Himax Technologies, Inc. Q3 2019 Unaudited Financials and Investor Update Call

Conference Details: Conference Topic: Himax Technologies, Inc. Third Quarter 2019 Earnings Conference Call Conference ID: 5086829 Date of call: 11/7/2019 Time of call: 08:00 a.m. EST Pre-Record Message: No Moderator: Maili Bergman	**Participant Dial-In Numbers:** TOLL-FREE: (866) 444-9147 TOLL/INTERNATIONAL: (678) 509-7569 CONFERENCE ID: 5086829
Moderator/Speaker Dial-In Numbers (for Maili Bergman, Jordan Wu, Jackie Chang and Ophelia Lin): Leader Dial in (toll free) (855) 842-5904 Leader Dial in (international) (720) 634-2980 Conference ID number: 5086829 **Direct URL to Live Call Console** http://www.leaderview.com/leaderview/la.jsp Conference ID number: 5086829 Web PIN: 1069	**Replay Dial-In Numbers:** TOLL-FREE: (855) 859-2056 TOLL/INTERNATIONAL: (404) 537-3406 From: 11/7/2019 at 11:30 am EST To: 11/15/2019 at 11:30 am EST Replay Pin Number: 5086829

Operator: Opening and standard introduction.

Maili Bergman: Welcome everyone to Himax's Third Quarter 2019 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 HIMX@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 events or results to differ materially from those described in this conference call 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, 2018 filed with the SEC in March, 2019.

Except for the Company's full year of 2018 financials, which were provided in the Company's 20-F and filed with the SEC on March 28, 2019, the financial information included in this conference call is unaudited and consolidated and prepared in accordance with IFRS 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 Ms. Jackie Chang. The floor is yours.

Q3 Results

Ms. Jackie Chang: Thank you Maili and thank you everybody for joining us. In today's call, we will first review the Himax consolidated financial performance for the third quarter, followed by the fourth quarter 2019 outlook. Jordan will then give an update on the status of our business, after which we will take questions. We will review our financials on both IFRS and non-IFRS basis. The non-IFRS financials exclude share-based compensation and acquisition-related charges.

Our third quarter 2019 revenues, gross margin and EPS all met our guidance issued on August 8th. For the third quarter, we recorded net revenues of $164.3 million, a decrease of 3.0% sequentially and a decrease of 12.8% year-over-year. The sequential decline was mainly due to the anticipated lower sales into TV and smartphone segments. Gross margin was flat sequentially at 19.5%. IFRS loss per diluted ADS was 4.2 cents. Non-IFRS loss per diluted ADS was 4.0 cents.

Revenue from large display drivers was $50.1 million, down 15.6% sequentially, and down 24.5% year-over-year. Clouded by panel makers' ongoing inventory correction driven by weak TV demand and industry-wide oversupply, our large panel driver ICs continued to experience lower shipments and pricing erosion in the third quarter. Large panel driver ICs

accounted for 30.5% of our total revenues for the quarter, compared to 35.0% in the second quarter of 2019 and 35.2% a year ago.

Revenue for small and medium-sized display drivers came in at $77.1 million, down 5.6% sequentially and down 9.2% year-over-year. The segment accounted for 46.9% of total sales for the third quarter, as compared to 48.3% in the second quarter of 2019 and 45.1% a year ago. The sequential revenue decrease was mainly due to lower smartphone TDDI and tablet sales, while automotive segment recorded better-than-expected sales. The year-over-year decline was mainly due to lower automotive and tablet driver IC sales. Automotive sales worldwide declined sharply since Q4 2018 over worries of economic slowdown and trade conflicts.

Sales into smartphones were down 7.7% sequentially but up 32.8% year-over-year. The sequential decline was mainly due to lower TDDI shipments. As indicated in the last quarter's earnings call, our TDDI sales were challenged by accelerating AMOLED display adoption and rapid ASP erosion caused by increased competition. On a year-over-year basis, our TDDI shipment doubled as our fulfillment was capped last year by capacity constraint. Sales of the traditional DDICs declined by 1.9% sequentially but increased 6.4% from last year. Display drivers for tablet and other consumer products were down 16.1% sequentially, better than our guidance of decrease by around 25%, because of customers' inventory replenishment and more sales into white-box market on the backdrop of a shrinking global tablet market. Year-over-year sales of this segment declined 33.9%.

Our driver IC revenue for the automotive application was up 6.1% sequentially. It was down 19.7% from the same period last year due to the declining auto shipments for the reasons stated earlier.

Revenues from our non-driver businesses were $37.1 million, up 31.1% sequentially and flat year-over-year. Non-driver products accounted for 22.6% of total revenues, as compared to 16.7% in the second quarter of 2019 and 19.7% a year ago. The sequential increase was mainly due to higher WLO and CMOS image sensor shipments, offset by lower timing controller sales.

Gross margin for the third quarter was 19.5%, flat sequentially but down 390 basis points from the same period last year. The year-over-year decline can largely be attributed to smartphone TDDI ASP erosion due to increased competition and significantly more shipments of TDDI for the low-end market. Moreover, our large panel driver IC businesses continued to experience pricing pressure caused by industry-wide TV panel oversupply and high material cost. Nevertheless, the gross margin of the WLO business improved from the same period last year because the increased shipments to an anchor customer have led to higher capacity utilization. Likewise, on sequential basis, the gross margin improvement delivered by more WLO shipments was offset by the slowdown in sales and downward price trends for smartphone TDDI and LDDIC.

Our IFRS operating expenses were $39.7 million in the third quarter, up 2.0% from the preceding quarter but down 8.5% from a year ago. The sequential increase was caused by increased salary expenses. The year-over-year decrease was mainly a result of reduced restricted share units (RSU) as we did not issue RSU like we did in previous years.

RSU is part of our share-based compensation which we usually reward employees at the end of each September. Non-IFRS operating expenses for the third quarter were $39.3 million, up 2.3% from the previous quarter and up 1.2% from the same quarter 2018.

On September 23, 2019, Himax's compensation committee approved an employee stock option plan of up to 3,000,000 units for the same number of Himax ADSs with exercise price being the fair market value of the grant date. On September 30, 2019, we granted 2,226,690 units of stock option to certain employees at an exercise price of $2.27. The remaining 773,310 units of stock option can be granted to employees by September 6, 2022 when the current long-term incentive plan will expire. For the portion which has been granted, we expect to recognize stock option related compensation expense of $0.33 million in each of Q4 2019 and Q1 2020, and additional $0.12 million in each of Q2 and Q3 2020.

IFRS operating margin for the third quarter was -4.7%, down from 0.4% in the same period last year and down from -3.5% in the prior quarter. The sequential decrease was primarily a result of lower sales and higher operating expenses. The year-over-year decline was a result of lower sales and gross margin, offset by lower operating expenses due to reduced RSU expenses as mentioned earlier.

Third quarter non-IFRS operating loss was $7.3 million, or -4.4% of sales, versus non-IFRS operating income of $5.4 million, or 2.9% of sales, for the same period last year and down from -3.2% a quarter ago. The sequential and year-over-year declines were for the same reasons stated above.

IFRS loss for the third quarter was $7.2 million, or 4.2 cents per diluted ADS, compared to loss of $5.2 million, or 3.0 cents per diluted ADS, in the previous quarter and IFRS profit of $0.9 million, or 0.5 cents per diluted ADS, a year ago.

Third quarter non-IFRS loss was $6.9 million, or 4.0 cents per diluted ADS, compared to non-IFRS loss of $4.8 million, or 2.8 cents per diluted ADS last quarter and non-IFRS profit of $4.5 million, or 2.6 cents per diluted ADS the same period last year.

Turning to the balance sheet, we had $128.0 million of cash, cash equivalents and other financial assets as of the end of September 2019, compared to $102.9 million at the same time last year and $122.4 million a quarter ago. The cash position increased $5.6 million from last quarter due primarily to operating cash inflow of $24.0 million and additional unsecured borrowings of $13.6 million, offset by a capex of $31.2 million. On top of the cash position, restricted cash was $164.0 million at the end of the quarter, almost the same as the preceding quarter and a year ago. The restricted cash is mainly used to guarantee the secured short-term borrowing for the same amount. We had $90.6 million unsecured short-term loan at the end of Q3 versus $77 million a quarter ago.

Our inventories as of September 30, 2019 were $167.6 million, down from $188.5 million a quarter ago but up from $145.8 million a year ago. Accounts receivable at the end of September 2019 were $157.3 million, down from $176.2 million last quarter and $187.6 million a year ago. DSO was 86 days at the end of September 2019, as compared to 96 days a year ago and 96 days at the end of the last quarter. As highlighted in the last earnings calls, in response to capacity shortage of foundry and certain packaging material, we had to keep the inventory level higher than usual last year. Given the prevailing

uncertain market conditions and easing of foundry capacity, we have started to control our inventory level since the first quarter of 2019.

Net cash inflow from operating activities for the third quarter was $24.0 million as compared to an inflow of $2.2 million for the same period last year and an outflow of $17.7 million last quarter. The QoQ and YoY cash flow change was mainly a result of lower receivables and inventory.

Third quarter capital expenditures amounted to $31.2 million, versus $8.2 million a year ago and $5.7 million last quarter. The majority of the third quarter capex, totaling $29.2 million, consisted of $27.5 million payment for land purchase, and ongoing payments for the new building's construction and WLO capacity expansion. The remaining $2.0 million was the investment in design tools and R&D related equipment for our traditional IC design business. By the end of Q3, we have concluded substantially all the capex payments for the new land, building and 3D sensing project with just $1.6 million left to be made in the fourth quarter.

As of September 30, 2019, Himax had 172.2 million ADS outstanding, little changed from last quarter. On a fully diluted basis, the total ADS outstanding are 172.6 million.

Q4 2019 Guidance:

For the fourth quarter, we expect revenue to be around flat sequentially. Gross margin is expected to be slightly up sequentially, depending on our final product mix. IFRS loss attributable to shareholders are expected to be in the range of around 3.0 to 4.5 cents per diluted ADS based on 172.6 million outstanding ADSs. Non-IFRS loss attributable to

shareholders are expected to be in the range of 2.7 to 4.2 cents per diluted ADS based on 172.6 million outstanding ADSs.

I will now turn the call over to Jordan.

2019 Outlook:

Mr. Jordan Wu:

Thank you, Jackie.

As I mentioned last quarter, 2019 has been a challenging year for Himax. Uncertainty in the global economy continues to overshadow the marketplace, where we are seeing waning demand in all industries that consume display. This, combined with the prevailing LCD industry capacity oversupply, has led to severe pricing pressure for panels which inevitably affected the sales and margin of display driver IC across all major product segments including TV, smartphone and automotive. As we look forward, although at this time we have limited visibility, we do not anticipate the business environment to improve in the near term. Our strategy is to focus on delivering P&L improvement by executing on the technologies we already developed for both driver IC and non-driver IC areas.

One of our major focus areas for business during 2019 has been TDDI for smartphone. This business was negatively impacted by the severe foundry capacity shortage that occurred during 2018 and resulted in our inability to meet customers' delivery requirements. Although the capacity constraint was resolved toward the end of 2018, the delay eliminated our ability to participate in major design-in opportunities that would have driven the

business in 2019. While we expect the 2019 smartphone TDDI sales to increase more than 40% against last year, the growth will be below the target we set for ourselves. Even the outlook for smartphone TDDI remain weak in Q4, we do anticipate a strong rebound for Q1 2020 and robust growth for 2020. I will elaborate on this in a few moments.

Now, let me give you update for some of our major business areas.

Display Driver IC Business

LDDIC

Let us start with the large-panel driver IC business update. The current market for television sales is weak, driving an overcapacity of LCD display. As a result, since our last earnings call in August, many large-panel makers have cut back their production output. The combination of weak TV sales, and reduced production output, as well as relatively high upstream material costs, has put pressure on driver IC demand, negatively impacting our results for the third quarter. For the fourth quarter, we expect business to remain flat sequentially for our large display driver IC segment. At this time, we are seeing continued concern in the industry over display capacity oversupply extending into 2020. Conversely, Himax and some of our major panel customers foresee a potential foundry capacity shortage of 8-inch silicon wafers for display driver ICs. Anticipating the 8-inch foundry capacity constraint, we have already prepared to provide 12-inch foundry capacity and backend packaging and testing to cover the potential 8-inch capacity shortfall for large panel driver ICs. We are working closely with panel customers as well as our foundry and backend partners to secure production plans for 2020. Our design project coverage is strong across all leading panel makers. This provides us with good ongoing opportunities for 2020.

SMDDIC

Now let's turn to the small and medium-sized display driver IC business, beginning with an update on our smartphone segment. As stated in previous earnings calls, in 2018, limited by capacity constraints, we chose to focus our shipments of smartphone TDDI to higher-end FHD+, as opposed to HD+, projects in an effort to yield higher revenue and better margin. As we entered 2019, equipped with our newly developed foundry capacity, we expected significant TDDI growth from these FHD+ projects during the second half of this year. Unfortunately, the strong growth from FHD+ projects we expected did not materialize due to accelerating adoption of AMOLED displays that, unlike TDDI displays, are able to take advantage of under-display fingerprint sensing technology. Facing the AMOLED competition, TDDI adoption is shifting more towards mid- to low-end models with HD+ resolution. Since we chose to focus on FHD+ in 2018, we passed on many HD+ opportunities and started 2019 with very low market share of HD+ solutions. As a result, we have not benefitted from the shift in the HD+ marketplace. The combined result was weaker than expected smartphone TDDI growth during the first nine months of 2019 and a muted outlook for the fourth quarter. That said, we expect to record more than 40% growth in this segment for the full-year 2019. Since these missteps we have worked hard to raise our visibility in the HD+ market and have already begun HD+ mass production with a top-tier end customer earlier this year. We have also expanded the HD+ coverage to further customers. Based on the current pipeline, our Q1 TDDI smartphone shipments will include significant amount of both FHD+ and HD+ products. We anticipate a strong rebound for Q1 2020 and robust growth for the whole of 2020. For the fourth quarter, we expect TDDI revenue to decline by more than 30% from the previous quarter.

Regarding TDDI for other applications, our solutions for tablet and automotive continue to make good progress. I will elaborate more a bit later. While we expect only small volume shipments in 2019, both represent better ASP and margin for our TDDI solutions long-term and the tablet products, in particular, are expected to deliver strong volume starting next year.

Our traditional discrete driver IC sales into smartphones posted a slight sequential decline for the third quarter, versus our original expectation of a substantial decline, due to a Chinese smartphone maker's delivery pull-in request. Despite this, we continue to see the traditional discrete driver ICs' addressable market being quickly replaced by TDDI and AMOLED in smartphone. We expect traditional discrete driver ICs for smartphone to decrease substantially in the fourth quarter of 2019.

Combining TDDI and discrete drivers, our Q4 sales into the smartphone market is expected to decrease by around 25% sequentially.

As discussed earlier, a major development we are seeing is increasing utilization of the OLED display for smartphone, triggered by growing AMOLED capacity and the under-display fingerprint technology which is only applicable in the AMOLED display for the time being. We have been collaborating closely with leading panel makers across China for AMOLED product development. While we do not expect revenue contribution anytime soon, we do believe AMOLED driver ICs will be one of the long-term growth engines for our small panel driver IC business.

In the automotive display segment, the slowing economy and rising concern over tariffs have caused subdued new car sales across all major markets, particularly in China. However, our automotive business delivered a modest sequential growth in the third quarter as reported earlier. We expect the positive momentum will carry into the fourth quarter, attributable to market share gains of a certain of our customers. Q4 sales for this segment will increase by more than 15% sequentially. Looking forward, the overall automobile display market is forecast to increase from 2020 onward as the number of displays per vehicle continues to rise. While we don't expect the same kind of growth that we enjoyed in the past several years, due to saturation in the automotive space, we believe that by capturing the demand for display specification upgrades we will deliver automotive sales growth going forward. The market is quickly shifting towards a number of new technologies including higher resolution, in-cell touch, slim border, giant pillar-to-pillar screens, local dimming for higher contrast, and plastic AMOLED for free form design, all of which play to our advantage in advanced automotive display technologies. We are working closely with major automotive panel makers and leading tier-1 vendors over all of the technologies mentioned above.

On tablet and consumer electronics businesses. Although the overall markets remain weak, we expect the tablet business to increase by around 35% in the fourth quarter mainly due to major earlier design-wins for high-end tablet going into mass production with a number of leading end customers. The design-wins include display driver IC with COF packaging for large-sized tablets with narrow borders and our world leading in-cell TDDI with active stylus functionality for tablet. Combining tablet and other consumer electronics businesses, we expect sales to increase by around 20% sequentially in the fourth quarter. The shipment momentum for these high-end design-wins will carry into next year.

For fourth-quarter, revenue for the small and medium-sized driver IC business is expected to be around flat sequentially.

Non-Driver Product Categories

Now let me share some of the progress we made on the non-driver IC businesses in the last quarter.

WLO

First on our WLO business. As anticipated, the third quarter WLO revenue increased substantially thanks to a pickup in shipments to fulfill an anchor customer's higher seasonal demand. The sequential shipment increase has led to higher capacity utilization, also resulting in positive contribution to our Q3 gross margin. Based on the customer's shipment forecast, we expect a slightly lower shipment volume sequentially in the fourth quarter.

3D Sensing

Next is 3D sensing business update. In the smartphone segment, we have advanced our WLO optics solution to cover both structured light and time-of-flight (ToF) 3D sensing. Separately, as I reported in the last earnings call, our structured light-based 3D sensing total solution business targeting Android smartphone's front-facing application was unsuccessful. We have since adjusted our structured light-based 3D sensing development to focus on applications for non-smartphone segments that require high level of depth accuracy. That the customer in non-smartphone segments almost always requires a total solution for 3D sensing also plays to our advantage. Looking at ToF-based 3D sensing solution for smartphone where our strategy is to provide WLO optics, we are seeing

increasing ToF adoption by smartphone makers for rear-side cameras to enable advanced photography, distance/dimension measurement and 3D depth information generation to enable AR. We are actively pursuing smartphone makers' ongoing ToF 3D sensing projects by teaming up with our ecosystem partners.

Our non-smartphone engagements have been focused on smart door lock and industrial automation segments. We are collaborating closely with industry-leading facial recognition algorithm and application processor partners to develop new 3D sensing applications for smart door lock and have started design-in projects with certain end customers. We are in the process of revamping the solution based on customers' technical requirements. Separately, we are working with partners who wish to take advantage of our 3D sensing know-how to automate traditional manufacturing, thereby improving efficiency and reducing cost. Our 3D solution for shoe factory automation production line, announced in August, has gained tractions among footwear OEMs, ODMs and machinery suppliers.

Ultra-low power smart sensing

Next on WiseEye, our AI-based ultra-low power smart sensing solution. The demand for battery-powered smart device with AI intelligent sensing is rapidly growing. Our total solution is built on Emza's unique AI-based algorithm, on top of Himax's proprietary computer vision processor and CMOS image sensor, all equipped with ultra-low power design. Currently laptop is the market of focus. Himax WiseEye 2.0 NB solution provides a 'laptop-ready' 3-in-1 RGB/IR/AI solution, respecting privacy while enhancing security for notebook users. The prototype we announced during Computex 2019 has been well received by leading CPU platform providers and laptop end customers who are now

actively evaluating the technology. We are expected to demo the mass production version on laptops at the 2020 CES.

In addition to providing a total solution for ultra-low power smart sensing, we also provide individual parts of the total solution separately to address the market's different needs. For example, the ultra-low power computer vision processor we developed as part of the WiseEye 2.0 NB solution can also be used for AIoT applications. The WiseEye WE-I Plus, the AI-enabled ASIC platform that we recently announced, can support popular machine learning frameworks for the system customer to develop a wide range of video and audio AI applications where power is a strict constraint and on-device memory is limited. Typical applications include smart home applications and surveillance systems.

CMOS Image Sensor

On CMOS image sensor business update. CMOS image sensor is another critical part of the WiseEye 2.0 NB solution I just mentioned. To support the lean camera design and high-quality image needed for laptops with thin bezels, we have made a 2-in-1 sensor that offers the duo capabilities of high quality HD image capturing and ultra-low-power, low resolution visual sensing in one single sensor, the industry's first with the innovative design. With this sensor, laptop makers can simplify their next generation product design and save costs by eliminating the need for an additional camera in their effort to offer context awareness for better user experience. In addition, our sensor has incorporated an RGB-IR design to enable Windows Hello facial recognition. The new CMOS sensor will be available by the end of 2019.

For the traditional human vision segments, we see strong demand in notebooks, where we are one of the market leaders, and increased shipments for multimedia applications such as car recorders, surveillance, drones, home appliances, and consumer electronics, among others. Additionally, we have seen increased shipments and new design-wins in the automotive segment covering before-market solutions such as surround view and rear-view camera.

LCOS

Lastly, on LCOS. We continue to focus on AR goggle devices and head-up-displays (HUD) for automotive. Our technology leadership and proven manufacturing expertise has made us a preferred partner for customers in both areas for their ongoing engineering projects. Separately, one of our customers has recently announced an advanced LiDAR solution that utilizes Himax's proven LCOS technology and tailor-made manufacturing service. This is another solid evidence of our leadership position in this complex emerging technology. LCOS represents a long-term growth driver for us.

For non-driver IC business, we expect revenue to decrease by around mid-single digits sequentially in the fourth quarter.

That concludes my report for this quarter. Thank you for your interest in Himax. We appreciate you joining today's call and 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 continue to attend investor conferences. We will announce the details as they come about. Thank you and have a nice day!