TEXAS INSTRUMENTS INC
Form 10-Q
April 30, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2019

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ___________ to ___________

Commission File Number 001-03761

TEXAS INSTRUMENTS INCORPORATED

(Exact Name of Registrant as Specified in Its Charter)

Delaware	75-0289970
(State of Incorporation)	(I.R.S. Employer Identification No.)

12500 TI Boulevard, Dallas, Texas	75243
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code 214-479-3773

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes No

Indicate by check mark whether the Registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit such files). Yes No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the Registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No

938,206,171

Number of shares of Registrant's common stock outstanding as of

April 23, 2019

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

PART I - FINANCIAL INFORMATION

ITEM 1. Financial statements

Consolidated Statements of Income (Millions of dollars, except share and per-share amounts)	For Three Months Ended March 31, 2019	 2018
Revenue	$ 3,594	$ 3,789
Cost of revenue (COR)	1,333	1,342
Gross profit	2,261	2,447
Research and development (R&D)	389	385
Selling, general and administrative (SG&A)	414	433
Acquisition charges	79	80
Restructuring charges/other	—	1
Operating profit	1,379	1,548
Other income (expense), net (OI&E)	36	28
Interest and debt expense	38	23
Income before income taxes	1,377	1,553
Provision for income taxes	160	187
Net income	$ 1,217	$ 1,366
Earnings per common share (EPS):		
Basic	$ 1.29	$ 1.38
Diluted	$ 1.26	$ 1.35
Average shares outstanding (millions):		
Basic	939	983
Diluted	956	1,005

A portion of net income is allocated to unvested restricted stock units (RSUs) on which we pay dividend equivalents. Diluted EPS is calculated using the following:

Net income	$ 1,217	$ 1,366
Income allocated to RSUs	(8)	(11)
Income allocated to common stock for diluted EPS	$ 1,209	$ 1,355

See accompanying notes.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income (Millions of dollars)	For Three Months Ended March 31, 2019	2018
Net income	$ 1,217	$ 1,366
Other comprehensive income (loss), net of taxes		
Net actuarial losses of defined benefit plans:		
Adjustments	(2)	(16)
Recognized within net income	10	9
Prior service credit of defined benefit plans:		
Recognized within net income	—	(1)
Other comprehensive income (loss)	8	(8)
Total comprehensive income	$ 1,225	$ 1,358

See accompanying notes.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Consolidated Balance Sheets	March 31, 2019	December 31, 2018
(Millions of dollars, except share amounts)		
Assets		
Current assets:		
Cash and cash equivalents	$ 3,720	$ 2,438
Short-term investments	366	1,795
Accounts receivable, net of allowances of ($17) and ($19)	1,440	1,207
Raw materials	191	181
Work in process	1,016	1,070
Finished goods	924	966
Inventories	2,131	2,217
Prepaid expenses and other current assets	294	440
Total current assets	7,951	8,097
Property, plant and equipment at cost	5,642	5,425
Accumulated depreciation	(2,324)	(2,242)
Property, plant and equipment	3,318	3,183
Long-term investments	281	251
Goodwill	4,362	4,362
Acquisition-related intangibles	549	628
Deferred tax assets	290	295
Capitalized software licenses	98	89
Overfunded retirement plans	96	92
Other long-term assets	498	140
Total assets	$ 17,443	$ 17,137
Liabilities and stockholders’ equity		
Current liabilities:		
Current portion of long-term debt	$ 750	$ 749
Accounts payable	477	478
Accrued compensation	342	724
Income taxes payable	113	103
Accrued expenses and other liabilities	477	420
Total current liabilities	2,159	2,474
Long-term debt	5,057	4,319
Underfunded retirement plans	120	118
Deferred tax liabilities	43	42
Other long-term liabilities	1,545	1,190
Total liabilities	8,924	8,143
Stockholders’ equity:		
Preferred stock, $25 par value. Authorized – 10,000,000 shares		
Participating cumulative preferred – None issued	—	—
Common stock, $1 par value. Authorized – 2,400,000,000 shares		
Shares issued – 1,740,815,939	1,741	1,741
Paid-in capital	1,927	1,950
Retained earnings	38,396	37,906

Treasury common stock at cost		
Shares: March 31, 2019 – 802,016,668; December 31, 2018 – 795,665,646	(33,080)	(32,130)
Accumulated other comprehensive income (loss), net of taxes (AOCI)	(465)	(473)
Total stockholders' equity	8,519	8,994
Total liabilities and stockholders' equity	$ 17,443	$ 17,137

See accompanying notes.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Consolidated Statements of Cash Flows (Millions of dollars)	For Three Months Ended March 31, 2019	2018
Cash flows from operating activities		
Net income	$ 1,217	$ 1,366
Adjustments to net income:		
Depreciation	166	137
Amortization of acquisition-related intangibles	79	80
Amortization of capitalized software	13	12
Stock compensation	61	70
Gains on sales of assets	(2)	—
Deferred taxes	4	(31)
Increase (decrease) from changes in:		
Accounts receivable	(233)	(176)
Inventories	86	(97)
Prepaid expenses and other current assets	223	356
Accounts payable and accrued expenses	(67)	(51)
Accrued compensation	(373)	(372)
Income taxes payable	(94)	(131)
Changes in funded status of retirement plans	7	(15)
Other	20	(36)
Cash flows from operating activities	1,107	1,112
Cash flows from investing activities		
Capital expenditures	(251)	(189)
Proceeds from asset sales	2	—
Purchases of short-term investments	(149)	(996)
Proceeds from short-term investments	1,584	1,455
Other	(13)	(4)
Cash flows from investing activities	1,173	266
Cash flows from financing activities		
Proceeds from issuance of long-term debt	743	—
Dividends paid	(724)	(611)
Stock repurchases	(1,152)	(873)
Proceeds from common stock transactions	151	178
Other	(16)	(11)
Cash flows from financing activities	(998)	(1,317)
Net change in cash and cash equivalents	1,282	61
Cash and cash equivalents at beginning of period	2,438	1,656
Cash and cash equivalents at end of period	$ 3,720	$ 1,717

See accompanying notes.

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TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Notes to financial statements

1. Description of business, including segment and geographic area information

We design, make and sell semiconductors to electronics designers and manufacturers all over the world. We have two reportable segments, which are established along major categories of products as follows:

- Analog – consisting of the following product lines: Power, Signal Chain and High Volume.
- Embedded Processing – consisting of the following product lines: Connected Microcontrollers and Processors.

We report the results of our remaining business activities in Other. Other includes operating segments that do not meet the quantitative thresholds for individually reportable segments and cannot be aggregated with other operating segments. Other includes DLP® products, calculators and custom ASIC products.

Our centralized manufacturing and support organizations, such as facilities, procurement and logistics, provide support to our operating segments, including those in Other. Costs incurred by these organizations, including depreciation, are charged to the segments on a per-unit basis. Consequently, depreciation expense is not an independently identifiable component within the segments' results and, therefore, is not provided.

Segment information

	For Three Months Ended March 31,	
	2019	2018
Revenue:		
Analog	$ 2,518	$ 2,566
Embedded Processing	796	926
Other	280	297
Total revenue	$ 3,594	$ 3,789
Operating profit:		
Analog	$ 1,088	$ 1,166
Embedded Processing	249	328
Other	42	54
Total operating profit	$ 1,379	$ 1,548

Geographic area information

The following geographic area information includes revenue based on product shipment destination. The revenue information is not necessarily indicative of the geographic area in which the end applications containing our products are ultimately consumed because our products tend to be shipped to the locations where our customers manufacture their products. Specifically, many of our products are shipped to our customers in China who may include these parts in the manufacture of their own end products, which they may in turn export to their customers around the world.

For Three
Months Ended

	March 31,	
	2019	2018
Revenue:		
United States	$ 477	$ 504
Asia (a)	2,092	2,215
Europe, Middle East and Africa	743	771
Japan	191	220
Rest of world	91	79
Total revenue	$ 3,594	$ 3,789

(a) Revenue from products shipped into China was $1.7 billion and $1.6 billion in the first quarters of 2019 and 2018, respectively.

2. Basis of presentation and significant accounting policies and practices

Basis of presentation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) and on the same basis as the audited financial statements included in our annual report on Form 10-K for the year ended December 31, 2018, except for the effects of adopting Accounting Standards Update (ASU) No. 2016-02, Leases (Topic 842). The Consolidated Statements of Income, Comprehensive Income and Cash Flows for the periods ended March 31, 2019 and 2018, and the Consolidated Balance Sheet as of March 31, 2019, are not audited but reflect all adjustments that are of a normal recurring nature and are necessary for a fair statement of the results of the periods shown. Certain information and note disclosures normally included in annual consolidated financial statements have been omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. Because the consolidated interim financial statements do not include all of the information and notes required by GAAP for a complete set of financial statements, they should be read in conjunction with the audited consolidated financial statements and notes included in our annual report on Form 10-K for the year ended December 31, 2018. The results for the three-month periods are not necessarily indicative of a full year’s results.

Significant accounting policies and practices

Leases

We determine if an arrangement is a lease at inception. Leases are included in other long-term assets, accrued expenses and other liabilities, and other long-term liabilities on our Consolidated Balance Sheets.

Lease assets represent our right to use underlying assets for the lease term, and lease liabilities represent our obligations to make lease payments over the lease term. On the commencement date, leases are evaluated for classification, and assets and liabilities are recognized based on the present value of lease payments over the lease term. We use our incremental borrowing rate based on the information available at commencement in determining the present value of lease payments. Operating lease expense is generally recognized on a straight-line basis over the lease term. Our lease values include options to extend or not to terminate the lease when it is reasonably certain that we will exercise such options.

We have agreements with lease and non-lease components, which are accounted for as a single lease component. Leases with a lease term of 12 months or less are not recorded on the balance sheet; we recognize lease expense for these leases on a straight-line basis over the lease term.

Earnings per share (EPS)

We use the two-class method for calculating EPS because the restricted stock units (RSUs) we grant are participating securities containing non-forfeitable rights to receive dividend equivalents. Under the two-class method, a portion of net income is allocated to RSUs and excluded from the calculation of income allocated to common stock, as shown in the table below.

Computation and reconciliation of earnings per common share are as follows (shares in millions):

	For Three Months Ended March 31,					
	2019			2018		
	Net Income	Shares	EPS	Net Income	Shares	EPS
Basic EPS:						
Net income	$ 1,217			$ 1,366		
Income allocated to RSUs	(8)			(11)		
Income allocated to common stock	$ 1,209	939	$ 1.29	$ 1,355	983	$ 1.38
Dilutive effect of stock compensation plans		17			22	
Diluted EPS:						
Net income	$ 1,217			$ 1,366		
Income allocated to RSUs	(8)			(11)		
Income allocated to common stock	$ 1,209	956	$ 1.26	$ 1,355	1,005	$ 1.35

Potentially dilutive securities representing 9 million and 5 million shares of common stock that were outstanding during the first quarters of 2019 and 2018, respectively, were excluded from the computation of diluted earnings per common share during these periods because their effect would have been anti-dilutive.

Derivatives and hedging

We use derivative financial instruments to manage exposure to foreign exchange risk. These instruments are primarily forward foreign currency exchange contracts, which are used as economic hedges to reduce the earnings impact that exchange rate fluctuations may have on our non-U.S. dollar net balance sheet exposures. Gains and losses from changes in the fair value of these forward foreign currency exchange contracts are credited or charged to OI&E. We do not apply hedge accounting to our foreign currency derivative instruments.

In connection with the issuance of long-term debt, we may use financial derivatives such as treasury-rate lock agreements that are recognized in AOCI and amortized over the life of the related debt. The results of these derivative transactions have not been material.

We do not use derivatives for speculative or trading purposes.

Fair values of financial instruments

The fair values of our derivative financial instruments were not material as of March 31, 2019. Our investments in cash equivalents, short-term investments and certain long-term investments, as well as our deferred compensation liabilities, are carried at fair value. The carrying values for other current financial assets and liabilities, such as accounts receivable and accounts payable, approximate fair value due to the short maturity of such instruments. The carrying value of our long-term debt approximates the fair value as measured using broker-dealer quotes, which are Level 2 inputs. See Note 4 for a description of fair value and the definition of Level 2 inputs.

Changes in accounting standards – adopted standards for current period

ASU No. 2016-02, Leases (Topic 842)

We adopted ASU No. 2016-02, Leases (ASC 842) effective January 1, 2019, using the modified retrospective transition method applied to leases existing at, or entered into after, the adoption date. The reported results for 2019 reflect the application of the new accounting guidance, while the reported results for prior periods are not adjusted and continue to be reported in accordance with our historical accounting under ASC 840, Leases. In addition, we elected the package of practical expedients permitted under the transition guidance that allowed us to apply prior conclusions related to lease definition, classification and initial direct costs.

The adoption of the new standard resulted in the recognition of $229 million of lease liabilities with corresponding lease assets as of January 1, 2019. The standard did not materially impact our consolidated results of operations and had no impact on cash flows.

Other standards

The following standards were also adopted:

ASU	Description	Adopted Date

ASU No. 2017-12	Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities	January 1, 2019
ASU No. 2018-14	Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20): Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans	January 1, 2019

Changes in accounting standards – standards not yet adopted

ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments

This standard requires entities to use a current lifetime expected credit loss methodology to measure impairments of certain financial assets. Using this methodology will result in earlier recognition of losses than under the current incurred loss approach, which requires waiting to recognize a loss until it is probable of having been incurred. There are other provisions within the standard that affect how impairments of other financial assets may be recorded and presented, and that expand disclosures. This standard will be effective for our interim and annual periods beginning January 1, 2020, with early adoption permitted beginning January 1, 2019, and must be applied on a modified retrospective basis. We are currently evaluating the potential impact of this standard, but we do not expect it to have a material impact on our financial position and results of operations.

Other standards

We are evaluating the impact of the following standards, but we do not expect them to have a material impact on our financial position and results of operations. We plan to adopt these standards as of their effective dates.

ASU	Description	Effective Date
ASU No. 2018-13	Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement	January 1, 2020
ASU No. 2018-15	Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract	January 1, 2020

3. Income taxes

Our estimated annual effective tax rate is about 16%, which does not include discrete tax items. This differs from the 21% statutory corporate tax rate due to the effect of U.S. tax benefits.

Provision for income taxes is based on the following:

	For Three Months Ended March 31, 2019	For Three Months Ended March 31, 2018
Taxes calculated using the estimated annual effective tax rate	$ 220	$ 316
Discrete tax items	(60)	(129)
Provision for income taxes	$ 160	$ 187
Actual effective tax rate	12 %	12 %

4. Valuation of debt and equity investments and certain liabilities

Debt and equity investments measured at fair value

Available-for-sale debt investments and trading securities are stated at fair value, which is generally based on market prices or broker quotes. See Fair-value considerations below. Unrealized gains and losses from available-for-sale debt securities are recorded as an increase or decrease, net of taxes, in AOCI on our Consolidated Balance Sheets. Other-than-temporary impairments on available-for-sale debt securities are recorded in OI&E in our Consolidated Statements of Income.

We classify certain mutual funds as trading securities. These mutual funds hold a variety of debt and equity investments intended to generate returns that offset changes in certain deferred compensation liabilities. We record changes in the fair value of these mutual funds and the related deferred compensation liabilities in SG&A.

Other equity investments

Our other investments include equity-method investments and non-marketable equity investments, which are not measured at fair value. These investments consist of interests in venture capital funds and other non-marketable equity securities. Gains and losses from equity-method investments are recognized in OI&E based on our ownership share of the investee’s financial results.

Non-marketable equity securities are measured at cost with adjustments for observable changes in price or impairments. Gains and losses on non-marketable equity investments are recognized in OI&E.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Details of our investments are as follows:

	March 31, 2019			December 31, 2018		
	Cash and Cash Equivalents	Short-Term Investments	Long-Term Investments	Cash and Cash Equivalents	Short-Term Investments	Long-Term Investments
Measured at fair value:						
Available-for-sale debt securities:						
Money market funds	$ 1,073	$ —	$ —	$ 747	$ —	$ —
Corporate obligations	865	266	—	473	748	—
U.S. government agency and Treasury securities	1,497	100	—	988	1,047	—
Trading securities:						
Mutual funds	—	—	250	—	—	226
Total	3,435	366	250	2,208	1,795	226
Other measurement basis:						
Equity-method investments	—	—	27	—	—	21
Non-marketable equity investments	—	—	4	—	—	4
Cash on hand	285	—	—	230	—	—
Total	$ 3,720	$ 366	$ 281	$ 2,438	$ 1,795	$ 251

As of March 31, 2019, and December 31, 2018, unrealized gains and losses associated with our available-for-sale investments were not material. We did not recognize any credit losses related to available-for-sale investments for the first three months of 2019 and 2018.

Proceeds from sales, redemptions and maturities of short-term available-for-sale investments were $1.58 billion and $1.46 billion for the first quarters of 2019 and 2018, respectively. Gross realized gains and losses from these sales were not material.

The following table presents the aggregate maturities of our available-for-sale debt investments as of March 31, 2019:

	Fair Value
One year or less	$ 3,644
One to two years	157

There were no other-than-temporary declines and impairments in the values of our debt investments in the first three months of 2019 or 2018.

Fair-value considerations

We measure and report certain financial assets and liabilities at fair value on a recurring basis. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

The three-level hierarchy discussed below indicates the extent and level of judgment used to estimate fair-value measurements.

- Level 1 – Uses unadjusted quoted prices that are available in active markets for identical assets or liabilities as of the reporting date.
- Level 2 – Uses inputs other than Level 1 that are either directly or indirectly observable as of the reporting date through correlation with market data, including quoted prices for similar assets and liabilities in active markets and quoted prices in markets that are not active. Level 2 also includes assets and liabilities that are valued using models or other pricing methodologies that do not require significant judgment since the input assumptions used in the models, such as interest rates and volatility factors, are corroborated by readily observable data. We utilize a third-party data service to provide Level 2 valuations. We verify these valuations for reasonableness relative to unadjusted quotes obtained from brokers or dealers based on observable prices for similar assets in active markets.
- Level 3 – Uses inputs that are unobservable, supported by little or no market activity and reflect the use of significant management judgment. These values are generally determined using pricing models that utilize management estimates of market participant assumptions. As of March 31, 2019 and December 31, 2018, we had no Level 3 assets or liabilities.

The following are our assets and liabilities that were accounted for at fair value on a recurring basis. These tables do not include cash on hand, assets held by our postretirement plans, or assets and liabilities that are measured at historical cost or any basis other than fair value.

	March 31, 2019			December 31, 2018		
	Level 1	Level 2	Total	Level 1	Level 2	Total
Assets:						
Money market funds	$ 1,073	$ —	$ 1,073	$ 747	$ —	$ 747
Corporate obligations	—	1,131	1,131	—	1,221	1,221
U.S. government agency and Treasury securities	1,597	—	1,597	2,035	—	2,035
Mutual funds	250	—	250	226	—	226
Total assets	$ 2,920	$ 1,131	$ 4,051	$ 3,008	$ 1,221	$ 4,229
Liabilities:						
Deferred compensation	$ 266	$ —	$ 266	$ 246	$ —	$ 246
Total liabilities	$ 266	$ —	$ 266	$ 246	$ —	$ 246

5. Goodwill and acquisition-related intangibles

Goodwill was $4.36 billion as of March 31, 2019, and December 31, 2018. There was no impairment of goodwill during the first three months of 2019 or 2018.

The components of acquisition-related intangibles are as follows:

	Amortization	March 31, 2019			December 31, 2018		
	Period (Years)	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Developed technology	7 - 10	$ 2,125	$ 1,627	$ 498	$ 2,125	$ 1,573	$ 552
Customer relationships	8	810	759	51	810	734	76
Total		$ 2,935	$ 2,386	$ 549	$ 2,935	$ 2,307	$ 628

Acquisition charges

Acquisition charges represent the ongoing amortization of intangible assets resulting from the acquisition of National Semiconductor Corporation. These amounts are included in Other for segment reporting purposes, consistent with how management measures the performance of its segments.

Amortization of acquisition-related intangibles was $79 million and $80 million for the first quarters of 2019 and 2018, respectively. Fully amortized assets are written off against accumulated amortization.

6. Postretirement benefit plans

Expense related to defined benefit and retiree health care benefit plans is as follows:

	U.S. Defined Benefit		U.S. Retiree Health Care		Non-U.S. Defined Benefit	
For Three Months Ended March 31,	2019	2018	2019	2018	2019	2018
Service cost	$ 4	$ 5	$ 1	$ 1	$ 8	$ 9
Interest cost	9	9	3			