600 MIPS external memory, also it's a voice and noise and audio functionality and features, that's a much more expansive and expensive device than what we were selling a few years ago. Obviously that doesn't stop there, we're using that, we're migrating



that down to 55-nanometer as I said, adding more MIPS, adding more memory, driving the Always-On Voice power down along with the rest of the type of -- the rest of the functions of power that we're trying to reduce.

So it's really been an expansive growth plan within the smart codec opportunity itself. But it's not the only trend in addition to the smart codecs, we've gone from an opportunity where there might have been one microphone in a phone some number of years ago, to now two and three and people are talking about significantly higher numbers of microphones into the future. So not only is that a microphone opportunity for us in the long-run but it expands the requirements on the signal processing power of the smart codec that we provide as well.

Similarly in amplifiers, three or four years ago would typically be one amplifier that was integrated into the codec, it might deliver a few hundred milliwatts to the speaker typically, remember the phone probably wasn't loud enough to actually use as a speakerphone in most environments. Now customers are adding one or two external boosted amplifiers to get the signal to be very, very loud. Some companies offer stereo, so that really is an -- and this is a product line that for us literally didn't exist prior to 2012.

So 2012 which really started to grow that business and today it's a significant part of the product line that we have. I think there is sometimes a little bit of a misperception that this is a type of socket that we should have the same dominance that we have in smart codecs. Amplifiers do tend to be a little bit more of a competitive product line, there is some other competitors out there, it's a little less of a sticky socket than a smart codec.

So you shouldn't view that as a market where it's kind of a winner-takes-all or one socket matters as much as the smart codec. The smart codec by virtue of the fact that it gets intertwined with an OS, it's intimately tied to the user experience. It's heavy analog and mixed signal content, nobody likes to take functions and features out of a flagship product like a phone, you're going to tend to add more and more and more over time. So that obviously we still have to execute; we have to deliver value for our customers when you did not disappoint anybody, but that is a much -- I view that is probably one of the stickier sockets in the industry.

So it's really a great expansion of what we used to do versus the potential content, you know, it's not meant to depict any one particular opportunity, but the potential content in a high-end phone going forward really expands a lot. And then additionally these same kinds of features and functions are percolating down the product line you know, from what would have only been considered in a flagship high-end phone and we want to have a pallet of these same features and functions that are available, further and further down to manufacturer of product line.

So, the great thing about mobile phones is the volume is so high there that it enables us to innovate at real high-rate that typically the phones are refreshed every year, if not more often. That gives us an opportunity to introduce new devices, get a lot of cycles of learning under our belt and really improve rapidly on the kinds of technologies that I was just talking about. But there is a lot of other great applications where maybe we wouldn't be able to do that yet, a lot of emerging wearable opportunities, things in automotive, things in the home and the great thing is that a lot of these signal processing capabilities that we're perfecting in mobile phones are directly applicable to wearables, automotive, home over time.

It's not, none of those are explosive near-term opportunities for us. We've said that we don't expect wearables to be a huge component of our revenue anytime soon. But we do see those as very good ways to leverage the investment we've made in mobile phones into other markets going forward. And these are markets that we're well engaged in today.

We sell Audio D/A Converters, codecs, you name it across the whole array of audio applications. Automotive is a great market for us. It's something that we think can grow rapidly in the long-run as functions again that were traditionally constrained high-end cars percolate down the whole of a manufacturers product line. Ford Sync is a real good example of that.

So we see a lot of opportunity there. It's a market where again we're engaged with a lot of the market leaders. It's a market where people care about the fact that we've been around for 30 years and we can look serious when we're signing the contract that says we're going to sell a device for 10 years. They care about quality, they care about reliability and we've got a great reputation for both of those. We've got a very comprehensive product portfolio and we see a real good opportunity over time to migrate our DSP technology into sockets that traditionally we only served with say a simple D to A Converter and a A to D Converter.



So earlier this year, we were following a period of a number of years where it just, it didn't feel like there were that many customers that were heavily interested in differentiating on what we do especially well the voice and on audio signal processing. We were in a strategy meeting early in the year and looked at it as there was no possible way we could staff everything that we really want to go do.

So we made the difficult decision to focus a lot more resources that we're previously looking at energy on audio. So that we could accelerate some of our programs there. And it's still there was just no way to staff everything we wanted to do or hire quickly enough to do so. So we started talking to the Wolfson folks and that was really the synthesis of that where that acquisition came from. And it turns out that they had quite the same problem of course they were much, much smaller company.

So they had a challenge with their scale, but putting the two companies together, rationalizing the road map, so that we're not duplicating each other's work is something that we've been hard at work at since the acquisition closed. That's certainly freed up a fair amount of resources from competing with each other, but even combined the two companies, we were still having to prioritize a lot of the things that we want to do. So, but we have accelerated our roadmap. We're broadening out the smart codec roadmap rapidly.

We're investing more in MEMS microphones. So I think for Wolfson, the MEMS microphone effort was quite a challenge to fully fund. Fortunately Cirrus already had an effort started with a number of people looking at the ASIC portion of the microphone. So we're able to combine those efforts and invest a little bit more in microphones. So hopefully over time we'll establish ourselves as a supplier, a capable supplier of high volume microphones. Wolfson really just started shipping that product line late last year.

So we're still in the process of proving ourselves there. There's certainly a category of the market where we probably won't participate the long run. The very low end of the microphone market, but it's an area where if we can simply design our codecs and our microphones to work really well together. And we moved forward to an era where a phone might have three or four microphones per, well, if we can get those three or four microphones that are attached to our codec that will be a great start in that business.

And then broadening out the embedded software suite that we provide for our customers is another good angle. So we're participating in some really exciting market. We got a lot of great trends going for them. And we feel like we've got a number of advantages that no other supplier brings to the table. So looking real quickly at our financials. We've got a very healthy balance sheet. We did take on some debt to finance the acquisition about \$226 million. We still have a \$143 million as of the end of the last quarter in cash that is.

So obviously uses of cash, a number of them. We do, we have executed on buybacks in the past. Actually we repurchased little over half a million shares already this quarter following the market's reaction to what we view it as being good news on every front at our last earnings call. So we are looking at becoming a cash taxpayer towards after this year.

The great news, another great bit of the news on the Wolfson front is that, that gives us a large established base of operations in the UK. And so that certainly gives us potentially some avenues to get the tax rate a little bit lower than what we previously been expecting to see.

So we said on our earnings call, we expect to be for FY16 somewhere in the 30% total range maybe a little higher early in the year and a little lower later in the year as we're able to work through our operating structure and get that all [running out]. So we do generate a lot of cash. We consider a variety of uses of that obviously acquisitions being one of them. I'm fairly skeptical in general of acquisitions, a lot of them don't work out in our industry. But every once in a while, if you look hard enough you find one that works out very well and I think the Wolfson acquisition is definitely in that camp.

You can imagine that we'll make a priority of repaying the debt, paying that down we do like share repurchases that's one very efficient way to return cash to shareholders especially for a volatile stock as we sometimes are and as well we spend a lot of money improving the infrastructure. That's a photo there of our new reliability and quality lab in Austin. I don't think there is another company our size that has a facility like that. That enables us to really make our customers confident that we're not going to have any quality and reliability problems for them.



So expense profile, it's a big jump up in R&D portion of our OpEx, obviously associated with the Wolfson opportunity or the Wolfson acquisition. We see that as a really great opportunity for us as we're spending more in R&D in audio than anybody else out there and as I've been talking about, it's for a great opportunity.

Our target over the long run is a 20% operating profit so that's an annualized number. Obviously, we're in a very cyclical industry, we can't manage our business on a quarter-to-quarter basis. We take a very long-term view of the industry, but we do take -- we do believe strongly that we need to remain in that 20% operating category.

So guidance for the December quarter, \$265 million to \$285 million. Margins I think there is a little bit of confusion on that as associated with the acquisition, purchase accounting requires us to write up their inventory to the full resale price and then when we sell that inventory out, it sells out at zero margin. So we reflect that difference in the GAAP to non-GAAP difference in the margins. But our business ex that accounting factor should be right in line with the guidance we've been giving for some time on margins in the mid-40s, so nothing catastrophic to see there. So and for the accountants and the mix, I'm sure you'll enjoy reconciling our GAAP and non-GAAP numbers.

So any questions in the last four seconds? Yeah.

QUESTIONS AND ANSWERS

Unidentified Audience Member

Apple is not one of your customers, at least it wasn't on your chart at the beginning. What do you think you would have to do to break into that?

Jason Rhode - *Cirrus Logic, Inc. - President and CEO*

I suggest you read our filings.

Unidentified Audience Member

Say it again.

Jason Rhode - *Cirrus Logic, Inc. - President and CEO*

We don't talk about customers that don't like to be talked about. So we count as our largest customer, the most valuable customer in the market. They're a fairly dominant portion of our revenue.

Unidentified Audience Member

(inaudible).

Jason Rhode - *Cirrus Logic, Inc. - President and CEO*

Yes.



Unidentified Audience Member

Some of your competitors are looking to improve the link between MEMS microphones and gyroscope/accelerometers through software packages all in one systems on chips. Is that a source of threat to your business?

Jason Rhode - *Cirrus Logic, Inc. - President and CEO*

I think it's an opportunity. I definitely see there being opportunity to combine audio data in with the rest of a sensor fusion kind of a functionality. We've got a lot of MIPS sitting there ready to do that kind of processing. So we see that as a great opportunity for us going forward.

Unidentified Audience Member

(inaudible - microphone inaccessible)

Jason Rhode - *Cirrus Logic, Inc. - President and CEO*

Yes, absolutely. And frankly, as I mentioned, as the only company out there that currently supplies audio DSP, codec and microphones, we see if we optimize the microphones, together with the codec to work in a way that's better together than you could possibly achieve by buying the best microphone or the best codec separately. So we see that as a real opportunity in long-run as well.

All right, well thank you very much for your time and for your questions.

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