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EDITED TRANSCRIPT

ADI - Analog Devices Inc at Citi Global Technologies Conference

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PRESENTATION

Chris Danely - *Citigroup - Analyst*

Still Chris Danely, still the semiconductor analyst here at Citigroup. Next up is Analog Devices, absolutely nothing going on with these guys. I think it was clearly the most dramatic and unexpected M&A deal of the year for Linear. We, frankly, think it's going to fit like a glass slipper. Now you'll have a leader in converters and a leader in power management, and we actually think that they can improve the margins at Linear. I know some people might not think that's possible, but if you look at what the man to my left, the Ben Affleck of semis, what Dave Zinsner, the CFO of ADI, did to margins when he went to Analog Devices, where several people didn't think that he could boost those margins, operating margins went up a solid five to seven points.

QUESTIONS AND ANSWERS

Editor

So, here today to talk about it is Dave. And I guess I'll start with why don't you just maybe refresh us on the timeline of the Linear acquisition, what sort of accretion you can get there, milestones? Kind of give us the rundown, and then we'll start from there.

David Zinsner - *Analog Devices - SVP and CFO*

And timeline as it relates to closing?

Chris Danely - *Citigroup - Analyst*

Exactly. Why so long -- is that long?

David Zinsner - *Analog Devices - SVP and CFO*

Talk to your local government. Yes, so we announced it at the end of July. We have gone through, I guess, our initial process with the regulatory agencies. I believe we have about seven countries that we have to seek approval from. The two most significant ones are the US, obviously, and China. And I think China most likely will be the longer -- the long pole in the tent in terms of completion.

So, as I said I think at the call, we expect to have that all worked out by the middle of next year, which judging from some of the other transactions that have gone on in the past in the tech space, that seems to be kind of a general good rule of thumb, as it takes almost a year from the time you announce to closing.

In that timeframe, we'll go through the integration process and just start to plan it out. There are certain things obviously we can't do because we're two separate companies, but we can begin to plan how we might combine, and then of course, when we close, we'll begin in earnest to really integrate the two companies.

Our goal is to -- and we also announced this -- is to take about $150 million of cost out of the combined businesses within 18 months. If you look at the total amount of spend between the two companies, it's about $3 billion, so $150 million's about 5%. So, judging just from past deals that we've done and kind of a high level look at what the combined business has in terms of resources, we think that $150 million's probably pretty reasonable number to estimate.

Through the process of integration, we'll certainly refine that number and have a much better sense of where all of that money, $150 million of savings, will come from, and we'll update investors as we kind of proceed here.

Chris Danely - *Citigroup - Analyst*

And out of that $150 million, do you think any of that can be attributed to cost of goods, or is it mostly everything else?

David Zinsner - *Analog Devices - SVP and CFO*

Yes, roughly about two-thirds we estimate is going to be operating expenses. About a third of that is cost of goods. And again, I don't know that we had it down to the decimal place as to exactly where all the costs would come from. So, like I said, when we go through the integration process, we'll have a much more fulsome kind of analysis of where the savings might like, and I think it's possible that that could shift around a little bit.

Chris Danely - *Citigroup - Analyst*

Sure. And now that the S4 is out, I think [there's] been a year-long process. How did it take so long? Why then, why now? What sort of spurred the catalyst there?

David Zinsner - *Analog Devices - SVP and CFO*

Well, I think we -- really, since I came to ADI, I think we thought that the combination of Linear Tech and ADI made a lot of sense. We were both focused on the high performance part of the market. We both valued innovation, and we invested a lot in R&D. They were very strong on the power side. We weren't very strong on the power side. We're very strong in data converters and amplifiers and the signal conditioning side. They weren't as strong there. And so, it seemed like the perfect marriage in terms of just philosophy around innovation and around what markets we went after, and the ability to get good synergies by combining the two companies from a revenue perspective.

And it takes kind of the right moment, I guess. Both companies have to be in the right mindset. We have to have all our ducks in a row in terms of other things we wanted to fill in first, completed, like Hittite, and so -- yes. So, then, in July we kind of -- I think in July of last year or August of last year, we started to talk to them. And then, it's a matter of just getting to the right price that both parties can live with and make sure that we can justify it from an economic perspective, which takes a while to figure out.

Chris Danely - *Citigroup - Analyst*

Sure. Did you consider any other companies when you were making the final decision on where to go for acquisition, or was it always kind of Linear was the bee in your bonnet?

David Zinsner - *Analog Devices - SVP and CFO*

Yes, Linear was plan A, and we didn't have a plan B.

Chris Danely - *Citigroup - Analyst*

[So they're] plan A, B, and C.

David Zinsner - *Analog Devices - SVP and CFO*

And not that we -- we didn't have a gun to our head to do the transaction, but we thought if we could do it in the right way financially, that it would make an unbelievably great combination. And I'm glad it worked out the way it did, because I think -- got to get through the closing process, but I presume we will successfully, and I think it's going to be an unbelievable combination.

Chris Danely - *Citigroup - Analyst*

Yes. I think the only people happier than you guys are the Linear shareholders. I'm curious, because Bob Swanson has always said we're not for sale, we don't do M&A, so shmoes like me always assume that this would never happen. What was their first reaction when you called them up? Did they hang up the phone? Did they give you the courtesy buzz-off? Was there openness there? How'd it go when the first contact was made?

David Zinsner - *Analog Devices - SVP and CFO*

Well, obviously in the August discussion they said no, because we had to go back to the drawing board. I think that the Linear folks understood kind of the rationale for combining the two companies in a way that that would make a greater company. But, I do think that there was a value they placed on going it alone, and we had to exceed that value in order for them to be interested. And that's, I think, what tipped them over to our thinking.

Chris Danely - *Citigroup - Analyst*

And valuation, I think it's nine or 9.5 times sales. Can you just help us get comfortable with the valuation?

David Zinsner - *Analog Devices - SVP and CFO*

Well, I mean, it's tough to look at it from a sales perspective, because their revenue is so profitable that the value of every dollar of revenue is going to be significant. And when you can get the expense and revenue synergies over time, it actually is a pretty easy number to overcome, believe or not.

But, when you look at it from a valuation perspective, or valuing it on an EBITDA multiple basis, I mean, you'd look at their EBITDA multiple under the $60 price range, and it's kind of in the range of what most of these transactions have executed at. So, from that perspective, it's reasonable. I mean, we expect that their growth rates are going to be kind of reasonably aligned with our growth rates, kind of GDP-plus kind of growth rates. We do think they have some very specific kind of idiosyncratic growth drivers that will allow them to grow faster than that, over time. For example, their automotive business has been growing in kind of the low double-digits, as is our automotive business outside of the passive safety part of our market.

So, I think there was a good underlying growth business there that was very, very profitable. We thought we could get good revenue synergies by combining our capability around signal processing with their capability around power to accelerate that growth, and we thought we could get reasonable expense synergies. And then, add on to that fact that we will structure this in a way that's highly tax-efficient just seemed like a really good kind of return for our investors.

Chris Danely - *Citigroup - Analyst*

Yes. And then, just to talk about the synergies, you said two-thirds non-COGS, one-third COGS. Any insights you can give us specifically as to where you think you can take costs out besides not needing two CFOs, two CEOs, et cetera?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. Hopefully that's not me.

Chris Danely - *Citigroup - Analyst*

Hey, at least they're finally going to get--.

David Zinsner - *Analog Devices - SVP and CFO*

--Guess we'll find out. Yes, so clearly there's public company expenses that go away when you combine the two businesses. There's certainly inefficiencies where we are duplicative in how we're spending our resources versus how they're spending their resources. And so, I think we'll be able to get some efficiency out of that. There's purchasing power that we'll get by combining these two businesses, particularly given that we were so outsourced. They are in the process of moving more to an outsource model. We'll be able to help them in terms of purchasing leverage, so that's going to help. We'll be able to -- I'm sure we were chasing after similar sockets at times in the signal processing area, and so we'll be able to not do that, going forward, and rationalize our investments.

And then, there's really some efficiencies that I think we can get [on] ADI side that we just probably haven't tackled, and this provides a pretty good opportunity as you're looking about how to really manage the business as efficiently as possible. I think there are opportunities within ADI that we can start to look at and start to address.

Chris Danely - *Citigroup - Analyst*

Can you talk about those a little bit? What efficiencies do you think this sort of opens up at ADI?

David Zinsner - *Analog Devices - SVP and CFO*

Well, I do think that probably not with any specificity, because we've got to go through that process to really analyze them, but--.

Chris Danely - *Citigroup - Analyst*

--Yes, no pink slips yet.

David Zinsner - *Analog Devices - SVP and CFO*

What's that?

Chris Danely - *Citigroup - Analyst*

No pink slips have been issued?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. No, that's not -- but when you've been around for 50 years, you start to develop processes that over time just become overly complicated, and at the end of the day probably don't add much value. And so, those are the things that I think we will look at and address as we're combining the two companies.

Chris Danely - *Citigroup - Analyst*

Yes. My wife always tells me you've been around for 45 years and (inaudible) a lot of over-complicated processes that don't add up to anything, so let's change them.

Getting back to Linear, I think the only person who was even close to being as surprised as I was was Bob Swanson, judging from his comments on the call. Can you just talk about what Bob and the other Bob, Bob Dobkin, mean to Linear? What are the plans to keep them? Are there plans to keep them? Do you think they'll stick around? How do you keep those guys in the picture, or will they still be in the picture?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. Well, they're massively important to that company, and they've built an unbelievable company. In fact, I was talking earlier to somebody that they kind of developed the idea of leaning before I think Lean was even a term. They're just -- really just a really well-run business. They have a certain way of going about it, and they don't deviate from that approach. And so, I think that those are really powerful processes and approaches that I think we can actually adopt at ADI and make the combined company an even greater company.

I don't know what the plans are, or what either Bobs' plans are in terms of sticking with the Company on a go-forward basis. I imagine that, over the process of this period from now to close, there'll be a lot of discussions with our Board and with Vince and with those two individuals to decide how they want to go forward with the Company. I'm sure that they will have some impact in the Company well beyond the close, and it's just a matter of for Vince and those guys to kind of determine what that should be.

Chris Danely - *Citigroup - Analyst*

And then, maybe just talk about -- on that note, talk about the difference in cultures. You guys are two very similar companies, but I would imagine there's also some difference in the cultures, as well. Have you picked up anything, noticed anything?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. Well, they're very lean in the way they think. They don't spend a dollar unless they really can identify where the return's going to come from. And while I think that that's true at ADI, it's probably not to that extent. And so, again, I'd like to figure out a way to infuse that kind of culture because -- since I'm the finance guy, into that [kind of] thinking around the ADI approach.

They are more focused, I would say, in the small and medium-size customers than we are. We're probably a little bit more geared towards the larger OEMs. They're a bit more kind of horizontal product-oriented, where we are more vertical in nature, so we look at trying to integrate technology and create kind of application-specific products. They think more about developing just a general suite of products that can be used throughout different applications and markets.

So, bridging those two things together is going to be I think the real challenge, but I think it's very doable. It's just a matter -- quite honestly, at the end of the day, what I'd like to do is see that both kind of approaches live on in the combined company. So, we do a very good job of servicing the small and medium-size customers. We bring a lot of technology to them. But, we also figure out a way to vertically integrate products and create more application-specific products that combine the capabilities of both Linear and ADI to our larger customers.

And so, there's obviously challenges around integrating those two schools of thought, but I think if we do it right, it will be an unbelievable combination.

Chris Danely - *Citigroup - Analyst*

Yes. Maybe you can send a team of executives out there every year for a Linear boot camp, or something like that.

David Zinsner - *Analog Devices - SVP and CFO*

Exactly.

Chris Danely - *Citigroup - Analyst*

How about on the engineer side? Have you been out and visited the Linear people yet? Do you notice any difference between the engineers there versus the engineers at ADI?

David Zinsner - *Analog Devices - SVP and CFO*

Yes, so Vince and I did go out a couple weeks ago, and we did a few roundtables with some of the senior engineers at Linear Tech. I would say really, when you talk to them, what they have to say and what they're curious about and interested in is very much the same things that our engineers are interested.

Chris Danely - *Citigroup - Analyst*

They're all (inaudible), yes.

David Zinsner - *Analog Devices - SVP and CFO*

They're all a little nerdy. But, I think they're a very proud organization. I think they give their engineers quite a bit of autonomy to go out and try to figure out things that customers might not even know they need yet, and allow them to invent those products. We're probably a little bit more controlling in that we probably do have kind of a structure around what engineers work on. And part of that's by virtue of the fact that we have large routines, and when you're doing kind of more vertical products, you do require a little bit more orchestration around that activity.

But, for the most part, I would say that the average engineer at Analog is probably not very different than the average engineer at Linear Tech, very proud, very technical, very smart, very hard-headed.

Chris Danely - *Citigroup - Analyst*

How about compensation structure? Is there any difference in comp structure between you guys and Linear?

David Zinsner - *Analog Devices - SVP and CFO*

It's a little different. They are a bit more variable on their compensation. We gear our bonus structure towards a combination of growth and profitability. They really skew it almost virtually over to profitability. And so, we'll have to align that comp structure over time, but we're going to leave both structures in place at least for the next year, and then we'll figure out how to integrate them in a way that works. We're not looking --

the way they compensate their employees creates a mindset about being very careful around spending, and so we certainly don't want to disrupt that.

On the flip side, I think our structure does, at least at certain levels, does drive a growth mentality that I think is pretty valuable for the ADI side of the equation. So, we'll have to figure out how to kind of balance this out, and it's certainly going to be different over time. But, I think, at the end of the day, we'll drive the same behaviors that it did before.

Chris Danely - *Citigroup - Analyst*

And what do you think is going to be the hardest aspect to change over there?

David Zinsner - *Analog Devices - SVP and CFO*

Well, I'm not certain we're looking to change a whole heck of a lot. I would say the biggest challenge we're going to have is, where Hittite was 20 minutes north of our largest location in Wilmington, this one's all the way on the other side of the country. So, Vince and I will probably spend a lot of time over there getting to know the people and making sure everything's going as expected. I do think that that comp structure has to get figured out, over time. That will be challenging, but I think very doable. And somehow we've got to figure out how to do the things that Linear does really well and port them over to ADI, and do the things that ADI does really well and port them over to the Linear Tech people so that, on a combined basis, the Company is way better than the two companies operating separately.

Chris Danely - *Citigroup - Analyst*

Yes. So, no truth to the rumor that this was your way to get back to California?

David Zinsner - *Analog Devices - SVP and CFO*

Well, to be honest with you, I mean -- so, Vince has assigned me -- I'm not sure this was a good thing, but he assigned me the task of managing the integration. And as a result, since a lot of that activity obviously is going to be on the West Coast, I actually am going to probably spend a fair amount of my time over there. I'm going to figure out how to do most of that during the winter months so that I can get out of the Boston winters. But, it's going to be pretty heavy over there, I'd say, for me.

Chris Danely - *Citigroup - Analyst*

Well, considering the Boston winter lasts, like, nine months, you could probably spend plenty of time out (inaudible) West Coast.

You bring up an interesting point. So, when you got to ADI, their operating margins I think had been kind of the low to mid 20s for a long time, and there was some skepticism as to whether you could take them up or not, and you took them up pretty substantially. Do you see any similarities, maybe share some of your experiences, how you improved the op margins at ADI? Do you think some of that pixie dust can work at Linear?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. Well, again, I'm not so certain that it has to all be at Linear, where we improve the op margins. But, I do believe that we can improve the op margins on the combined company from where they are kind of on a pro forma basis today. There's no question about that. We will get efficiencies. There are certainly efficiencies to be gained by just operating some of the processes that Linear Tech did, or does, within ADI.

But also, I think that there's just an opportunity as a $5 billion company to get leverage in areas that you couldn't get as much at $3.5 billion. So, I'm pretty optimistic that we'll be able to improve the operating margins. And as we get closer to the close, we'll probably come out with a model, one of which states -- it's not difficult math, but one which states kind of where we are today on a pro forma basis with the two companies, but also where we want to take the operating margins over time, which I do think will be significantly higher than where they are today.

Chris Danely - *Citigroup - Analyst*

And what's the combined balance sheet going to look like? And then, what will the usage of cash be after everything is done?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. So, for a moment in time, we'll actually borrow about $11.5 billion, although $4 billion of that will get paid back within probably 60 days. And it's the way we're doing the structure requires that we borrow money that we will eventually utilize the cash on the balance sheet to pay down within 60 days. What we'll be left with is about the $7.5 billion that we'll have raised for the purchase of Linear, plus $1.8 billion or so that we have on the balance sheet today. So, that's roughly about $9 billion of debt.

That's about kind of high threes, like 3.8 debt to EBITDA kind of levels, which we're very comfortable with. In fact, the rating agencies were very comfortable with it. We got a triple-B rating out of S&P. We got a BA-1 rating out of Moody's. So, those are actually well into the investment-grade, so no problems there.

Having said that, that's not really where we want to maintain the business. We did recognize that we had way more cash, and we didn't have the most efficient capital structure. So, this is an opportunity to get us back into a place where our capital structure's more efficient.

And so, ideally what we'll do is we'll take the leverage ratio back down to about two, paying debt down at a rate of about $1 billion a year. And so, we'll be about two within three years, I would say. And then, at that level, then I think we probably will operate the business somewhere in that range.

Chris Danely - *Citigroup - Analyst*

How much cash will you have again on the combined company when all is said and done?

David Zinsner - *Analog Devices - SVP and CFO*

We'll have probably about $800 million of cash.

Chris Danely - *Citigroup - Analyst*

And will that be the usual, like 10% US and 90% offshore?

David Zinsner - *Analog Devices - SVP and CFO*

No, it's probably going to be 50%-50%.

Chris Danely - *Citigroup - Analyst*

Okay, got it. And then, how confident are you that no other bids are coming? Is there a breakup fee, I assume?

David Zinsner - *Analog Devices - SVP and CFO*

There is a breakup fee. I should have remembered what this was, but now I can't remember now what the number is. It was a few hundred million dollars, I think, about $500 million, I think it was. I think it was $490 million.

There's always a change another bidder could come. That's not what we expect, but there's always that risk. But, we're operating it as if we're going to close this transaction in the next 12 months or so, and so now it's kind of on to the integration.

Chris Danely - *Citigroup - Analyst*

If there is a competitive bid, are you prepared to go higher would you consider it?

David Zinsner - *Analog Devices - SVP and CFO*

I don't know. I mean, I haven't really thought about it, because I'm hoping that it doesn't happen. But, we'll deal with it if it does.

Chris Danely - *Citigroup - Analyst*

SoftBank's still out there (inaudible) the next 300 years. You never know. And then, how about in terms of overlap? Any anti-competitive issues? You guys have a small power management business. Is there any overlap there with Linear?

David Zinsner - *Analog Devices - SVP and CFO*

On the power management side? No, I don't think so. Our power management is pretty narrowly focused on kind of attached power relative to theirs, which is just a very broad catalog of power capability. So, there's really no overlap.

And really in the data converter and signal processing side, one of their kind of approaches was to kind of avoid ADI and try to compete where we weren't. That's how you get margins like Linear Tech gets. So, I don't envision there being a regulatory issue with this.

Chris Danely - *Citigroup - Analyst*

Okay. And then, maybe talk -- I know it's super-early stage, but talk about cross-pollination. You talked a lot about operations. How about on the product side?

David Zinsner - *Analog Devices - SVP and CFO*

Yes, I think that's going to be very good. So, for example, let's take communications for a starter. So, we have a communications business. They have a communications business, and they're roughly about the same percentage of revenue in total, about 20%.

But, interestingly, most of their revenue comes from the wireline side, whereas most of our revenue comes from the wireless side. So, they're kind of not very well positioned with the wireless customers, and we could say the same thing about ADI on the wireline side. I think that's a tremendous opportunity to drive each technology into the other market.

In the automotive business, they have much more significant exposure into Asia. More of our exposure is into Europe and the US. So, that one, from a geographical standpoint, I think we have opportunity to kind of cross-pollinate those products.

There is certainly in a lot of our application-specific solutions need for power. And quite honestly, because of the limited catalog we've had, we haven't been able to provide that. So, in some cases, we've been designing it. In a lot of cases, we've had to look through everyone's catalog and say, okay, these are the parts that'll work. Clearly now, the parts that will work will be Linear parts, and so we'll be driving that technology into all of the verticals that we want to -- or rather [our] application-specific areas where we have a good attach opportunity.

What else? In the industrial space, there is continually a need for increasing amounts of power. I think we have a good position across a lot of different larger customers where they don't have quite the position. And so, I think we'll be able to pull them in. By the way, they'll be able to do the same thing to us on the smaller customer side, because I do think they have a better position with smaller customers.

And so, I think we'll have a very good cross-selling of the product portfolio and a very good opportunity to get significant revenue synergies. I mean, the issue is that it doesn't show up in any of the numbers we've quoted, because most of these products are somewhere between five- and 10-year design cycles. So, we didn't expect to get it any time in the next few years, but we do expect, once you start to get into 2022, 2023, those kind of time periods, we'll start to see some meaningful revenue synergies out of the combined businesses.

And just -- I can always tell, and we notice this with Hittite is, when the salespeople are really, really excited about something, you know it's going to be good. And they were very excited about Hittite, and I would say the buzz talking to salespeople around ADI early on was that this was incredibly good for their portfolio and their ability to sell more and get more [bomb] with customers.

Chris Danely - *Citigroup - Analyst*

Yes. How about the customer reaction? Did you pull any customers before? Anybody come up to you afterwards and say this is great?

David Zinsner - *Analog Devices - SVP and CFO*

We didn't do it before just because we're trying to keep this -- keep a lid on this as much as we could. The larger customers, which are obviously mainly customers of ADI, have been remarkably positive about this. They really see -- in fact, they've even been quoting what our business level will increase by virtue of the fact -- or at least the opportunity will increase by virtue of the fact that we have the Linear portfolio.

I'd say, on the smaller customer side, we have actually gotten feedback, which is kind of -- I kind of find it interesting. I'm sure the customers are a bit concerned, and they were saying, look, we have an unbelievably good model with Linear in terms of service, and we don't want to see that disrupted as you combine ADI and Linear Tech. And so, I think that's something we obviously want to pay attention to. It's one of the reasons we really liked Linear Tech, was they did do a very good job servicing the small and medium-size customers. And so, we're going to be very careful about making sure not only that we keep that intact from a Linear Tech perspective, but also broaden it to the horizontal products within ADI.

Chris Danely - *Citigroup - Analyst*

Yes, and this clearly vaults you up the scale range. One of your competitors actually is next here. TI talks about the power of scale. Maybe just spend a few minutes on that. Does that factor into the [ammunition]?

David Zinsner - *Analog Devices - SVP and CFO*

Yes, in a minor way. I mean, I do think that TI, for example, they do have a different approach to the market where scale does matter. It matters from sales force and manufacturing prowess, kind of. For us, I would say the real scale opportunity was to take R&D to $900 million-plus I think is what it is on a combined basis, and really use that as the kind of -- kind of our force and drive within the marketplace. So, our focus is not necessarily a manufacturing scale.

I don't think we got anything like that by acquiring Linear. I do think that certainly we'll have more feet on the street, but I would say it's more the benefit of having now -- I don't know, I think we'll have 360 FAEs or something like that. That's a significant FAE force out there, which is an augmentation of our R&D development. And then, like I said, $900 million of R&D to throw at the toughest problems out there, and that's the kind of scale aspect, or scale benefit that we're going to get from this.

Chris Danely - *Citigroup - Analyst*

Great. Before I go on, I'd like to open it up to the audience for any questions. In the front?

Unidentified Audience Member

Yes, just kind of a two-part question here. I think on the call when you announced the Linear acquisition -- on the call announcing the Linear acquisition, I think you talked about optimizing the capital structure with your new 2X leverage target versus your prior 1X leverage target. I guess first part of the question is why is two times optimal versus one time, or say three times, or pick a number, why is two times optimal?

And then, historically, you've run below your prior one time leverage target being in a net cash position. Once you do hit two times, will you revert back to your kind of 80% free cash flow payout, or how should we think about capital allocation once you do hit that target in the next three years or whenever?

David Zinsner - *Analog Devices - SVP and CFO*

Yes. I'm not sure that we had a target, per se, to get to the 1X, although I felt we could comfortably get to 1X. But, this is more math that I understand, but I would say is, when the investment bankers kind of model out what an optimal capital structure looks like for us, given the kind of stability of the cash flows of an analog company, for example I think on a combined base, ADI and Linear without any synergies or anything added, would have generated $700 million of free cash flow in 2007, which was probably the worst year in 20 years [since] semiconductors.

So, this is a business that has very good sustainable, predictable cash flows. You can operate in some reasonable level of leverage.

As you get kind of in -- if you're going to say you're permanently kind of three or four, I think you start to get into kind of non-investment grade territory, and then the pricing starts to get more expensive. And so, I think for us, we thought, well, we want to be a strong investment grade, but we want to have a capital structure that's more efficient relative to one where we've got so much cash generating 20 or 30 basis points while having to borrow at 3% or 4%.

So, that's kind of -- it wasn't a massive amount of science to it, but that's kind of why I thought two times leverage made a lot of sense. Once we get to the two times leverage and we pay the debt down to that level, I think we're then in a position where we can start providing -- we'll obviously play the two off each other to make sure we're making the right decisions.

But, I think in general, our approach would be to begin to buy back process again and start to ramp that up. And obviously we're going to generate $1 billion-plus of cash flow that goes in addition to the dividend, that we can make a determination as to whether it makes more sense to do some of that in terms of the continual debt buy-down, some of that in terms of buyback, or maybe we find some other acquisition that might make sense.

Chris Danely - *Citigroup - Analyst*

Can you continue to increase the dividend with the current--?

David Zinsner - *Analog Devices - SVP and CFO*

--Yes, our plan is to increase the dividend at kind of our stated range, which is 5% to 10%.

Chris Danely - *Citigroup - Analyst*

Great. Rob in the back?

Unidentified Audience Member

Dave, just on the tax structure and the cash location, where it'll be generated, will it look like ADI, or will it be a blended -- going forward, once Linear is closed?

David Zinsner - *Analog Devices - SVP and CFO*

Okay, so we -- as part of the approach to close, one of the other things we're doing is valuating -- or valuing their intangibles and making some assessment as to how this tax structure's going to work out. I wouldn't say -- we don't have it all buttoned up yet.

But, the early modeling was that roughly about a third of the cash flow would be generated onshore, and about two-thirds would be generated offshore. So, that's pretty close to what we have today.

Unidentified Audience Member

First, on the COGS synergies that you talked about, are you guys going to be letting that flow all the way through the model, or do you plan on using some of that to allow the Linear product to have maybe a different price point and allow you to be a bit more aggressive on pricing and growth than maybe Linear had been, just given the margin structure?

And then, the second question I have is around the US cash, and the US cash you're going to be generating enough to pay the dividend? You mentioned you're going to have -- I think you said $800 million afterwards, and about a third of each of your companies has US cash generation. So just can you talk about sort of the US cash generation capability of the combined company and your ability -- I think the share count's going to go up 20%. So, you paid $500 million-something of dividends last year, call it $600 million-plus. I mean, how do you think about US cash generation and giving yourself enough coverage on your dividend?

David Zinsner - *Analog Devices - SVP and CFO*

Yes, okay. So, okay, what was the first question again? Oh, COGS, yes. Okay, so I don't know the answer just yet. There is an argument -- like I said, we do want to try to take their product portfolio into our larger customers in a bigger way. I think to do that, you have to be a bit more flexible in terms of pricing than perhaps they had operated. Having said that, I do think that their pricing discipline in general hasn't lost them tons of business, particularly at the small and medium size customers. So, in some ways, we might want to leverage their model into our businesses, although having said that, we do get pretty good gross margins in the small and medium size customers, I would guess probably pretty similar to what Linear gets in terms of gross margins.

So, I guess the short answer is probably there was some opportunity to drive faster growth rate through a little bit more focus on the larger OEMs than perhaps they had had in the past. But, I think at our larger customers, we get almost corporate average gross margins, so I'm not sure that it's massively dilutive, either.

On the cash flow question, let me see if I can take a crack at this. So, I think on a pro forma basis, we generate on a combined basis, like, $1.7 billion or so of free cash flow. Obviously hopefully that'll go up with growth rates and synergies and so forth, but let's kind of pick a number, $1.8 million because I can do the math better on that. So, roughly about $600 million of that would be generated onshore, and then the rest, $1.2 billion, would be generated offshore. That would kind of go to the dividend, and so that would kind of manage the dividend flow, and then the rest of it would be all offshore. Initially it would be mostly paying down debt.

And then, as we get towards kind of what I would consider a more optimal debt level, so somewhere in the two times, then I think we'd start to bring the buyback up, which then we'll have to determine how we want to do that. And some -- in the ways we've done it in the past, we've actually borrowed on onshore and kind of like -- just kind of synthetically used the international cash to do it. Whether that makes sense or not, I don't know. We have a few years to figure that out, [apparently].

Unidentified Audience Member

Can you just talk about how this deal kind of accelerates your targeted $5 in earnings for 2020? And then, secondly, what are the assumptions kind of embedded as a standalone ADI within that $5 target? [And do you see]--?

David Zinsner - *Analog Devices - SVP and CFO*

--Yes. I would say obviously it's a pretty good down-payment on the $5. It might even hit it. It kind of depends on what growth rates we see for the combined company through 2020. There probably won't be much in the way of revenue synergies by that point, so it'll all be how those two business organically grow through 2020 and getting the $150 million in synergies, and then having this kind of deleveraging that goes on.

So, I don't know exactly where we'll end up, but I think we're going to be in the zip code of $5, if not exceeding $5, by 2020. On a standalone basis, had we not done this, I'd say we're probably looking kind of low in the mid fours, again depending on the growth rates and so forth.

Unidentified Audience Member

And then just one more follow-up. Talk about -- does this deal kind of -- does this provide any kind of cushioning in the amplitude of cycles as you bring these portfolios together [in envisioning] kind of what a down-cycle looks like?

David Zinsner - *Analog Devices - SVP and CFO*

Maybe to some extent. I mean, obviously they have a broad horizontal market, as do we, but we were more exposed to the consumer space. That did have a bit more volatility as we experienced in the fourth quarter of last year into the first quarter of this year. That large customer that we have will go under 10% on a combined basis. Consumer will be a smaller percentage of revenue -- I forget what the exact number was -- mid-teens or something on a pro forma basis. So, I think that will help kind of minimize the volatility within the businesses.

Chris Danely - *Citigroup - Analyst*

Great, thanks. That's all we have time for. Dave, I'd like to point out, it's probably been at least a year since you went through a whole presentation without a single Apple question.

David Zinsner - *Analog Devices - SVP and CFO*

Thanks.