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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Texas Instruments second quarter 2013 earnings conference call. At this time, I'd like to turn the conference over to Ron Slaymaker. Please go ahead, sir.

Ron Slaymaker, Vice President, Head of Investor Relations

Good afternoon, and thank you for joining our second quarter earnings conference call. As usual, Kevin March, TI's CFO, is with me today. For any of you who missed the release, you can find it and relevant non-GAAP reconciliations on our website at ti.com/ir. This call is being 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 earnings release published today, as well as TI's most recent SEC filings, for a more complete description. Our midquarter update to our outlook is scheduled this quarter for September 10. At that time, we expect to adjust the revenue and earnings guidance ranges as appropriate.

The second quarter was another solid quarter for TI. Revenue came in as we expected, up 6% sequentially, and up 8% if you exclude legacy wireless revenue, which declined to less than 5% of TI revenue in the quarter. Analog and Embedded Processing increased to 78% of TI revenue. Our overall backlog continued to increase. Visibility into the second quarter has improved, and we expect another quarter of solid growth in the third quarter. The industrial and automotive markets were once again important drivers of TI revenue growth. More than 35% of our product revenue in

the first half of 2013 came from these important markets. Although we continue to have exposure to the PC and handset markets, these are now much smaller percentages of our revenue. We believe this increased diversity of markets and customers should make for steadier growth and financial returns.

The strength of our business model continues to give us confidence that we can sustainably generate $0.20 to $0.25 of free cash flow for every dollar of revenue and then return all of it to shareholders, except what is required to repay debt. As we've said previously, free cash flow is an important consideration for a couple of reasons. First, net income has generally lagged the amount of free cash flow that we have generated for the past two years and will continue to lag in the years ahead. This is because of significant noncash items on the income statement, including amortization of acquisition intangibles, as well as the large amount by which depreciation exceeds our capital expenditures. The second reason free cash flow is important is that cash returns are a big part of our long-term shareholders' return. The more free cash flow we generate, the more we return in the form of dividends and stock repurchases. For the trailing-12-month period, free cash flow was 24% of revenue, a point higher than last quarter. And once again, we returned all of that and more to our shareholders, consistent with our capital management strategy.

Earnings in the second quarter were strong, a result of good operational execution, an improving product mix, and a transfer of wireless connectivity technology to a customer, reflecting our continued monetization of the legacy wireless business, even as its product revenue declines.

Let me walk through a few details of revenue. Analog revenue grew 6% sequentially. Silicon Valley Analog, High Volume Analog & Logic, and High Performance Analog all contributed to the sequential growth. Power was about even, as growth in broader markets was offset by weaker demand at certain handset customers and game console manufacturers, which were preparing for a product transition. SVA, with its strong participation in the industrial and automotive market, has been the leading driver of growth within our Analog business. Additionally, it has outgrown the Analog market over the past three quarters. From a market share perspective, SVA troughed in the second half of 2012, and its share has significantly rebounded as it has grown since then. As we have communicated to you previously, our original expectation for SVA was that it would continue to lose share in the first year after the acquisition, grow similar to the market in this second year, and then gain share in the upcoming third year. We're running a full year ahead of this plan.

Embedded Processing revenue grew 10% sequentially, with Processors up the most, followed by growth in Microcontrollers and Connectivity. Although Connectivity was the smallest contributor, its growth rate was the highest, as a range of customers embrace our low-power product. In Processors, communications infrastructure had solid growth, reflecting increased operator spending, especially in North America.

In our Other segment, sequential growth in most product areas was largely offset by the decline in legacy wireless. Legacy wireless revenue fell by $62 million sequentially to $148 million. Calculators grew, as retailers prepared for back-to-school demand. DLP grew, driven by demand for high-resolution front projectors. And custom ASIC revenue was about even. Royalties declined.

Turning to distribution, resales grew 5% sequentially. Distributors' inventory levels held about even on a dollar basis, and declined by about 1 day.

Now Kevin will review profitability and our outlook

Kevin P. March, Senior Vice President and Chief Financial Officer

Thanks, Ron, and good afternoon, everyone. Our earnings in the quarter included a gain of $315 million associated with the transfer of wireless connectivity technology to a customer. This gain was recorded on the "Restructuring charges" line of our income statement and in our Other segment. The gain was partially offset by related expenses. The net gain was not included in the guidance we provided you previously. In addition, restructuring charges were higher than we originally expected. The net impact of these items was a $0.16 benefit to earnings per share in the quarter.

Gross profit was $1.57 billion, up 14% sequentially. Gross margin was 51.5% of revenue and expanded 390 basis points sequentially. This strong profit fall-through was a result of our increasing leverage of the low-cost capacity we have in place and our improving product mix as lower-margin legacy wireless revenue continued to wind down and higher-margin Analog and Embedded Processing revenue grew.

Operating expenses of $860 million were reduced by $18 million sequentially. Operating profit was $906 million or 29.7% of revenue. Net income in the second quarter was $660 million or $0.58 per share.

Let me now comment on our capital management, starting with our cash generation. Cash flow from operations was $674 million in the quarter. I should note that the gain on the technology transfer did not impact cash flow, as payment was not due in the quarter. You can see this impact on the "Prepaid expenses and other current assets" line of the cash flow statement. We increased our inventory by $20 million compared with the prior quarter. Inventory days increased to 105 days, consistent with our model of 105 to 115 days. Capital expenditures were $97 million in the quarter, and free cash flow was $577 million. Although cash flow from operations was about the same as a year ago, our free cash flow was higher, as our capital spending needs are lower.

On a trailing-12-month basis, cash flow from operations was $3.32 billion, up 3% from year ago. Trailing-12-months capital expenditures were $427 million, down 28% from a year ago. As a result, free cash flow was $2.90 billion, up 10% from a year ago. Free cash flow was 24% of revenue for the trailing-12-month period, within our expected range of 20% to 25% of revenue.

In the year-ago trailing-12-month period, free cash flow was 20% of revenue. Capital expenditures for the past 12 months were about 3% of revenue. Our low capital spending level is a direct result of the strong capacity position that we have built with our strategic investments of the past few years. The cash flow that will result as we continue to fill up this capacity should be strong in the years ahead.

I'll note that depreciation expense for the past 12 months exceeded our capital expenditures by $495 million. As a percent of revenue, depreciation was more than 400 basis points higher than our capital expenditures. This is one of the reasons why our free cash flow has been trending higher than our net income. Of course, depreciation will decline to the rate of capital spending over the next few years, benefiting gross margin as it does. Another major reason why free cash flow has trended higher than net income is the amortization expense of $80 million to $85 million per quarter that will remain on our income statement for another six years. In the trailing 12 months, amortization expense was $341 million or about 3% of revenue.

And as we've said, strong cash flow, particularly free cash flow, means that we can continue to provide strong cash returns to our shareholders. In the second quarter, TI paid $309 million in dividends and repurchased $721 million of our stock. Our capital management strategy is to return all of our free cash flow to shareholders except for what we need to repay debt.

In the second quarter, we reduced our debt level by $500 million. We also benefit from proceeds from employee stock option exercises that have allowed us to return more than 100% of our free cash flow to our shareholders while maintaining our targeted level of cash. For the past 12 months, we have paid $971 million in dividends or 34% of our free cash flow. Similarly, we have repurchased $2.6 billion of our stock or 90% of our free cash flow. In total, we returned 123% of free cash flow in the past 12 months.

Fundamental to our cash return strategy are our cash management and tax practices. We ended the second quarter with $3.24 billion of cash and short-term investments, with 82% of that amount owned by TI's U.S. entities. Because our cash is largely onshore, it is readily available for a variety of uses, including paying dividends and repurchasing our stock. TI's orders grew 6% sequentially, and our book-to-bill ratio was 1.03, as our backlog expanded again this quarter.

Turning to our outlook, we expect TI revenue in the range of $3.09 billion to $3.35 billion in the third quarter. At the middle of this range, revenue would increase about 6% sequentially, despite our assumption that revenue from our legacy wireless products will decline by about $90 million in the quarter. For the rest of our revenue, that would result in growth of about 9% at the middle of our range.

This quarter, I'll provide some additional detail to our outlook than what we typically provide. This is in consideration of the unusual items in our second quarter and to help baseline your models. We expect operating expense in the third quarter to decline a couple percent compared with the second quarter. The combination of our "Acquisition charges" line and our "Restructuring charges" line should be about $100 million in the quarter. We expect earnings per share to be in the range of $0.49 to $0.57.

In the third quarter, investors will see for the first time the Analog and Embedded Processing company that we've been building over the past years without the distraction of the wireless business we've been unwinding. Legacy wireless revenue should be less than 2% of total TI revenue in the third quarter. Even with depreciation levels continuing well above our capital spending, we expect gross margin to again move up notably in the quarter. And we expect to produce ongoing strong free cash flow in the years ahead that results from this business model.

For the year, our estimate for R&D expense is unchanged at $1.5 billion. Our estimate for capital expenditures remains $500 million, well below our depreciation estimate of $900 million. Our estimated effective tax rate has been revised up to 24% from our prior estimate of 22% as a result of our higher 2013 profit forecast.

In summary, we are seeing our company develop into what we planned. Our business, focused on Analog and Embedded Processing, is highly diverse across customers and markets. Therefore, we believe TI can deliver more stable growth in years ahead with a business model that delivers good profitability and low capital intensity. As a result, free cash flow should continue to be strong, $0.20 to $0.25 of every dollar of revenue. This will allow us provide a rare combination of growth and high cash returns to our shareholders.

With that, let me turn it back to Ron.

Ron Slaymaker, Vice President, Head of Investor Relations

Thanks, Kevin. Operator, you can now open the lines up for questions. In order to provide as many of you as possible an opportunity to ask your questions, please limit yourself to a single question. After our response, we will provide you an opportunity for an additional follow-up. Operator?

QUESTION AND ANSWER SECTION

Operator: Okay, thank you. [Operator Instructions] And at this time, we'll take a question from Glen Yeung [Citigroup]. Please go ahead.

<Q – Glen Yeung – Citigroup Global Markets Inc. (Broker)>: Thank you. Great quarter, guys. Kevin, can you walk us through the gross margin expectations for the third quarter? Just what are the puts and takes on how you get to what I think you called notable gross margin improvement in that quarter?

<A – Kevin March – Texas Instruments Incorporated>: Yeah, Glen, I think what you're going to see, with legacy wireless declining by about $90 million next quarter, that lower-margin revenue is going to be displaced by higher-margin revenue with the form of Analog and Embedded Processing taking up a bigger piece. In addition, with our growing backlog and higher revenue expectations for the quarter, we'll be utilizing more of our factory capacity.

So as you kind of run through all that, I talked a moment ago about our operating expenditures; we'd expect to be down a couple percent quarter over quarter and our restructuring and acquisition costs to be about $100 million in the quarter. So you squeeze that math on through, and you'll see that our gross profit margin will continue to increase as it has this last quarter.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Do you have a follow-on, Glen?

<Q – Glen Yeung – Citigroup Global Markets Inc. (Broker)>: I do have a follow-on. If I look at your – and forgive me if I'm doing this math wrong, but I think I got it right. If I look at your revenues less wireless year on year in the June quarter, it was still actually a negative number. And I think based on your guidance, it will be positive in the third quarter. Question is do you think that your revenues less wireless will actually be positive for the year?

<A – Ron Slaymaker – Texas Instruments Incorporated>: Oh, Glen, I don't – I'll let you try to extrapolate what we've done year to date out into fourth quarter. Clearly, with the legacy wireless down as significantly as it will be in the third quarter, and we've said before that we expect it to be pretty much zero by the time we get into 2014, that variable was pretty much filled in for fourth quarter. But you can make some estimates on what the rest of the revenue could look like to make the assessment of whether we're going be up overall without legacy wireless.

<Q – Glen Yeung – Citigroup Global Markets Inc. (Broker)>: Thanks, Ron.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay, Glen, thanks for your questions. And we'll move to the next caller, please.

Operator: At this time, we'll take a question from Jim Covello with Goldman Sachs.

<Q – Jim Covello – Goldman Sachs & Co.>: Great, guys. Thank you so much for taking the question. Maybe, Ron, first, if I could just ask this. The improvement that we're seeing across the industry in the comms business, early stages, can you offer some perspective on that and how long you think that could potentially last, what the puts and takes there would be?

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay, and I think you're talking specifically about infrastructure there, so – at least that's what my comments will be.

<Q – Jim Covello – Goldman Sachs & Co.>: Sure.

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<A – Ron Slaymaker – Texas Instruments Incorporated>: We've actually seen pretty broad growth across geographies. It is being led by North America, and it's being led by some of the players that late last year, in terms of operators, announced that they would be doing capital spending increases this year. So after several quarters of what I'll say is not a lot of activity, we did see real results in third quarter. But, again, it was broader than North America.

Looking into the back half of the year, I think we're still optimistic that – well, actually, first of all, let me say that what we're seeing in North America is a combination of continued W-CDMA deployment but also accelerating LTE deployments as well. So, again, as you know, we play quite strongly across both the new LTE technology as well as the more entrenched W-CDMA. So we're seeing strength on the combination.

In terms of China, we, like many other people, are waiting to see the impact of – and whether in fact we'll see second-half deployments. But clearly that's our expectation. We've seen some activity, more so from the standpoint of customers getting prepped for that in Japan. But we haven't actually seen the bigger lift. And I think that's pretty much consistent with at least my understanding of what other players have been describing as well there.

Do you have a follow-on, Jim?

<Q – Jim Covello – Goldman Sachs & Co.>: Sure. Thank you for that. And I apologize if I missed this, because I got cut off briefly, but did you say what your plans for factory loadings would be for the back half of the year compared to the first half?

<A – Kevin March – Texas Instruments Incorporated>: Jim, if I heard your question correctly, I think you were asking what our plans were for factory loadings in the back half of the year versus the first half. Clearly, our loadings have been stepping up. Second quarter was higher than first. And we would expect third quarter to be higher than second on the basis of our growing backlog. Beyond that, we don't have enough visibility to really comment on what the fourth quarter might look like. And so we'll wait another 60 to 90 days before we comment on that.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay, Jim, thank you. And we'll move to the next caller, please.

Operator: And the next question will be from Stacy Rasgon with Sanford Bernstein.

<Q – Stacy Rasgon – Sanford C. Bernstein & Co. LLC>: Hi, guys. Thanks for taking my question. Question on – first on profitability. You have Analog and Embedded Processing today pretty close to historical highs. I think Analog may be high – at historical highs. Embedded Processing is close. Profitability, though, looks a little bit pressured, though, even with less OpEx and higher gross margins this quarter. I assume that's going to get better next quarter as margins go up and OpEx comes down a little bit. But could you give us, I guess, a little more color on how you see profitability by your business, how it's kind of trending as we go forward through the year? And maybe you can share anything around longer-term targets that you might want to give us.

<A – Kevin March – Texas Instruments Incorporated>: Yeah, Stacy, I'd begin by reminding you that, especially if you look at the compares to prior, certainly compares year over year, the profitability in those two segments are going to be somewhat pressured by the – simply by virtue of the fact that we've eliminated the wireless segment. And so that means the remaining corporate expense is spread over fewer business units. And so therefore the corporate allocations are higher. So that alone is going be depressing any comparisons to prior periods.

The other thing I guess I'd talk about on the Embedded Processing – you may recall that about two years ago we significantly began to step up the investments that we had in that area, especially in

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support of our objectives for our microcontroller products. And as I mentioned on last quarter's call, those investments are at a sufficient level now that they do not need to be increased any more. So we're at the point now where we're really looking for revenue growth in the Embedded Processing segment to begin to generate some real profit.

You may also recall that one of our more profitable pieces of that is into the comms infrastructure, and to the question we had just a moment ago, we're beginning to see some signs of that picking up this past quarter, and ideally that continues, and that generates quite a bit of additional profit fall-through as well. Did I answer your question there, Stacy?

<Q – Stacy Rasgon – Sanford C. Bernstein & Co. LLC>: No, you did. That's very helpful.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Stacy, if I can just add one thing.

<Q – Stacy Rasgon – Sanford C. Bernstein & Co. LLC>: Yes.

<A – Ron Slaymaker – Texas Instruments Incorporated>: I think if you look at the same thing at the company level and just try to go back and, at least when we just kind of went back and looked at versus prior periods in history, you can find, at least compared with second quarter, historical periods where revenue was similar but margins maybe were a little higher or whatever. And as we – a lot of that really just comes down to the difference in capacity. So, for example, I think one of the ones, if I remember right, was late in 2009, when we were absolutely capacity constrained. And if you look at where we are today, and our position to be able to support growth and provide service levels that our customers expect from us based upon the capacity we have, it's just really a world of difference. So we like where we are right now, and we like how things are headed into the third quarter on that front as well.

Do you have a follow-on?

<Q – Stacy Rasgon – Sanford C. Bernstein & Co. LLC>: I do. Along those lines, around the gross margin for next quarter, my math suggests you may be implicitly guiding to a margin of 54%, maybe even a little more. I guess can you give us some feeling whether or not that math is accurate and some feeling of the relative magnitudes of drivers? We have wireless mix obviously going down. Mix within the rest of it is maybe going up, utilization going up. I think you also had some fab closures, the 6-inch fabs, that start to hit in Q3 if I'm not mistaken. If you'd give us some, I guess, some feeling for the relative magnitudes of some of those drivers, I'd appreciate it.

<A – Kevin March – Texas Instruments Incorporated>: Stacy, you did a good job citing the answer I would've given you to that question as to what's driving that increase in gross profit margins. You're exactly right on those points. We're probably seeing utilization lifting a bit, mix improving quite a bit, and we're beginning to see the early signs. Third on that list would be some of the savings from the closure of those two older 6-inch factories that we talked about. But I think that it's probably a toss-up between mix and improved utilization that we see going on there. And I think as we move forward after that, it's really going to be mix that's going to be impacting favorably our gross margins as we keep moving forward.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay, Stacy. Thanks for your questions. And we'll move to the next caller.

Operator: Next question will be from Ross Seymore with Deutsche Bank.

<Q – Ross Seymore – Deutsche Bank Securities, Inc.>: Hi, guys. Congrats on the solid quarter. It looks to me like you're guiding your core business, like you said, Ron, up about 9%, about double

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normal seasonality. Could you give us any color on either the product segments or the end markets that are driving that 2x normal seasonality, please?

<A – Ron Slaymaker – Texas Instruments Incorporated>: Ross, I really don't – as is normally our practice – I don't really want to try to dissect it by end market or by product line beyond what we've identified typically. I think seasonally we see a little additional lift from calculators, and no different this time, but that's not a big factor. Probably the biggest single swing factor will be what we've described already in terms of the decline for legacy wireless. And, of course, that would depress from that 9% to the total amount for the company. But beyond that, we really – I would say probably more of what we've seen in second quarter, but also I think some of the areas that were still not really lifting in second quarter and maybe holding back growth even in second quarter seasonally, typically, are stronger in third quarter. And so beyond just noting that some of the computing and handset areas see seasonal strength in third quarter, let me just kind of stop there, if I can.

Do you have a follow-on, Ross?

<Q – Ross Seymore – Deutsche Bank Securities, Inc.>: Yes, and hopefully get a little closer with this one. When we talk about the OpEx side, Kevin, your color was great for the third quarter and for the full year. How should we think – when you get to that normalized OpEx level for TI, and all the cost savings, et cetera are gone – how should we think about the growth rate in OpEx versus whatever we assume core growth in revenues would be going forward into 2014, et cetera? Thank you.

<A – Kevin March – Texas Instruments Incorporated>: Well, the kind of high-level OpEx guidelines that we have offered to the investor community is that we would expect to be operating with OpEx between 20% and 30% of revenue. And clearly what that would mean is that in periods of lower revenue, we'll be in a higher percent, and periods of higher revenue, a lower percent.

More specifically to your question as to cost trends, as I'd mentioned earlier, we've stepped up investment quite a bit over the last couple years, mainly in the Microcontroller portion of Embedded Processing, and also in the overall sales footprint that we have on a global basis. I would expect, as we look out over the next year to two years, that that rate of investment increase is going to slow down considerably as we begin to get revenue leverage off of that investment. So as we look forward, I would expect our revenue growth to probably pretty – provided we've got growing markets and a growing global economy, I would expect revenue growth to outstrip our OpEx growth by a fairly sizable portion. Beyond that, I won't be any more specific, but I think what you can really take that to say is that we expect our overall bottom-line results to continue to improve, as you've seen these last few quarters.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay. Thank you, Ross. Next caller, please?

Operator: We'll move to John Pitzer with Credit Suisse.

<Q – John Pitzer – Credit Suisse Securities (USA) LLC (Broker)>: Yeah, good afternoon, guys; congratulations. Ron, in your prepared comments, you talked about SVA gaining share in the June quarter. I'm just kind of curious, given the core business expectations of kind of high single digit sequential growth, to what extent do you think this is share gain versus what you're seeing in the overall market? And I'd be kind of curious, if industrial and auto really drove Q3, do we expect sort of the consumer market with normal seasonality to be a bigger driver in the core business for September, sorry?

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<A – Ron Slaymaker – Texas Instruments Incorporated>: I think, first of all, your comment on SVA, it did gain share in Q2. But I also said it gained share in Q1, as well as in Q4. So for the last three quarters, it has gained market share. I think probably what we would expect in Q3, very likely, given that we've been gaining share, we would expect to continue to gain share in Q3. But, John, until everybody comes out with their Q3 guidance, maybe more importantly, when they actually come out with actual results, we're just speculating about market share. I think it's what you said. It's probably more continued strength in the industrial and automotive areas, as well as some broadening of strength into other areas.

And I think you've probably heard from multiple companies reporting now, as well as what we've said – and there are certain players in the handset market that were running relatively weaker demand in Q2. And probably a lot of that had to do with them resetting some inventory levels in their channels, that our expectation is we'll see that strengthen back up, to call it more normalized run rates for those players, in addition to the seasonal lift that comes along in the third quarter.

Do you have a follow-on, John?

<Q – John Pitzer – Credit Suisse Securities (USA) LLC (Broker)>: Yes, follow-on for Kevin. Kevin, I guess as we're thinking about the new business model, you guys in the past have had kind of a target gross/op margin of, I believe, 55% and 30%. If you look at the implied guidance for the September quarter, you're basically a stone's throw away from those numbers. Kind of curious, as wireless goes to zero and you start to see continued leverage in the business model, should we start to be thinking about just structurally higher target gross and op margins than you've given out in the past? Thanks.

<A – Kevin March – Texas Instruments Incorporated>: Yeah, John, we gave those kind of guidelines a number of years ago when we made the decision to discontinue further investment in our baseband portfolio so that we could at least give the analyst community and investors a sense as to what to expect this portfolio to be able to do. And, clearly, we're beginning to see those results play themselves out.

What we have talked about here in the last few quarters – in fact, we even started talking about probably a year, year and a half ago at our analyst meeting, is really a focus on cash flow. And what I would really tell you to think about is in terms of what our objectives are is to be converting 20% to 25% of our revenue into free cash flow, which as you've heard us mention several times now, we intend to return 100% to our shareholders through dividends and buybacks, less any amount that we have to use for debt repayment. So that's really the bottom line, is our cash flow objective on this. And I expect that actual margins and PFO, they will fall out, they will be richer than we've historically had in the past, just by virtue of the construct of our portfolio. But I won't try to offer any new numbers as to what we think target numbers are on those, because we really don't want to set ourselves that kind of limit. We're really aiming at maximizing free cash flow for our shareholders.

<A – Ron Slaymaker – Texas Instruments Incorporated>: So, John, since that was your follow-up question, I don't believe you're on the line. Let me ask and in fact answer the natural follow-up to your follow-up, which is, okay, so with free cash flow margin objectives of 20% to 25%, and us just reporting 24% for the trailing-12-month period, are those objectives in fact something that should be reviewed?

And I guess the way we look at that – now I'm in the answer part of your question. The way we look at that is that at current levels, we're now operating in the top 15th, 1-5, top 15th percentile of the S&P 500. And that really just reflects the strength of our business model. And so, do we – is 20% to 25% the right number going forward? The way we will evaluate that is if we get to the point where we're consistently performing above that level, we'll then consider whether we should change the

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range. But right now our margin objective as a corporation is to convert 20% to 25% of revenue to free cash flow, as Kevin said.

So John, thanks for those great questions, and we'll move to the next caller, please.

Operator: At this time, we'll go to Christopher Danely with JPMorgan.

<Q – Chris Danely – JPMorgan Securities LLC>: Hey, thanks, guys. Can you just talk about the linearity of bookings during the quarter? And then considering how the product mix or end market mix has changed, what should we be thinking about for normal seasonality for Q4?

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay. So the linearity question, the answer's probably pretty similar to what it normally is, which is orders were noisy in the quarter. You can't look at it month to month and try to draw any straight line one direction or the other. It probably was a little bit even more so this quarter, Chris, because you noted we said that customers were giving us more extended visibility. And so, depending upon when those customers chose to load up in terms of the backlog for the out quarter, that drove some of the noisiness. So it was a little more so than normal.

And I'll give you one example. Comms infrastructure had an especially strong May, and that was exactly what I was describing. They were going from – I don't know their exact numbers, but let's say, if they had three months of visibility on our backlog placed and they were pushing out to four, four and a half months, that pretty much got loaded in during the month of May and created some of the noisiness, so there was some of that stuff going on.

I don't know, in terms of with all the changes in our portfolio, whether that's going to translate to anything different for Q4, Chris. I think we kind of just have to move forward. We're probably, given the breadth of Analog and Embedded Processing, you can probably just go look at more industry numbers and try to assess. Clearly Q3, if you just look at average growth, has historically, five-year average, been 5%. Again, we always give the caution the range on that is huge. It was 0% to 17%. So I'm not sure how useful that amount, that 5% number, is.

Fourth quarter is down more so. In fact, if you just look at the average, it's down 8%. I think that is a completely not useful number, because of the noise that fourth quarter 2008, I believe it was, introduced into that, where we had a down 26% quarter. The high point on that is down – or I'm sorry, the range was minus 26% to plus 4%. I think, kind of gut, what a normal Q4 is probably down a little bit, because semiconductor products probably tend to move more sideways in a Q4 type of time period. And then you'd probably have some – the pressure of calculators coming off of their back-to-school peak in Q3 pushing down into Q4. But that's clearly not evident in the average five-year growth rate numbers that I just gave you.

Do you have a follow-on, Chris?

<Q – Chris Danely – JPMorgan Securities LLC>: Yes. Can you just maybe give us a sense of what the disty inventory did during the quarter and how their bookings patterns, or any commentary you're hearing from them?

<A – Ron Slaymaker – Texas Instruments Incorporated>: I don't have bookings. I think we said in prepared remarks that disty inventory declined, and yet – so that actually at an absolute dollar basis, went down to a little under five and a half weeks. I'm sorry, let me start that over. From an absolute dollar standpoint, distributor inventory was stable. From a days, it went down about a day to below 5.5 weeks in the quarter.

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

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Operator: We'll go to Ambrish Srivastava with the Bank of Montreal.

<Q – Ambrish Srivastava – BMO Capital Markets (United States)>: Thank you, Ron. And this is not a follow-up to any follow-up, but it's a follow-up to your prepared remarks. Clarification on the connectivity. Who did you sell it to? And then I'm assuming this includes only the handset-related business and not the Embedded part?

<A – Kevin March – Texas Instruments Incorporated>: Ambrish, we won't disclose who it was we entered into that transaction with. I would just mention again it was further efforts on our part to try to monetize those prior investments in that technology. What we transferred was a right for that buyer to use that technology, including some tangible deliverables that we provided to that particular buyer. It's a nonexclusive arrangement. It allows us to fully use the technology just as we have in the past, and, importantly, to continue to pursue the market strategies that we have for that, which is really to take that technology into places where it's beginning to emerge in the, I think the common term is the Internet of Things, but to more and more different areas where we're finding wireless connectivity kind of technology being useful and emerging.

<A – Ron Slaymaker – Texas Instruments Incorporated>: But think of it more along the lines of the legacy wireless as opposed to the Embedded business. So we don't believe this will have any impact, you might say, on our Embedded opportunity going forward. Again, it's just a means by which we're continuing to monetize that legacy wireless business.

Do you have a follow-on, Ambrish?

<Q – Ambrish Srivastava – BMO Capital Markets (United States)>: Yes, I did. On the core business, Ron and Kevin, good to see the SVA kind of on that trajectory that you've laid out the last couple of quarters. It's done well. Can you just help us understand, and I don't mean to make light of it, because market share gains are never easy, but was it just blocking and tackling stuff? Or – because it couldn't be new products that have been developed since the acquisition. So just any color you could provide on what has been working would be great. Thank you.

<A – Kevin March – Texas Instruments Incorporated>: Well, I would think, Ambrish, perhaps what you're beginning to see here – but remember that that's really – SVA has a lot of its revenue going to the industrial channel as well as the automotive. And clearly those markets have been doing well but, importantly, industrial means a lot of customers, including a lot of small customers. And that's where the benefit of an extremely large sales force plays in, versus what National could have done on its own in the past. It simply didn't have the sales force scale to be able to reach out to as many customers.

So I think the combination of nice growth in the markets in which it's in, and the fact that we're able to get the products out to a lot more customers in those spaces, are coming together to help us see some nice growth in that. And then overall, it's just better commercial terms with customers. You may recall that they had previously gotten themselves into a little bit of hot water with some customers where they were no longer welcome on designs, and we've been welcomed back in. And some of those designs are in fact already beginning to turn into – some of those design wins are already turning into incremental revenue.

<A – Ron Slaymaker – Texas Instruments Incorporated>: But let me just add, Ambrish, you recall that when we announced that acquisition, we said the entire basis on which we're going to generate a return on this acquisition is based on revenue synergies that we thought possible, not really cost synergies. I mean, there were some cost synergies, but they were minor compared to the revenue synergies that we thought were possible through our combination. So it's absolutely – I'll understate it and call it encouraging to see those revenue synergies coming through, coming

through at the rate they are, and on the timeline they are. So really good news from our perspective there.

Okay, Ambrish, thanks for your questions. We'll move to the next caller.

Operator: At this time, we'll go to Sumit Dhanda with ISI Group.

<Q – Sumit Dhanda – International Strategy & Investment Group, Inc.>: Hey, Kevin or Ron, just one question on the under-utilization charges. What were they in the second quarter, and what do you project that number to be in the third quarter?

<A – Kevin March – Texas Instruments Incorporated>: Sumit, we haven't been providing a projection on that, but they were a little bit less than $100 million in the quarter.

<A – Ron Slaymaker – Texas Instruments Incorporated>: And down, so as we said, that was beneficial to TI last quarter.

Do you have a follow on, Sumit?

<Q – Sumit Dhanda – International Strategy & Investment Group, Inc.>: I do. Just a clarification again. You said that dollar inventories were roughly flat in distribution, down on a days basis. But you said resales were up 5%, but your organic business grew 8%. Just trying to understand what's sort of the – how do I reconcile all of that? In other words, the organic business being up 8%, but your resales being up only 5%, but inventories being flat?

<A – Ron Slaymaker – Texas Instruments Incorporated>: I think obviously there's just different cross-currents in distribution and that customer base than what we have overall, and what we have associated with our direct business. So I wouldn't – I mean, I think we clearly understand it. But I guess I would say it's really – gets to be very customer specific in terms of – I think what you're really asking is, Why were resales growing slower than TI's revenue overall? And I would just say it tends to get customer-specific that I don't want to get into. Also, keep in mind, our overall business benefits from the lift that we see in calculators. And, again, that would be TI revenue as opposed to the resales, and then also some of the market-specific things. But, again, it gets somewhat market specific, but also customer specific there.

Okay, Sumit. Thank you for your questions. We'll move to the next caller.

Operator: And we'll move along to Mark Lipacis with Jefferies.

<Q – Mark Lipacis – Jefferies LLC>: Thanks for taking my question. Kevin, on the – the prepaid was about a $300 million use of cash due to the – my understanding, I guess, is the tech transfer. So does that reverse and unwind? Does that become a source of cash? And could you just go through the accounting mechanics on that? Thanks.

<A – Kevin March – Texas Instruments Incorporated>: Sure, Mark. The way that works is, as we had met the requirements of the agreement that we signed late in the quarter, it was a recognizable event and therefore was recognized into earnings. The payment terms were such that we don't expect to get paid on the majority of that until this quarter. So, in fact, exactly what you said is what'll occur. Because it's in net income, it's taken out on the prepaid line and other assets. So that appears to be a use of cash, and in fact, it'll reverse itself when we move into the third quarter, because we in fact have already received the payment that was due in the third quarter.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Do you have a follow-on, Mark?

<Q – Mark Lipacis – Jefferies LLC>: Yes. And a simple question. So when your dollars of distributor inventories are flat, does that mean your resales equal your sell-in?

<A – Ron Slaymaker – Texas Instruments Incorporated>: When dollars are flat, does that mean resales equal sell-in? Not necessarily, because it depends upon what the distributors were doing with inventory in the prior quarter. So for example, if – and this, you just have to play with the numbers. But if they were reducing inventory one quarter, they held that inventory flat the next quarter, you could see resales trend – resale growth trend well below our revenue growth as revenue kind of call it snaps back to the rate at which they're shipping out. But there's not always a direct – what do I say? There's not always a direct alignment between revenue growth or shipment into distribution and what they're shipping out, because it varies based upon what they've been doing in terms of adding or depleting inventory.

<Q – Mark Lipacis – Jefferies LLC>: And so...

<A – Ron Slaymaker – Texas Instruments Incorporated>: Clearly with us having customers – I'm sorry, distributors converting to consignment, that could impact it as well, because the impact of a consignment conversion is basically they're depleting inventory and depleting it at a lesser rate as we go forward.

<Q – Mark Lipacis – Jefferies LLC>: So, Ron, so just – and I apologize if I missed this. So what were resales versus sell-in?

<A – Ron Slaymaker – Texas Instruments Incorporated>: I don't know. I had resales about – let's see, we said resales were up 3%. Off the top of my head, I don't have – I don't – I have sell-in. Actually, it was up just slightly more than that. A couple points more than that, is what it looks like.

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

Operator: And moving forward, we'll go to Joseph Moore with Morgan Stanley.

<Q – Joe Moore – Morgan Stanley & Co. LLC>: Hi, thank you. Any notable change in lead times, and anything that you might – that you think might drive lead times higher in the back half of the year?

<A – Ron Slaymaker – Texas Instruments Incorporated>: Lead times, I would say, generally pretty stable, with the vast majority of our products shipping in less than six weeks. So no real change there, Joe.

Do you have a follow-on?

<Q – Joe Moore – Morgan Stanley & Co. LLC>: Yeah, and just any color you can give us on end market dynamics other than the stuff you've mentioned in terms of computing or automotive or anything like that.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay, I have a couple comments here. So industrial, I guess you've seen from what we're saying already, that market continues to recover. I would say in general, customers in that space are pretty hand-to-mouth. They're keeping inventories lean. We have not seen signs of any kind of broad replenishment there. And lead times for our products there are short, and they're taking advantage of that.

In terms of automotive, you've heard us say our revenue was strong. That goes across both Analog as well as Embedded Processing. Part of that is clearly the market. The end market is strong. Part of it is TI is benefiting from design wins, really in a couple of areas. One is the Advanced Driver

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Assistance Systems, as well as infotainment. We're also seeing new opportunities in a couple of areas. Advanced Radar Systems, you've seen, for example. That's partly the driver assist, such as blind spot detection, but we're seeing radar technology in automobiles start to get deployed much broader than just – or at least considerations much broader than just blind spot detection.

Computing, no surprise there. The news flash is the overall PC market has been weak, continues to be weak. We'll see what happens when some of the new processors get introduced here in second half, but that space has been weak.

Comms infrastructure, I think I've pretty much said what I can say about that.

Communications – or handsets, rather – probably the big story for TI is just the ongoing declines in legacy wireless. I think we're actually doing pretty well in the broader handset market with some of the other products we have, like audio amplifiers, et cetera. But if you just look at that market overall, it's getting, for TI, swamped out by what's happening at certain customers in terms of their own adjustments, but then also our legacy wireless trends.

And then consumer, I would just say that game consoles were weak last quarter, as we have manufacturers in that space preparing for new product interruptions and transitions here in the second half. Television I would describe as generally weak. I think there's some new technologies that are being introduced that hold some promise for growth there. But overall I would say the market is weak. And that's about it.

So all right, Joe. Thank you for your questions. And we'll move to the next caller.

Operator: And we'll move along to Vivek Arya of Bank of America Merrill Lynch.

<Q – Vivek Arya – Bank of America Merrill Lynch>: Thanks for taking my question. I wanted to address this demand environment question I think being asked in different ways from a geographic perspective. How much of the growth that you're seeing right now is U.S. centric versus, say, coming from China and Europe? Because the macro data points from China and Europe are still quite mixed. So if you could just give us a sense of how demand is from a geographic perspective?

<A – Ron Slaymaker – Texas Instruments Incorporated>: So let me just give you the data, and then I'll let you figure out how to interpret it. But if you look at our revenue in the second quarter, we saw the highest growth – and this is just on a dollar basis – out of Asia, followed by the U.S., followed by Japan. Europe was down what I would characterize as a little, meaning a couple percent. But all regions were up. Asia was the strongest from a dollar standpoint, but it's also where over, what, 60%, 65% of our revenue is shipping these days. And then U.S. was the strongest in terms of percentage growth but is much smaller than what Asia is for us.

And then the only caution, Vivek, that I always attach to that is you have to be a little careful. I mean, Asia is where a lot of products are being manufactured and then turned around and shipped back to other markets such as the U.S. for consumption. So it's not a statement about economic conditions or changes there in those markets. It's strictly a matter of our customers manufacturing in those various regions.

Do you have a follow-on, Vivek?

<Q – Vivek Arya – Bank of America Merrill Lynch>: Yes. Thanks, Ron. Just as a clarification, what percentage of the sales now are disty versus direct? And then within that, if you could give us a split of sell-in versus sell-through? Thank you.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay. So 55% of our revenue goes through distribution now. If you look at that distribution revenue, about 50% of that is now supported by consignment. So that's a proxy for your sell-in versus sell-out. Officially and technically, we're on sell-in recognition with distribution, but the half of the revenue that's on consignment behaves like sell-out in that the distributors' revenue doesn't get recognized until they pull it out of that consignment hardware – out of that consignment inventory to then directly ship it to a customer. So it behaves like sell-out.

Just more broadly, about 45% of our overall revenue now is supported by consignment and/or JIT programs. And so if you kind of put all that together, that means that only about a quarter of our revenue is not on consignment or in distribution. And the reason I point that out is because where we have consignment, we have really good visibility into that customer's or distributor's TI inventory levels. And, in fact, for distributors more broadly, even where they're not on consignment, we know what their TI inventory is. So the point being, for about 75% of our I'll call it revenue coverage, we have pretty good insight into inventories. And when we characterize them as lean or well managed, I guess is maybe a different word to think of as of now, we do that with pretty direct visibility.

The 25% that's not on consignment or not at distribution, we have the same kind of visibility as any supplier would that's on a normal backlog where you talk to customers. But we're not seeing it directly. But for 75%, we have good visibility, and we feel good about where inventories are right now in our channels and at our customers.

Okay, Vivek. Thank you for your questions. And, operator, we'll go to the next caller.

Operator: At this time we'll take a question from Chris Caso with Susquehanna Financial Group.

<Q – Chris Caso – Susquehanna Financial Group LLP>: Hi, thank you. Just a question about some of the extended visibility you said your customers are providing to you. With the lead times not really changed, why do you think the customers are giving you that extended visibility? I guess is it just as simple as they're feeling more confident about their business in the second half? Could you give a little more color on that?

<A – Ron Slaymaker – Texas Instruments Incorporated>: I think it's a combination of things. I think that's part of it. So as they get more comfortable with their own forecast and their own outlook, they're more comfortable putting, call it, the commitment that's associated with backlog on their suppliers. So I think that's part of it. I think the other part of it, and I don't know how to weight one versus the other, is that, frankly, I think some of TI's competitors are out talking to customers kind of signaling potential upcoming lead time extensions. And when that happens, the customers, for their own benefit, go ahead and try to get backlog placed. And typically when they do that, they don't just place backlog where they think lead times are going out. They're going to place backlog for a full system. And so we're seeing some of that as well.

So I think, again, some of it's customers – I'm sorry, competitor induced, where they're concerned about their ability to support the full customer demand and their capacity situation. And then the other part of it is just customers' increased confidence in their own – demand for their own products.

Okay, Chris, do you have a follow-on?

<Q – Chris Caso – Susquehanna Financial Group LLP>: Yes. Thank you. And I guess just following up on that, and I guess to the extent that you have the visibility, do you see the customers and the distributors wanting to put on a little more inventory as we go through the holiday season? And, again, realizing that your capacity utilization is still probably a lot lower than your competitors', I guess you would see that as an opportunity to kind of pick up some market share there?

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<A – Ron Slaymaker – Texas Instruments Incorporated>: Again, I don't know that. There's probably some natural inventory that goes along with getting ready for a seasonal holiday build. I don't know at this point that I would try to distinguish between just higher demand versus inventory replenishment, especially where we have consignment. As I said, for – or distribution – that's 75% of our revenue, inventory build of TI chips. Now, that's not reflecting of anything about the customers' end product inventory situation. But inventory of TI chips, there is no such thing. Basically, we manage the consignment inventory to a certain turns level. So we take responsibility for that.

Okay, Chris, thank you for your questions. And, operator, I think we have time for one final caller.

Operator: Okay, this question will come from Tore Svanberg with Stifel.

<Q – Tore Svanberg – Stifel, Nicolaus & Co., Inc.>: Yes. Thank you. My first question is on CapEx. I know in the past you've talked about having sufficient capacity right now to get to about $18 billion in revenue, meaning keeping the CapEx level pretty low. But is it safe to say that $97 million here this quarter is sort of the low for at least the near term?

<A – Kevin March – Texas Instruments Incorporated>: Tore, we are still holding our forecast for the year at about $500 million. We, as you point out, spent $97 million this quarter, and we spent about $84 million last quarter. You may recall that we did announce that we were acquiring an assembly test site in Chengdu, China. And of course that will require some cash in the second half for us to go ahead and close on that transaction. So I expect that we'll still stay in our $500 million – inside that overall budget for the year.

And then going forward, again for modeling purposes, I would expect us to be at about 4% of revenues going into CapEx up through $18 billion of revenue, at which point in time that may change, although I would also point out it is or objective to keep watching for inexpensive capacity. And to the extent that we can get that and extend that $18 billion ceiling for very low prices, we will be very opportunistic and open to that strategy.

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay, Tore, do you have a follow-on question?

<Q – Tore Svanberg – Stifel, Nicolaus & Co., Inc.>: Yeah, just one follow-up. I know this is a segment that you didn't discuss much on this call, but it's certainly a high-profile segment. But the Analog business that sell into smartphones and tablets, could you talk a little bit about how that's faring in the current environment, please?

<A – Ron Slaymaker – Texas Instruments Incorporated>: Okay. I guess what I would say is, from a – just even things like I probably mentioned midquarter, and I probably might have mentioned earlier in this call. In areas like audio amplifiers, relatively low-profile devices, they don't get headlined a lot or whatever, but we have a pretty strong and broad position in the handsets with those types of products. So we feel good about our progress there and position.

That also being said, those markets are more vertical. They're more concentrated. And so in this kind of environment, meaning second quarter, when you have big customers making an – inventory adjustments or whatever, they catch up that part of our business as well as all of our competitors that play into those spaces. So we did see some softness associated with that in the second quarter. The good news is, again, our exposure there is much lower than it has historically been, as it is in the PC market. And so when you get those vertical markets making those kinds of adjustments, it doesn't have the same kind of impact on TI that certainly it would have in our past. So hopefully that answered your question.

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Ron Slaymaker, Vice President, Head of Investor Relations

And with that, we're going to wrap up. Thank you for joining us. A replay of this call is available on our website. Good evening.

Operator: And, again, this does include today's conference call. Thank you all for your participation. You may now disconnect.

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