Vishay Intertechnology NYSE: VSH
Q3 2018 Earnings Call Transcript
Tuesday October 30, 2018 9:00 a.m. ET

Operator:
Ladies and gentlemen, thank you for standing by, and welcome to the Q3 2018 Earnings Conference Call.

All lines have been placed on mute to prevent any background noise. After the speakers remarks there will be a question-and-answer session. To ask a question during this time simply press star then the number one on your telephone keypad.

Thank you. I will now turn the conference over to Mr. Peter Henrici. Please go ahead.

Peter G. Henrici
Thank you, (Crystal). Good morning, and welcome to Vishay Intertechnology's Third Quarter 2018 Conference Call. With me today are Dr. Gerald Paul, Vishay's President and Chief Executive Officer; and Lori Lipcaman, our Executive Vice President and Chief Financial Officer.

As usual, we'll start today's call with the CFO, who will review our third quarter financial results. Dr. Gerald Paul will then give an overview of our business and discuss operational performance as well as segment results in more detail. Finally, we'll reserve time for questions-and-answers.

This call is being webcast from the Investor Relations section of our website at ir.vishay.com. The replay for this call will be publicly available for approximately 30 days.

You should be aware that in today's conference call, we will be making certain forward-looking statements that discuss future events and performance. These statements are subject to risks and uncertainties that could cause actual results to differ from the forward-looking statements.

For a discussion of factors that could cause results to differ, please see today's press release and Vishay's Form 10-K and Form 10-Q filings with the Securities and Exchange Commission. In addition, during this call we may refer to adjusted or other financial measures that are not prepared according to generally accepted accounting principles.

We use non-GAAP measures because we believe they provide useful information about the operating performance of our businesses and should be considered by investors in conjunction with GAAP measures that we also provide.

Additional factors are described in our earnings release for third quarter of 2018. Our estimates may change and the company assumes no obligation to update forward-looking statements to reflect actual results, changed assumptions or other factors, except as required by law.

This morning, we filed a Form 8-K that outlines the various variables that impact the diluted earnings per share computation. On the Investor Relations section of our website, you can find a presentation of the specific third quarter 2018 information the CEO and CFO will be discussing on the call.

Now I turn the call over to Chief Financial Officer, Lori Lipcaman.

Lori Lipcaman:
Thank you, Peter, and good morning, everyone. I am sure that most of you have had a chance to review our earnings press release. I will focus on some highlights and key metrics.

Vishay reported revenues for quarter 3 of $781 million. EPS was $0.51 for the quarter. Adjusted EPS was $0.60 for the quarter. All of the reconciling items between GAAP EPS and adjusted EPS are tax related, primarily due to the continuing evolution of our accounting for U.S. tax reform as permitted by SEC Staff Accounting Bulletin 118. There were no reconciling items impacting gross margin or operating margin.

During the quarter, we continued to execute transactions in response to U.S. tax reform. We completed the second phase of our program to repatriate some of our foreign earnings to the United States. The repatriation transactions resulted in the payment of $65 million of foreign withholding and other taxes during the quarter, on top of the amounts paid in Q2.

These taxes have been accrued at the enactment of U.S. tax reform in Q4 2017. The payment of these taxes is reflected as an ongoing – as an operating cash flow on the statement of cash flows. I will elaborate on these transactions in a few moments.

Revenues in the quarter were $781 million, up by 2.6 percent from previous quarter and up by 15.2 percent compared to prior year. Gross margin was 30.3 percent. Operating margin was 17.7 percent. There were no reconciling items to arrive at adjusted operating margin. EPS was $0.51. Adjusted EPS was $0.60. EBITDA was $175 million or 22.4 percent. There were no reconciling items to arrive at adjusted EBITDA.

Reconciling versus prior quarter, operating income quarter 3 2018 compared to operating income for prior quarter, based on $20 million higher sales or $27 million higher excluding the exchange rate impacts, operating income increased by $15 million to $138 million in Q3 2018 from $123 million in Q2 2018.

The main elements were average selling prices had a positive impact of $4 million, representing the 0.6 percent ASP increase; volume increased with a positive impact of $11 million, equivalent to a 3.1 percent increase in volume; variable and fixed cost increased with a negative impact of $3 million; exchange rates had a positive impact of $5 million.

Versus prior year, operating income quarter 3 2018 compared to adjusted operating income in the prior year, based on $103 million higher sales or $105 million excluding exchange rate impacts, adjusted operating income increased by $39 million to $138 million in Q3 2018 from $99 million in Q3 2017.

The main elements were: average selling prices had a positive impact of $4 million, representing a 0.5 percent ASP increase; volume increased with a positive impact of $53 million, representing a 15.1 percent increase including the UltraSource contribution; variable cost increased with a negative impact of $5 million; fixed cost increased with a negative impact of $13 million, primarily due to wage increases, incentive compensations, legal and other fees, acquisitions and R&D expenses.

Selling, general and administrative expenses for the quarter were $98 million lower than expected due to exchange rate impacts, lower legal and other fees.

For quarter 4 2018, our expectations are approximately $101 million of SG&A expenses and approximately $404 million for the full year at constant exchange rates.

As mentioned in my opening remarks, during the third quarter we continued to process our cash repatriation to the U.S. Recall that while such amounts are no longer subject to U.S. federal taxes, they are subject to foreign withholding and other taxes and some state income taxes.

We have accrued about $232 million of taxes on approximately $1.2 billion of foreign earnings available for eventual repatriation, most of which was accrued upon enactment of U.S. tax reform in the fourth quarter of 2017.

In total, we received approximately $450 million for the quarter and approximately $724 million year-to-date in the United States. We utilized much of this – much of these amounts to reduce the outstanding balance of our credit facility to 0 and to repay certain intercompany indebtedness. As a result of these transactions, we paid approximately $65 million for quarter 3 and $157 million year-to-date of foreign withholding and other taxes.

Additionally in Q2, we paid the first installment of the U.S. transition tax of $14 million. These tax payments are reflected as operating cash flows on our statement of cash flows, thus explaining the negative free cash for year-to-date. This leads to about $300 million of cash available for repatriation with taxes accrued. We are still evaluating the time of such repatriation, but do not expect it to be in 2018.

We had a total liquidity of $1.7 billion at quarter end. Cash and short-term investments comprised $1.1 billion and there are no amounts outstanding on our $640 million credit facility. For several years, substantially all of our cash and cash equivalents and short-term investments were held by subsidiaries outside of the United States.

At the end of Q3, following these repatriation transactions, the uses of such cash described above, we have approximately $425 million of cash and cash equivalents and short-term investments in the United States. We are continuing to evaluate the future utilization of the remaining repatriated cash.

The U.S. parent company and our U.S. operating subsidiaries have significant financing and operating cash needs. Our Board of Directors has authorized us to repurchase certain convertible debt instruments in open market repurchases or through privately negotiated transactions, subject to market and business conditions, legal requirements and other factors.

Such authorization does not obligate us to acquire any particular amount of convertible debt instruments and it may be terminated or suspended at any time at our discretion in accordance with the applicable laws and regulations. We expect to fund any repurchases through cash on hand, including repatriated cash, and if necessary borrowings under our revolving credit facility.

The carrying value of our debt of $588 million is net of the unamortized issuance cost of $18 million and includes $114 million remaining of the convertible debentures net of unamortized discount issued in 3 tranches and due in 22, 23 and 24 years respectively and $492 million of the new convertible notes, net of unamortized discount, due in 2025. The principal amount or face value of the converts totaled $886 million, $600 million related to the new notes and $286 million related to the remaining debentures.

As I said no amounts are outstanding on our revolving credit facility at the end of Q3. No principal payments are due until 2025. However, the convertible debentures may be redeemed if certain stock price thresholds are met. At the end of Q3, 2018, the convertible debentures due 2040 and 2042 are redeemable for the next quarter.

Accordingly, for those tranches, we have reclassified the difference between the carrying value and the principal amount from stockholders equity to a separate line between liabilities and equity on our consolidated balance sheet. If the debentures are converted, we had fund the principal amount with borrowings on our revolving credit facility and net share settle amount in addition to the principal amounts.

This criteria is measured quarterly and measured separately for each tranche and the amounts presented as temporary equity will revert to regular equity, as the criteria are not met for that particular tranche of debentures.

As permitted by SEC Staff Accounting Bulletin 118, we continue to evaluate the impact of enactment of U.S. tax reform. Based on additional analysis completed in the third quarter, we've recorded an additional $13 million of tax expense related to the enactment.

This includes an approximately $7 million adjustment to the accrual for incremental foreign income taxes and withholding taxes payable to foreign jurisdictions related to our repatriation plans and an approximately $6 million adjustment to the transition tax obligation. These amounts related to the enactment of tax reform should still be considered provisional as permitted by SEB 118, subject to finalization in Q4.

Additionally, our U.S. GAAP tax expense for the quarter and year-to-date periods include adjustments to remeasure the deferred tax liability related to those incremental foreign taxes payable upon repatriation, such as foreign currency effects. A similar remeasurement will occur quarterly until such amounts have been repatriated. That remeasurement adjustment was $1 million expense for the third quarter and represents a benefit of about $7 million year-to-date.

Our GAAP tax rate for the year-to-date period, primarily due to unusual tax items recorded in Q2 and Q3, was approximately 23 percent. This mathematically yields a rate of approximately 38 percent for Q3. Our normalized effective tax rate, which excludes the unusual tax items, was approximately 28 percent for the year-to-date period.

This mathematically yields a rate of 27 percent for quarter 3. We expect our normalized effective tax rate for the year to be about 28 percent. We continue to be impacted by the new GILTI tax, the new (B) tax and the limitation on deductibility on some of our interest expense. We continue to evaluate the provisions of the U.S. tax law.

We may further adjust our financial and capital structure to reduce our effective tax rate. Our consolidated effective tax rate is based on an assumed level and mix of income among our various taxing jurisdictions. A shift in income could result in significantly different results.

Total shares outstanding at quarter-end were 144 million. The expected share count for EPS purposes for the fourth quarter 2018, based on the average stock price fourth quarter to date, is approximately $150 million.

For a full explanation of our EPS share count and variables that impact that calculation, please refer to the 8-K we filed this morning. Cash flow from operations for the quarter was $71 million. Capital expenditures for the quarter were $50 million. Free cash for the quarter was $21 million.

For the trailing 12 months, cash from operations was $232 million. Capital expenditures were $212 million, split approximately for expansion, $122 million; for cost reduction, $24 million; for maintenance of business, $66 million. Proceeds from the sales of property and equipment were $9 million for the trailing 12 months. Free cash generation for the trailing 12 months was $28 million.

Both the quarter and the trailing 12 months include significant cash taxes related to U.S. tax reform and cash repatriation. Vishay has consistently generated an excess of $100 million cash flows from operations in each of the past 23 years and greater than $200 million for the last 16 years.

Backlog at the end of quarter 3 was at $1,560,000,000 or 6.0 months of sales. Inventories increased quarter-over-quarter by $19 million excluding exchange rate impacts. Days of inventory outstanding were 82 days. Days of sales outstanding for the quarter were 46 days. Days of payables outstanding for the quarter were 34 days, resulting in a cash conversion cycle of 94 days.

Now I will turn the call over to our Chief Executive Officer, Dr. Gerald Paul.

Gerald Paul:
Thank you, Lori, and good morning, everybody. Vishay also in the third quarter continued to enjoy excellent business conditions in virtually all of its markets. Inventories in the supply chain in general show some increases, but there are no tangible signs of a slowdown in our industry.

Record volume and good efficiencies supported the further substantial increase of revenues and profitability. Vishay in the third quarter achieved a gross margin of 30 percent of sales, operating margin of 18 percent of sales, GAAP earnings per share of $0.51 and adjusted earnings per share of $0.60. We continue to be a reliable generator of free cash. However, the year 2018 will be burdened by approximately $157 million of foreign cash taxes related to our announced cash repatriation.

Let me talk about the economic environment. In general, the economic environment in the third quarter, as I said, continued to be very friendly. In particular, Vishay's key markets, automotive and industrial, do well. The manufacturing output of suppliers starts to catch up to market demand, about lead times still remain long in general. Distributors have started to clean up backlogs and inventories mainly in Asia.

Coming to the regions. All regions, also in the third quarter, continued to do very well. The Americas show very robust economic conditions and an exceptionally strong industrial market. Europe is still driven by strong automotive and industrial market. We have seen some normal seasonality. Growth in Asia continues in particular in automotive and industrial segments. There are some concerns starting to build in the market related to new U.S. tariffs.

Distribution – worldwide distribution continued strong, also in the third quarter. There was another slight increase of POS quarter-over-quarter by 1 percent, but the major increase of 14 percent year-over-year. So POS remains very strong. Distributors continue to enjoy high-order rates with book-to-bill substantially above 1.

Inventory distributors increased by 9 percent in the quarter. Inventory turns of distributors slightly reduced to 3.5 as compared to 3.7 in prior quarter and to 3.7 also in prior year. But this is still a healthy situation.

Some details by regions in the Americas, inventory turns were 2.3 after 2.4 in the second quarter and 2.2 in prior year. In Asia, 4.5 turns vis-à-vis 4.7 in Q2 and 5.1 last year. In Europe, 3.8 turns after 4.3 and 4.2 in prior year.

Coming to the industry segments, automotive continues to be the main driver of growth in our industry, with general electrification of the vehicle driving new programs in several sectors. Also, industrial markets remained strong across all regions and across a wide range of product segments.

Fixed telecom shows some signs of recovery, starting to be supported by 5G projects. PCs and mobile phones on the other hand remain relatively weak. AMS and medical continued to look positive with steady growth expected for 2018 and beyond.

Let me comment on our business development in the third quarter. Sales in Q3, excluding exchange rate impacts, came in at the midpoint of our guidance. We achieved sales of $781 million versus $761 million in prior quarter and $678 million in prior year.

Excluding exchange rate effects, sales in the third quarter were up versus prior quarter by $27 million or by 3.6 percent, and up versus prior year by $105 million or 15.6 percent. We have seen a book-to-bill ratio of 0.95 in the third quarter, 0.80 for distribution, after 1.23 in the second quarter, 1.15 for OEMs after 1.08 in the second quarter, 0.87 for actives after 1.06 in the second quarter. 1.02 for passives after 1.29 in the second quarter. 1.06 for the Americas after 1.29. 0.69 for Asia after 1.09. 1.16 for Europe after 1.18.

There has been a cleanup of backlogs mainly by Asian distributors for semi conductive products. Orders from OEMs on the other hand continue to be steady and strong. Backlog started to normalize, but still at a very high level of 6 months, which is practically twice – 2x the normal situation, historically.

We have a 6.3 months in actives and 5.7 months in passives. Selling prices continue to go up in general, 0.6 percent versus prior quarter and plus 0.5 percent versus prior year. For the actives, we see plus 0.4 percent versus prior quarter and plus 0.7 percent versus prior year. And for the passives, plus 0.7 percent versus prior quarter and plus 0.2 percent versus prior year. Some highlights of our operations.

Also in Q3, we were able to offset the negative impact of inflation on the contributive margin by cost reduction and by innovation. SG&A costs in the quarter came in at $98 million, lower than expectations. Also due to x-rate effects. Manufacturing fixed cost on – in the quarter were $126 million, lower than expectations also due to x-rate impacts.

Total employment at the end of the third quarter was 24,130 people, 1.7 percent up from prior quarter. Naturally, the consequence of further increasing capacities for most of our product lines. Excluding exchange rate impacts, inventories in the quarter increased by $19 million, raw materials by $9 million and we are (in process and finished) goods by $10 million.

Despite this inventory increase, inventory turns in the third quarter remained at a very satisfactory level of 4.4 after 4.6 in prior quarter. Capital spending in the quarter was $50 million versus $36 million in prior year, $34 million for expansion, $3 million for cost reduction and $13 million for the maintenance of the business. For the year 2018, we continued to expect CapEx of approximately $220 million.

Concerning cash flow. We, in the third quarter, generated cash from operations of $71 million versus the generation of $118 million in prior year. Cash from operations in the third quarter was burdened by cash taxes, paid related to cash repatriation of $65 million. We generated $232 million on a trailing 12 months basis, cash from operations on a trailing 12 months basis was burdened by $157 million.

We generated in the third quarter, free cash of $21 million versus a generation of $82 million in prior year. Free cash generation in the quarter was burdened by $65 million of cash taxes paid. We generated $29 million on a trailing 12 months basis. Free cash generation on a trailing 12 months basis was burdened by $157 million.

Coming to our product lines. Resistors and inductors first. Vishay's traditional, and since years, most profitable business grew steadily. With resistors and inductors, we enjoy a very strong position in the industrial, auto mil and in the medical market segments worldwide.

Sales in the third quarter were $253 million, up versus prior quarter by $4 million or by 1 percent and up versus prior year by $37 million or by 17 percent, excluding exchange rate impacts.

Book-to-bill in the third quarter was 1.02 after 1.16 in prior quarter. Backlog was stable on a very high level of 5.4 months. Gross margin in the quarter remained at quite excellent 34 percent of sales. Inventory turns in the third quarter were at a very satisfactory level of 4.2, slightly down from prior quarter at 4.4.

There were price increases plus 0.4 percent versus prior quarter and plus 0.2 percent versus prior year. We continued to invest in manufacturing capacities of power inductors, metal strip resistors and thin film resistor chips as well as MELF thin film resistors.

Our new acquisition, UltraSource, was solid and profitable at a gross margin of 40 percent, 4-0 percent.

Coming to capacitors. Our business with capacitors is based on a broad range of technologies with a strong position in American and European market niches. We enjoy increasing opportunities in the fields of power transmission and electro cars, namely in Asia, especially in China.

Sales in the third quarter were at $116 million, 5 percent above prior quarter and 22 percent above prior year, which again excludes exchange rate effects. Book-to-bill in the quarter was at 1.03 after a spike of 1.59 in previous quarter. Backlog was stable at a very high level of 6.3 months. Gross margin in the quarter increased to 23 percent of sales from 22 percent in prior quarter.

Inventory turns in the quarter were at a satisfactory level of 3.5. Selling prices were increasing by 1.5 percent versus prior quarter and 0.4 percent versus prior year and we remain confident for the future of capacitors in view of growing opportunities in particular in Asia.

Opto products. Vishay's business with Opto products consists of infrared emitters, receivers, sensors and couplers as well as LEDs for automotive applications. Sales in the quarter were $76 million, 2 percent above prior quarter and 1 percent above prior year, which excludes exchange rate impacts. Book-to-bill in quarter 3 was 0.88 after 1.20 in prior quarter. The backlog decreased to 5.0 month from 5.4 in Q2, it's healthy the situation here.

Gross margin in the quarter increased further to a quite excellent level of 36 percent of sales after 35 percent in the second quarter. Inventory turns of 5.1 were good. Moderate price decline we have seen of minus 1.1 percent versus prior quarter and minus 2.6 percent versus prior year. We do expect increasing opportunities in sensors going forward.

Coming to diodes. Diodes for Vishay represents a broad commodity business where we are largest supplier worldwide. Vishay offers virtually all technologies as well as the most complete product portfolio. The business has a strong position in the automotive and industrial market segments and keeps growing steadily and profitably since years.

Sales in the quarter were $187 million, 3 percent above prior quarter and 16 percent above prior year, excluding exchange rate effects. Book-to-bill of 0.86 in the quarter after 1.08 in the second quarter. The backlog for diodes has started to normalize. We are at 6.8 months, which is down from 7.4 months in prior quarter and still very high.

Gross margin in the quarter defended it's Q2 record level of 29 percent of sales. Inventory turns remained at a very satisfactory level of 4.7. Also for diodes, we have seen increasing prices, 1.1 percent up versus prior quarter and 2.4 percent up versus prior year. And we do continue to expand critical manufacturing capacities.

Last but not least, the MOSFETs. Vishay continues to be one of the market leaders in MOSFET transistors. MOSFETs, over the last years, developed a strong and fast-growing position in automotive. Sales in the quarter were $144 million, 6 percent above prior quarter and 14 percent above prior year, excluding exchange rate impacts.

The book-to-bill, for the MOSFETs was 0.88 in quarter 3 after 0.96 in the second quarter. And like for the diodes, we see a normalization of backlogs continuing 6.3 months now coming down from the 7 months in the second quarter, like for diodes still a extremely high backlog. Gross margin in the quarter was at 27 percent of sales, slightly below its record level of 28 percent in prior quarter. Simple reason, there was no further inventory build.

Inventory turns were very satisfactory at 4.9 turns. Selling prices continue to increase plus 0.3 percent versus prior quarter and also plus 0.3 percent versus prior year. We in process to expand manufacturing capacities in house and at foundries.

Let me summarize. Carried by a broad and an enormously strong demand for most of our product lines, Vishay enjoys another very successful year. We presently see first signs of a normalization of inflated backlogs for commodity product, which is nothing but normal when supply starts to catch up with demand.

Most important, overall consumption of OEMs continued strong and so does POS of distributors. For the mid- and long-term, we trust in an accelerated growth trend of our key markets, automotive and industrial.

In order to be prepared, we continue to raise critical manufacturing capacities by remaining careful in adding operational fixed costs. Even in times of higher-than-normal capital expenditures, we remained to be a strong generator of free cash, working also on the optimization of our capital structure.

All in all, Vishay maintains to be a financially successful, solid and predictable enterprise, selling, innovative and competitive products to promising and growing markets.

For the fourth quarter, we guide for the sales range between $745 million and $785 million at gross margins of 28.0 percent to 29.5 percent of sales at the third quarter exchange rates. Thank you very much. Peter?

Peter G. Henrici:
Thank you, Dr. Paul. We'll now open the call to questions. (Crystal), please take the first question.

Operator:
Our first question comes from the Shawn Harrison from Longbow Research.

Gausia Fatima Chowdhury:
Good morning this is Gausia Chowdhury on for Shawn. First of all, was Asia at 0.69 and distribution at 0.80, it's surprising that (sales) guidance is not weaker. So how should we consider this dynamic? Is there more risk maybe for the first quarter to be more – much more versus seasonal? Maybe you're just not seeing it in the fourth quarter?

Gerald Paul:
Well, the backlog was extremely high to say it even unheard of. And we expected, since a long time, some normalization – some bookkeeping, if I may say, on the side of the distributors. And this is taking place now. Pretty much always the 13-week shippable backlog, this has no impact yet, really not. So we don't see a major change of the situation except for some corrections, which were expected.

Gausia Fatima Chowdhury:

OK. And then, can you give us more color on what you're seeing in China specifically? If there's any concerns or pockets of weakness within any of the end markets or any areas?

Gerald Paul:
Well, there is some concerns in China as I try to say concerning the new U.S. tariffs there. But this may also come – lead to some slowdown in automotive, which is seen. On the other hand, the slowdown is in pieces of auto, of cars. On the other hand there is an increasing electrification in the cars and we see no decline at all in the demand of our automotive customers, which cover also China.

So obviously, this increase in electrification of sets, some reduction of the car – of the new cars, as a matter of fact. We do not see for us, major changes in the trend. And again, the distributors normalize at the moment their backlogs and operation. This is going on, which doesn't mean at all that the end customers take this.

Gausia Fatima Chowdhury:
OK, great. And then just one more for me about just the lead times. I think you said that they are pretty stable – are there any pockets of change that you've seen? Or are they increasing in any areas?

Gerald Paul:
No, the easy answer for to give us, because we have a very broad portfolio, because the situation is different in different segments of our portfolio. In general, the lead times are decreasing, no question, but they are still very high, very high.

Even to the point that we do have problems with certain customers, as you can imagine. Customers are still very keen to get product. The lead times in certain cases have come down, as I said, because we increased capacity.

On the other hand, overall, I would say, my long career I haven't seen such a situation as we have today concerning long lead times. It's even in a way – I still have the feeling that we do not fulfill customers, which is why we add capacity and continue to do so.

Operator:
Again, if you have a question please press star one on your telephone keypad.

And our next question comes from the line of Ruplu Bhattacharya with Bank of America Merrill Lynch.

Ruplu Bhattacharya:
Dr. Paul, I wanted to start by asking you about margins. Opto margins were at 36 percent, very high margins. Do you think this is the sustainable level of margins going forward, based on the demand that you are seeing? And the same for resistors, even resistors margins were pretty high at 34 percent. So if you can just give us your thoughts on that?

Gerald Paul:
Ruplu, neither is the margins for resistors, inductors nor the margins for Opto value. We were at this level quite often to say it frankly. It all depends on the volume. And as long as the volume holds and this looks that way, we also hold to this margins.

So there's no question as to where the volume came and again, this was not a spike. Resistors were – it's a good margin also for resistors, (34 percent) we know that. But very often it's above 30 percent. And for Opto, we were always around 33 percent, 35 percent. So it's not a spike in that sense. Yes, the answer is if the volume holds, we can hold these margin.

Ruplu Bhattacharya:
OK, OK, and that's helpful. And then, overall in terms of supply and demand, I think you've talked about supplying catching up with demand and normalization on backlog. Overall, your incapacity competitors are adding capacity, when do you think industry supply comes into balance with demand based on what you're seeing in the market?

Gerald Paul:
I have to take some. Because I don't know exactly, of course, what happens in the market, I don't have the crystal ball. But for sure, we are in the process, but it's a slow process of normalization, slow process as I see it. And the end markets they are strong, at least from the standpoint of electronic component makers. They are strong.

And we don't see our decline in our key markets in automotive and in industrial. In fact, we are in midst of negotiations with the major automotive customers and the demand goes up for next year. So we are quite optimistic that good situation which we enjoy since 2 years now, will continue. Sooner or later, of course, there is a no demand which will not be fulfilled. So but I think it's a slow process.

Ruplu Bhattacharya:
Yes, that makes sense. And in terms of the capacity that you're adding, which areas are you adding capacity in? And if you can give us any guidance on how should we think about CapEx in fiscal '19. Do you think it will be higher or lower than this year?

Gerald Paul:
OK, I'll start with the letter. Will be somewhat lower. It will be between $180 million and $200 million as we see it at the moment, but which is absolutely required to fulfill the requirements of our customers, as a matter of fact.

And not exactly at (220), but not too much below, between $180 million and $200 million. And really, we put – we have to expand the diodes like MOSFETs, we have to expand resistors, we have to expand also certain lines in Opto. So it's a broad expansion. But believe me, we will not go overboard.

Ruplu Bhattacharya:
OK, the last question for me. With respect to your authorization for convert repurchase, is there a limit? Is there a certain dollar amount that you can repurchase?

Gerald Paul:
Well, as a matter of fact, this is a very flexible thing. We go ahead and in a certain way, opportunistically, buyback these converts. As a matter of fact, this is what I would like to state. It's a very important program I believe and we are going to start fast.

Operator:
Our next question comes from the line of Jim Suva with Citi.

Jim Suva:
Can you talk a little bit about pricing versus normal trends currently in going forwards? Because I believe a lot of your contracts may be like more than 1 quarter in nature? And so they maybe coming up for renewals?

And I guess, it would be fair to overly assume that maybe pricing going forward will continue to be stronger-than-expected? Is this correct? Or can you help correct me if not?

Gerald Paul:

No, you are absolutely right. We are in contract negotiations with large automotive customers. But on the other hand, there are contract negotiations with others throughout the year.

Still, the big automotive guys they are on the schedule now. And the today's price pressure as always is maybe not as hard as it used to be, because it is still – there are some shortages to say it. And the major customers, they want to be safe. And we feel less pressured than we historically have felt.

Operator:
Our next question comes from the line of Harlan Sur, JPMorgan.

Harlan Sur:
Can you help us understand, what are the biggest drivers of the gross margin declines in the December quarter? Are fixed costs rising as you guys bring in more capacity?

Gerald Paul:
Well, it has less shipping days, first of all. So it's a volume thing. So really, if you took the trust – the sales for which we have to forecast, Harlan. Not because of a lack of orders, it's because of lack of the shipping days and manufacturing days in that sense, as we compare to the third quarter.

This is a major driver of all that. Basically, also there we had a positive development in SG&A, which was a singularity which normalizes to an extent in the fourth quarter. And this basically makes the difference.

Well, there's also some on inventory. We have built inventory in the third quarter, some inventory – we are going to reduce inventory in the fourth quarter. These are the major drivers of the gross margin.

Harlan Sur:
I appreciate the commentary there. And maybe similar to the last earnings call, I am just curious, as we've headed into the fourth quarter we – as you mentioned, we are continuing to hear about some slowdown industrial in greater China and like goods and various other aspects of the geography there.

Maybe similar to last quarter, I'm just curious, what is the book-to-bill that the team is currently seeing right now thus far here in December quarter?

Gerald Paul:
Well, above 1. It's better than in the third quarter. So it's 1.12. I expected the question somehow. It's 1.12 in October.

Harlan Sur:
And then as you look into – go ahead.

Gerald Paul:
By the way, just wanted to add. In this positive book-to-bill, it's equally existent for semi conductors and for passives now.

Harlan Sur:
That makes sense. And so as we think about kind of a normal seasonal transfer for you guys, obviously, industrial/auto always tends to be, I think, seasonally stronger in the first half of next year.

Gerald Paul:
(This is very true), very true.

Harlan Sur:
And so given the trends that you're seeing (inaudible) book-to-bill, sounds like you're still anticipating kind of normal seasonal trends as you enter 2019?

Gerald Paul:
As I try to say, we see no tangible signs for a product downturn. (No real) changes in the downturn.

Harlan Sur:
Maybe just my last question. Obviously, you guys are a leader in diodes. I'm just curious, you're adding more capacity there? Can you just help us understand, what are the sum of the summer categories within diodes that you are still see some tightness?

Gerald Paul:
Well, it's all over – all rectifiers are tight and we have delivery times, which I am embarrassed to talk about even, it's long and we work against these long delivery times. And its really on the

(rectifier side) very strong. But we are leading in rectifiers, (maybe there for a) good position, especially in automotive.

Operator:
Again, if you have a question press star one.

And at this time, there are no further questions.

Peter G. Henrici:
Thank you. This concludes our Third Quarter Conference Call. Thank you for your interest in Vishay Intertechnology.

Operator:
Thank you. This concludes today's conference call. You may now disconnect, and have a wonderful day.

END