MANAGEMENT DISCUSSION SECTION

Operator: Thank you for standing by and welcome to the Texas Instruments second-quarter 2010 mid-quarter update conference call. Today's call is being recorded.

At this time, I would like to turn the conference over to Ron Slaymaker.

Ron Slaymaker, Vice President, Investor Relations

Good afternoon, and thank you for joining TI's mid-quarter financial update for the second quarter of 2010. In a moment, I will provide a short summary of TI's current expectations for the quarter, updating the revenue and EPS estimate ranges for the company. In general, I will not provide detailed information on revenue trends by segments or in markets, and I will not address details of profit margins. In our earnings release at the end of the quarter, we will provide this information.

As usual with our mid-quarter update we will not be taking follow-up calls this evening. Considering the limited information available at this point in the quarter and in consideration of everyone's time, we will limit this call to 30 minutes. For any of you who missed the release you can find it on our website at TI.com/ir. This call is broadcast live over the web and can be accessed through TI's website. A replay will be available through the web.

This call will include forward-looking statements that involve risks and uncertainties that could cause TI's results to differ materially from management's current expectations. We encourage you to review the Safe Harbor Statement contained in the news release published today as well as TI's most recent SEC filings for a more complete description.

We have revised our expected range for TI's revenue and earnings to the upper half of our previous ranges. We now expect TI revenue between 3.45 and $3.59 billion. This is a range of sequential growth of 8 to 12%. We expect earnings per share between $0.60 and $0.64.

Operator, you can now open the lines for questions. In order to provide as many of you as possible the opportunity to ask a question, please limit yourself to a single question. I will provide you the opportunity to ask a follow-up question. Dwayne?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] We'll first go to Tore Svanberg with Thomas Weisel Partners.

<Q – Tore Svanberg>: Thank you, Ron. I was hoping you could just talk a little bit also about all the dynamics like lead times, distribution, inventory, what you're seeing in the channel. If you could just add some color there, that would be great.

<A – Ron Slaymaker>: Okay, let's start with I guess distribution. In general, I guess we would expect strong resale or sales out of our distribution channel this quarter. From an inventory perspective, I guess I would just characterize that we believe distribution inventory remains lean by historical standards, similar to what you've seen more recently.

I believe your other question that you asked was with respect to lead times. And I guess as we've indicated recently, including at our analyst meeting, we're making good progress on bringing up our additional capacity. And so as a result, our lead times are being reduced and they're being reduced in an orderly manner. They're not as short as we want them yet. But I would say the capacity additions certainly have helped and will continue to help. Lead times are coming in. They're coming in because of higher levels of capacity, not because of any slowing of demand.

I guess another point I would make is that our customers are telling us that as we have reduced our lead times, in fact many of our competitors' lead times have been extending. So certainly that encourages us that our capacity additions have been both timely and frankly the right strategic move in an environment that is increasingly supply constrained. I guess just a final note on this one is that again, demand, whether you measure it by revenue or whether you measure it by orders, has remained strong in the quarter, even as we've reduced our lead times. Did you have a follow-on, Tore, or was that your follow-on?

<Q – Tore Svanberg>: I think that was great, Ron. I really appreciate it, thank you.

<A – Ron Slaymaker>: Okay, Tore, thank you and let's go to the next caller, please.

Operator: All right, the next question is from Doug Freedman with Gleacher & Company.

<Q – Doug Freedman>: Great. Thanks, guys, for taking my questions. Ron, can you talk a little bit about the end markets and are where you're seeing the most strength and maybe any signs of weakness that you're seeing regarding possible cancellations?

<A – Ron Slaymaker>: I would say in general, we're seeing pretty broad-based strength. So from an end market standpoint, I would say continuing the trend really that we talked about even in the first quarter, maybe even late 2009, industrial will probably be the strongest market this quarter, really reflecting that its recovery lagged some of the other market segments last year but has certainly been powerful in the first half of this year.

From a product line perspective, TI product areas that should benefit from the strength that we're seeing in industrial include areas like high-performance analog, the power analog products, as well as our catalog embedded processing products. Did you have a follow-on there, Doug?

<Q – Doug Freedman>: Yes, if I could. Have the European concerns and changing exchange rates had any impact on management's expectations or strategic plans?

<A – Ron Slaymaker>: Doug, I would say we are not seeing anything from Europe yet. So from a growth standpoint, core Europe is growing at about the same sequential pace as our overall revenue. Of course, we're being watchful, but we haven't seen any change yet in the demand out of our European region. Okay, Doug, thank you, let's move to the next caller.

Operator: The next question is Jim Covello with Goldman Sachs.

<Q – James Schneider>: Hi, it's Jim Schneider calling for Jim Covello. Thanks for taking questions, Ron. I guess first of all, could you talk about your expectations for the quarter, whether you think you'll be building inventory at distributors or whether you'll be able to do that this quarter?

<A – Ron Slaymaker>: Jim, I don't have anything specific on the distribution inventory trends at this point other than what I indicated before, that it's our belief that distribution inventory remains lean. Do you have a follow-up?

<Q – James Schneider>: Yes, there has been a lot of chatter about noise in the PC and handset supply chains in particular. I was wondering if you could comment on what you're seeing on those two end products in particular.

<A – Ron Slaymaker>: Again, what we're seeing is pretty broad-based strength. I don't know that I have PC specific comments other than where we're selling for example in the peripherals, such as storage products. That area has seen growth very consistent with our overall growth trends. We haven't seen any real inflection in demand there.

With respect to wireless, I guess what I would say is that wireless is growing. In fact, let me step back and kind of talk from the segments overall. We are expecting all of our segments to grow sequentially this quarter, although growth should be strongest in our Analog and Embedded Processing segments. In Wireless, growth there will be driven by the connectivity and the OMAP application processor products. And although baseband revenue, we would expect to change minimally from the first-quarter level, as a percentage of our total revenue, we expect that it will decline really due to the strong growth in the core business areas; so again Wireless overall up driven by connectivity and OMAP, baseband relatively flat to last quarter's level.

Okay, Jim, thanks for your questions, and let's go to the next caller.

Operator: That will be Chris Danely with JP Morgan.

<Q – Venk Nathamuni>: Hi, thanks for taking my call. This is Venk on behalf of Chris Danely. Ron, I have a couple of questions. In terms of the backlog for the second half of 2010, have you seen any change in the backlog as it declined and could you comment on that, please?

<A – Ron Slaymaker>: I don't have a specific response for you on backlog other than I would say orders are growing. I guess what you really get to with part of your question is book-to-bill going to be above one and therefore is backlog expanding.

<Q – Venk Nathamuni>: Right.

<A – Ron Slaymaker>: And we've always tried to stay away from describing book-to-bill trends at the mid-quarter update just because it's tricky when you have both the numerator and denominator changing. So I'll ask if you wait, we'll describe that of course at our earnings release. But I will describe orders are strong and we expect them to be up sequentially. Did you have a follow-on, Venk?

<Q – Venk Nathamuni>: Okay, that's fair, and a quick follow-up. You said your Analog business segment is doing well. Can you comment on the relative performance of the three segments within Analog?

<A – Ron Slaymaker>: Okay, I guess to start with, I would say all three are contributing strongly to growth this quarter. And so probably at the highest level, it would be Power and HPA because of their exposure to industrial. And as I noted before, industrial is doing exceptionally well. But right behind that is HVAL. HVAL is growing and contributing very strongly to that Analog number, so not a lot of distinction between the areas.

Okay, Venk, thank you for your question. Let's move to next caller.

Operator: The next question is from Shawn Webster with Macquarie.

<Q – Shawn Webster>: Thank you. Can you hear me okay?

<A – Ron Slaymaker>: I sure can.

<Q – Shawn Webster>: Okay. Can you talk about utilization rate trends in Q2 and what you expect for Q3? And then my follow-up would be, can you comment on your own inventories and do you think they'll be up in dollars and/or days for Q2? Thanks.

<A – Ron Slaymaker>: Okay, Shawn, with respect to utilization, I guess as far as I would go is to say we expect that utilization in 2Q will be up a little bit from the first-quarter level. I really don't have a forecast on what utilization in third quarter would be.

In terms of our own inventory levels, I think what we would expect is that we should be able to grow our inventory some this quarter. But from a days of inventory, just given the fact that demand is continuing upside – [inaudible], days of inventory will most likely remain low.

Okay. Let's move to next caller then. Thank you, Shawn.

Operator: Next is from Cody Acree with Williams Financial Group.

<Q – Cody Acree>: Thanks, guys. Thanks, Ron. Ron, you mentioned earlier the constraints you're seeing in some of your peripheral competitors, that it's actually giving you some comfort that they're seeing constraints and lead times expand and you've got supply. Doesn't that – hasn't that in previous periods led us into a point where maybe TI starts to begin to see those same issues, if not backlash, at least correct?

<A – Ron Slaymaker>: I think it's I would say the same that we've been saying for the last few quarters. Most of our products, as you know, are proprietary. And with proprietary products, generally there's a sole source situation or close to that anyway. So the customers tend not to have a lot of flexibility to move from TI to our competitors or from our competitors to TI.

I think probably what is more pertinent is that as we had – we probably ran into some of these constraints earlier than many of the competitors just based on the growth that we saw sequentially in second and third quarter of last year. We responded earlier, both initially with bringing on the back end capacity but then also some of the investments that we've made to bring on fab capacity. And I think what's probably most pertinent is the customers see the kind of investments that we're making currently, the roadmap that we're laying in front of them. And to a large part even though these competitors are seeing lead times extend, they're really not seeing action out of them in terms of increased investment levels. Certainly, as you know at this point, the equipment lead times are pretty much extended anyway, so their ability to respond in the short term will be somewhat limited.

So probably how that will play out for us will be more in terms of longer term benefit, customers that are increasingly comfortable that TI is the analog and embedded processing supplier to bet on in order to avoid these kind of constraints in the future just given the investments that we're making, both in fab as well as assembly/test. Okay, do you have a follow-on, Cody?

<Q – Cody Acree>: Yes, I guess just continuing with that theme then, is there a point where – is it just a matter of tool constraints of ramping of capital at some of the foundries that starts to put resources into the channel that you obviously have already spent and got ahead of but then can change some of the landscape and maybe create some more volatility?

<A – Ron Slaymaker>: I don't know. I think in some cases it's tools. I think in other cases if you just pull back and look, there have been an awful lot of fabs taken permanently offline through this down cycle. So I don't know that you make up for that by adding a piece of equipment here or there. There are new wafer fab facilities that will have to be built over the course of time and certainly that's a longer lead time on it.

Okay, Cody, thank you, and let's go to the next caller.

Operator: Next will be Srini Pajjuri with CLSA.

<Q – Srini Pajjuri>: Thanks, Ron. Ron, given the strength in the first half of the year and also the fact that your Wireless business may not be as strong this year, I'm just trying to understand how we should think about the seasonality in the second half for you.

<A – Ron Slaymaker>: Yes, Srini, I don't have – certainly as you understand from us, we basically take these forecasts a quarter at a time. I don't know that the strength we've seen in first half necessarily translates to anything about the second half. It probably reflects more the weakness that we saw in 2009 as opposed to setting us up for any necessarily different seasonal trend in second half. But beyond that, I really don't have much to say about second half. Did you have a follow-on?

<Q – Srini Pajjuri>: Yes, just quickly on the hard drive market, you said that you're not seeing any change to your forecast. Just a clarification, were you expecting growth in this business when you gave the original guidance?

<A – Ron Slaymaker>: I'm sorry. Again, which business did you refer to?

<Q – Srini Pajjuri>: The disk drive business.

<A – Ron Slaymaker>: I don't know what we had in the forecast. What I was describing was simply the sequential growth pattern from first to second. I don't have the first quarter – the second-quarter growth expectation for storage.

<Q – Srini Pajjuri>: Okay, but what you said is it hasn't changed since you gave the guidance?

<A – Ron Slaymaker>: I don't know that it had changed. I'm just saying that sequential growth in storage runs very consistent with our overall growth rate for the company, and I'm not trying to make a characterization against our expectations. Okay. Srini, thanks for your questions. Let's move to the next caller.

Operator: Next is Ramesh Misra with Brigantine Advisors.

<Q – Ramesh Misra>: This is Ramesh Misra. Thanks, Ron. I wanted to ask you about your currency hedging program. Can you talk a bit about it, especially related to the euro?

<A – Ron Slaymaker>: Okay. Maybe the way to think about is this is that most of our sales in Europe are transacted in US dollars, so we have little direct exposure except to the degree that a weak euro of course would make these dollar-based transactions relatively more expensive for our customers than in the past. We have employees and factories located in Europe, so changes in that euro exchange rate would affect our US dollar equivalent cost for payroll and locally sourced purchases in Europe. And then specifically to your question, we have hedges in place for balance sheet items, but again not income statement items. Did you have a follow-on, Ramesh?

<Q – Ramesh Misra>: Yes, very quickly. So if the weakness in the euro persists, would you be able to load your European fabs a little more than the US fabs in order to cater to European demand? Do you have that flexibility or is that somewhat limited?

<A – Ron Slaymaker>: I would say somewhat limited. I mean the fab loadings tend to be very product driven and things like that that I don't know that we strategically, or tactically maybe is a better word, try to load fabs based upon currency swings.

Okay, Ramesh, thank you, and let's move to the next caller.

Operator: It is Uche Orji with UBS.

<Q – Uche Orji>: Thank you very much. Ron, just I'm not sure if you commented on this earlier. On your gross margins, given that the revenue and the earnings tightening seem to be in sync, can you just talk about what may have affected gross margin? Is there any leverage left on the gross margin line? That's my first question. I have a follow-up.

<A – Ron Slaymaker>: Okay. I think you've seen us. Probably we're not at our gross margin goal. So I think clearly I would say we believe there's some room for additional expansion there. I think as you've noted, factory utilization will be less of a factor looking forward maybe than it has been over the last year just considering that we're back at normal utilization levels again. So probably the biggest driver of gross margin expansion will likely be product mix. That really just reflects as we continue to increase our focus on analog and embedded processing.

I guess the final point I would note is we do continue to work to lower our manufacturing costs. For example, bringing up 300-millimeter production for analog we believe will be a cost benefit for TI; so again, probably some room for additional gross margin expansion. But when you move to earnings growth overall, certainly our view is that the biggest driver of earnings growth is going to be top line growth. And certainly you guys probably heard this at our analyst meeting. But along those lines, we really believe that the gross margin goals, the business model goals that we've outlined previously for 55% gross margin and 30% operating margin really provides a good balance of profitability and growth opportunity.

So specifically, as we've described, our goal is to grow revenue in our core businesses of Analog and Embedded Processing at twice the rate of the respective markets, and then continue to gain share as well in the fast-growing smartphone chip market with our OMAP and connectivity products. So on the growth side, we're certainly making good progress toward this growth objective. This quarter certainly is shaping up not to be an exception to that. But we certainly realize we need more time and results behind us on that. Do you have a follow-on, Uche?

<Q – Uche Orji>: Yes, I do. A quick question, June quarter, how back-end loaded is it? Everyone thought – no one seems to see any problem in Europe yet, but does this sound like 2008 where we didn't see anything until suddenly September. Is there any parallel from what you see now vis-à-vis what you saw back in 2008?

<A – Ron Slaymaker>: June quarter is not exceptionally dependent upon the month of June just normally. Probably the two quarters that tend to have a little variation in terms of linearity would be historically first quarter, where it's a little more back-end loaded because of weakness in the month of January; and then similarly, fourth quarter where December, the final month in the quarter, tends to be weaker. Second, third quarter, there really is not a big difference in that monthly linearity. But specific to this second quarter, I would just say April and May were both strong months. And to meet this guidance that we're providing today, we really just need a normal June. We're not expecting an exceptionally weak or strong June, just a normal June to be able to hit this guidance.

Okay, Uche, thank you, and we'll move to the next caller.

Operator: That is Patrick Ho of Stifel, Nicolaus.

<Q – Patrick Ho>: Thanks a lot. Ron, I know it's difficult to probably measure, but could you just characterize how much of the tightening of the range to the high end is driven by the overall demand in the environment versus some of the market share gains you guys have been achieving over the past few years?

<A – Ron Slaymaker>: I'm sorry. You're saying how much of the raise in this guidance?

<Q – Patrick Ho>: Yes.

<A – Ron Slaymaker>: Okay. I don't know, I think it's both. I think on the one hand, we're continuing to see strength in our markets and markets like industrial, for example, that are continuing to gain momentum. And then in addition to that, we believe we're continuing to gain share, especially in analog and embedded processing, but that's a belief statement. We really need to see our competitors in those markets report before we can say that with strong conviction. But we certainly believe we're doing very well from a relative perspective in markets that seem like they're continuing to strengthen for us. Do you have a follow-on, Patrick?

<Q – Patrick Ho>: Yes. In terms of the back-end capacity that has been tight for you guys for some quarters but I think you've mentioned it has become alleviated somewhat. What do you feel you're along in terms of the back-end test/assembly capacity in terms of getting to what you feel is I guess more normal levels?

<A – Ron Slaymaker>: I guess I would just reiterate what we've said on our CapEx plans that I think we said this year 900 million for the year, but we expected it to be more front-half weighted as we brought on that assembly/test equipment and even made some of these fab expenditures. So that would say that the equipment generally in-house by the time we finish first half, and then maybe still some lag time in terms of ramping it up and putting it in production. But that would say we think we're generally getting in pretty good shape from an equipment perspective. Then certainly – and that's the equipment on the back-end side. And then as you've certainly seen from us, the investments that we're laying out for RFAB and even some of the 200-millimeter equipment expenditures that we're making are really focused at making sure that we also have the front-end capacity to support our growth objectives in the years ahead.

So certainly assembly/test is a more near-term focus type of investment to pull lead times in and alleviate those constraints. But what you see with the fab would be a more longer-term multiyear commitment to make sure we're in a position to support our customers and their growth expectations.

Okay, Patrick, thank you, and we'll move to the next caller, please. And operator, this will probably need to be our last caller.

Operator: Yes, and that is Craig Berger with FBR Capital Markets.

<Q – Craig Berger>: Hey, guys. Thanks for squeezing me in. I guess my first question is what does it take for the company to get more aggressive on share buyback given your 10 times earnings multiple? And as part of that, do you see any reason why earnings levels can't generally sustain here on a go-forward basis?

<A – Ron Slaymaker>: Craig, I really don't have anything to forecast for you on buybacks. We will certainly report what we've done in the quarter in July when we report our earnings. But it's probably not in our best interest to give you a mid-quarter update on our repurchase activity or plans.

But I will also point back to last quarter. I think you saw a nice step up. I believe it was on the order of a $0.5 billion repurchase that we conducted in first quarter, which is about half of what we did all of 2009. And I would even say 2009 repurchases were relatively aggressive in that we stayed committed into the market every quarter through the course of that downturn, whereas you saw many companies really pulling back when the markets got dark there. So I think we've been buying back aggressively. And beyond that historical statement, I'll just say stay tuned until July. Do you have a follow-on, Craig?

<Q – Craig Berger>: That's helpful, thanks for that. Sorry to steer the conversation away from macro and Europe, but one bit of push-back I get when pitching the TI story is that with baseband going away, it increasingly puts the application processor business at risk in years coming as integration eventually wins out. How would you respond to that potential risk or investor criticism?

<A – Ron Slaymaker>: I think clearly we don't believe – our view is much different than that. I think Greg Delagi probably gave a more thorough response at the analyst meeting. And certainly that webcast is still available through our website in terms of the archive of it for investors that might want a more detailed response.

But just in general, I'll say you see a lot of customers very aggressively working to commoditize that baseband function. The last thing I believe those customers want is for a supplier to come along that's providing an apps processor to integrate the baseband functionality such that they then only have that one source for their baseband. That goes against a lot of efforts that you've seen over the past few years for these customers to multi-source the baseband and commoditize that function.

Then secondly just from a system architecture perspective, the customers generally will have an applications platform, and then they will want to ship that smartphone into different regions of the world, different service operators that have different baseband or communications standards that they're dealing with. So for them to try to create one big super chip that has baseband and applications all integrated together means they have to do an awful lot of versions of that super chip to be able to support all those different communications standards.

So our view is architecturally there are very strong benefits to: one, letting baseband commoditize, which is clearly well along the path to success there. And then secondly, by keeping those separate, they can have an applications platform that they basically just snap on different baseband modems to support different standards. This is not just TI's biased view on it. I think if you look at the customer trends over the last year or so, there has been a significant shift toward dis-integrating those functions as opposed to customers that have moved forward with integrated versions. So again, that's a very quick and high-level view, but I would refer you to Greg Delagi's webcast of the analyst meeting or the webcast of his presentation for a more thorough response there.

Ron Slaymaker, Vice President, Investor Relations

Okay, Craig, thank you for your questions, and thank all of you for joining us. Before we end the call, let me remind you that the replay is available on our website. Thank you and good evening.

Operator: This does conclude today's conference call. Thank you for your participation.