



Himax Technologies, Inc. Q4 and FY 2016

Unaudited Financials and Investor Update Call

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Operator: Opening and standard introduction.

Greg Falesnik: Thank you, operator. Welcome everyone to Himax's fourth quarter 2016 earnings call. Joining us from the company are Mr. Jordan Wu, President and Chief Executive Officer, and Ms. Jackie Chang, Chief Financial Officer. After the

company's prepared comments, we have allocated time for questions in a Q&A session. If you have not yet received a copy of today's results release, please email greg.falesnik@mzgroup.us, or access the press release on financial portals, or download a copy from Himax's website at www.himax.com.tw.

Before we begin the formal remarks, I'd like to remind everyone that some of the statements in this conference call, including statements regarding expected future financial results and industry growth, are forward-looking statements that involve a number of risks and uncertainties that could cause actual events or results to differ materially from those described in this conference call. Factors that could cause actual results include, but are not limited to, general business and economic conditions, the state of the semiconductor industry; market acceptance and competitiveness of the driver and non-driver products developed by Himax; demand for end-use application products; the uncertainty of continued success in technological innovations; as well as other operational and market challenges and other risks described from time to time in the Company's SEC filings, including those risks identified in the section entitled "Risk Factors" in its Form 20-F for the year ended December 31, 2015 filed with SEC in April, 2016.

Except for the Company's full year of 2015 financials, which were provided in the Company's 20-F and filed with the SEC on April 13, 2016, the financial information included in this conference call is unaudited and consolidated, and prepared in accordance with US GAAP accounting. Such financial information is generated internally and has not been subjected to the same review and scrutiny, including internal auditing procedures and external audits by an independent auditor, to which

we subject our annual consolidated financial statements, and may vary materially from the audited consolidated financial information for the same period. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

I will now turn the call over to Mr. Wu. Jordan – the floor is yours.

Q4 & FY 2016 Results

Mr. Jordan Wu: Thank you Greg and thank you everybody for being with us for our earnings call, on which we will detail results from the fourth quarter and full year 2016, as well as provide our first quarter 2017 guidance and outlook. Our CFO, Jackie Chang, will give further specifics on our financial performance after my overview.

Our 2016 fourth quarter revenue, gross margin, GAAP and non-GAAP earnings per diluted ADS were as pre-announced on January 26th. For the fourth quarter, we reported net revenues of \$203.4 million, representing a 6.7% sequential decrease and in-line with our original guidance of a 4.0% to 9.0% sequential decline issued on November 10, 2016 while gross margin and EPS were below the guidance due to an additional inventory write-down. Gross margin for the quarter was 19.1% versus guidance of “slightly down” from 25.6% reported in the third quarter of 2016. The lower gross margin is the result of an additional one-time, non-cash inventory write-down totaling \$12.0 million. Excluding this additional inventory write-down, gross margin would have been 25.0% and met the guidance. The \$12.0 million inventory write-down is on top of the \$2.7 million original inventory write-off estimate for the

fourth quarter. In comparison, the inventory write-off amounts were \$2.5 million, \$3.0 million and \$2.5 million for the first, second and third quarter of 2016, respectively. The vast majority of the additional write-down was related to certain aged inventories of traditional human vision CMOS image sensors (“CIS”) with smaller amounts also covering driver IC and other products. Earlier in 2016, we decided to focus our CIS business on smart sensor, machine vision segments, as opposed to the traditional human vision segments. As part of this new strategic direction, we made a decision recently to expedite the sales of some aged inventories of human vision sensors. We believe it is appropriate that we write-down the inventory at this time, as we anticipate the need to offer discounted prices to accelerate the sales of some products and, for some other products where the potential revenues do not justify the efforts, stop the sales all together. Our new CIS strategy is backed by new products such as the Always-on-Sensor (AoS) and the structured light 3D depth scanning total solution, which offer unique and market leading features. The new strategy is also backed by close collaboration and intensive development activities with certain heavyweight partners and customers. I will elaborate further a bit later. Following this one-time write-down, we believe our inventory will be healthy across CIS, driver IC and all other product areas.

The impact to earnings per diluted ADS of the aforementioned inventory write-down is 6.0 cents. Following the write-down, GAAP earnings per diluted ADS was 2.6 cents, below the Company’s guided range of 8.5 to 11.0 cents. Non-GAAP earnings per diluted ADS was 2.8 cents, below the guided range of 8.7 to 11.2 cents. Excluding the additional inventory write-down, GAAP and Non-GAAP EPS would have been 8.6 cents and 8.8 cents, respectively, and met our original guidance.

The fourth quarter revenues of \$203.4 million represented a 6.7% sequential decrease and a 14.3% increase year-over-year. The sequential decline was a result of lower sales in our large panel driver IC business from a single customer's inventory adjustment, decreased smartphone sales due to the slowdown in China's smartphone market towards the end of the quarter, and a decrease in non-driver revenues for lower WLO and LCOS demand from our major AR customer. The combination of a few favorable factors across all our product lines led to the strong year-over-year growth: robust large panel driver IC sales benefiting from our leading market share in China, strong driver IC shipments for smartphone, tablet and automotive applications and growth in the AR/VR related business from our leading U.S. customer.

Revenue from large panel display drivers was \$67.7 million, down 6.0% sequentially, and up 9.0% from a year ago. Large panel driver ICs accounted for 33.3% of our total revenues for the fourth quarter, compared to 33.0% in the third quarter and 34.9% a year ago. The sequential decline was the outcome of one single customer's inventory adjustment. Nevertheless, our large panel products actually enjoyed 9.0% year-over-year growth thanks to strong demand from Chinese and Taiwanese panel customers during the quarter. In China, our driver IC business for large panel grew more than 10.0% year-over-year during the quarter. In comparison, worldwide large-size TFT-LCD panel shipments declined around 1.5% in the same period. It is especially worth highlighting that our engineering collaboration and design-in activities with large panel customers across China, Taiwan and Korea all remain robust and we expect these trends to continue into this year.

Revenue for small and medium-sized drivers came in at \$99.7 million, up 0.4% sequentially and up 21.8% from the same period last year. Driver ICs for small and medium-sized applications accounted for 49.0% of total sales for the fourth quarter, as compared to 45.5% in the third quarter and 46.0% a year ago. As opposed to original guidance of low single digit sequential growth, our small and medium-sized panel driver business grew just 0.4% because of lower-than-expected smartphone driver IC sales. Sales into smartphones, while increased close to 25.0% year-over-year, declined high-single-digits sequentially due to the slowdown in China's smartphone market starting around December. The strong growth of our smartphone driver IC business compared to the same year ago period came from our long-standing leading market share in China where our end brand customers were performing strongly. Our revenues from automotive applications also contributed to the segment and continued solid momentum, growing close to 10.0% during the fourth quarter, both sequentially and year-over-year.

Revenues from our non-driver businesses were \$36.0 million, down 22.9% sequentially and up 6.0% from the same period last year. Non-driver products accounted for 17.7% of total revenues, as compared to 21.5% in the third quarter and 19.1% a year ago. The sequential decline was primarily due to lower LCOS and WLO shipments for AR applications. As we highlighted in the last earnings call, a major AR customer asked that we reduce shipment for their current generation device to a minimum. To a lesser extent, lower sales of touch panel controllers and ASIC chips also contributed to the sequential decline. This decline was partially offset by the

increased sales of timing controllers and CMOS image sensors. It is worth noting that despite the near term headwinds, we remain positive on the long-term prospect of our WLO and LCOS product lines, judging by the expanding customer list that covers some of the world's biggest tech names, and the busy engineering activities going on with such customers right now. I will elaborate on this a bit later.

Our GAAP gross margin for the fourth quarter was 19.1%, down 650 basis points from 25.6% in the third quarter, and down 380 basis points from the same period last year. The decline was due to the aforementioned additional inventory write-down. Excluding the additional inventory write-down, gross margin would have been 25.0% for the quarter.

Jackie Chang, our CFO, will now provide more details on our financial results. After Jackie's presentation, we will further discuss our full year results, 2017 outlook and first quarter guidance.

Jackie.....

Ms. Jackie Chang: Thank you, Jordan. I will now provide additional details for our fourth quarter financial results.

GAAP operating expenses were \$32.1 million in the fourth quarter of 2016, down 20.7% from the preceding quarter and down 0.2% from a year ago. The sequential decrease was primarily the result of the difference in RSU charges. In accordance with our protocol, we grant annual RSUs to our staff at the end of September each

year, which, given all other items equal, leads to higher third quarter GAAP operating expenses compared to the other quarters of the year. The fourth quarter RSU expense was only \$0.2 million while it was \$9.2 million in the third quarter. Excluding the RSU expense, operating expenses increased 2.2% from the third quarter and decreased 0.1% year-over-year.

GAAP operating margin for the fourth quarter of 2016 was 3.4%, down from 4.8% for the same period last year and down from 7.0% in the third quarter. The GAAP operating income decreased 55.1% sequentially and 20.3% year-over-year. The sequential decrease was primarily a result of the aforementioned additional inventory write-down and lower sales, offset by the lower RSU expense.

Fourth quarter non-GAAP operating income, which excludes share-based compensation and acquisition-related charges, was \$7.4 million, or 3.6% of sales, down from 5.1% for the same period last year and down from 11.5% a quarter ago. The non-GAAP operating income decreased 70.7% sequentially and 19.3% from the same quarter in 2015. Excluding the aforementioned inventory write-down, non-GAAP operating margin would have been 9.5% for the quarter, as compared to 11.5% in the previous quarter.

Our GAAP net income for the fourth quarter was \$4.4 million, or 2.6 cents per diluted ADS, compared to \$13.6 million, or 7.9 cents per diluted ADS, in the previous quarter and GAAP net income of \$6.1 million, or 3.6 cents per diluted ADS, a year ago. GAAP net income decreased 27.6% year-over-year and 67.4% from the previous quarter.

Fourth quarter non-GAAP net income was \$4.8 million, or 2.8 cents per diluted ADS, compared to \$21.3 million last quarter and \$6.5 million the same period last year.

I will go through 2016 full year financial results and a balance sheet analysis a little later after Jordan's 2016 full year business review.

I will now turn the floor back to Jordan.

2016 Full Year Summary

Mr. Jordan Wu: Thank you, Jackie.

We delivered solid results to achieve both top and bottom line growth during 2016 as our driver and non-driver business segments both performed strongly.

We increased market share in our core driver IC business in 2016 and continued to solidify our leading position through technology advancement and customer engagement. Our large panel driver IC business grew from the added capacities from China and higher 4K TV penetration last year. In terms of small and medium sized driver ICs, our smartphone driver IC business rebounded well, reflecting our leading position in the Chinese smartphone market where demand was stimulated by the rising adoption of 4G network and our end brand customers performed strongly in 2016. Driver ICs for automotive applications, where we have a leading market share, continued its growth trajectory as more panels were going into vehicles.

We continued to lead the market in major new driver IC technology trends, including higher display resolution, AMOLED and in-cell TDDI. We collaborated closely with leading panel makers across China for AMOLED product development. On the TDDI front, we made volume shipments to a leading Chinese smartphone customer and were busy with design-in activities with Korean, Chinese and Taiwanese panel makers. Our non-driver businesses experienced tremendous growth during 2016, primarily driven by the LCOS and WLO businesses due to shipments to one of our leading AR device customers. We also made solid progress in new territories such as 3D depth scanning, IoT and machine vision with our latest CIS and WLO products, evidenced by more design-ins and engagements with certain heavyweight partners.

Now, we will have a quick overview of the 2016 full year financial performance. Our revenues totaled \$802.9 million in 2016, representing a 16.1% increase over 2015.

Revenues from large panel display drivers increased 21.6% year-over-year, representing 34.0% of our total revenues, as compared to 32.4% in 2015. Our large panel driver sales totaled \$272.9 million for the year. The strong year-over-year growth originated from our focus in China starting in 2012 and our efforts to achieve a more diversified customer base by adding new customers in Taiwan, China and Korea.

Small and medium-sized driver sales increased 9.8% year-over-year, representing 46.0% of our total revenues, as compared to 48.6% in 2015. Contributing to this growth was the strong momentum in driver ICs for smartphone and automotive

applications. We have the most comprehensive coverage of leading Chinese smartphone names and their fast growing market share has led to our good result last year. Automotive driver IC sales registered the strongest growth in this segment to increase about 26% year-over-year.

Non-driver products increased 22.6% year-over-year, representing 20.0% of our total sales, as compared to 19.0% a year ago. This growth was primarily due to higher LCOS and WLO shipments to a major AR customer during the year. Other product lines such as timing controller and ASIC also delivered strong growth, but offset by sales declines in CMOS and PMIC.

Gross margin in 2016 was 24.2%, a 60 basis-point increase from 23.6% in 2015. The increased gross margin was primarily due to a more favorable product mix in small and medium-sized driver ICs, increased LCOS and WLO shipments for AR applications and certain engineering fees from AR/VR new project engagements. The gross margin increase for the whole year was, however, offset substantially by the aforementioned inventory write-down. Gross margin improvement remains one of our business focuses.

Our GAAP net income for the year was \$50.9 million, or 29.5 cents per diluted ADS, up from \$25.2 million, or 14.6 cents per diluted ADS, in 2015. GAAP net income and GAAP earnings per diluted ADS grew 102.1% and 101.7% year-over-year, respectively. The increase in GAAP net income was a combination of higher revenue, improved gross margin, and a lower income tax, partially offset by higher operating expenses.

In August 2016, we paid an annual dividend of 13 cents per ADS, or 89.0% of 2015 GAAP earnings per diluted ADS. We remain committed to paying annual dividends, the amount of which is based primarily on our prior year's profitability. The high payout ratio in 2016 is an illustration of our confidence in our future profitability.

I will now ask Jackie to go through some details of our full year financial results.

Ms. Jackie Chang: Thanks again, Jordan. For 2016, our GAAP operating expenses were \$135.1 million, up \$2.6 million or 2.0% compared to last year.

GAAP operating income of \$59.2 million represented a 93.1% increase versus 2015. Non-GAAP net income for 2016 was \$59.7 million, or 34.7 cents per diluted ADS, up from \$30.6 million, or 17.8 cents per diluted ADS, for 2015. Non-GAAP net income and Non-GAAP earnings per diluted ADS grew 95.2% and 94.8% year-over-year, respectively.

Turning to our balance sheet, we had \$194.6 million of cash, cash equivalents and marketable securities as of the end of December 2016, compared to \$148.3 million at the same time last year and \$153.4 million a quarter ago. On top of the above cash position, restricted cash was \$138.2 million at the end of the quarter, up from \$138.0 million in the preceding quarter and down from \$180.4 million a year ago. The restricted cash is mainly used to guarantee the Company's short-term loan for the same amount. We continue to maintain a very strong balance sheet and remain a debt-free company.

Our inventories as of December 31, 2016 were \$149.7 million, down from \$171.4 million a year ago and down from \$169.4 million a quarter ago. Accounts receivable at the end of December 2016 were \$191.0 million as compared to \$177.2 million a year ago and \$208.4 million last quarter. DSO was 87 days at the end of December 2016, as compared to 93 days a year ago and 95 days at end of the last quarter.

Net cash inflow from operating activities for the fourth quarter was \$47.2 million as compared to an inflow of \$25.9 million for the same period last year and an inflow of \$2.9 million last quarter. Cumulative cash inflow from operations in 2016 was \$84.7 million as compared to \$22.5 million in 2015. The increase in cash inflow was a result of improved profitability and lower working capital.

Capital expenditures were \$2.2 million in the fourth quarter of 2016 versus \$3.6 million a year ago and \$1.9 million last quarter. The capital expenditure in the fourth quarter consisted mainly of purchases of R&D related equipment. Total capital expenditures for the year were \$7.9 million versus \$10.0 million a year ago.

As of December 31, 2016, Himax had 172.0 million ADS outstanding, unchanged from last quarter. On a fully diluted basis, the total ADS outstanding are 172.4 million.

I will now turn the floor back to Jordan.

Q1 2017 Outlook

Mr. Jordan Wu: Thank you, Jackie.

We are mindful that 2017 will likely be a year of macro uncertainty, marked by currency fluctuations and the risk of China's slowdown. However, looking into the new year, we believe our overall financial performance will be resilient to the potential macro headwinds. Particularly, following many years of R&D and investment, various areas of our non-driver IC businesses may start to contribute significantly to our overall financials.

Before we detail the prospect for our driver and non-driver businesses in 2017, we thought it's important that we update this year's CAPEX plan as its scale will be unprecedented in our history. Being a fabless company for our IC business, we have typically had a low annual CAPEX, as in the case of the last two years - \$10 million in 2015 and \$7.9 million in 2016. The regular CAPEX is primarily for the investment of design tools and testing equipment for our IC design business. This year's CAPEX plan will, however, include the construction of a new building, which we have announced before, and an increase of our WLO capacity, on top of the regular CAPEX. The new building, located nearby our current headquarters, will house the next generation LCOS and WLO production lines and provide the extra office space that is desperately needed as we already have to take up sizable leases outside to cope with the current office space shortage. The progress of the new building construction is in line with our plan as we have completed the design stage and are moving on to construction stage as we speak. More specifically, we have budgeted \$50.0 to \$55.0 million CAPEX for the new office/fab construction in 2017, covering land, building, facilities and clean rooms. The new building will be completed and

ready for personnel and equipment move-in by early 2018. The CAPEX budget for 2018 for the new building is around \$10.0 million. Now, let me move on to talk about the increase of our WLO capacity. To meet the strong demand of new customers for our WLO technology, we are accelerating our WLO capacity expansion. Rather than waiting for the new building to complete, we are now investing around \$25.0 million in new WLO capacity during the first half of 2017, to be located in the existing headquarter building by retrofitting certain areas for the new equipment. If everything goes as planned, we will see revenue and bottom-line contributions from the new WLO investment starting the second half of 2017.

The CAPEX budget for 2017 and the dividend for the year of 2016 will be funded through our internal resources and banking facilities.

With that, I will now provide our first quarter guidance, followed by a more detailed outlook.

Q1 Guidance:

The first quarter is traditionally the bottom of the year in terms of sales because it has fewer working days due to the Chinese New Year. The scale 5.6 earthquake that struck Tainan in early February also somehow impacted some of our customers' productions and therefore our driver IC shipment. We expect the first quarter revenues to be down 18.0% to 25.0% sequentially. Gross margin is expected to be around 23.0% to 24.0%, depending on our final product mix. GAAP earnings attributable to shareholders are expected to be in the range of 0.5 to 2.0 cents per diluted ADS based on 172.4 million outstanding ADSs.

In providing the above earnings guidance, we have assumed a 16.5% income tax rate for 2017, calculated based on exchange rate of NTD 31.0 against the USD, which is also the exchange rate as of beginning of February 2017.

Q1 2017 Outlook

Now let me provide you with some details behind our guidance and trends that we see developing in our businesses.

During 2017, we expect our **large panel driver IC** business will continue to benefit from continued increase of 4K TV penetration and, starting the second half of 2017, Chinese panel customers' ramping of a brand new Gen 8.5 and another Gen 8.6 fab. However, first quarter will see mid teen's sequential decline in our large panel driver IC revenue due to fewer working days in China and Taiwan and phase-out of certain customers' old models. Despite the temporary slowdown, our leadership in this segment stays strong. In our previous earnings calls, we mentioned that our large panel customers are increasingly demanding a total solution from IC vendors in addition to their constant request for better IC solutions to support their high-end and high-resolution products. We believe our technology strength and total solution capability are significant differentiators against most of our competitors and will further solidify our leading position as Chinese customers continue to expand their capacity and the industry further upgrades to 8K TVs. We are one of the pioneers in product development of 8K TVs with our Chinese and Korean panel customers and have already shipped small volume to a leading Korean panel maker.

The other segment within our driver business is ICs used in **small and medium-sized panels** for applications including smartphones, tablets and automotives. First quarter sales for smartphones are likely to decline by close to 45% sequentially on weak market, seasonality, customers' inventory adjustment for HD720 driver IC and less addressable market for smartphones using pure TFT-LCD driver ICs due to higher TDDI adoption rate. Compared to overall market, HD720 accounted for a relatively high percentage of our total smartphone driver IC shipment in 2016. Due to the panel supply shortage, most notably in the HD720 segment, in the second half of 2016, some of our China customers pulled in excess inventory of HD720 driver ICs and panels. Many of them have therefore substantially slowed down their new panel purchases in the first quarter. After customers' seasonal inventory adjustment, we expect the smartphone driver IC momentum to recover sequentially in the second quarter. We are mindful of the trend that higher in-cell panel and TDDI adoption rate will reduce the addressable market for smartphones using traditional TFT-LCD driver ICs. We are confident that our TDDI solutions and business will pick up soon. We will elaborate on this in the non-driver IC business discussion a bit later. On the AMOLED front, we have been collaborating closely with leading panel makers across China for AMOLED product development. With fewer competitors and higher barrier of entry, we believe AMOLED driver ICs will be one of the long-term growth engines for our small panel driver IC business.

Among driver ICs used in small and medium-sized panels, the best-performing category in recent years has been automotives. We expect the category's Q1 revenue to be down high-single-digits sequentially and grow more than 15.0% year-over-year. With leading market share and numerous tier 1 automobile brands as our

indirect end customers, we have successfully engaged all key panel manufacturers and module houses worldwide for long-term partnerships and secured many of their key projects pipelined for the next few years. To address the growing demand of larger automotive displays with higher resolution and built-in on-cell or in-cell touch screen features, we continue to develop advanced solutions to enable new automotive display applications and provide our customers with the most comprehensive and state-of-the-art solutions in the industry. As such, we are well positioned to take advantage of the growing automotive display market and anticipate the strong growth will likely continue into the next few years. However, our driver ICs used in tablets will decline close to 40.0% sequentially for slow season. Overall, we expect the small and medium-sized driver IC segment to decrease sequentially by around 30.0% in the first quarter.

For the **non-driver IC** business segments, we anticipate near-term headwinds as we mentioned in the previous earnings call and expect about high teen's sequential decline in our non-driver revenues for the first quarter. Sales of CMOS image sensors will deliver strong growth in the first quarter, but those of WLO, LCOS micro displays and touch panel controllers will decline sequentially. I will now highlight some of the non-driver product lines.

First on the touch panel controller product line. On top of several projects entering volume shipment featuring our on-cell solution, we continue to secure new design-wins from Chinese smartphone brand customers for their 2017 models. We have also seen significant traction in customer adoption and design-wins of our discrete touch solutions to break into several leading Chinese and international end brand

customers with new models to enter mass production from the first quarter of 2017. On TDDI, we are seeing rapid adoption of in-cell displays among smartphone brand customers for their new generation mid-to-high end models recently and expect TDDI to continue to expand in the smartphone and tablet market in next few years. We have comprehensive design-in activities with Korean, Chinese and Taiwanese panel and end product customers. We are also aggressively developing new products and strengthening our team to expand our product portfolio and roadmap. With very comprehensive joint development engagements covering many leading panel makers, we are confident that we can leverage our long-standing and widespread relationships with panel makers to increase our market share in TDDI. TDDI is a major long-term growth engine for our small panel business and will contribute to our business starting the second half of 2017.

I will now turn to the LCOS product line. As we warned in the last earnings call, we expect our LCOS sales to decline in the first quarter, as well as over the next few quarters in 2017, because one of our leading AR device customers decided to reduce shipment of their current generation device to a minimum, and instead, to focus on the development of future generation devices which we are still a critical part of. While the revenues for LCOS may subside over the next few quarters, they will come from a much more diversified customer base in 2017. Quite a few of our other customers are expected to launch their AR products starting 2017, although we are still uncertain of their volume potential given that they are still early generation products. Having invested in related technologies for over 15 years, we are uniquely positioned as the provider of choice for micro display and related optics, both of which critical enablers to AR devices. With little competition, we are currently working

with over 30 customers on various current and future generation AR devices using LCOS micro display. Our increasing design engagements cover not only leading tech companies, but also niche AR players which bring in innovative product ideas.

Switching gear to WLO, as in the case of LCOS that we just mentioned, we expect the near term business prospect to be affected by the reduced shipment of a major AR customer. However, we continue to partner with numerous industry leading companies using our cutting edge and industry-dominant WLO technology. In addition to AR application, our WLO technology is adopted by our customers to enable new things such as 3D depth scanning and machine vision, which can in turn be used in a wide variety of industries such as consumer, industrial, IoT, AI, medical, automotive, military and surveillance. Our customer base for this business is extremely diversified, covering numerous major tech names throughout the world, many of which leading end brand players or semiconductor platform solution providers. Himax is one of the very few players in the market with WLO technology and the one possessing the best mass production proven track record with expertise ranging from design and high yield production to cost and quality controls. We are very happy with our current development and business progress in this area. As mentioned earlier, given the aforementioned exciting growth opportunities, we are accelerating our WLO capacity expansion to meet strong customer demand in the near term.

Earlier in 2016, we decided to switch our strategy of the CIS business to focus on smart sensor and machine vision segments, as opposed to the traditional human vision sensors. We have launched two smart sensor product lines, i.e., near infrared

("NIR") sensor and Always-on-Sensor ("AoS"). We continue to make great business progress with these two smart sensor products. In addition to close collaboration and intensive development activities with certain heavyweight partners and customers, our smart sensors have garnered lots of customers' interests during the recent demonstrations at CES and the Japan Auto Expo.

By combining a NIR sensor and a structured light projector consisting of a laser diode and DOE with collimator fabricated using our WLO technology, we are offering the most effective 3D depth scanning total solution with the industry's smallest form factor to enable easy integration into next generation smartphones and other consumer electronics devices such as AR/VR. We are targeting to work with our partners to have the structured light 3D depth scanning total solution embedded in next-generation smartphones in 2017. We also attracted heavyweight potential customers' interest following the recent press release of our NIR sensor for its outstanding technical performance. With regards to our AoS product, the sensor can be bundled with our WLO lens to support super low power computer vision to enable new applications across a very wide variety of industries. After recent demonstrations at CES and the Japan Auto Expo, our AoS has gained significant customer interests especially in smart home, industrial IoT and surveillance applications. In a recent joint-press release with CEVA Inc. and Emza Visual Sense Ltd., we announced the industry's first intelligent always-on visual sensor specifically designed to overcome the power and cost constraints of vision processing for IoT applications. The ultra-low power, always-on vision sensor is a powerful solution capable of detecting, tracking and recognizing its environment in an extremely efficient manner using a few milliwatts of power. As our long-term goal is to provide complete solutions for always-

on computer vision applications, we decided to form a strategic alliance with Emza, an Israeli company dedicated to developing extremely efficient machine vision algorithms that enable smart IoT visual sensors. We will report business developments in these new territories in due course. Lastly, for the traditional human vision segments, we maintain a leading position in laptop applications and expect mass production of several design wins for notebooks and increased shipments for multimedia applications such as surveillance, drones, home appliances, and consumer electronics, among others, during the first quarter.

In summary, we are seeing weak seasonality and market demand in the driver IC business, which will lead to sequential revenue decline in the first quarter. We also expect our gross margin to be under pressure in the short term due to continuous pricing pressure and less favorable product mix of driver IC products, lower revenues from high-margin AR/VR related businesses and lower NRE income. Nevertheless, after many years of R&D and product development, we may see significant business progress in our non-driver business to contribute to both top and bottom lines out of WLO and CIS areas as early as the second half of 2017.

Thank you for your interest in Himax. We are now ready to take questions.

OPERATOR TO QUEUE QUESTIONS

Jordan's closing remarks

As a final note, Jackie Chang, our CFO, will maintain investor marketing activities and attend future investor conferences. We will announce the details as they come about. Please contact our IR department and/or Greg Falesnik if you are interested in speaking with the management. Thank you and have a nice day!