

Ed FINAL
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Earnings Script Q4 FY '07

Good afternoon, everyone, and thanks for joining us. I will review some of the highlights of Q4 and our 2007 fiscal year, and review plans for the upcoming year. I will then turn the call over to Andy who will cover the details of our financial performance, and our guidance for Q1 2008.

We are proud of our many accomplishments during the last year.

First, we are pleased to report smartphone sell-through grew 34% to 2.7 million units for the year and now represents 80% of our total revenue, up from 69 percent last year. In the fourth quarter, our smartphone sell-through reached another record high at 750,000 units up 43% year over year.

Second, we launched several new smartphone products since last June and are excited about our recent launch of the Foleo. We strongly believe that this will be another major growth category for Palm, and the dawning of another major design era of mobile computing.

Finally, we believe our recently announced deal with Elevation Partners sets us up well to attract the world-class talent we are going to need to scale our business and to make the investments in our business for future expansion.

We are at the beginning of a major shift in the mobile communications market as users demand more and more capabilities and performance from their mobile products. Palm is committed to building the most compelling and intuitive mobile computing solutions in the world. This is going to take extraordinary focus, and all the dedicated efforts of our team. Fortunately, we have an excellent team with the experience and knowledge to deliver great solutions. And, with our recent announcement and expected closing of our transaction with Elevation Partners, we are going to add significantly to our strengths.

I am delighted that my team and I were able to bring the Elevation deal from concept to reality. Elevation will bring a group of partners with a unique perspective in the mobile device, online content and Web 2.0 arena. Jon Rubinstein will bring outstanding experience in small form factor device integration, and high volume product delivery capabilities with high quality standards. I am already consulting with Jon on the plan to build our product delivery capabilities and establish strengthened relationships with key companies in our industry. We expect to schedule our shareholder vote at the end of August or early September depending on various regulatory approvals. We spent several days meeting with investors and are very excited about the response we are getting to the announcement.

For the year ahead, we expect to continue to drive for great product execution and differentiation, and to build our intellectual property position and defensibility. These efforts will be combined with a relentless focus on continuous improvement on quality, our ability to reach more carriers and more geographies more quickly, and a strong drive for revenue growth and profitability.

As a part of our long-term planning, I recently made some changes to increase the effectiveness of our organization and drive our performance. I reorganized our team around two distinctive product lines. Our Windows Mobile products will be developed under a highly leveraged ODM model where we can take advantage of the strong capabilities of our ODM partners. These products will be designed and specified by our internal Windows Mobile group, but more execution of the products will be done in conjunction with our ODM partners using their Windows Mobile expertise and radio designed platform. We believe this will enable us to get a broader range of solutions to market faster, to leverage our brand and customer connections, and to deliver more compelling solutions for our medium-sized business and enterprise customers who are demanding Windows mobile-based solutions.

Our second major product group will be focused on building solutions for our consumer, prosumer and small business customers. This group will focus on leveraging our Palm system software efforts, our in-house hardware platform designs, and our services initiatives to create the most compelling end user solutions. Our goal is to deliver

the best, most flexible mobile computing solution, and one which we believe will prove to be more compelling than any other mobile consumer solution on the market.

Finally, as you may know, we have recently announced our Foleo mobile companion products. They will work in conjunction with, and in support of, both our Windows Mobile and Palm OS-based products. Foleo has had mixed reviews from the pundits, but an extremely enthusiastic response from potential customers. I am completely confident that we have redefined what it is to be a full function mobile computer. You can think about laptops today as the next generation desktops, desktops that you dock and can take with you, but they're still desktops with all the baggage and complexity of a heavy operating system and hardware computing environment. Foleo is the first mobile device designed from the ground up as a mobile computing solution focused on the true usage patterns and necessities of the mobile user. It's simple, instant on, instant application switching environment is based on a small hardware and cost footprint and we believe it's simple, solid state design will prove to be the fundamental design center of future mobile computers. Both the sophisticated and the novice user values simplicity, and that is the basis of Foleo – the most simplified, yet powerful computing solution for you on the go. Palm has defined two categories of mobile computing in the past, and Foleo is the third.

Foleo was designed with significant focus on our ability to develop the best software environment for user and developers. Some of our efforts on both future Treo platforms and for Foleo are already being supported by a broad range of developers, and we expect that support to continue to grow. So today, Foleo is a companion to your smartphone targeted squarely at robust email access, but tomorrow it will be a full fledged mobile computing platform with a broad range of application support. We are very excited about those possibilities, and so are our customers. We have already been approached by a wide range of customers from all walks of life dying to get their hands on Foleo. Enterprises want a more simplified solution for some of their knowledge workers that they can easily configure and update, educational institutions feel it truly could be the first, accessible computer from a cost and form factor standpoint. Vertical applications in the military, pharmaceuticals, utilities and other areas find a low

cost, small form factor, Linux-based alternative very attractive. And, of course, your average computer user who is frustrated and intimidated by the complexity of standard computing platforms finds it incredibly desirable. All of these will be opportunities for Foleo as the platform matures.

During the year ahead, we will also focus on efficiency and quality. As noted earlier, I've already begun the year by making changes to our organization that I believe will make us more effective in delivering our products to the market. I also recognize that we have to improve our efficiency as our R & D spending has continued to climb as a percentage of our revenue. We expect it to trend down during this fiscal year, but today, this investment is critical to delivering the kind of products necessary to compete and excel in this very competitive environment. I am incredibly excited about our future products, but to get there we have to make the critical investments, and we appreciate your support in making these investments. We believe our investments today will result in significant shareholder value creation in the future.

For our 2008 fiscal year, you can expect to see a number of major new product deliveries. Of course, the Foleo will be delivered, but also a range of smartphone products that will reach new customers and new demographics, as well as expand our carrier reach.

For this fiscal year we have set five core objectives, and we will track our progress throughout the year based on these objectives.

One, We expect to deliver revenue growth and profitability, with significant increases in our smartphone sell-through.

Two, We will deliver major new platforms on both the hardware and software fronts to increase our differentiation and build our defensibility.

Three, We will drive hard on improving quality, predictability and time to market while working to drive out costs throughout our supply chain

Four, We will do a better job of leveraging our ODM partners to more effectively scale our product line, and better leverage our Windows Mobile partnership with Microsoft.

Finally, we will establish Foleo as a new category in computing by creating and nurturing a strong developer community, expanding our distribution and delivering a world-class product experience.

Let me close by saying that we believe we have just thrown out the first pitch in a nine inning game. The shifts in the computing and communications markets are just beginning. We are energized by the opportunities that our expected partnership with Elevation Partners will bring to the game. Both we and Elevation are confident that Palm is in the beginning stages of one of the biggest market and growth opportunities in the history of technology. We are committed to building the most compelling and intuitive mobile computing products in the world and honoring your investment in us by delivering great long term shareholder value.

A big thanks to our team who has stayed focused and continues to deliver great mobile computing solutions, customer support and services to our customers. I know they are reenergized and totally focused on executing at an even higher level this year.

I'll now turn the call over to Andy to discuss the details of our Q4 and FY '07 results, and our guidance looking forward to Q1 of FY'08.

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Andy's Q4 script

Thanks, Ed, and good afternoon, everyone. Before I start, I would like to reiterate that all the commentary today is based on non-GAAP financial measures except where specifically identified as GAAP. I encourage you to refer to the reconciliation of GAAP to non-GAAP financial results that is posted to the Palm website and included with the press release.

Focusing on the full year's results, our revenue for fiscal 2007 declined 1% to \$1.56 billion from fiscal 2006. Fiscal 2007 gross margins increased to 37% from 33% in the year ago period, driven by reduced royalty costs and continued reduction of component costs. Our operating expenses increased year-over-year by 24% to \$477 million as we continued to invest in our product delivery engine and sales and marketing to expand our global presence and brand. This resulted in operating margin of 6.4% versus 8.6% in fiscal 2006 and diluted earnings per share of \$0.70 cents compared to \$0.85 cents in fiscal 2006.

Smartphone revenue grew 15% to \$1.25 billion on unit shipments of 2.7 million. Unit sell-through for smartphones grew 34% year-over-year to 2.7 million units while overall channel unit inventories remained flat. Smartphones represented 80% of our overall revenues in 2007 versus 69% in fiscal 2006. The growth in smartphones was more than offset by accelerated declines in the handheld business, where we experienced a 37% year-over-year decline in net revenue. Handheld units shipped declined 35% and handheld sell-through declined 31%, which accelerated in the 2nd half of the year to almost 40%. We expect our handheld business to continue to decline at similar rates as we move into fiscal 2008.

Looking more closely at Q4 of fiscal 2007, revenue was \$401.3 million, down slightly from \$403.1 million in Q4 fiscal 2006. During the quarter we saw record sell-through for smartphones offset by declines in the handheld business.

Gross margin for the quarter increased to 38.3% compared with 37.2% in the year ago period and 37.0% sequentially. Gross margin was positively impacted by an update to the redemption rate assumptions for our mail-in rebate reserves based on new data received from our carrier partners. Had this not occurred gross margins would have been approximately the same as Q3.

Operating expenses for the quarter were \$130.4 million, slightly higher than we had expected, primarily due to increased product development costs for future products and legal action settlement costs. This resulted in operating income of 5.8% of revenue and earnings per diluted share of \$0.17 cents.

Revenue mix for the quarter was 86% smartphones and 14% handhels, unchanged from the previous quarter.

Smartphone revenue for the fourth quarter was \$344.2 million on shipments of 730,000 units. Smartphone sell-through continued to be robust at a record 750,000 units. This represents a year-over-year increase of 43% as customers continue to make Treo their smartphone of choice.

Handheld revenue for the quarter was \$57.1 million a 43% decline year-over-year, reflecting sales of 298,000 units. Handheld sell-through for the quarter was 314,000 units, a 36% decline year-over-year and inventory held by our channel partners was 6.1 weeks.

In Q4 2007, we generated 76% of our revenues from the US and 24% internationally, substantially unchanged from the prior quarter.

Looking at the balance sheet, our cash and short-term investment balance increased from the prior quarter to \$546.7 million dollars. The cash balance does not include proceeds from the land sale which closed on June 20th, with net proceeds to the company of approximately \$64 million. Cash flow from operations was strong at \$42.9 million for the quarter and \$168.2 million for the full fiscal year. Accounts receivable decreased sequentially to \$204.3 million and DSOs were 46 days, in our expected range. Inventories increased sequentially to \$39.2 million dollars and turns decreased slightly to 26 times, also in our expected range.

Looking to Q1 fiscal 2008, I will be providing guidance assuming no changes for the recapitalization we expect to complete in August or September - once that occurs we may update guidance as appropriate. We currently expect revenue to be between \$355 million and \$365 million dollars. We expect sell-through for smartphones to have healthy year-over-year growth, with handholds declining at a similar rate to what we experienced in Q4 on a year-over-year basis. Factored into our outlook is the expected seasonal slowdown particularly in Europe and the uncertainty around competitive product launches.

We anticipate gross margin will be in the range of 37% to 37.5%, consistent with what we have seen in the 2nd half of fiscal 2007. We do however anticipate that gross margin will moderate during the year towards the 34% to 36% range as we introduce new products starting in fiscal Q2.

Operating expenses are expected to be in the range of \$125 million to \$128 million dollars, slightly lower than Q4 fiscal 2007, as we see savings from the recent changes we have made, particularly in the product development area. We expect that product development costs will remain relatively flat on a quarterly basis throughout the year as we leverage our ODM partners more effectively.

The annual tax rate for Q1 is expected to be 40% resulting in earnings per diluted share of \$0.07 to \$0.09 cents.

On a GAAP basis we expect a \$8.0 to \$9.0 million total charge to earnings for the recently implemented organizational changes, which will include severance and facility closure costs. Of this we expect \$6.5 to \$7.5 million will be incurred in Q1 with the remainder in Q2.

I will now turn the call over to the operator for your questions.