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Lattice Semiconductor Q3 2006 Earnings Call

Question-and-Answer Session

Operator

Thank you. Today's question-and-answer session will be conducted electronically. (Operator Instructions). Let's take our first question from Shawn Webster with J.P. Morgan. Mr. Webster, please go ahead. Your line is open.

Shawn Webster - J.P. Morgan

Oh, yes, sorry. This is Shawn Webster for Chris Danely. Could you please comment a little bit more on your gross margins, what drove them down in the quarter? I understand it was mix, but maybe you could give us a better sense on the sensitivity, maybe looking into Q4 in the first half of next year on where your margins could go and how sensitive they are to the new product mix? And then I have a follow-up, please.

Steve Skaggs

Well, we've said for some time now that our new products are priced for penetration. We expect with yield and wafer price cost projections to earn corporate margin targets on those products over time, which is 55 to 60%. But really, in terms of the way we think about managing our business, our new products are lower than the corporate margin target and the mature products are higher than the corporate margin target and the mainstream products tend to be at the corporate margin target. We've continued to make good progress with regard to cost reductions and are satisfied with where we are in that regard. It's very difficult for us to project mix at a very fine level, so last quarter, we had good growth in new products, but also growth in the consumer market segment and those products also tend to carry lower margin and more than anticipated shrinkage in the mature products, which tended to drive the margin down a little bit. So, that's basically the additional granularity I can give you on looking backwards.

Shawn Webster - J.P. Morgan

Okay.

Steve Skaggs

Looking forward, really, we believe that the margin will continue to be hard to predict, hence the wide range. We do anticipate continued cost reduction and yield improvements on our own 130 nanometer products and we also have negotiated cost reductions on our older processes that will impact positively the fourth quarter. That's something we do on a regular basis and we've made very

good progress there with our cost structure on our older products. On the other hand, the consumer market is very strong and it tends to be seasonally strong in the fourth quarter, so we anticipate a big growth in revenue in the consumer market in the fourth quarter, so that's going to depress the margin some what. And additionally, we're running additional engineering and risk production wafers on our the 90 nanometer products in order to meet our aggressive release schedules and what frankly is very strong early prototyping demand for those products, like at the early stage of production, the cost structure is higher on those products and that's to be expected. So really, we expect margin to be flat, but there may be a wider variability depending on how each of those factors play out during the quarter.

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