MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome, everyone, to the Garmin Ltd. Second Quarter 2012 Earnings Conference Call. Today's call is being recorded. At this time I'd like to turn the conference over to Kerri Thurston. Please go ahead, ma'am.

Kerri R. Thurston, Manager – Investor Relations

Thank you and good morning, everyone. We'd like to welcome to you to Garmin Ltd. Second Quarter 2012 Earnings Call. Please note that a copy of the press release concerning this earnings call is available at Garmin's Investor Relations site on the Internet at www.garmin.com/stock. Additionally this call is being broadcast live on the Internet. Please note that this webcast does include slides which can be viewed during this call. An archive of the webcast will be available until October 1, and a transcript of the call will be available on the website under the events calendar.

This earnings call includes projections and other forward-looking statements regarding Garmin Ltd. and its business. Any statements regarding our future financial positions, revenues, earnings, market share, product introductions, future demand for our product and objectives are forward-looking statements. The forward-looking events and circumstances discussed in this earnings call may not occur, and actual results could differ materially as a result of risk factors affecting Garmin. Information concerning these risk factors is contained in our Form 10-K for the year ended December 31, 2011 filed with the Securities and Exchange Commission.

Attending today's call on behalf of Garmin Ltd. Are Dr. Min Kao, Chairman and Chief Executive Officer; Cliff Pemble, President and Chief Operating Officer; and Kevin Rauckman, Chief Financial Officer and Treasurer. Presenters for this morning's call are Cliff and Kevin. At this time I'd like to turn the call over to Cliff.

Clifton A. Pemble, President and Chief Operating Officer

Thank you, Kerri, and good morning, everyone.

As we announced earlier this morning, Garmin delivered strong revenue and margin performance resulting in pro forma EPS growth of 56% in the second quarter. Consolidated revenues increased 7% year-over-year to $718 million, with growth in Outdoor pacing all other segments at 24%. Our traditional markets of Aviation, Marine, Outdoor and Fitness contributed 45% of the total revenue mix.

Gross margins improved to 59% from 48% in the prior year. Kevin will discuss specific items impacting margin performance later during his remarks. Operating margins also improved significantly to 28%, with our traditional markets posting 10% operating income growth in the quarter. Revenue growth combined with improved margins resulted in both operating income and pro forma EPS growth. Operating income for the quarter grew 55% to $204 million while pro forma EPS was $0.98, a 56% improvement over the prior year. We sold 3.9 million units in the quarter, up 4% year-over-year.

Next, I'll walk you through the financial and strategic highlights segment-by-segment.

Starting first with Marine, revenue in the Marine segment declined 14%, driven by weak economic conditions around the world. However, better gross margins largely offset the lower sales. Sales in Europe were down sharply, while sales in other regions were comparatively better, but still soft during the normally robust second quarter selling season. Industries statistics indicate that boating sales have improved, the trend seems to be towards low end boats where there's little to no marine electronics content. We maintain a high level of confidence in our long term opportunities in the marine segment and are continuing to invest in new product development and strategic alliances that position us for market share gains. As we have mentioned previously, these investments will create near term operating margin compressions.

In Aviation we posted revenue growth of 4% as improvements in OEM deliveries were partially offset by weakness in the aftermarket. In recent quarters, operating margin has trended below historical norms, as new programs require a higher level of R&D investments compared to what we have seen in the past. We remain confident that these investments will lead to stronger revenue and operating margin for the future.

During the quarter we made additional announcements that demonstrate the progress we are making to expand our presence in the business jet market. Cessna selected are G5000 Integrated Flight Deck for the new Citation Longitude, which is the longest range business jet operating in the Cessna line up. This expands upon the already successful relationship we have had with Cessna for many years now.

In addition, we announced a new relationship with Bombardier. They selected the G5000 for the new Learjet 70 and 75, which are scheduled for delivery in 2013. Due to the steadily increasing number of new cockpit certifications that are in progress, we thought it would be helpful to provide a summary of the major wins that have been announced so far, and projected entry into service based on publicly available information, from the aircraft manufacturers.

In 2013 we anticipate entry into service of the Citation M2 with the G3000 Integrated Cockpit System, the Citation Ten with the G5000 Integrated cockpit system and the Learjet 70 and 75 also with the G5000 system. In 2015 we anticipate entry into service for the Citation Latitude, which will be equipped with the G5000 system. And finally, in 2017 we anticipate entry into service for the Citation Longitude, which will be equipped with the G5000 system. We expect these wins, along with other initiatives to deliver revenue growth in Aviation that outpaces that of the overall industry.

Turning next to Outdoor, the Outdoor segment continued to perform well in the quarter with 24% revenue growth and 23% operating income growth driven by new products and category expansion. In the golf market we are experiencing growth across our product offerings with our high-end wristwatch, the Approach S3, and our newest handheld, the Approach G6, both contributing to the strong results. In early July we introduced yet another innovative product in the Outdoor category which is thefenix. This rugged yet stylish wristwatch integrates best-in-class outdoor watch functionality with GPS navigation. In addition to the GPS functionality, which we are known for, the built-in sensors include an altimeter for elevation, a barometer for providing weather information, and a compass for navigation and tracking. The watch can also be paired with additional sensors to provide temperature, heart rate and cadence. We believe this is a highly attractive offering at the value price of $400.

Looking next at the Fitness segment, revenue grew 5% while operating income grew 35% on a year-over-year basis. This lower revenue growth, but stronger margin performance, are attributable to variability in our product cycle during the past year. In 2011 we delivered the Forerunner 610, which positively impacted revenue through channel fill, while discounts on the end of life Forerunner 305 drove additional volumes. But that negatively impacted margins. So far in 2012 there have been no major product announcements. However, we have experienced good demand for our high end products, including the Forerunner 910XT, the Forerunner 610 and the Edge 500. We anticipate revenue growth rates will improve later this year as we launch new products in time for the holiday season.

Late in the quarter we launched the Garmin Swim, our first fitness product that targets the swimming market. This training watch tracks stroke type, stroke count, distance, pace and length. This information can be uploaded to Garmin Connect for a post-workout analysis. Garmin Swim was introduced at the U.S. Masters Summer Swimming Championships where it was well received by the swimming community, including both former Olympians and Olympic hopefuls.

Our Automotive/Mobile segment experienced another strong quarter with revenue growth of 8% along with strong margins. Our strong margin performance was partially due to a one-time benefit of $21 million, due to an overpayment of certain royalties. Kevin will provide additional details in a moment.

We gained additional market share in the second quarter, and now estimate that our market share in North America exceeds 70%, with European market share of approximately 35%. While we have posted three consecutive quarters of revenue growth in the segment, we continue to expect that the overall PND market will decline approximately 10% to 15% in units and value for the year. This decline is consistent with our prior expectations for the market.

During the quarter we introduced an update to our zumo product family, which is designed specifically for the motorcycle market, and represents an important customer base for us.

We remain focused on OEM market opportunities, and are excited to partner with Suzuki as they launch their 2013 models with the Garmin branded infotainment system.

Turning next to guidance; having passed the halfway point for 2012 we are updating our full year guidance. In light of our solid first half performance, we are narrowing our revenue range to $2.75 to $2.8 billion, which is at the high end of prior guidance. Additionally we have raised our margin expectations for both gross and operating margins. As a result, we are increasing our pro forma EPS guidance to a range of $2.70 to $2.85, an increase of approximately 10%.

That concludes my remarks. Next, Kevin will walk you through additional details on our financial results. Kevin?

Kevin S. Rauckman, Chief Financial Officer

Thanks, Cliff. Good morning, everyone. I'd like to begin by reviewing our income statement and margin results, then move to the balance sheet and cash flow statement, and conclude with a few comments regarding our full year 2012 expectations.

You saw that we posted revenue of $718 million for the quarter, with pro forma net income of $193 million. Our pro forma EPS was $0.98 per share, which excludes the foreign currency loss. Our revenue represents an increase of 7% year-over-year. Gross margin came in at 59%, which was a 1100 basis point improvement from the prior year. I will discuss this in further detail by segment a little bit later.

Operating margin was 28%, up 890 basis points from the prior year. The components of this increase were gross margin being favorable by 1100 basis points, offset by advertising 20 basis points unfavorable, which was up $4 million on a year-over-year basis. SG&A at 110 basis points unfavorable, up $13 million on a year-over-year basis. Our R&D was 70 basis points unfavorable, up $9 million on a year-over-year basis. Each of these expense categories will be discussed further on a later slide.

Our pro forma EPS of $0.98 represents a 56% increase year-over-year, driven by increasing revenues, good gross and operating margins. Units shipped increased 4% year-over-year as 3.9 million units were delivered during the quarter and our total company average selling price was $184 per unit, up 3% from Q2 of 2011.

According to U.S. GAAP we must defer revenue on certain products and this table summarizes the net impact of the deferral and amortization of revenue, and related costs, in the second quarter of 2012 and 2011. In the current quarter we deferred on a net basis approximately $16 million of revenues, resulting in $0.05 of tax-effected, deferred, earnings per share during the quarter. In the second quarter of 2011 we deferred net revenue of $62 million or $0.23 of tax effected EPS. While we are deferring revenue according to U.S. GAAP, we are collecting the cash at time of sale as reflected in the statement of cash flows. We expect to have a negative revenue and EPS impact due to referrals in the upcoming quarters, but do not expect the impact to be as significant as the amounts that we deferred in 2011.

With this said, the total of our revenues increased 7% during the second quarter with all segments, excluding Marine, contributing to the growth. During the second quarter we generated an 8% revenue increase within the Automobile segment, as volumes increased due to our 2011 acquisition of Navigon, we continue to gain market share and we benefited from a reduction in deferred revenue.

Our Outdoor segment posted the strongest revenue growth at 24%, due primarily to market share gains within the GPS enabled golf market, strong consumer reception for our recent product refreshes, and the acquisition of Tri-Tronics in the back half of 2011.

The Fitness segment continued to grow with a 5% revenue increase when compared to Q2 of 2011. The slower growth resulted from an exceptional Q2 2011 when we were heavily promoting the Forerunner 305 and had just begun delivery of the Forerunner 610. We will have new Fitness products in the back half of 2012.

Aviation segment revenues increased 4% compared to Q2 of 2011 with growth in OEM, partially offset by a slowdown in the aftermarket.

And finally, Marine segment revenues decreased 14% compared to Q2 last year as both the aftermarket and OEM markets slowed down due to a global decline in the marine electronics market.

For Q2 both the Americas and EMEA posted revenue growth with a slight decline in APAC. The decline in APAC is the result of a change in shipment locations for our major OEM customer. Without the impact of this change, our APAC region would've grown approximately 10%. For Q2 of this year, the Americans represented 55% of revenue compared to 53% in Q2 2011. EMEA decreased from 38% of totals in Q2 2011 to 37% in Q2 2012, while Asia decreased from 9% to 8% in the same period.

The Auto/Mobile segment represented 55% of our total revenue during Q2, up slightly from 53% in Q2 2011 due to the contributions from our acquisition of Navigon. Outdoor grew to 14% of revenues in the quarter, an increase from 12% in 2011. And due to the improved profitability of Auto/Mobile in the second quarter, the operating income contribution of the segment increased to 43% from only 19% in the prior year. In absolute dollars our traditional segments of Aviation, Marine, Outdoor and Fitness contributed $117 million of operating income in the quarter, a 10% increase over the second quarter of 2011.

Moving next to the margin analysis, our second quarter Auto/Mobile gross margin and operating margin were 51% and 22%, respectively. The year-over-year improvement in gross margin was primarily driven by the amortization of previously deferred high-margin revenue, which contributed 590 basis points. A one-time royalty fee adjustment of $21 million, contributing 510 basis points, and product mix shifting toward more full featured large screen devices. Operating margin improvement resulted from the strong gross margins with only a slight offset in SG&A expenses due to a legal settlement during the period.

Q2 Outdoor gross margin was 67%, up from 65% year ago quarter. Operating margin was 44%, flat to the year ago quarter as improved gross margins were offset by a slight increase in operating expenses.

Q2 Fitness gross margin, 69%, up from 58% in the year ago quarter when we were heavily discounting the Forerunner 305 product. Operating margin is 42%, again up significantly from the year ago quarter as improved gross margins were only slightly offset by increased advertising costs in the segment.

Q2 Marine gross margin was 64% compared to 56% a year ago, as product mix shifted toward higher margin products. Operating margin was 27%, down from 30% a year ago as the gross margin improvement was offset by increased R&D expenses to support our long-term marine OEM strategy and cooperative advertising with our marine partners.

Our second quarter Aviation gross margin was 71%, up from 69% in Q2 2011. Operating margin was 27% for the quarter, down from 30% in the prior year due primarily to increased R&D expense associated with new OEM programs that will begin to contribute to revenue in 2013, and increased SG&A costs due to a bad debt credit that we booked in Q2 of last year.

Our second quarter operating expenses increased by $27 million on a year-over-year basis from $191 million in Q2 2011 to $218 million in Q2 2012, and increased 200 basis points as a percentage of sales.

R&D increased $9 million year-over-year in the second quarter and 70 basis points to 11% of sales as head count increased with our recent acquisition and we continued to invest in OEM opportunities.

Our ad spending increased $4 million over the year ago quarter, and increased 20 basis points as a percentage of sales to 5% in Q2 of 2012. This was largely driven by additional costs associated with acquired entities and cooperative advertising and promotional activities in our Outdoor, Fitness and Marine segments.

And SG&A increased $13 million compared to the year ago quarter, which was a 110-point basis point increase to 14% of sales. The increase is primarily attributable to acquisitions and a $9 million legal settlement.

Moving next to the balance sheet, we ended the quarter with cash and marketable securities of over $2.6 billion. Our accounts receivable increased sequentially to $486 million due to seasonal strength in the second quarter. Accounts receivable accounted for approximately 62 days of sales when calculated on a trailing four quarters, compared to 66 days of sales in the second quarter last year. Our inventory balances decreased to $384 million on a sequential basis at the close of the second quarter. And our days of inventory metric was 98 days compared to 106 days in the second quarter of 2011. The dividend payable now reflects three remaining quarterly payments of $0.45 per share, which was approved by our shareholders on June 1 at the annual meeting.

We continue to generate significant free cash flow across our business as cash from operations was $223 million during the second quarter. CapEx was $12 million during Q2. Therefore we generated free cash flow of $211 million during the quarter. Cash flow invested during Q2 was $146 million, which was including $12 million in CapEx and $132 million net purchase of marketable securities. Financing activities were an $86 million use of cash during the Q2 due primarily to the dividend payment on June 29. We earned an average of 1.3% on all cash and marketable securities balances during the second quarter.

With our strong free cash flow generation year-to-date we are making good progress toward our forecast of $650 million, which will fund our annualized dividend of $1.80 per share or approximately $350 million. We also continue to pursue acquisitions in adjacent niche markets, and tuck in technologies which fit with our core markets. As has been Garmin's practice, acquisitions will continue to be evaluated by technology, value, compatibility and strategic fit. Our tax rate for Q2 was 10.4% due to the release of reserves following the expiration of the statute of limitations. We expect the full year 2012 tax rate to be approximately 13%.

Finally, as Cliff mentioned, we're updating our full year 2012 guidance given current trends across our segments. Let's review the total company guidance. So here we just provide additional detail on revenue by segment. At a high level we have increased our growth expectations for Auto/Mobile and Outdoor, our two largest segments, while Fitness and Marine expectations have been reduced.

The up side in Auto/Mobile is the result of better than expected market share gains and product mix. Deferred revenue has also proven to be less of a headwind than expected. Outdoor revenue guidance is being raised due to the continued strength we are achieving in golf and dog-related products. Offsetting these positives, we reduced our Fitness forecast due to new product delays, and our Marine forecast due to a weak marine environment, which we view as a macro economic problem.

While on the surface this revised guidance may appear conservative given our strong first half performance, we do have a number of contributing factors to consider. First our first half revenue growth was positively impacted by our acquisitions of Navigon and Tri-Tronics, which were completed in the third quarter of 2011. Our Outdoor segment had very strong fourth quarter 2011 due to new product introductions, and a strong holiday season for our golf devices. Also, the European macroeconomic situation and subsequent weakening of the euro creates possible headwinds for us in the back half of the year.

This concludes our formal remarks this morning.