Magnachip Semiconductor
Prepared Remarks for Q2 2023 Investor Conference Call
August 7, 2023

Yujia Zhai

Hello everyone. Thank you for joining us to discuss Magnachip's financial results for the second quarter ended June 30, 2023. The second quarter earnings release that was issued today after the market close can be found on the Company's investor relations website. The webcast replay of today's call will be archived on our website shortly afterwards.

Joining me today is YJ Kim, Magnachip's Chief Executive Officer. Shinyoung Park, Magnachip's Chief Financial Officer, has returned from maternity leave. YJ will discuss the Company's recent operating performance and business overview, and Shinyoung will review financial results for the quarter and provide guidance for the third quarter of 2023. There will be a Q&A session following the prepared remarks.

During the course of this conference call, we may make forward-looking statements about Magnachip's business outlook and expectations. Our forward-looking statements, and all other statements that are not historical facts, reflect our beliefs and predictions as of today and therefore are subject to risks and uncertainties as described in the Safe Harbor statement found in our SEC filings.

During the call we also will discuss non-GAAP financial measures. The non-GAAP measures are not prepared in accordance with generally accepted accounting principles but are intended to illustrate an alternative measure of Magnachip's operating performance that may be useful. A reconciliation of the non-GAAP financial measures to the most directly comparable GAAP measures can be found in our second quarter earnings release in the investor relations section of our website. With that, I now will turn the call over to YJ Kim. YJ?

YJ Kim

Hello everyone, thank you for joining us today and welcome to Magnachip's Q2 earnings call.

Starting with our financials. Q2 revenue was $61 million, down 39.8% year-over-year and up 7% sequentially. Gross margin was 22.2%, up 100 basis points from Q1 driven by higher utilization at our Gumi Fab. Our year-over-year results continued to be impacted by macro challenges that I will detail in each of our business sections, but I am pleased to see sequential improvement in our Power business driven by Industrial and Automotive applications. These positives were offset by weaker OLED smartphone revenue during the quarter from our top Korea panel customer.

During the quarter, we also completed the $25.5 million of our remaining stock buyback program, and today I'm pleased that our Board approved a new stock buyback authorization of $50 million, which signifies our confidence in our long-term business and unwavering commitment to enhance shareholder value.

Finally, earlier in the second quarter, we announced that our Board approved the recommendation of its Strategic Review Committee to separate our Display and Power business into separate legal entities. Broadly speaking, this strategic separation represents a significant milestone for Magnachip and highlights our commitment to unlock long-term value for our shareholders. We are currently working through the process of separating the businesses so they will have distinct ERP (Enterprise Resource Planning) and accounting systems. The process is expected to be completed at the end of 2023 and go live in January 2024. Post-separation, the board and management team will continue to oversee both businesses. This internal separation is aimed at enhancing transparency, accountability, business flexibility as well as business focus and strategic optionality and we look forward to providing further updates on our upcoming earnings calls.

Let me now provide updates into each of our business segments:

Beginning with our Display business. Q2 revenue came in at $9.7 million, down 65.9% year-over-year and down 10.9% sequentially. Year-over-year, our results reflect the ongoing smartphone inventory correction and the continued impact of the last two year's supply shortage of 28nm 12-inch OLED wafers that affected our 2nd half 2022 design wins. Sequentially, our OLED revenue declined from Q1 due to decreased demand from our large Korean panel customer. Despite these near-term hurdles, we remain focused on expanding our customer base to include all major global panel customers to deliver highly competitive products to achieve sustainable long-term growth as an industry leader in display.

- **At our new global Tier 1 panel customer**, we delivered our second-OLED DDIC project sample in Q1 but due to spec changes by the customer, we revised and shipped a second chip at the end of June. We aim to receive final qualification in a few months and anticipate production at the end of the year.

- Additionally, we have sampled the third chip in Q2, which has been evaluated by the global panel customer, and is now at the design-in evaluation stage by a smartphone maker for first half 2024 launch.

- Further, with our new global panel customer, we continue to collaborate on new projects. In Q2, we began developing a 4th OLED

DDIC project for our global panel maker that has the potential to contribute revenue around mid-year 2024. Additionally, we started work on a mass-market OLED display driver, 5th chip, aimed at expanding market share of the low-to-mid-range OLED smartphone display market, which we expect to drive revenue growth in the second half 2024 and beyond.

- Given these developments, we feel confident about our odds of winning additional Asian smartphone designs and capturing significant market share over the longer-term in Asia. It is estimated that in Q2'23, China panel makers already have captured almost 40% of worldwide OLED smartphone panel production.

- **With regard to our large panel customer in Korea,** we began production shipment of our first OLED automotive chip in Q2 targeted for two different car models for a leading European Automaker. Following the quarter end, in July, we also initiated production shipment targeted to another top-tier European car manufacturer. We anticipate these three models to provide revenue beginning in the 2nd half of this year and beyond.

- Further, we secured two new design wins with a third European Automaker in Q2, with mass production slated for 2nd half 2025. With these wins, we now have five cumulative design wins targeted for car models from leading European automakers.

- For our smartphone DDIC project at our large panel customer in Korea, we are awaiting our customer's alignment with Chinese Smartphone OEMs, and look for such alignment by the end of the year.

Moving on to our Power business: Q2 revenue was $41.7 million, down 33.7% year-over-year and up 2.6% sequentially due to strength in Industrials and Automotive markets.

- As we stated in our last quarter call, we believe we hit the bottom in Q1'23 and we saw progress in inventory on hand. The demand improvement in Q2 was broad based. For instance, we saw a revival in demand for TVs, solar, and lighting markets.

- Additionally, we continued our strong momentum of design activities in Q2 propelled by our robust product portfolio across automotive, industrial, and computing applications, in particular. Notably, 35% of the design-ins and wins are attributed to new products and customers, while more than 17% emerged from new applications. One key design win was at a leading home appliance maker in Korea, with production slated to begin in Q3'23.

- Power products ASP remained strong, increasing 25.3% YoY and down slightly by 2.2% sequentially on lower Premium product mix.

- We also continue to innovate. In early July, we announced four new low voltage MOSFETs using super-short channel technology that significantly improves power loss of smartphone batteries when charging or discharging.

In summary, in our Power business, our product design-in/win rate is stronger than ever and we're rolling out next generation power products throughout this year. Looking ahead, we are seeing some improvements in our customer base, and we expect further sequential growth in Q3.

In our Display business, we're very optimistic about the long-term growth of our OLED business. We continue to collaborate closely with our new global panel customer and we are excited about the additional new products that we are rolling out in the next 6 months. These new products offer compelling competitive advantages and are strategically aimed at tapping into the rapidly expanding OLED market in the Asian region.

Thank you to our shareholders for your patience, and we appreciate your support as we work towards our goals. I will now turn the call over to Shinyoung to go over the financials in detail.

Shinyoung Park:
Thank you YJ, and welcome to everyone on the call. Let's start with key financial metrics for Q2.

Total revenue in Q2 was $61 million, up 7% sequentially and down 39.8% year-over-year. Revenue from the standard products business was $51.4 million and revenue from Transitional Foundry Services was $9.6 million. Within standard products, Display business revenue was $9.7 million and Power business revenue was $41.7 million. As YJ mentioned, while our results are still muted, we see sequential improvement in Q3.

Gross margin in Q2 was 22.2%, up from 21.2% in Q1. We expect our Q3 2023 gross margin will gradually improve as utilization continues to improve with higher demand in our Power business.

As we have stated on prior calls, we are planning for a wind-down in our Transitional Foundry Services over the next several quarters following the end of our contractual agreement with Key Foundry at the end of August 2023. Transitional Foundry Services accounts for approximately 25% of our Gumi capacity. We anticipate to begin the process of converting portions of the idle capacity to Power Standard products around the middle of 2024.

Turning now to Operating Expenses. Q2 combined R&D and SG&A was $23.4 million. This compares to R&D and SG&A of $25.5 million in Q1 2023 and $26.1 million in Q2 last year. Our lower R&D and SG&A was primarily driven by our voluntary resignation program that we executed at the end of Q1. Stock compensation charges included in operating expenses were $2.0 million in Q2 compared to $1.1 million in Q1 and $1.9 million in Q2 last year.

Q2 operating loss was $10.7 million. This compares to an operating loss of $21.8 million in Q1 and an operating income of $2 million in Q2 2022. On a non-GAAP basis, Q2 adjusted operating loss was $7.8 million, compared to adjusted operating loss of $12.2 million in Q1 and adjusted operating income of $4.8 million in Q2 last year.

Q2 adjusted EBITDA was negative $3.6 million. This compares to a negative $7.9 million in Q1 and a positive $8.5 million in Q2 last year.

Net loss in Q2 was $3.9 million as compared with a net loss of $21.5 million in Q1 and a net loss of $3.3 million in Q2 last year.

Our GAAP diluted loss per share in Q2 was 9 cents, as compared with diluted loss per share of 49 cents in Q1 and 7 cents in Q2 last year.

Our non-GAAP diluted loss per share in Q2 was 6 cents. This compares with non-GAAP diluted loss per share of 24 cents in Q1 and an earnings per share of 23 cents in Q2 last year.

Our weighted average diluted shares outstanding for the quarter were 41.7 million shares, which reflects shares repurchased as part of our expanded share repurchase program. Our stock buyback in Q2 2023 amounted to approximately 2.5 million shares or $25.5 million. Cumulatively, since September last year to the end of Q2 this year, we've repurchased 4.9 million shares or $50 million.

Moving to the balance sheet:

We ended the quarter with no debt and cash of $173 million, down from $212.1 million at the end of Q1 2023. The primary cash outflows during the quarter were approximately $25 million of stock buybacks and payment of

$11.4 million related to the voluntary resignation program including one-time package cost of $8.4 million.

Net accounts receivable at the end of the quarter totaled $35.0 million, which represents an increase of 8.9% from Q1 2023. Our days sales outstanding for Q2 was 52 days and compares to 51 days in Q1.

Inventories, net at the end of the quarter totaled $32.3 million. This compares to $36.4 million in Q1 2023. Our average days in inventory for Q2 was 62 days and compares to 73 days in Q1.

Lastly, Q2 CAPEX was $1.4 million. We currently expect our CAPEX in 2023 to be approximately $7 million, which is about 30% lower from our previous forecast of $10 million and nearly 70% lower from the 2022 level.

Now moving to our third quarter guidance:
While actual results may vary, for Q3, Magnachip currently expects:

- Revenue to be in the range of $59 million to $65 million, including about $8 million of Transitional Foundry Services.

- Gross profit margin to be in the range of 22.5% to 24.5%.

Thank you and now I will turn the call back over to Yujia

Yujia Zhai
Thank you. That concludes the prepared remarks section of our call today, operator you may now open up the call for questions.

Yujia Zhai – Closing Remarks

Thank you! This concludes our Q2 earnings conference call. Please look for details of our future events on Magnachip's Investor Relations website.

Thank you and take care.