

FINAL TRANSCRIPT

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AUTH - Q1 2008 AUTHENTEC INC Earnings Conference Call

Event Date/Time: Apr. 28. 2008 / 5:00PM ET

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PRESENTATION

Operator

Good afternoon and welcome to AuthenTec's first quarter 2008 results conference call. (OPERATOR INSTRUCTIONS). As a reminder, this conference call is being recorded today, Monday, April 28, 2008. I would now like to turn the call to Kellie Nugent of The Shelton Group, the investor relations agency of record for AuthenTec.

Kellie Nugent - The Shelton Group - Investor Relations

Thank you, [JD]. Thank you, everyone, for joining us today to discuss AuthenTec's first quarter 2008 financial results. With me on today's call are Scott Moody, Chairman and CEO, Gary Larsen, CFO, and Larry Ciaccia, President. As JD mentioned, this call is being recorded. It is also being broadcast live in voice mode over the Internet and may be accessed in the investor relations section of AuthenTec's Web site, at investors.AuthenTec.com.

After the market closed today, AuthenTec issued a press release discussing the financial results for the first quarter ended March 28, 2008. By now everyone should have access to the press release and the financial tables. However, if you do not, they are available on the Company's Web site.

Please be advised that the matters discussed in this teleconference contain forward-looking statements regarding future results or events. We caution you that such statements are in fact predictions that are subject to risks and uncertainties that could cause actual events or results to differ materially. Additional risks and uncertainties that could cause actual events or results to differ materially from these forward-looking statements may be found in the Company's filings with the Securities and Exchange Commission. Forward-looking statements are based on the Company's beliefs as of today, Monday, April 28, 2008. AuthenTec

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undertakes no obligation or responsibility to publicly update any forward-looking statements for any reason except as required by law, even as new information becomes available or other events occur in the future.

Additionally, in the Company's press release and during the teleconference, management will discuss certain measures and information in GAAP and non-GAAP terms. A reconciliation of GAAP to non-GAAP results is provided in the financial tables following the text of the press release.

I will now turn the call over to AuthenTec's Chairman and CEO, Scott Moody.

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Thanks, Kellie. Welcome to our first-quarter conference call. I'd like to thank everyone for taking the time to join us this afternoon.

I'm pleased to report our first-quarter results, in which we achieved a 67% increase in revenue, a 350 basis point improvement in gross margin, and an \$0.11 non-GAAP improvement in profits over the same quarter a year ago.

Starting with revenue, we finished the quarter at \$15.5 million, thus exceeding the top-end of our guidance, which was 15 to \$15.3 million. These revenues were driven by continued strength in the PC market as we saw our attach rates in laptops increase across both existing and new OEM accounts.

With respect to margins, we continued to experience the benefits of a favorable product mix shift to our new higher-margin products, as well as lower manufacturing costs during the quarter, resulting in gross margins of 49.6%.

And with respect to profitability, on a GAAP basis, we finished at \$0.01 per share, while our non-GAAP earnings came in at \$0.02 per share. I'll note that our non-GAAP EPS results were at the top-end of our guidance of \$0.01 to \$0.02, even with the impact of an in-process R&D charge we took for the EzValidation asset acquisition. Had it not been for this charge of \$0.01, our non-GAAP EPS would have come in at \$0.03 per share.

While on the subject, let me provide a few quick points regarding the EzValidation transaction. As some of you have read in our press release, EzValidation was a California-based provider of fingerprint authentication and user interface software for PCs. We acquired the software assets of EzValidation for \$250,000 in cash; that included their EzPassport PC client-based software. Client-based software resides specifically on the PC, as opposed to residing on, say, a server, or some kind of enterprisewide-type solution.

As you know, we already offer a number of client software elements, including such things as the drivers and matching algorithms. Adding select features of EzPassport, including password replacement, file encryption, network log-on and the like, will further enhance the user experience associated with our fingerprint (technical difficulty). Our software team is already hard at work integrating EzPassport features into our TrueSuite application, which we will begin demonstrating to PC customers in the third quarter.

Of course, we continue to work with a number of partners as part of our Solution Provider Network, who interface with our products at the client level to provide those server-based software solutions I just mentioned.

From an overall business perspective, we continued to execute on three key objectives that will extend our reach in what we believe is a 1 billion-plus unit market opportunity for our products. As a reminder, these objectives include -- ramping new products and executing on our new product roadmap, as evidenced by the fact that we introduced two new products and one new technology during this last quarter; expanding fingerprint sensor attach rates with existing customers, while also diversifying our customer and market base, as evidenced by our 60% plus revenue growth; and finally, integrating new functionality into our products and solutions, as highlighted by our Ez acquisition.

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Moving to our market segment, in the PC market we officially introduced our fifth-generation sensor, the AES2810. The 2810, which had been code-named (inaudible), is the most highly integrated single chip match-on solution in the market, and is targeted for notebooks, desktops and PC peripherals. Every year, millions of dollars worth of corporate and personal information is lost and stolen by way of unprotected laptops, stolen passwords, or data breaches. The 2810 establishes a new benchmark for security and cost-effectiveness, and will be introduced in both commercial and consumer products by three of the top five PC OEMs during the second quarter. As we've said before, we estimate that as many as one in four notebook PCs shipped in 2008 will include a fingerprint sensor. A noteworthy number of these will ship with our 2810, creating a new generation of highly secure PCs. We expect the 2810 to make a material impact on our revenues starting this quarter.

In addition to the success of our new products, our existing products continue to be adopted as a standard security feature across a wide range of notebook PC models, including some of the most innovative notebooks being offered today.

As an example, in February we announced that our AES1610 was integrated in two of the world's first notebooks to offer 1 terabyte, that's 1 trillion bytes, of disk storage capacity. ASUSTeK's new M50 and M70 entertainment PCs, unveiled at the Consumer Electronics Show, offer AuthenTec security to protect the large amounts of data and multimedia content that will be stored on these new notebooks. Our sensors also bring the convenience of password replacement, since these entertainment notebooks will likely be connected to MP3 and video download sites, requiring a login and a password.

I would like to note that AuthenTec achieved strong growth in the PC market despite the fact that Q1 is historically a seasonally slow quarter for PCs. Our sensors are now integrated into consumer and enterprise notebooks from eight of the nine leading notebook manufacturers.

Turning now to wireless, as discussed on our last quarter's call, our largest wireless customer shifted production from one phone model to their next AuthenTec-enabled product, as they have historically done in the first quarter. This is what led to the slight decrease in our sequential sales of about \$200,000. However, despite this transition, we realized a 100% year-over-year revenue growth in wireless, and achieved several key milestones during the quarter as well.

Also during last quarter's conference call, I briefly mentioned that we are on track to announce our fourth-generation product targeted specifically to the low-power needs of the mobile wireless market. In February we officially announced the AES1711, which is already designed into new mobile phones that will ship in the fourth quarter of this year. The 1711 offers both power savings and added durability needed for today's mobile devices, and provides new revenue opportunities for service providers and OEMs by giving device users quick and secure access to mobile content and applications.

As in the PC market, our existing wireless products continue to be incorporated into new fingerprint-enabled phones to protect sensitive phone data and, in certain geographies, even mobile commerce transactions.

In March, we announced that the AES1710 would provide security and navigation to the first fingerprint-enabled phone ever offered by ASUSTeK, one of the world's largest and fastest-growing mobile device manufacturers. The [M3-536] world phone incorporates our 1710 to protect sensitive personal data, enable convenient access to Internet portals, and to provide on-screen navigation.

The 1710 has also been incorporated into two new Fujitsu phones, including the new DoCoMo FOMA 905i world phone, and Fujitsu's first-ever fingerprint-enabled Windows mobile phone, the FOMA 1100. Fujitsu has now deployed and shipped 15 AuthenTec-enabled mobile phones, with plans to launch several additional models in 2008 and beyond.

Although Japan is presently the largest market for fingerprint-enabled phones, we are now seeing carriers outside of Japan add an AuthenTec-enabled mobile device to their subscriber offerings. Highlighting the broadening of the market, the HTC Shift, which incorporates an AuthenTec fingerprint sensor, is now available in both the UK and the United States. Specifically, Orange in the UK announced in February they would carry the Shift, which is a UMPC [lite] device, which supports 3G in Europe and Quad Band GSM in the USA.

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Following this rollout in the UK, in March, Sprint and HTC announced that Sprint would be -- that the Shift would be available to US subscribers, marking the first fingerprint-enabled mobile device supported by a US carrier. The Shift will operate on the Sprint mobile broadband network and will be available nationwide.

We believe these are the first signs of AuthenTec-enabled phones beginning to proliferate outside of Asia, not necessarily just related to mobile commerce, but focused on protecting the information on the phone, protecting the network links back to the office, or even to your personal bank account, and securing the asset itself from theft.

As a way to showcase our new wireless sensors and technologies during the quarter, AuthenTec hosted customers and prospects at major wireless venues, including CES, the GSM World Congress, and CTIA.

At CTIA, we unveiled our new TouchStone packaging technology. This technology will enable a new class of fingerprint sensors that combine all the features of TruePrint technology with highly durable, easy-to-integrate, waterproof and surface mountable package capability. TouchStone will help expand the aesthetic and product integration options available to makers of cellphones, ultra-mobile computers, and other consumer electronics. The first products with TouchStone will be introduced later this year, but more importantly, we are very excited about our product roadmap around TouchStone. Future TouchStone variants will be available across all our market segments as well in the future.

Technologies such as our RF-based TruePrint live layer sensing technology and our new TouchStone packaging technology have helped us not only in essence create the consumer and enterprise markets for fingerprint sensors, but have established AuthenTec as the market leader. Our intellectual property, which includes more than 60 filed and pending US patents, is one of our most important assets, and a true competitive advantage for AuthenTec.

To protect our portfolio, we recently filed a patent infringement lawsuit against a small privately held competitor. The suit was initially filed alleging infringement on three AuthenTec patents, but has since been expanded to include a total of five US patents. While the market for fingerprint sensors is expansive and allows for multiple competitors, we will continuously vigorously protect our technologies and IP.

In summary, during the first quarter we focused on execution and progress toward the achievement of our strategic objectives. We introduced two new products that will contribute to increased revenue during the course of the year, as well as strategically invested in R&D that will further advance our new product roadmap. We also took steps to expand our software offering in order to provide a more complete solution for our customers, and unveiled new packaging technologies which will expand design options and help guide down product costs over time. And finally, we drove increased revenues and profitability as we expanded our customer base and increased attach rates with existing customers.

Now I'll turn the call over to Gary for a detailed review of our financial results.

Gary Larsen - AuthenTec, Inc. - CFO

Thanks, Scott. Good afternoon, everyone. Revenue for the first quarter of 2008 was \$15.5 million, which, as Scott mentioned, exceeded our guidance range of 15.0 to \$15.3 million. This compares to \$9.3 million reported in the first quarter one year ago, and \$15.7 million reported in the fourth quarter 2007.

The 67% revenue growth compared to the prior year reflects strong growth in the PC market, as the attach rate for our products increased and we further penetrated new customers. Revenue was relatively flat on a sequential basis, as growth in shipments in the PC market were offset by lower wireless revenue as the customer transitioned from one phone model to their next AuthenTec-enabled product.

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On a non-GAAP basis, gross margin, including stock-based compensation, was 49.6% in the first quarter. This represents a 350 basis point improvement when compared to the 46.1% that was reported one year ago. First-quarter gross margin was comparable to the 50.0% reported in the fourth quarter 2007. As Scott mentioned, the year-over-year gross margin expansion was primarily due to a continued favorable product mix shift of higher-margin sensors and lower production costs.

Operating expenses, excluding stock-based compensation, were \$7.9 million, compared to \$6.1 million in the first quarter one year ago, and \$7.4 million in the fourth quarter 2007. Operating expenses as a percentage of revenue declined 51% in the first quarter 2008 from 65% in the year-ago quarter. The sequential increase in expenses primarily reflects higher R&D spending to support product development initiatives, as well as a \$250,000 R&D charge related to the EzValidation transaction.

On a GAAP basis, net income for the first quarter 2008 was \$188,000, or \$0.01 per share. This compares to a net loss of \$5.7 million, or \$7.30 per share, in the first quarter of 2007, and net income of \$898,000, or \$0.03 per share, in the fourth quarter 2007.

Non-GAAP net income in the first quarter 2008 was \$587,000, or \$0.02 per share, which excludes stock-based compensation charges of \$399,000. This compares to a net loss of \$1.7 million, or \$0.09 per share, in the first quarter 2007, and net income of \$1.3 million, or \$0.04 per share, in the fourth quarter of 2007. Non-GAAP earnings per diluted share for the first quarter of 2008 were computed using 30.5 million shares.

Turning to the balance sheet, we ended the first quarter with \$67 million in cash and investments, compared to 66.3 million at the end of the fourth quarter of 2007. Operating cash flow was \$545,000 in the quarter.

As of March 28, 2008, accounts receivable was \$6.5 million, nearly flat with the \$6.4 million in the fourth quarter of 2007. Our collections remain strong, with DSO of 38 days in the first quarter, roughly flat with the DSO of 37 days in the fourth quarter 2007.

At the end of the first quarter, inventory was \$4.1 million, which represents 48 days on hand. These levels reflect an 11-day improvement in our inventory management from the 59 days on hand at the end of the fourth quarter. Capital expenditures for the first quarter were \$190,000, and appreciation was \$239,000.

With regard to guidance, we expect our strong growth to continue for the remainder of 2008, driven by new product introductions and a robust pipeline of design wins. For the second quarter of 2008, we anticipate revenue to be in the range of 17.2 million to \$17.8 million, driven by the start-up of volume shipments of the AES2810 into the PC market. The midpoint of this range represents 42% growth over the prior year, and 13% sequential growth when compared to the first quarter of 2008.

Gross margins in the second quarter are expected to range from 47 to 49%, reflecting the ramp-up of the AES2810 and the initial lower yields in production and efficiencies typically experienced with a new product introduction. In order to continue our momentum, we plan to accelerate our R&D investments in the second quarter to support several new product developments and other initiatives. Correspondingly, we expect our non-GAAP earnings per share to range between \$0.02 to \$0.03 per share, which is an improvement over the loss of \$0.03 per share in the same period one year ago.

Let me now hand the call back to the operator, who will facilitate our Q&A session.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS). John Barton, Cowen & Co.

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John Barton - Cowen & Co. - Analyst

Scott, as you look into the June quarter here, obviously, that's some great growth forecasted at 13% sequentially. Could you kind of break that down? Obviously, the PC market in general will probably be slightly down. How much of that is share gains, increased attach rates? I know you highlighted the 2810 as a driver, but if you could break it down anymore, that would be great. Thank you.

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Frankly, John, I don't think we have that level of specificity between new customers, or existing platforms versus new platforms. Clearly, a good part of our growth in the second quarter will be driven by two material new accounts for us, one particularly in Q2, another one a little bit more in Q3 and Q4. As we mentioned earlier, the 2810 has three major design-ins right now. Three of the top five PC OEMs have designed it in. One of those is an existing account; two of those are, in essence, new accounts. In terms of the ramp over this quarter, a good bit of that is directly associated with the 2810. I'm not sure I gave you the level of specificity that you wanted, but hopefully that was good enough.

John Barton - Cowen & Co. - Analyst

Good enough. Thank you. As far as the annual revenue for the calendar year, if I'm not mistaken, you had originally targeted a 72 to 78 range. Your closure of March, your new -- your view of June now, does that change that range whatsoever for the year?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

We're only providing annual guidance twice a year, as a result of the Q4 quarterly call, and then again for the Q2 quarterly call. So we won't provide that until we -- an update to that. So right now we're staying with our 72 to \$78 million, which is an increase from about 52 million last year.

John Barton - Cowen & Co. - Analyst

On the acceleration of the R&D spending, could you give us an idea of how that should trend as we go out further in time and the specific area that its intended to be targeted on, please?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

If you look at it, we're flowing through not quite \$2 million of incremental revenue from at least what many of the analysts had been expecting. And we're taking probably a quarter of that, and instead of letting it just flow to the bottom line, we're investing that in R&D, as you've picked up.

For one, yes; we're very happy with our growth. Clearly, our volumes and our revenues are picking up. But we're still a relatively small part of the total available market that we think is in front of us. Last year we shipped about 13 million sensors, but we believe that's part of a 1 billion-unit market opportunity. So we see this, really, as an opportunity, the accelerating revenue, to actually advance our R&D projects.

Specifically in that, I mentioned TouchStone. It's a pretty exciting technology, really, being developed by our packaging engineers as part of operations. And we're accelerating -- we're working to accelerate as much of that technology as possible. We're introducing -- the first one is going into production now, the first version of that technology. As I mentioned, but we're pretty

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excited about the product roadmap. And really, instead of waiting until next year, we're trying to move it in as fast as we can. So, packaging is one thing.

Software, we mentioned the EzValidation. In the past, we've only provided the drivers, the matching algorithms. We didn't usually go up to the point of offering the application, i.e. the graphical user interface, the actual password replacement capabilities. And now with the EzValidation acquisition, which I think we've done at a very good price, we will be able to add that capability. So software is another area where we're adding resources.

And that's going to do two things for us. One, it's going to make the user experience better. And then second, in terms of our long-range margins, obviously, software can be a profitable business, and that will incrementally improve our margins as well.

And then finally, we saw this as an opportunity to try to pull in some of our silicon -- new silicon products. We're really not talking about them yet. We will probably talk about them a little bit more as part of the Q2 earnings call.

So in summary, we're taking as much of that as (1) possible and (2) reasonable, and allocating it toward TouchStone, our software TrueSuite, and then, of course, our silicon products. So a little bit of a lot of things.

John Barton - Cowen & Co. - Analyst

Last question if I could, and that is you mentioned the expanded legal strategy, so to speak, at least the one initiative. How should we be thinking about legal expense as we look out the next four quarters or so?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Obviously, the actual timing and amount of the expense is going to be dependent on the court and the schedule it puts together. We do have some rough estimates. We think it will be about 150,000 in Q2, and probably about \$0.5 million in the second half of the year.

John Barton - Cowen & Co. - Analyst

Thank you.

Operator

Brian Ruttenbur, Morgan Keegan.

Brian Ruttenbur - Morgan Keegan - Analyst

Excellent quarter. The first question I have is on your long-term investments. Are any -- is any of that in option rate securities? I don't recall the answer.

Gary Larsen - AuthenTec, Inc. - CFO

We re-classed about 9 million of option rate securities from short-term to long-term. They had (inaudible). None of these -- all of these are AAA or AA-rated securities, and we don't see any kind of default risk with them. They're parked in long-term until they become liquid again.

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Brian Ruttenbur - Morgan Keegan - Analyst

How much in total do you have in option rate? Is that the 17 million, and that's it? (multiple speakers)

Gary Larsen - AuthenTec, Inc. - CFO

There's some other investments, CDs, and some other notes and stuff that are in there, that are all -- those all come due the first -- the second quarter of next year. So there's no issue with those. So only 9 million of the 17 (multiple speakers)

Brian Ruttenbur - Morgan Keegan - Analyst

That clears that up. The R&D -- I was a little bit confused. I know it's already been hit upon, going up. So you went up from quarter-to-quarter from about 500,000. Should we expect, basically, this level, about 4.1 million going forward? Because I know some of it was the in-process R&D charge.

Gary Larsen - AuthenTec, Inc. - CFO

So in the first quarter, about 250 was the in-process R&D. So as we talked -- as Scott talked about, we are expecting -- we are going to be making some more investments. So we do expect it to go up in Q2, somewhere above 4 million.

Brian Ruttenbur - Morgan Keegan - Analyst

So basically holding it flat from where your actual number was, about 4 or 4.1, is where you're going to run going forward, is the correct answer?

Gary Larsen - AuthenTec, Inc. - CFO

I think for Q2, somewhere in that range.

Brian Ruttenbur - Morgan Keegan - Analyst

Do you expect 100,000, \$200,000 growth a quarter? What do you see project-wise?

Gary Larsen - AuthenTec, Inc. - CFO

What I was just referring to was specifically for Q2.

Brian Ruttenbur - Morgan Keegan - Analyst

Okay. I was trying to get more information out of you for the next -- the third and fourth quarter, but I'm probably reaching. Let me go on to another question, because --

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Scott Moody - AuthenTec, Inc. - Chairman and CEO

The one thing I would say, Brian, is percentage of our revenues, our operating expenses continue to drop, obviously, materially from a year ago. But even with that, our ramping and spending a little bit more, our operating expenses as a percentage of revenue will go down Q1 to Q2. So what we've done, I think, is we're managing those expenses associated with our revenues. They will continue to go down, as per our objectives to reach our long-term objectives. And it will probably kind of go consistent with that philosophy, driving them down. But of course, any revenue ramps, we do want to use that as an opportunity to secure future R&D.

Brian Ruttenbur - Morgan Keegan - Analyst

The last question I have is -- you talked about the laptop market; you hope to have 25% penetration. I assume that's the worldwide laptop market for new laptops. Is that correct, first of all?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

That's correct. And that's our estimate of total fingerprint sensors, ours and others. (multiple speakers)

Brian Ruttenbur - Morgan Keegan - Analyst

You have dominant market share, like 90-plus%, right?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

That's in the cellphone market. We believe that of all the cellphones shipped, we have a probably 90% plus (multiple speakers)

Brian Ruttenbur - Morgan Keegan - Analyst

What's your market share for laptops then?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Again, it's an estimate, obviously; we have to estimate what competitors. Last year we had been usually saying around by midyear 50%. We believe that went up as the year went along. And this year we're probably looking at -- again, it's a guess -- but, say, 60%

Brian Ruttenbur - Morgan Keegan - Analyst

What kind of movement market penetration -- the main question I had was on the PC market. What kind of penetration do you have there, and where do you see it going?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

That's where we would probably say -- again, let me refer to all fingerprint sensors into the market, last year, we probably estimated that 15 to 20% of all new laptops, to your point earlier, included a fingerprint sensor. We believe that during the course of this year, that number will move up 20 to 25, and that's when we said as many as one in four. We do believe that probably one in four laptops, certainly by the end of the year, will be shipping with -- with a fingerprint sensor. And again,

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roughly, we believe that -- and I haven't run these numbers all the way through, frankly -- but probably a 60% market share for us is not unreasonable.

Brian Ruttenbur - Morgan Keegan - Analyst

I'm sorry; I was talking about desktops, PC desktops. Do you have any kind of market penetration numbers on the actual stand-alone hard desktops versus a laptop?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

I'm sorry about that. My apology for answering the question wrong. In the desktop, we're still relatively negligible. There are several laptops and PC -- desktops and PC peripherals out there, but relatively low volume. I don't think that you'll start to see anything in that market that's anymore material until the fourth quarter of this year.

Brian Ruttenbur - Morgan Keegan - Analyst

Thank you very much. Great quarter.

Operator

Romit Shah, Lehman Brothers.

Serv Vadasai - Lehman Brothers - Analyst

This is [Serv Vadasai] for Lehman Brothers. Just a couple of questions. With respect to the ASPs, can you remind us what the ASPs -- average ASPs were last quarter, and any color on what they might be in this quarter?

Gary Larsen - AuthenTec, Inc. - CFO

The average ASP last quarter was about \$3.90. So we expect quarter-on-quarter probably something like 2% erosion.

Serv Vadasai - Lehman Brothers - Analyst

Just with respect to gross margins, in order to get to your longer-term target of 52% to 55%, what kind of revenue run rate are you looking for?

Gary Larsen - AuthenTec, Inc. - CFO

The revenue run rate that we're looking for our overall target model is 150 million per year.

Serv Vadasai - Lehman Brothers - Analyst

One last question. In regards to the solid quarter-to-quarter, is that pulling from the second half, or do you feel that -- I know the Street has your modeled at roughly 30% in the third quarter, and then 25% in the fourth quarter. Do you see those kind of levels achievable? Or was this quarter reflective of some pull-ins in the third quarter?

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Scott Moody - AuthenTec, Inc. - Chairman and CEO

I don't necessarily think it's pulling from the third quarter, just looking at it a slightly different way. What I do see is just an increase as customers are -- I think their forecasts, frankly, were a little bit light, particularly on the 2810, and we're seeing that. But I don't necessarily think it's a pull-in. Whatever kind of numbers that were out there for Q3 and Q4 probably -- and to be honest, I don't remember what those are right off the top of my head -- but are probably still right. The growth numbers might not be the same, by definition, because Q2 is going to be much higher than a number of analysts had in their models to start with. I think a lot of them -- a lot of the folks had something in the mid 15s, say, 15.5. So now we're looking at the midpoint of 17.5, and then of course Q3 and Q4. So -- but I don't think it's a pull-in (technical difficulty) Q3 at all.

Serv Vadasai - Lehman Brothers - Analyst

Do you think it's safe to still assume that (inaudible) possibly the 30% improvement Q-over-Q in the third quarter, or do you think that might need to be adjusted a little bit?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

I probably would adjust that. Again, I don't have these numbers in front of me, but remember (technical difficulty) the number that you're quoting is right, 30% growth from Q2 to Q3. That was when Q2 was at a level of 15.2. So, if you assumed Q3 is stable to where it was before -- and again, I don't know that number is, then the growth rate over 17.5 would be, obviously, less.

Serv Vadasai - Lehman Brothers - Analyst

Thank you.

Operator

Steve Smigie, Raymond James.

Steve Smigie - Raymond James - Analyst

I was hoping you could talk a little bit about EzValidation a little bit more. Will you have a GUI interface available sometime relatively soon for people to use? Is the point of this to make it so that people who are getting their PCs, it'll sort of automatically pop up and let them use it? I know a challenge you've been having a little bit is just making people really aware they've got the sensor there and they could be using it.

Scott Moody - AuthenTec, Inc. - Chairman and CEO

To some extent your answer is right on. What we're going to be providing is, of course, the graphical user interface. In terms of enrollment or day-to-day use, obviously, the application (technical difficulty) go along with that, the password replacement, the fast user switching, file and folder encryption, all of those kind of things. So now we'll do all that. You had mentioned soon; it really will be something we'll start demonstrating or demoing to customers in the third quarter.

Steve Smigie - Raymond James - Analyst

Is the plan to have that sort of automatically ship with your sensor on the PC?

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Scott Moody - AuthenTec, Inc. - Chairman and CEO

At the end of the day it's up to our customer. They can use our software, their own software, which some customers have, and/or a partner's software. So, our customers will have available all three choices. But for the first time, to your point, that choice will be available from AuthenTec.

Steve Smigie - Raymond James - Analyst

Can you say what the percent of revenue was in PC versus handset versus access control of revenue?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

It was pretty close to what we ended the last year. It was about 15 wireless, 5% access control, and the remainder PC.

Steve Smigie - Raymond James - Analyst

You picked up some very interesting stuff on the handset side. It sounds like it will be shipping on a product with Sprint. Is that one mostly at this point just, as you mentioned, for protection of data? And if that's the case, has Sprint or anybody talked to you about when they might be rolling out (inaudible) services?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

First off, it is focused -- as I expected, in Japan when we first were rolled out, it was really focused on protecting the information on the phone, so that for a business guy that might be e-mails; for a consumer it might be some teenage girl's pictures. So it really plays to both markets. Then it rolled in Japan into m-commerce as another value-added feature. I think that same thing is happening. ASUS introduced it focused on protecting the information on the phone. And again, in the Sprint case, or the HTC case, it's protecting the information on the asset.

With respect to m-commerce and/or our conversations with any mobile provider, we can't really go specifically into those. But I can say that we are talking to everyone out there, and it remains relatively optimistic that we will see relatively large uptick in our wireless revenues in 2009. Not saying that we have a design win, etcetera, etcetera, that would drive that volume at this point. But, based on discussions, I am more optimistic.

I've always joked with people -- never confuse interest with demand. But the fact of the matter is there are different levels of interest, and those interest levels go everywhere from coming to contractual agreements in terms of vendor requirements, to just more generic discussions. So, these discussions are going forward with a lot of different companies, both OEMs and service providers. So again, without claiming a design win that would drive that kind of volume that you're looking for, I am more and more optimistic each day that will happen in 2009.

Steve Smigie - Raymond James - Analyst

On the PC side, I think you said you're in -- on the notebook side you said you're in with eight of the nine largest. Would one of those nine be Apple? You're not on Apple; is that correct?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

That would be correct.

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Steve Smigie - Raymond James - Analyst

Any difference in ASP, handsets versus notebooks?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

It's still relatively minor. I don't think with the introduction of some new products later this year -- and again, I'll address those a little bit more in the second-quarter call. There's not that much of a difference right now, and you won't see any, I don't think, until next year.

Steve Smigie - Raymond James - Analyst

Last question. Could you say what your top five customers were as a percent of revenue?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

They were about 79% in Q1, and that's actually down from 85% in '07. So we are starting to see some of our concentration dissipate.

Steve Smigie - Raymond James - Analyst

Thanks a lot.

Scott Moody - AuthenTec, Inc. - Chairman and CEO

[That will] continue during the course of the year, actually.

Operator

(OPERATOR INSTRUCTIONS). Steve Dyer, Craig-Hallum.

Steve Dyer - Craig-Hallum - Analyst

Just kind of drilling down a little bit further in the upward revision for Q2, it sounds maybe like [Bora] is shipping in volume a month or two earlier than you initially thought. Is that fair?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Yes. It's shipping a little earlier than at least our customers were forecasting at some point. Luckily, Steve, we at times thought those forecasts were a little bit low. So, we did make some investments in inventory, so we'll be able to meet all of our customer requirements. But definitely a good part of that uptick is associated with, if you will, increased forecasts for the 2810.

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Steve Dyer - *Craig-Hallum - Analyst*

In talking to you guys, and after your Q4 call, it sounded like people were a little bit gun-shy, just looking out over the course of the year. It seems like visibility has just gotten better, and maybe people's outlooks were initially kind of conservative relative to how sales have held up.

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

First off, we're really not seeing too much of an impact of, if you will, what you read in the paper or see on the news every night. At least we're not seeing it. We tried to go into the year with some conservatism ourselves. And the bottom-line, really, is that again, while we shipped a lot of units in the last -- some 4 million units last quarter, it's still a very small part of the total available market out there. So we're really not impacted too much by overall demand for total laptops, if you will, or total cellphones. So we're not as seasonal, maybe, or as impacted by, let's say, a recession, by some others that may be on all PCs or all cellphones. So, our customers seem to be and continue to be positive about the market.

Steve Dyer - *Craig-Hallum - Analyst*

Have you seen any changes, really, in the take rate? Obviously, they continue, I think, to tick up a little bit, or is that too hard to tell sort of intra-quarter?

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

I'm sorry; I'm not sure I understood your question.

Steve Dyer - *Craig-Hallum - Analyst*

I think the overall take rate you had assumed would tick up as the year goes on to maybe 25% of all people taking one by the end of the year. Has that trended faster, slower than you expected?

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

Probably not faster than I expected -- parsing words here a little bit -- but maybe a little bit faster than the forecast we had gotten from our customers, i.e. that's why our Q2 numbers have gone up.

Steve Dyer - *Craig-Hallum - Analyst*

Just lastly, did you bring any headcount from EzValidation, or was that strictly software?

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

It was strictly software. We are working with some people that worked there on a contractual basis to help us integrate it into our own product. So that's some of the R&D expense that I mentioned earlier.

Steve Dyer - *Craig-Hallum - Analyst*

Thank you.

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Operator

Steve Smigie, Raymond James.

Steve Smigie - *Raymond James - Analyst*

Are you able to talk about any 10% customers in the quarter, who they were, and what they were as a percent of revenue?

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

We don't disclose that; only in the 10-K at the end of the year. To that point, and to the point I made earlier, you saw a slight decrease between '07 and Q1 with respect to the top five. And you will -- as our other customers ramp -- and I've mentioned a few times these new customers coming online, and now in eight of the top nine PC manufacturers, even those top five will continue to go down during the course of the year.

Steve Smigie - *Raymond James - Analyst*

Can you talk about how many notebook models you're actually shipping on, say, Q2, Q3 type timeframe, and [similarly], handsets?

Larry Ciaccia - *AuthenTec, Inc. - President*

I would say by Q3, once Montevina fully launches, that number's got to be 50 to 75 new models shipping across the customer base, at least.

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

We can get back on that number. That's a good question. I don't know that we've counted them all up.

Steve Smigie - *Raymond James - Analyst*

The last question was just -- can you talk about penetration into the GPS devices, and any other sort of peripheral device penetration you can talk about, please?

Scott Moody - *AuthenTec, Inc. - Chairman and CEO*

GPS in terms -- okay. We didn't really talk too much about that, or actually at all, during the call. As I said before, our real focus is in the PC and the cellphone. We generally announce usually some smaller volume opportunities associated with access control, GPS devices, and other consumer electronics. So that's still -- Gary had talked about the 5% -- that generally is still a very small piece of our business. Some of the work that we're doing in new products will allow us to have new products that are better suited toward some of those end markets, i.e. access control, which I think is a huge market, as well as GPS PND devices. So, it's an area that I can say that we're not really focused on. We still do continue to get design wins, but I don't think it'll start to become more material until the '09 timeframe.

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Steve Smigie - Raymond James - Analyst

As sort of a follow-up on that, I think you guys have, maybe, a contract with the US government for a number of handheld devices for the census. I'm curious what year that ramps, and if that's -- if you're building that in '09 for like a 2010 census, or something like that. Is that part of your assumption about greater -- being on more handset devices in 2009, or is that separate?

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Most of those will be built in '08 and '09. The volume now -- frankly, to be honest -- I guess we were excited about it when we first had it. But as a percent of our total volume, it's now getting smaller and smaller. But that's not what I'm talking about. When I'm talking '09, I'm talking about cellphones for real people.

Steve Smigie - Raymond James - Analyst

Thanks a lot.

Scott Moody - AuthenTec, Inc. - Chairman and CEO

With all due respect for census workers.

Operator

There are no more questions at this time. I'll turn the call back over to Scott Moody for closing remarks.

Scott Moody - AuthenTec, Inc. - Chairman and CEO

Thanks, everyone, for again taking the time to join us today. Before we conclude the call, I'd like to take a moment to thank Kent Buchanan for his contributions to our Board of Directors, and welcome onboard Chris Fedde. Chris is a well-respected leader in the information security industry, and we believe he is a very positive addition to our Board. He brings a great depth of security and management experience, and we look forward to his insights as we build upon our leadership position and address the exciting growth opportunities that we have ahead.

As a reminder for everybody, we are scheduled to host our 2007 annual stockholder meeting on May 9, just about two weeks from now. Additionally, we will participate in a number of financial conferences in the coming months, including those being hosted by Cowen, Craig-Hallum, JMP Securities, Lehman Brothers, Morgan Keegan, and Oppenheimer. Please visit our Web site for updates on these and other exciting upcoming events.

Thanks again, and have a great evening, everybody. JD, you can disconnect now. Thank you.

Operator

Thank you for your participation in today's conference, this concludes our presentation and you may now disconnect.

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