



## Himax Technologies, Inc. Q2 2020 Unaudited Financials and Investor Update Call

<p><b>Conference Details:</b>          Conference Topic: Himax Technologies, Inc. Second Quarter 2020 Earnings Conference Call          Conference ID: 4668914          Date of call: 8/6/2020          Time of call: 07:45 a.m. EDT          Pre-Record Message: No          Moderator: Mark Schwalenberg</p>	<p><b>Participant Dial-In Numbers:</b>          TOLL-FREE: (866) 444-9147          TOLL/INTERNATIONAL: (678) 509-7569          CONFERENCE ID: 4668914</p>
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**Operator:** Opening and standard introduction.

**Mark Schwalenberg:** Welcome everyone to Himax’s second Quarter 2020 Earnings Call. Joining us from the Company are Mr. Jordan Wu, President and Chief Executive Officer; Ms. Jessica Pan, Chief Financial Officer and Mr. Eric Li, Chief IR/PR 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](mailto:HIMX@mzgroup.us), access the press release on financial portals or download a copy from Himax's website at [www.himax.com.tw](http://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, 2019 filed with the SEC in March, 2020.

Except for the Company's full year of 2019 financials, which were provided in the Company's 20-F and filed with the SEC on March 25, 2020, 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 Mr. Eric Li. The floor is yours.

## **Q2 Results**

**Mr. Eric Li:** Thank you Mark and thank you everybody for joining us. My name is Eric Li and I am the new Chief IR/PR Officer. Joining me are Jordan Wu, our CEO, and Jessica Pan, our newly appointed CFO. On today's call, we will first review the Himax consolidated financial performance for the second quarter, followed by the third quarter 2020 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.

We pre-announced preliminary key financial results for the second quarter on July 6, 2020 with revenues, gross margin and EPS all exceeding the guidance issued on May 7, 2020. Today, our reported results for revenues, gross margin and EPS were all in line with the pre-announced results. For the second quarter, we recorded net revenues of \$187.0 million, an increase of 1.3% sequentially and an increase of 10.4% compared to the same period last year.

The 1.3% sequential increase of revenue exceeded our guidance of a slight decrease within 5% quarter-over-quarter. Higher demand of large display drivers for monitors and greater-than-expected shipment volume for both smartphone and tablet contributed to the better-than-

guided sales. Gross margin was 21.0%, exceeding the prior guidance of between 20.2% to 20.6% due to a more favorable product mix among large display products. IFRS profit per diluted ADS was 0.8 cents, exceeding our guidance of a loss of 1.5 cents to 0.5 cents. Strong sales, improved gross margin and lower-than-expected operating expenses contributed to the better-than-expected earnings results. Non-IFRS profit per diluted ADS was 1.0 cents, exceeding our guidance of a loss of 1.3 cents to 0.3 cents.

Revenue from large display drivers was \$59.5 million, down 3.1% sequentially and up 0.2% year-over-year. The sequential decline was driven by lower shipments into TVs due to weakness in the global TV market which was severely impacted by Covid-19 outbreak. TV segment revenues decreased 21.7% year-over-year. Offsetting the weakness in the TV segment was a surge in demand for telework and online education tools that spurred the sales in our monitor and notebook segments to an increase of around 60.0% year-over-year in Q2. Large panel driver ICs accounted for 31.8% of total revenues for the quarter, compared to 33.2% in the first quarter of 2020 and 35.0% a year ago.

Revenue for small and medium-sized display drivers was \$98.8 million, up 12.9% sequentially and 20.9% year-over-year. The sequential growth was driven primarily by tablet and smartphone sales but offset by a decrease in the automobile segment. The strong year-over-year growth was attributable to remarkable tablet sales, especially our TDDI products for tablet. The segment accounted for 52.8% of total sales for the quarter, compared to 47.4% in the first quarter of 2020 and 48.3% a year ago.

Sales into smartphones were up 10.9% sequentially but down 26.8% year-over-year. Our smartphone TDDI was up 69.0% sequentially and up 0.3% from the same period last year.

Strength in the smartphone TDDI segment reflected customers' aggressive new product launch plans with our TDDI solutions. We reported earlier that the launch of several customers' new smartphones with our TDDI solution inside were delayed because of the pandemic. Many of those projects started mass production in Q2, leading to the strong sequential growth. Sales of traditional DDICs for smartphone declined by 43.6% sequentially and were down 58.3% from same period last year. Our traditional DDIC, which represents just 26.3% of the smartphone segment in Q2, declined significantly, a trend that was expected as we have repeatedly reported that the traditional DDIC was quickly being replaced by TDDI and AMOLED for smartphone application. We expect to see a short-term spike of traditional DDIC demand for smartphone during the third quarter, arising from orders from certain brand customers. However, again, barring short-term fluctuations, we expect to see continuous declines in the traditional DDIC for smartphone.

The ongoing Covid-19 pandemic has eroded worldwide smartphone market demand with a more than 10.0% expected decline during 2020, according to several research institutes. Despite these challenging conditions, we expect to see strong smartphone TDDI sales in the second half of 2020 due to a more diversified customer base, strong product roadmap and enriched product portfolio.

As anticipated, boosted by the strong momentum in both traditional discrete driver IC and TDDI product lines, tablet was the best performing product category of all in Q2, up 55.1% sequentially and 174.8% year-over-year. It represented around 23.0% of our total sales in Q2. We expect this product segment to continue to grow in the second half as the overall market for tablet looks to remain robust thanks to work-from-home and online education demands. In addition, there is new demand for tablet TDDI, of which the sales were up 83.2% sequentially

in Q2, as in-cell touch display is quickly becoming a new mainstream for the Android tablet. Jordan will elaborate on the outlook of tablet TDDI in a few minutes.

Boosted by demands for remote work and education, the revenue of traditional discrete driver ICs for tablet delivered a more than 40.0% sequential growth and more than 70.0% year-over-year in the second quarter. Specifically, we shipped more of the higher ASP ICs with high resolution and CoF packaging for large-sized slim bezel tablets to certain leading brand names.

As expected, our driver IC revenue for the automotive application was down 15.2% sequentially as a result of global production and car sales coming to a sudden halt in most of the world. However, on a year-over-year basis, automotive driver IC revenue was up 0.1% despite the effects of the pandemic.

Second quarter revenue from our non-driver businesses was \$28.7 million, down 19.5% sequentially but up 1.7% year-over-year. The sequential decrease was mainly due to significant shipment reduction of the WLO product to an anchor customer and lower engineering fee income for other non-driver products. Offsetting the weakness in WLO, CMOS image sensors had a higher revenue contribution from notebook and IP camera applications for remote work and online education purposes. Non-driver products accounted for 15.4% of total revenues, as compared to 19.4% in the first quarter of 2020 and 16.7% a year ago.

Gross margin for the second quarter was 21.0%, down 170 basis points sequentially but up 150 basis points from the same period last year. The sequential decrease was caused by lower WLO shipment and weak automotive sales, two of our higher gross margin products. A decline in engineering fees received was also a factor behind the sequential decline. On a

year-over-year basis, it was up 1.5% mainly due to a more favorable product mix with more shipments of WLO and Tcon products.

Our IFRS operating expenses were \$37.6 million in the second quarter, up 0.9% from the preceding quarter but down 3.3% from a year ago. The year-over-year decrease was a result of decreased salary and travelling expenses. Non-IFRS operating expenses for the second quarter were \$37.2 million, up 1.4% from the previous quarter but down 3.2% from the same quarter in 2019.

IFRS operating margin for the second quarter was 0.9%, down from 2.5% in the prior quarter but up from -3.5% in the same period last year. The sequential decrease was mainly due to lower gross margin. The year-over-year improvement was primarily a result of higher sales, better gross margin and lower operating expenses. Second quarter non-IFRS operating profit was \$2.1 million, or 1.1% of sales, lower from non-IFRS operating profit of \$5.3 million, or 2.9% of sales last quarter, but up from -3.2% for the same period last year.

IFRS profit for the second quarter was \$1.4 million, or 0.8 cents per diluted ADS, compared to profit of \$3.3 million, or 1.9 cents per diluted ADS, in the previous quarter and loss of \$5.2 million, or 3.0 cents per diluted ADS, a year ago.

Second quarter non-IFRS profit was \$1.7 million, or 1.0 cents per diluted ADS, compared to non-IFRS profit of \$3.8 million, or 2.2 cents per diluted ADS last quarter and non-IFRS loss of \$4.8 million, or 2.8 cents per diluted ADS for the same period last year.

Turning to the balance sheet, we had \$107.1 million of cash, cash equivalents and other financial assets as of the end of June 2020, compared to \$122.4 million at the same time last year and \$126.6 million a quarter ago. The lower cash balance as of the end of the second quarter was mainly a result of a repayment of unsecured borrowings of \$9.4 million and an operating cash outflow of \$9.2 million during the quarter. On top of the cash position, restricted cash was \$164.0 million at the end of the quarter, 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 \$58.4 million of unsecured short-term loan as of the end of Q2, compared to \$67.9 million a quarter ago and \$77.0 million at the same time last year.

Accounts receivable at the end of June 2020 were \$206.1 million, up from \$186.7 million last quarter and \$176.2 million a year ago. DSO was 101 days at the end of quarter, as compared to 96 days a year ago and 92 days at the end of the last quarter.

Inventories as of June 30, 2020 were \$161.5 million, up from \$148.4 million last quarter but down from \$188.5 million a year ago. In response to an industry-wide foundry capacity shortage and in preparation for a strong Q3 forecast, we had to increase inventory levels during Q2. We believe our inventory position is healthy given the solid forecast and purchase orders received from customers. While we monitor our inventory carefully by working closely with our customers, we will continue to build up our inventory position aggressively in the foreseeable future given the prevailing severe foundry capacity shortage in the market place. We expect the inventory level to be significantly lower over the course of Q3, again, because of very tight foundry capacity and strong customer demands.

Net cash outflow from operating activities for the second quarter was \$9.2 million as compared to an outflow of \$17.7 million for the same period last year and an inflow of \$10.6 million last quarter. Net cash outflow was mainly caused by more aggressive inventory buildup.

Second quarter capital expenditures amounted to \$0.7 million, versus \$5.7 million a year ago and \$3.1 million last quarter. As reported in the last earnings call, the capex for both the new building construction and the 3D sensing capacity expansion were already concluded in the fourth quarter 2019. The second quarter capex was for R&D related equipment for our IC design business.

Before concluding my report of the second quarter results, I would like to provide an update on dividend. We typically make annual cash dividend payment at the middle of the year based on the prior year's profitability. Our Board of Directors has decided that we will not pay cash dividend in 2020. The decision was made with full consideration of Himax's 2019 financial results as well as 2020 operations and capital requirement.

As of June 30, 2020, Himax had 172.3 million ADS outstanding, little change from last quarter. On a fully diluted basis, the total number of ADS outstanding was 173.2 million.

**Q3 2020 Guidance:**

At this point, we expect to deliver strong growth for the third quarter. We see very good momentum in our smartphone TDDI business against the backdrop of a depressed global smartphone market. Our tablet ICs, both discrete driver and TDDI, made remarkable contributions to our first half results and are on track to carry the nice momentum into the

second half. We also foresee decent growth for the notebook, TV and Tcon products for the next quarter. However, third quarter growth will be constrained due to an industry-wide foundry shortage.

Similar to our usual practice before 2019, we will grant RSUs, rather than stock options, on September 30 this year for employees' share-based compensation. As a reminder, we did not grant RSUs last year. Rather, 2,226,690 units of stock option were granted to the team at an exercise price of \$2.27 last September. Our third quarter IFRS earnings per diluted ADS guidance has taken into account the expected 2020 RSU grant, which, subject to the Board approval, is now assumed to be around \$3.0 million, or 1.3 cents per diluted ADS, almost all of which will be vested and expensed immediately on September 30, the grant date. The grant of RSUs would lead to higher third quarter IFRS operating expenses compared to the other quarters of the year.

For the third quarter, we expect revenue to increase by around 20% sequentially. Gross margin is expected to be flat to slightly down from the second quarter, depending on our final product mix. IFRS profit attributable to shareholders is expected to be in the range of around 2.0 cents to 2.8 cents per fully diluted ADS. Non-IFRS profit attributable to shareholders is expected to be in the range of 3.5 cents to 4.3 cents per fully diluted ADS.

I will now turn the call over to Jordan. Jordan, the floor is yours.

### **Q3 2020 Outlook:**

Thank you, Eric. While Covid-19 does not look to be going away anytime soon, most countries have greatly eased lockdowns while still taking measures to contain the spread of the virus. Although the pandemic has brought major disruptions to the markets we operate in, many of our panel customers have been fast to react to the changing environment by quickly shifting their production to where the demands are. What that reflected in our business is the very strong sales for notebook and monitor markets in the first half with the momentum now switching to TV and smartphone, while tablet is set to stay robust throughout the whole year. While businesses have been largely reopened, a big part of the society still stays mostly at home with much of the activity being operated online. The “stay-at-home” economy has proven to benefit several consumer electronics markets to which we supply our products. Our demand visibility has therefore been much improved from the first half. However, as Eric mentioned earlier, the industry is going through a severe foundry capacity shortage right now which is limiting the growth in almost all of our businesses, especially the smartphone and tablet TDDI as well as CMOS image sensor products.

Separately, we are working towards capitalizing on our unique non-driver technologies where we have invested heavily in the last few years, notably 3D sensing for smartphone and smart door lock as well as ultralow power smart image sensing for products such as notebook, TV, doorbell and air conditioner. I will elaborate on these a bit later.

As indicated in our guidance, we now expect a strong top line growth for Q3. Our next goal is to improve our gross margin. This will be an important target for Q4 and next year.

Now let me take you through each of our major business areas.

## **Display Driver IC Business**

### **LDDIC**

Let us start with the large-panel driver IC business update. For the third quarter, we expect the large display driver IC revenue to decrease by high-single-digit sequentially mainly due to weak demand for monitor ICs where our customers are going through an inventory adjustment after two quarters of strong shipments. However, TV and notebook ICs are picking up momentum in Q3.

The TV market, our biggest large display sector, is experiencing a solid rebound lately with panel prices rising and set makers rushing in for inventory replenishment after quite a few sluggish quarters. For the third quarter, we expect to deliver low-teens growth for TV display driver both sequentially and year-over-year.

For the monitor segment, following a demand surge in the previous two quarters, we expect customers' inventory to correct, resulting in a sequential decrease in Q3. In the notebook segment, as we mentioned earlier, we see continuous demand fueled particularly by enterprise and e-learning as we approach the back to school season. Our businesses in the high-end monitor and new generation low power notebook products, where we are the market leader in DDICs and Tcon, will benefit significantly from these trends.

## **SMDDIC**

Now let's turn to the small and medium-sized display driver IC business, beginning with an update on our smartphone segment. Our TDDI product roadmap as well as new design-wins with end customers position Himax well to gain market share throughout 2020.

The pandemic has negatively weighed on both smartphone production and consumer demand. While 2020 remains a challenging year for the smartphone market, China is already gradually recovering and other countries are moving in the same direction. Based on the current pipeline, we expect to more than double our smartphone TDDI shipments during Q3 compared to the previous quarter.

The smartphone market continues to embrace new technologies, moving toward higher frame rate displays to enable better screen viewing and gaming experience. Our high frame rate products have been adopted by several top-tier customers and have begun mass production in Q2.

As discussed previously, a major development we are seeing in the marketplace is the increasing utilization of the OLED display for smartphone. This is due to expanded AMOLED capacity as well as increased demand for under-display fingerprint technology that is only available in the AMOLED display currently. We are encouraged by the progress we have made and are collaborating closely with leading panel makers across China for AMOLED product development.

Additionally, we have made good progress in wearable AMOLED display driver ICs with leading Chinese panel makers. We believe AMOLED driver ICs will soon become one of the major growth engines for our small panel driver IC business.

Turning to the tablet business, we expect our tablet ICs to be a major growth area throughout 2020 with a strong forecast for both discrete driver ICs and TDDI in the third quarter. Tablet demand is picking up significantly in the wake of the Covid-19 outbreak that is fueling remote work and learning. As mentioned in previous earnings calls, Himax pioneered the TDDI solution for tablet and is the dominant supplier for literally all leading Android brand names. Tablet TDDI, just two quarters into mass production, already accounted for around 37.0% of our tablet IC sales and, if looked at as a separate product category, represented almost 9.0% of our total revenues in Q2. We expect an increase of more than 20.0% sequentially for our tablet TDDI next quarter with the momentum to continue into Q4. Tablet in-cell TDDI offers the benefits of lower cost and a simplified supply chain and represents an easier manufacturing process for panel makers. For consumers, it offers a lighter weight, slimmer and more stylish design as well as improved touch accuracy with added option for active stylus.

Similar to smartphone, demand for traditional DDIC for tablet is also being eroded by in-cell TDDI but at a more moderate pace. For the tablet segment, we expect to deliver another sequential growth of low-teens with shipments to almost quadruple that of the same time last year. Again, this is thanks to the sudden surge of tablet demand arising from the pandemic and the new TDDI revenue that did not exist last year.

It is worth highlighting that, while the tablet market is smaller than smartphone, the ASP and number of units for TDDI in each tablet are both higher than those for smartphone.

Turning to the automotive sector, the global automobile sector has been badly hit by Covid-19 and the market outlook remains uncertain during the second half of 2020. Himax commands more than 30% of the global automotive DDIC market and inevitably this business is impacted by the slow overall demand. However, while the sequential revenue was down 15.2 % in Q2, revenue for the first half was still up 3.3% year-over-year. Our technology and leadership in the automotive display market has helped us continue to gain ground with customers. We expect to deliver a mid-single-digit sequential increase in the third quarter, and we will remain the leader in this market as the major developing trends have not changed amid short-term challenges.

Backed by our leading market position in new technologies for automotive display, we have a strong and positive long-term outlook for the automotive segment. We are the primary partner for most of the world's automotive panel makers to enable new technologies. Specifically, Himax has been selected by many leading tier-1 and OEMs for their upcoming first launches of vehicles using displays with TDDI technology. While we only expect a small volume of shipments in 2020, we anticipate meaningful full production shipments of automotive TDDI as we move into 2021.

For the third quarter, revenue for the small and medium-sized driver IC business is expected to increase by over 40.0% 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 the WLO business. The second quarter WLO revenue declined sequentially due to lower shipment to an anchor customer. The factory to which we usually ship this product was ordered to shut down temporarily by the local government as part of their disease containment measures. However, our shipments to the anchor customer recorded a nice growth compared to the same quarter last year. We continue to engage several strategic customers and/or partners to develop new projects for DOE, diffuser, and optical lens solutions for future generation products covering a wide range of different applications.

## **3D Sensing**

Next is an update on the 3D sensing business. In smart phone application, most customer inquiries and design projects are moving toward ToF 3D sensing for world-facing camera that features longer range and wider-angle coverage for AR, 3D modeling and gaming features. With ToF, we provide optical components and/or projectors which are critical in the performance of the whole ToF solution. In this business, we have partnerships with ToF sensor providers, laser vendors and smartphone makers and are engaged for various stages of product development for next generation smartphones.

For non-smartphone 3D-sensing engagements, we focus on smart door lock and payment system applications where we provide structured light-based 3D sensing total solutions. To broaden our market reach, we also offer our market-leading 3D decoder ASIC as an individual component for integration into others' systems. Through such partnerships, we are able to reach out to markets that we are not yet familiar with, such as industrial robotics and access control systems. 3D sensing remains one of the main growth drivers for us.

## **Ultralow power smart sensing**

Now switching gears to the WiseEye smart sensing solution. As I mentioned in the last earnings call, in order for our WiseEye technology to reach its maximum potential, we have adopted a flexible business model whereby, in addition to a total solution where we provide processor, image sensor and AI algorithm, we also offer those individually as key parts in order to address the market's different needs and widen our market coverage. For customers who own their own algorithm and wish to develop their own applications, we can provide our ultralowpower AI processor and image sensor without algorithm. The customer can piggyback on our technology and focus their effort on bringing AI to edge devices by transforming a wide range of sensor data, including video, sound, movement, gesture, among others, into actionable information, all with extremely low power consumption. For those customers/partners whose main business is to provide AI processors, we can offer our ultralow power image sensors without our AI processor and algorithm.

For the total solution offering, we launched a computer vision human detection NB solution which has been well recognized and is being incorporated into the next generation premium notebook models of key OEMs and ODMs. Our total solutions are also being integrated into a wide range of other applications such as TV, doorbell, door lock, air conditioner, etc. by engaging leading players in those industries. For the other type of business model where we only offer key parts, our strategy is to actively participate in the ecosystems led by the world's leading AI and cloud service providers. A recent illustration of this strategy is an announcement for the collaboration with Google whereby, running on Google's TensorFlow Lite for Microcontrollers kernel, we provided our AI processor with CNN (convolutional neural network) based SDK (software development kit) for developers to generate deep learning

inferences with video and voice commands data to boost overall system performance while consuming extremely low power. Being an official partner of Google's TensorFlow, we get to enjoy the enormous network of its ecosystem participants. Just over a month after the announcement, we are already receiving inquiries from large corporations and individual AI developers alike with application ideas covering a broad range of industries. We are very encouraged by the enthusiastic discussions about possible WiseEye applications that are taking place in various user groups for emerging AI market ideas. Last but not least, we are working closely with other leading AI and cloud service providers worldwide to incorporate WiseEye edge AI solution into their ecosystems, in an attempt to reach the broadest market coverage possible. We are extremely excited about these developments.

### **CMOS Image Sensor**

Now turning to our CMOS image sensor business update. Due to the accelerated adoption of work-from-home and online education, demand for our CMOS image sensor for notebook and IP camera will remain strong during the third quarter.

Our industry-first 2-in-1 CMOS image sensor has penetrated into the laptop ecosystem for the most stylish super slim bezel design with 3 types of popular application features, namely RGB sensor for video conference, RGB/IR sensor for Windows Hello facial recognition, and/or ultralow power AI computer vision for human presence detection. We expect to see small volume in certain premium notebook models in late 2020 with more volume expected in the coming years.

For the traditional human vision segments, we also see strong demand in multimedia applications such as car recorders, surveillance, drones, home appliances, and consumer electronics, among others.

## **LCOS**

Lastly, on LCOS. We continue to focus on AR goggle devices and head-up-displays (HUD) for automotive. Many of our industry-leading customers have demonstrated their state-of-the-art products, including holographic HUD, AR glasses and LiDAR system, with Himax LCOS technology inside. Our technology leadership and proven manufacturing expertise have made us a preferred partner for customers in these emerging markets and their ongoing engineering projects in AR goggles and HUD for automotive applications.

For non-driver IC business, we expect revenue to increase by low teens sequentially in the third 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, Eric Li, our Chief IR/PR Officer, 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!