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SYNAPTICS – FIRST QUARTER, FISCAL 2023 CONFERENCE CALL
Prepared Comments

MUNJAL: SAFE HARBOR

Good afternoon and thank you for joining us today on Synaptics' first quarter, fiscal 2023 conference call. My name is Munjal Shah and I am the Head of Investor Relations. With me on today's call are Michael Hurlston, our President and CEO, and Dean Butler, our CFO. This call is also being broadcast live over the web and can be accessed from the investor relations section of the company's website at synaptics.com.

In addition to a supplemental slide presentation, we have also posted a copy of these prepared remarks on our investor relations website.

In addition to the Company's GAAP results, management will also provide supplementary results on a non-GAAP basis, which excludes share-based compensation, acquisition related costs, and certain other non-cash or recurring or non-recurring items. Please refer to the press release issued after market close today for a detailed reconciliation of GAAP and non-GAAP results, which can be accessed from the investor relations section of the company's website at synaptics.com.

Additionally, we would like to remind you that during the course of this conference call, Synaptics will make forward-looking statements. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance and business. Although Synaptics believes our estimates and assumptions to be reasonable, they are subject to a number of risks and uncertainties beyond our control and may prove to be inaccurate. Synaptics cautions that actual results may differ materially from any future performance suggested in the Company's forward-looking statements. We refer you to the Company's current and periodic reports filed with the SEC, including our most recent Annual Report on Form 10-K, for important risk factors that could cause actual results to differ materially from those contained in any forward-looking statement. Synaptics expressly disclaims any obligation to update this forward-looking information.

I will now turn the call over to Michael.

MICHAEL: BUSINESS OVERVIEW

Thanks, Munjal. I'd like to welcome everyone to today's call. We had solid results in our first fiscal quarter. Revenue increased 20% year-over-year and was slightly below the mid-point of our guidance due to weaker than anticipated sales into PCs. We maintained our profitability levels with GAAP and non-GAAP gross margin above the high-end of our guidance, benefitting from continued positive product mix in IoT. We delivered solid non-GAAP operating margin and our non-GAAP EPS was above the high-end of our guidance range.

Before providing our business update, let me highlight the macroeconomic challenges we are facing primarily due to a decline in global consumer spending. Never in my thirty-year career have I seen such an abrupt change in the demand environment with customers moving from shortage positions to excess inventory in the span of a few months. Given these macro uncertainties, customers are struggling to build confidence in their own forecasts and are instead focusing on depleting inventories. The challenges are most acute in our PC and smartphone businesses and in areas of the IoT portfolio that have consumer facing customers such as Virtual Reality headsets, wireless, and broadband operators. A large portion of the slowdown in IoT is due to an accumulation of inventory that we believe will correct over the next 2-3 quarters. The slowdown in our PC business is a combination of customers working through inventory and a reset of the TAM as we exit the pandemic. Meanwhile, our smartphone business has been affected by selling patterns greatly impacted by continued lockdowns and economic concerns in China.

Despite the macroeconomic headwinds, we grew our IoT business 67% year-over-year in the September quarter and had results in line with our prior guidance. Our Automotive products performed well and the long-term growth drivers for our Automotive products continue to be promising – the shift to electric vehicles, larger screen sizes, and increased adoption of integrated infotainment are all tailwinds for us. We have a strong pipeline of design-wins with nearly all major OEMs for center information displays and are gaining traction as the market conversion happens from discrete chipsets to our integrated solution. With increasing screen sizes, an additional semiconductor device is required to control timing between two or more TDDI devices. As these come online, our dollar content increases significantly.

Our video interface products continue to see tremendous new design activity as our customers develop new applications such as wireless docking. At the upcoming CES, we will be showcasing our wireless docking solution and we expect one or two marquee customers to have a similar product in their booths. In core docking applications, we are benefitting from growing attach rates and continue to win refreshed products. Our protocol adapter business is also gaining traction having won two new Intel reference platforms. Finally, we continue to successfully move into new applications such as networked displays, smart monitors, and conferencing systems.

In Wireless, our opportunities and design-wins are increasing. Our large customers, such as Amazon and Google, are releasing new Smart Home products based on our technology. We continue to benefit from the transition to Wi-Fi6 and 6E in IoT devices, which is on-going and still in its infancy. Customers are choosing Synaptics' solution for better power efficiency and higher throughput. We are shipping our wireless devices in Samsung's Matter-enabled Smart Home hub highlighting our competitive strength in the next-generation of products. Our wireless products for the security market are also gaining traction. The product ramps at ADT, which were launched last quarter, are doing very well. This quarter, we're proud to share that our focus on supporting the home security market has resulted in additional new wins with Verisure, Vivint, and others. Wireless connectivity is the right long-term secular opportunity for Synaptics and has become the glue that pulls together multiple pieces of our portfolio.

Finally, we continue to see more opportunities to cross-sell multiple technologies into different platforms across our customer base. For example, we are cross-selling our audio processors with video transport technology for docking applications. In UCC, two of the largest customers have introduced new VoIP phones utilizing 2-5 different devices from us. We have many opportunities like this in our near-term sales funnel and we continue to believe the ability to cross-sell will be a growth driver for Synaptics.

Let me move to our two non-IoT product groups. Despite the recent near-term volatility in the PC market, we see a path to demand stabilization during the upcoming calendar year. After several years, our customers are now looking to innovate this platform to improve user experience. Certainly, the use of haptics and force in the touch pads is driving additional content opportunity. Long term, we expect increasing video conferencing performance expectations on the laptop to unlock voice and video opportunity for us. In our smallest business, Mobile, we had forecasted a sequential decline in the September quarter and the customer pull was weaker than we originally predicted with an acute demand issue in China. As we look into the December quarter, we have several new handset launches that will likely drive marginal incremental demand, but we do not believe the underlying trends in the market have changed.

Now, let me update you on the Emza acquisition we announced last week. We acquired a small Israel-based team of engineers focused on algorithms for computer vision. The first application is for presence detection in PCs and the solution is already shipping at an existing Synaptics Tier-1 customer. We will offer the solution to additional PC customers, but also expect to sell into different areas such as automotive and smart home applications.

Before I conclude, let me share our perspective on our plans to navigate through this environment. Our customers have become cautious and there is inventory of varying degree in several pockets of the market. We are seeing requests for pushouts and cancellations of previously placed orders and we are working with customers to find a mutually beneficial solution. Our visibility into the macro issues is limited and unclear, but we believe the current quarter already reflects a material change in our business. Assuming there is no further economic deterioration, we believe the magnitude of change going forward will likely be small with a recovery and growth to resume in the second half of calendar 2023.

During this period, we plan to stay true to our capital allocation priorities. We will manage our expenses and prioritize money toward growth areas of the portfolio such as wireless and automotive. We will shift our inorganic focus to smaller, accretive tuck in acquisitions that seem to be coming on the market. With excess profits, we will continue our plan to buy back shares and paydown debt. By continuing to reshape our portfolio and focusing on internal execution, we expect to emerge from the current downturn as a stronger growth-driven company.

Let me now turn the call over to Dean to review our first quarter financial results and provide our outlook.

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DEAN: FINANCIAL RESULTS

Thanks Michael, and good afternoon to everyone.

I'll start with a review of our financial results for the recently completed quarter and then provide our current outlook. Revenue for the September quarter was $448.1 million, below the midpoint of our guidance due to weakness in the PC market. Revenue from IoT, PC, and Mobile were 76%, 15% and 9%, respectively.

Year-over-year, consolidated September quarter revenue was up 20%, as our IoT products continued to deliver strong growth. September quarter IoT product revenue grew 67% year-over-year and was up 3% sequentially despite the weakness in Virtual Reality we discussed in our last earnings call. Growth of IoT during the quarter was led by products for Automotive, Video Interface, and Wireless all growing strong double-digits year-over-year.

In PC, our September quarter revenue was down 20% sequentially and down 26% year-over-year, below our expectations due to a significant weakening of PC end demand and, as a result, an increase in inventory held by customers. Although commercial notebooks are not immune to economic downturns, we still expect Synaptics to outperform the overall PC market because of this higher commercial mix. As we look ahead, while demand visibility is limited, we expect PC market pressure to continue through mid-2023.

Our September quarter Mobile product revenue was down 36% sequentially and declined 49% year-over-year, lower than our prior expectations. Android based smartphone sell-through continues to be weak, prolonging the clearing of inventory. We expect the December quarter to marginally benefit from the ramp of several customer's new flagship products, but given the economic concerns in China, we expect this market to have a delayed recovery.

During the quarter, we had one customer greater than 10% of revenue, at approximately 13%, a distributor servicing multiple OEMs.

For the September quarter, our GAAP gross margin was a new company record at 57.1%, which includes $23.5 million of intangible asset amortization and $1.1 million of share-based compensation costs.

September quarter non-GAAP gross margin was also a new company record at 62.6% and above the high end of our guidance range driven by a 100 basis point benefit during the quarter, which is not likely to repeat, along with strong product mix.

GAAP operating expenses in the September quarter were $143.7 million, which includes share-based compensation of $31.5 million, acquisition related costs of $9.5 million consisting of intangibles amortization, and amortization of prepaid development costs of $2.5 million.

September quarter non-GAAP operating expenses of $100.2 million were down from the preceding quarter and below our guidance primarily due to lower than expected personnel related costs as we began to meter our hiring.

Our GAAP tax rate was 37.7% for the quarter, and non-GAAP tax rate was 17%. Both our GAAP and non-GAAP tax rates were impacted by tax law changes becoming effective in our fiscal 2023.

In the September quarter, we had GAAP net income of $64.6 million or GAAP net income of $1.59 per diluted share. Our non-GAAP net income in the September quarter was $143.1 million a decrease of 9% from the prior quarter and a 32% increase from the same quarter a year ago. Non-GAAP EPS per diluted share of $3.52, was above the high-end of our previous guidance range as strong gross margins and lower operating expenses flowed directly to the bottom line.

Now turning to the balance sheet.

We ended the quarter with $912 million of cash, cash equivalents, and short-term investments on hand; an increase of $36 million from the preceding quarter with cash flow from operations of $78 million, partially offset by $31 million of cash used for payroll taxes related to our equity compensation program and $13 million of cash used under our share repurchase program.

Cash paid for capital expenditures and depreciation for the quarter were both $6.2 million.

Receivables at the end of September were $284 million and days of sales outstanding were 57 days, down from 61 last quarter. Days of inventory were 96, above 82 days last quarter and ending inventory balance was $179 million as inventory turns have slowed. We are working with our supply partners to adjust to the current demand environment, but in the interim, we expect our inventory to increase again next quarter before beginning to bring the levels back down.

We restarted our share repurchase program in September and bought back approximately 120 thousand shares in the quarter for an aggregate cost of roughly $13 million. As we highlighted last quarter, with sufficient cash reserve 'dry-powder' available for tuck-in acquisitions, we plan to use excess cash flow toward the repayment of debt and share buybacks. We plan to continue to repurchase shares and at quarter end have $564 million available under our current authorization.

Now, let me turn to our December quarter outlook. As Michael mentioned, we are facing headwinds across our three product groups as customers have turned cautious with their orders. There are multiple requests from customers and channel partners for pushouts and cancellations of existing orders to reduce their inventory. As a result, we anticipate revenue for the December quarter to be in the range of $350 million to $380 million. A sequential decline of approximately 19% at the mid-point. We expect our revenue mix from IoT, PC, and Mobile products in the December quarter to be approximately 73%, 15% and 12%, respectively. Unless the macro economic environment further weakens, our expectation is that many of these customers will have depleted much of their inventory and be in a position to return to normal consumption levels by mid calendar 2023 and therefore resume growth in the second half.

We expect to maintain our strength in gross margins, with GAAP gross margin for the December quarter expected to be in the range of 53.0% to 56.0%. We expect non-GAAP gross margin in the range of 60% to 62%, which at the mid-point of 61% would be approximately 150 basis points higher than the same quarter one year ago.

We expect GAAP operating expenses in the December quarter to be in the range of $141 million to $146 million, which includes intangibles amortization, prepaid development cost amortization, and share-based compensation.

We expect non-GAAP operating expense in the December quarter to be in line with our September results and be in the range of $98 million to $102 million. We remain committed to funding our focus markets and technology roadmaps through these volatile times with an expectation of resuming our investment expansion as revenue growth resumes.

As a result, GAAP net income per diluted share for our December quarter is expected to be in the range of $0.55 to $0.85. And, non-GAAP net income per diluted share is anticipated to be in the range of $2.15 to $2.55 per share, on an estimated 40.5 million fully diluted shares.

We expect non-GAAP net interest expense to be approximately $8.5 million in the December quarter.

We expect our fiscal 2023 and long-term non-GAAP tax rate to remain in the range of 16 to 18%.

Lastly, we do not believe the newly imposed US Export controls has or will have any material effect on Synaptics' revenue or supply chain.

This wraps up our prepared remarks. I'd like to now turn the call over to the operator to start the Q&A session.

OPERATOR: Q&A

MICHAEL: FINAL REMARKS

I would like to thank all of you for joining us today. We look forward to speaking you at our upcoming investor conferences during the quarter.