OVERVIEW:
Co. reported 4Q17 sales of $1.15b and EPS of $0.42. Expects 1Q18 revenues to be around $1.02b.
CORPORATE PARTICIPANTS

Greg Johnson  Amkor Technology, Inc. - VP of Finance and IR
Megan Faust  Amkor Technology, Inc. - Corporate VP & CFO
Stephen D. Kelley  Amkor Technology, Inc. - CEO, President & Director

CONFERENCE CALL PARTICIPANTS

Anastazia Goshko  BofA Merrill Lynch, Research Division - MD
Atif Malik  Citigroup Inc, Research Division - VP and Semiconductor Capital Equipment and Specialty Semiconductor Analyst
Randy Abrams  Crédit Suisse AG, Research Division - MD and Head of Taiwan Research in the Equity Research Department
Shek Ming Ho  Deutsche Bank AG, Research Division - VP

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Amkor Technology Fourth Quarter and Full Year 2017 Earnings Conference Call. My name is Jimmy, and I will be your conference facilitator today. (Operator Instructions)

As a reminder, this conference call is being recorded. I would now like to turn the call over to Greg Johnson, Vice President of Finance and Investor Relations. Mr. Johnson, please go ahead.

Greg Johnson  Amkor Technology, Inc. - VP of Finance and IR

Thank you, Jimmy, and good afternoon, everyone. Joining me today are Steve Kelley, our Chief Executive Officer; and Megan Faust, our Chief Financial Officer. Our press release was filed with the SEC this afternoon and is available on our website.

During this conference call, we will use non-GAAP financial measures, and you can find a reconciliation to the U.S. GAAP equivalent on our website.

We will also make forward-looking statements about our expectations for Amkor’s future performance based on the environment as we currently see it. Of course, actual results could be different. Please refer to our press release and other SEC filings for information on risk factors, uncertainties and exceptions that could cause actual results to differ materially from these expectations.

Please note that the financial results discussed today are preliminary and final data will be included in our Form 10-K.

And now, I would like to turn the call over to Steve.

Stephen D. Kelley  Amkor Technology, Inc. - CEO, President & Director

Good afternoon, and thanks for joining the call. Today, I’ll discuss our fourth quarter and full year performance, our 2018 priorities and our first quarter forecast.

Fourth quarter results were above the high end of our guidance. Sales grew 12% year-on-year and 1% sequentially. We experienced strong demand across all of our end markets and benefited from good factory execution.
Our sales performance drove healthy profitability and solid free cash flow. For the full year, we delivered record sales of $4.2 billion, 8% higher than our 2016 sales. This growth, coupled with good CapEx discipline, allowed us to generate $210 million in free cash flow in 2017.

Sales into all of our end markets were up year-on-year. Communications grew 11% and accounted for 43% of total sales. Automotive and industrial increased 6% to roughly $1.1 billion, accounting for 26% of total sales. As the leading OSAT for automotive ICs, our focus on quality, consistent execution and reliable technology continues to pay dividends. Computing was up 5%, accounting for 18% of total sales. And consumer increased 3%, contributing 13% of the total.

Advanced products drove most of our growth in 2017. Our investments in capacity, capability and engineering talent continued to generate good returns for Amkor.

In 2017, we enhanced our capabilities by acquiring NANIUM, the leader in wafer-level fan-out technology. The integration of NANIUM with Amkor is now complete. We've been impressed with the capabilities of the NANIUM team and with the quality and output of the Porto factory. Over the past 8 months, we transferred NANIUM's fan-out process to our K5 facility and expanded capacity in the Porto facility. Customers now have a choice of 2 world-class fan-out manufacturing lines, one in Portugal, one in Korea.

Moving on to the status of our other initiatives. In Greater China, sales grew 60% year-on-year largely due to demand for advanced packages. Many of those packages were built and tested in our Shanghai factory, which we believe to be the most advanced OSAT factory in China. Advanced SiP sales totaled $825 million, an increase of 6% year-on-year. Our ability to build and test high-yielding complex SiP modules has made us a leader in the RF and front-end module space.

Balanced revenue growth continues to be our overriding objective for 2018, just as it was in 2017. We believe that engaging broadly across multiple markets and regions is the best way to improve our financial results. In 2017, gains in the automotive and computing markets complemented our gains in the communications market. And within the communications market, we increased our participation in all major ecosystems. We plan to grow in a similar way in 2018.

I would now like to provide a little more color on 2 of our key technologies: wafer-level packaging and advanced SiP. Wafer-level packaging sales grew by 26% in 2017, sparked by gains in the smartphone market. Wafer-level packages are smaller, thinner and less expensive than substrate-based packages. They are very reliable when manufactured by a first-tier OSAT such as Amkor. We operate high-volume wafer-level packaging lines in 4 countries and serve over 150 customers.

There are 3 basic types of wafer-level packages: wafer-level chip scale packages, also known as fan-in; low-density fan-out; and high-density fan-out. Amkor has long been a leader in wafer-level CSPs, which drive enormous volume. We're also a leader in low-density fan-out, helped by our recent acquisition of NANIUM. Finally, in high density fan-out, Amkor's SWIFT solution is a cutting-edge technology ideally suited for space-constrained or performance-oriented high pin count applications.

Now let's touch on advanced SiPs, which we define as 2 or more dissimilar ICs together with external components in a single IC package. Today, our most complex advanced SiPs contain up to 200 electrical components. Although smartphone applications drive most of our volume, we are seeing the adoption of advanced SiPs in other applications including automotive. Advanced SiPs improve performance by moving ICs and other components closer together. They also improve reliability by reducing the number and length of interconnects. They are the primary vehicle for package-level integration, which allows customers to combine ICs from different process nodes and different foundries. In many case, package-level integration offers the most economical way to miniaturize. This is particularly true as leading-edge silicon geometries shrink below 10 nanometers.

Our wafer-level packages and advanced SiPs are built in highly automated factories with very clean environments. At our newest facility, K5, robots are used to move product from one machine to another. This type of automation is greatly valued by smartphone, automotive and high-performance computing customers.

Then moving on to our guidance. We expect first quarter 2018 revenues to be just over $1 billion, up roughly 12% year-on-year. In other words, revenue will be up more than $100 million year-on-year in our trough quarter.
Before closing, I'd like to note that 2017 marks the 50th anniversary of Amkor's founding. That's a very long time in the semiconductor business. That Amkor has thrived for 50 years is a testament to the determination and talent of our founder and executive chairman, Jim Kim. At its core, Amkor is a stable and reliable manufacturing partner. We survived this long by focusing on the basics: execution, quality, technology and service. And that won't change.

Megan will now provide more detailed financial information.

Megan Faust - Amkor Technology, Inc. - Corporate VP & CFO

Thank you, Steve, and good afternoon, everyone. Today, I will review our fourth quarter and full year results, then provide some comments about our first quarter expectations.

Looking at the fourth quarter, sales of $1.15 billion were an all-time record and drove gross margin of 19.6%, well above the high end of guidance. Our results also benefited from the completion of our Japan factory consolidation in the quarter.

We earned $0.42 per share in the quarter. Net income includes an estimated onetime net tax benefit of $42 million or $0.17 per share due to the enactment of U.S. tax reform. The Q4 2017 tax benefit is driven by the reversal of a valuation allowance against certain deferred tax assets. In addition, we do not expect to pay any material taxes for the onetime toll charge on the deemed repatriation of earnings of our U.S.-owned foreign subsidiaries. We expect that our estimated toll charge of $160 million will be offset by the application of foreign tax credit.

2017 was a year of transition for Amkor with many notable accomplishments. We had record revenues of $4.2 billion. With CapEx discipline and prudent asset management, we delivered $210 million of free cash flow, up $70 million from 2016 and our third consecutive year of free cash flow growth. We completed factory consolidation efforts in Japan. We redeemed $200 million of the outstanding senior notes due 2021 using cash on hand, which is expected to produce pretax interest savings of approximately $13 million in 2018.

We opened, qualified and began production at our state-of-the-art K5 factory in Korea. We acquired and integrated NANIUM, the industry leader in wafer-level fan-out technology. We closed and sold our K1 factory in Korea, which resulted in a pretax gain of over $100 million. And even after excluding the proceeds from the sale of our K1 factory, we were able to maintain operating income levels consistent with 2016, despite the incremental costs associated with our multiple transition projects.

We also generated nearly $1 billion of EBITDA in 2017. And capital expenditures were $550 million, consistent with our guidance.

As of December 31, we had total debt of $1.4 billion and debt-to-EBITDA of 1.4x. This is a significant improvement from our ratio of 2.4x 2 years ago.

Our liquidity is solid. We had $600 million in cash and around $300 million in available undrawn loans at the end of Q4.

Before I review our first quarter expectations, I wanted to mention that there will be a change in our accounting for revenue recognition beginning in 2018. We do not expect this change to have a material impact on our annual revenue, and our guidance for Q1 reflects the new standard.

First quarter 2018 revenues are expected to be around $1.02 billion, up 12% year-on-year. The revenue increase is expected to drive a 40% increase in operating income over Q1 2017.

We expect first quarter gross margin to be between 14% and 16%. Our Q1 2018 gross margin guidance reflects about 100 basis points of unfavorable foreign currency impact when compared with Q1 2017.

Our full year 2018 forecast for capital expenditures is around $600 million.
Operating expenses are expected to be around $120 million for the first quarter. R&D expense includes labor, depreciation and other costs associated with K5. As we bring lines up to production, some of these costs transition to cost of goods sold. This transition began in 2017 and will continue through 2018 until K5 is fully operational. Our quarterly operating expenses will then return to more traditional levels of around $105 million.

We expect our 2018 full year effective tax rate to be around 25%. Our initial estimates of the financial impact of the U.S. tax reform act could change as we refine our analysis and if any additional guidance on this new law becomes available.

With that, we will now open the call up for your questions. Operator?
**Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director**

Yes, that's a good question because you're right, we're about 2 years into a bull market in general market semiconductors, which I define as everything but smartphone. And so thinking about that, we think there are some trends that are working in our favor that are offsetting the normal cyclical of the market. One of course is just the solid economic fundamentals. Right now, I think the IMF just revised their forecast worldwide growth to 3.9% for this year and 3.9% for next year. So that helps the whole industry. We're seeing the trend in electronic content and all types of vehicles and other electronic gadgets. And finally, the industry consolidation seems to be helping because there's less tendency to build inventory. So we continuously monitor the channel inventory, and we've been unable to detect any perturbations there. So the market is pretty healthy.

**Shek Ming Ho - Deutsche Bank AG, Research Division - VP**

Okay, maybe I can squeeze one more in. For the automotive market, your -- I think you mentioned, your growth was 6% last year, but I'm guessing currency was a headwind as well. How do you think the long-term potential for this market look like?

**Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director**

We're very excited about automotive. We have a great starting position. We're the #1 OSAT by far in automotive. And what we expect is that the market will grow at a CAGR of high-single digits, probably 8% or 9% a year. It's lumpy. We grew 6% in 2017. We grew over 20% in 2016. We think on average, we'll be growing in high-single digits, a little bit faster than the market, we think. The content story is tremendous, being driven by the safety area, the advanced driver assistance systems and certainly by smart vehicles. But throughout the car, the increasing sophistication of the sensors and the processing is really helping drive the OSAT automotive TAM upwards. The other good trend for us is that many of the new functions require advanced packaging, and so the advanced packaging tends to be done more in OSATs. In the mainstream packaging, the wirebond packaging, there are still a lot of capacity within the IDM customers. So there's less TAM available to us on the wirebond products.

**Operator**

And our next question comes from Randy Abrams with Crédit Suisse.

**Randy Abrams - Crédit Suisse AG, Research Division - MD and Head of Taiwan Research in the Equity Research Department**

I wanted to ask a question just more on the sales trend. I think you said, and just reiterate, for fourth quarter, where the upside, I guess, relative to your initial guidance came through. And then looking forward, I guess, just if you could take first quarter's relative strength and weakness. And then for the pickup as we go through the year, how you see second quarter get back to normal rebound. And then for full year, if you could give an initial view, Amkor relative to industry.

**Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director**

Okay, yes. So the fourth quarter upside was really a story of the iOS ecosystem. It continued very strong through the end of the quarter. We expect a little bit of a fade in December. It didn't happen. And so that's what caused us to end up well ahead of our midpoint guidance in Q4. As we look at Q1, we think the general market is going to stay quite strong. We don't see any letup there. The smartphone market is down off a very high Q4 '17. However, if you look Q1 of last year to Q1 of this year, the smartphone market is up significantly. So Q1 is over $100 million stronger than it was Q1 '17. So we're pretty happy with that since this is our trough quarter. Looking forward, we believe that this year will be one of normal seasonality. So we think Q2 is going to be better than Q1, and we think Q3 is going to be better than Q2. Q4 is always a question mark. It depends on the success of the phone launches. But I think Q4 is typically plus or minus the result in Q3.
Okay. The second question, on CapEx, the $600 million, if you could just go through the priorities for spending it, if there's any facility upgrades in there, warehouse (inaudible). Also on the...

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes, yes. So your question is about CapEx, right? You're just a little faint. So I'm going to -- I think I heard what you asked.

Randy Abrams - Crédit Suisse AG, Research Division - MD and Head of Taiwan Research in the Equity Research Department

Okay. Yes, just on CapEx, just what are your priorities for CapEx and whether you include like any fan-out, like stepped up fan-out investments.

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes, yes. So our CapEx in 2018 will be roughly $600 million. 70% of that will be spent on capacity expansion and maintenance and the other 30% on R&D and new facilities. Specifically with regards to fan-out, we expanded capacity in 2017. So we expanded the capacity in Porto, and then we also built some initial capacity in K5. And we're ready to expand it more as the demand develops. We have a number of customers who are in qualification. And if they're successful, then we'll go ahead and spend more to expand the fan-out capacity. This is the low density fan-out, the NANIUM processed. We're also building high-density fan-out on the same line in K5. And so we share equipment between the 2 lines, which makes everything more efficient for us.

Randy Abrams - Crédit Suisse AG, Research Division - MD and Head of Taiwan Research in the Equity Research Department

And the follow-up I have just on the fan-out, maybe your latest view on how it's progressing, if it still looks it needs more time in terms of whether it's technology or cost relative to mainstream flip chip, just to get into the high-volume mobile market. Just if you kind of have a feel for time line, if it looks like it's 2019, or if it looks like it's actually taking more time for that to really get into high commercial volume.

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes. The fan-out market is just a fraction of the size of the wafer-level CSP market. However, what we've seen is that the fan-out opportunities flex depending on what's happening in the next design iteration from the customer. Generally speaking, what we see is wafer-level CSP designs that migrate to wafer-level fan-out if the customer shrinks the die and, as a result, doesn't have enough room to put all the bumps on the service area of the die. And so the basic economic equation is, hey, if I could shrink the die and save enough money to pay for a slightly higher wafer-level fan-out package, then it makes sense to do it. The other, I think, deterrent for customers has been lack of expansion capacity. And with the purchase of NANIUM by Amkor, I think customers have been reassured that if the demand goes up, we'll stay with them. And we have multiple locations, so they have options within Amkor so that we can meet their capacity demands.

Randy Abrams - Crédit Suisse AG, Research Division - MD and Head of Taiwan Research in the Equity Research Department

Okay, and the last question for Megan, the -- you generated improving free cash flow at over $200 million. Just the outlook, another kind of good year for the industry and Amkor. Is it your view you'd just use that to continue the debt paydown? And do you see opportunities now from that rise in free cash flow?
Megan Faust - Amkor Technology, Inc. - Corporate VP & CFO

Yes, Randy, so as we continue to build cash, our first priority will always be to invest in the business and fund our capital expenditures. And then we will continue to look for opportunistic ways to delever. And as you noted, we did take that opportunity in 2017 with our increased cash flow to pay down $200 million of our highest-cost debt. So as we move forward into 2018, we'll keep those priorities.

Operator

And our next question comes from Ana Goshko of Bank of America.

Anastazia Goshko - BofA Merrill Lynch, Research Division - MD

I have a few questions. Just a follow-up on the previous question. So I think the free cash flow in 2017 included some sale proceeds from K1. So as we look into 2018, I just want to be clear that you do still expect to achieve free cash flow even without any sale proceeds.

Megan Faust - Amkor Technology, Inc. - Corporate VP & CFO

Ana, yes. So although we do have the proceeds from K1 in our 2017 free cash flow, we normally don’t guide 2018 free cash flow, but we do expect to be free cash flow positive.

Anastazia Goshko - BofA Merrill Lynch, Research Division - MD

Great. Okay. And then just on the uses of free cash flow, wondering on the back of the successful acquisition of NANIUM, if there are any other opportunities along those lines that you’re looking at for potential tuck-ins or other capabilities to be added via M&A.

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes, Ana, we’re always on the lookout for tuck-in acquisitions. We’ve had a good track record. Before NANIUM, we purchased a power discrete facility from Toshiba in 2013. That’s worked out very well for us financially. And of course, we purchased J-Devices 2 years ago, and that’s also working out well. So we’re always on the lookout. We’re opportunistic and looking for cost effective ways to expand our business.

Anastazia Goshko - BofA Merrill Lynch, Research Division - MD

Okay. And then on the gross margin target for the year. I know in the past, the company had said that 20% was an aspirational target. I wanted to understand if you believe that’s achievable.

Megan Faust - Amkor Technology, Inc. - Corporate VP & CFO

Yes, Ana. As far as the gross margin target of 20%, that does continue to be our objective from a corporate perspective. Just looking back at our performance in 2017, both Q3 and Q4 reached that 20% gross margin target after we would exclude the onetime costs for our Japan consolidation efforts. So we’re really pleased with that performance. So looking forward in 2018, now that we’ve completed the Japan consolidation activities, we’ve put ourselves in a better position to achieve that goal. And so we’ll expect to have those savings in 2018 that will help to offset the incremental costs that we’re expecting to incur with K5 ramp as well as any other manufacturing costs including FX headwinds.
Anastazia Goshko - BofA Merrill Lynch, Research Division - MD

Okay, great. And final question, promise. So you have been sitting with these bonds that have 6% coupons on them, which is relatively high for a company that's 1x levered. And given that we seem to be in a rising interest rate environment these days, have you given thought to refinancing those bonds?

Megan Faust - Amkor Technology, Inc. - Corporate VP & CFO

Yes, of course. We continue to evaluate our corporate capital structure and look for ways to optimize the cost of our debt. So we will be taking a look at that in 2018 and also consider our foreign versus U.S. held debt.

Operator

The next question comes from Atif Malik from Citigroup.

Atif Malik - Citigroup Inc, Research Division - VP and Semiconductor Capital Equipment and Specialty Semiconductor Analyst

First question on the auto market, Steve. If you can just talk about near term. We have seen some lower-than-expected results from Renesas microchip on analog auto side. Can you just talk about the health of the auto industry near term to what you're seeing?

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes, Atif. I think the automotive industry near term is relatively flat. So again, this market grows in fits and starts. The nice part about automotive, it rarely goes down very much. So I think we're going through one of those flat periods, and then things will take off again later this year.

Atif Malik - Citigroup Inc, Research Division - VP and Semiconductor Capital Equipment and Specialty Semiconductor Analyst

Okay. And then on your low-density fan-out and high-density fan-out packages, can you just talk about the applications you're using these packages for? Are these mostly for smartphone, or you plan to use these for data center and high-performance computing?

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes, Atif. The volume is driven by smartphone applications. So basically the customers, they're using the bulk of these fan-out products, are using those products in smartphone and other small form factor applications. So they're doing it for size. But we're also seeing a lot of interest from high-performance applications. It could be data center. It could be artificial intelligence. It could be automotive applications that require the type of performance you can only get with a fan-out package.

Atif Malik - Citigroup Inc, Research Division - VP and Semiconductor Capital Equipment and Specialty Semiconductor Analyst

Okay, the last one for Megan. Megan, assuming Japan consolidation benefits are in the March quarter guide, and you mentioned the sales are up $100 million year-over-year. Can you just talk about the gross margins, how much they are up or down year-over-year for the March quarter?

Megan Faust - Amkor Technology, Inc. - Corporate VP & CFO

Sure. So looking at our Q1 guidance, we're about $100 million more in revenue. And as mentioned, our Q1 gross margin does have an estimated 100 basis points impact due to foreign currency headwinds. So if we were to exclude that, our profitability year-over-year has also improved. So
we see that our expected Q1 performance is a really good start to 2018. And that's where we started to enjoy the benefits from the Japan consolidation activity.

Operator

(Operator Instructions)

Greg Johnson - Amkor Technology, Inc. - VP of Finance and IR

Okay. Thank you, Jimmy. That ends the Q&A portion of the call. I'd like to turn it back over to Steve for his closing remarks.

Stephen D. Kelley - Amkor Technology, Inc. - CEO, President & Director

Yes, I'd like to recap our key messages. First, 2017 was a very good year for Amkor Technology. We grew revenue 8% and generated good cash flow. We reduced our debt while making significant investments in capacity and capability. Q1 '18 revenues will be up roughly 12% year-on-year. And finally in 2018, our primary objective is balanced revenue growth, which will drive healthy operating cash flow and profitability. Thank you for joining the call today.

Operator

Ladies and gentlemen, this concludes today's conference call. You may now disconnect. Everyone, have a great day.