OVERVIEW:

Co. reported 3Q20 revenue of $1.46b, and adjusted EPS (excluding special items) of $1.36. Expects 4Q20 revenue to be $1.44b, plus or minus $70m, and adjusted EPS to be $1.32, plus or minus $0.10.
CORPORATE PARTICIPANTS

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Prashanth Mahendra-Rajah  Analog Devices, Inc. - Senior VP of Finance & CFO
Vincent T. Roche  Analog Devices, Inc. - President, CEO & Director

CONFERENCE CALL PARTICIPANTS

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PRESENTATION

Operator

Good morning, and welcome to the Analog Devices Third Quarter Fiscal Year 2020 Earnings Conference Call, which is being audio webcast via telephone and over the web.

I’d now like to introduce your host for today’s call, Mr. Michael Lucarelli, Senior Director of Investor Relations. Sir, the floor is yours.

Michael C. Lucarelli  Analog Devices, Inc. - Senior Director of IR

Thank you, Cheryl, and good morning, everybody. Thanks for joining our third quarter fiscal 2020 conference call. With me on the call today are ADI’s CEO, Vincent Roche; and ADI’s CFO, Prashanth Mahendra-Rajah. For anyone who missed the release, you can find relating financial schedules at investor.analog.com.

Now on to the disclosures. The information we’re about to discuss includes forward-looking statements including statements relating to our objectives, outlook and the proposed Maxim transaction. These forward-looking statements are subject to certain risks and uncertainties, as further described in our earnings release, our most recent 10-Q and other periodic reports and materials filed with the SEC. Actual results could differ materially from the forward-looking information as these statements reflect our expectations only as of the date of this call, and we undertake no obligation to update these statements, except as required by law.

Our comments today will also include non-GAAP financial measures, which exclude special items. Comparing our results to historical performance, special items are also excluded from prior periods. Reconciliations of these non-GAAP measures to their most directly comparable GAAP measures and additional information about our non-GAAP measures are included in today’s earnings release.

And with that, I’ll turn it over to ADI’s CEO, Vincent Roche. Vince?
Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

Thanks very much, Mike, and good morning to you all. I hope that you and your families are healthy and safe at this time.

So I’ll start my remarks today on our quarterly results and the current operating environment before providing you with an update on our priorities. This includes additional insight, of course, into our recently announced acquisition of Maxim Integrated.

ADI executed exceptionally well in the third quarter despite the highly uncertain environment. Demand was resilient, surpassing our expectations, leading to stronger-than-expected results. We saw continued strength in communications across both wireless and wireline applications, health care saw record demand and other parts of our industrial portfolio such as instrumentation tests also performed well. Unsurprisingly, the main area of weakness was automotive, driven by global factory shutdowns and lower vehicle sales.

Turning to supply. We’re operating at normal capacity, which helped us clear backlog and bring supply and demand into a better balance. Our team delivered third quarter results above the midpoint of our revised guide with revenue at $1.46 billion and EPS at $1.36. B2B revenue was flat year-over-year and increased 11% sequentially, and both gross and operating margins returned within the range of our financial model at 70% and 42%, respectively. We also generated $1.8 billion of free cash flow or 33% of revenue over the trailing 12 months. This continues to place ADI in the top 10% of the S&P 500. These results further underscore the strength and flexibility of our business model against any economic backdrop, and I’m proud of how the ADI team continues to deliver for our customers.

Now I’ll turn to an update on our strategic priorities. We’re focused on spending our capital efficiently, and the first call is funding new product development. During the quarter, we invested approximately $260 million in R&D, with more than 95% targeted at the most attractive B2B opportunities. This continued reinvestment in our business is leading to excellent customer engagements, and let me provide you now with a couple of examples.

In our communications business, we announced the collaboration with Intel to create a flexible radio platform that will enable customers to scale their 5G networks more quickly and more economically. The high-performance ORAN compliance solution leverages our market-leading software-defined transceiver technologies. This positions ADI to expand our market leadership.

In automotive, our new road noise canceling solution is gaining traction. Since announcing our initial win with Hyundai in February, we’ve added 5 more customers, including the North American leader in electric vehicles. This innovative solution reduces the car weights by almost 100 pounds and energy requirements by about 3%, while potentially doubling our content opportunity per vehicle. We’re seeing great design momentum across our diversified industrial market also. For example, in factory automation, customers are rethinking supply chains to make them more flexible with faster response times. And to quicken the pace of adoption, we have formed an alliance of partners to develop an open source architecture. I’m excited to announce a Fortune 500 health care customer is teaming with ADI to help upgrade its manufacturing capabilities using more connected robotics, thereby doubling our addressable market.

And in space, we have design wins going to production this year with traditional aerospace companies and new emerging disruptors that enable the proliferation of next-generation communication satellites. These satellites continuously change their position to earth and require space grade phased array and beam forming technology to create an uninterrupted connection. And we’re using this strong position in RF to attach power technologies, thereby increasing our addressable market by 1/3.

ADI also remains committed to strong shareholder returns. This quarter, we returned approximately $230 million through dividends. Recall that we paused share buybacks due to the pandemic. This has helped us further solidify our balance sheet with a cash balance of more than $1 billion.

At this point, I’d be remiss to not discuss our M&A strategy in the light of the Maxim acquisition. ADI selectively uses M&A to expand both our scale and our scope in order to better address the future needs of our customers and deliver sustainable, profitable growth. And while cost synergies are an important element in evaluating any acquisition, from our perspective, the most compelling benefits come from combining technology portfolios to capture new addressable markets and drive on term revenue synergies. This revenue takes time to realize, given the nature of the Analog business, but our products deliver recurring revenue streams and cash flow for decades. Therefore, we strive to achieve our return objective
within approximately 5 years. This time frame allows us to not only achieve the stated cost savings but also begin to capture the early revenue synergies. And I think the acquisition of LTC illustrates the benefits of our strategy.

Our top priorities there were harmonizing the 2 organizations to create an entity that is better than the sum of its parts. To that end, I'm proud to say that we've retained and invested in LTC's exceptional engineering talent. Together, we've created an exciting road map of high-performance analog and power solutions combined. We're exceeding our original $150 million cost synergy target, and we're on track to realize the next $100 million exiting fiscal '21.

And from a revenue perspective, we've more than doubled our pipeline value, and we have over $500 million of lifetime revenue coming to market this year, increasing our confidence in doubling LTC's historical growth rate. With LTC complete, we pursued the acquisition of Maxim to strengthen our leadership in the analog industry, better positioning ADI to capitalize on secular growth trends.

Over the last 5 years, Maxim has shifted its business strategy to focus on B2B markets while enhancing profitability. As a result, Maxim has increased its B2B revenue mix to approximately 80% of total from 55%, expanded its gross margins by more than 500 basis points and increased its free cash flow margin by over 600 basis points during this period. Combined, we're confident we will continue to improve Maxim's performance. This will be driven by our cadre of engineering talent, complementary technologies and breadth of market applications that I'd like to expand on a little here. The cultures of ADI and Maxim are very aligned. Both companies share a commitment to innovation and engineering excellence. With a combined team of more than 10,000 engineers and $1.5 billion of annual R&D investment, we will continue to be the destination for the world's best analog talent. And with 3x the field technical resources, we'll be better positioned to uncover cross-selling opportunities and serve existing and new customers who have an increased need for application and design support.

In the area of power management, Maxim's application-focused offerings are highly complementary with ADI's more general purpose or catalog power portfolio. Together, we will have a more comprehensive power portfolio with approximately $2 billion of revenue. This is particularly important as power is the largest and fastest-growing Analog subsegment and with increasing design complexity and the need for better efficiency, the system power challenges that our customers must overcome continue to rise and rise.

In automotive, Maxim has one of the premier franchisees, increasing revenue at a mid-teens rate over the last 5 years. They're a leader in high-speed data connectivity for cameras, radars and processors with serial link technology while ADI is a leader in audio solutions with our A2B platform, and both companies are well positioned in vehicle electrification, enabling us to better address automakers' EV requirements, which continuously evolve. Together, we will capture more of the increasing system content per vehicle and enable a better experience for the consumer.

Taking a step back, the combined company will have unique positioning with 85% exposure to highly profitable long life B2B markets. Maxim's strengths in the automotive and data center markets will complement ADI's strengths across the industrial, communications and digital health care markets. Additionally, the combined company will have increased financial strength. We expect the combination to be accretive to adjusted EPS within 18 months post close, with targeted cost synergies of $275 million by the end of the second year. We also expect to maintain an industry-leading financial profile. As always, we are committed to generating robust free cash flow, and our goal is to reach the high end of our margin range of 40%.

With our lower leverage ratio at close, we'll also have the opportunity to deliver enhanced cash returns to our shareholders. And I believe that together, we can grow revenue at mid-single digits due to our alignment with important secular growth trends, such as Industry 4.0, digital health care, next-generation communication systems and vehicle electrification as examples.

So in closing, we're seeing promising evidence that a broad-based recovery is underway. However, we recognize that the recovery is highly dependent on the future impacts of the pandemic. We've used this unprecedented time to better align our organization and investments into the most important areas. We believe we'll emerge stronger and are better positioned to drive profitable growth. And as I've shared today, we're very excited about the combination with Maxim, which will drive the next wave of disruptive innovation and deliver significant benefits for all stakeholders.

And with that, I'll turn it over to Prashanth to go through the financial details and outlook.
Thank you, Vince. Let me add my welcome to our third quarter earnings call. As a reminder, my comments, with the exception of revenue and nonop expenses will be on an adjusted basis, which excludes special items outlined in today’s press release.

When we provided quarterly guidance in May, we were facing tremendous uncertainty, just returning to normal capacity levels and experiencing volatile demand patterns across end markets. As we progressed through the quarter, we saw stronger-than-anticipated demand that resulted in less cancellations and higher-than-anticipated backlog conversion. With that as context, our results came in above the midpoint of our revised outlook, with revenue of $1.46 billion, operating margins over 42% and EPS of $1.36.

Let me start now with the end market color. Our B2B revenue was up 11% sequentially and flat year-over-year as strength across industrial and communications offset a sharp decline in automotive. Industrial, which represented 53% of revenue during the quarter, finished up 3% year-over-year. We experienced robust growth in health care, instrumentation test and energy applications. This strength was moderated by weaker trends across our broad market and automation businesses. Communications, which accounted for 25% of revenue, achieved a record quarter. Revenue finished up 14% year-over-year, driven by double-digit increases across both wireless and wireline. This strength came from our leadership position in 5G wireless systems and our solid position in optical connectivity used in carrier networks and data centers.

Automotive, which represented 11% of revenue, decreased 29% year-over-year, with all applications declining due to global factory shutdowns and lower vehicle sales. And while no business is immune to the current environment, our BMS and A2B solutions fared quite well. BMS revenue increased sequentially and was down just modestly year-over-year due to our strong penetration across the ecosystem and increasing consumer preference for electric vehicles. And given the continued adoption of our A2B audio platform, A2B revenue has increased over 70% year-to-date despite lower vehicle sales.

Consumer, which also represented 11% of revenue, was down 13% year-over-year. Relatively flat portable revenue was more than offset by double-digit declines in prosumer due to the pandemic-related softness. We continue to expect 2020 to be the bottom for our consumer business.

In addition to the end market commentary, we wanted to provide some insight by geography as we believe it is helpful to investors in this current climate. Most geographies declined year-over-year. We saw double-digit declines in Europe and Japan, while the decline in North America was less pronounced. The rest of Asia increased and China increased double digits year-over-year, largely driven by the robust growth in communications, given our solid position as well as strength in industrial.

Now moving on to the P&L. Gross margins returned to our model at approximately 70%, down modestly year-over-year from lower fab utilization. We’ve accelerated the planned LTC factory closings and have started to realize these benefits in the third quarter. We expect additional savings in the fourth quarter, and we’ll exit fiscal 2020 with nearly half of the $100 million savings in our run rate.

OpEx was $402 million, up 3% sequentially, yet down 8% year-over-year. We maintained a focus on controlling expenses, which included a 1-week global shutdown during the quarter. OP margins finished at 42.3%, the highest level since the third quarter of 2018. Nonop expenses were $46 million, down $3 million sequentially and more than $10 million year-over-year, driven by lower levels of debt and lower interest rates. Our tax rate for the quarter was approximately 11.5%, and all told, third quarter EPS came in at $1.36.

Now moving on to the balance sheet. We finished the quarter with over $1 billion of cash and about $5.6 billion in total debt. This resulted in a leverage ratio of 1.8x on a trailing 12-month basis. Inventory dollars increased $22 million sequentially, but declined year-over-year. Days of inventory remained basically unchanged at 125. Channel inventory remains lean and is below the low end of our 7- to 8-week target range. Cash from operations was $557 million, and CapEx was only $21 million as we proactively reduced CapEx spend in the current environment. This resulted in free cash flow of $536 million, up 8% year-over-year.

Our long-term CapEx target remains the same at approximately 4% of sales. And as Vince mentioned, on a trailing 12, we generated $1.8 billion of free cash flow. Over the same period, we’ve returned around $860 million to shareholders via dividends and additional $410 million via buybacks. This equates to a free cash flow return after debt reduction of nearly 80%, which is below our 100% return target as we paused our buyback program.
Now I’d like to expand on Vince’s commentary and discuss how our combination with Maxim will further enhance our financial profile. At deal announcement, ADI and Maxim had a combined pro forma leverage ratio of 1.2x, which will decrease between today and deal close. The main driver being Maxim, which is in cash accumulation phase. They will pay one more quarterly dividend before suspending it for 4 quarters, and their buyback is on pause. Said another way, all the cash generation for the 12 months beginning in the second quarter of their fiscal 2021 will be added to the balance sheet. And for reference, over a trailing 12-month period, Maxim generated $730 million of free cash flow. ADI plans to continue to pay and grow our dividend. And as I mentioned earlier, our buyback program was paused during the height of COVID-19 and will remain on hold for now. When circumstances permit, our intention is to reinstate the program, which has nearly $2 billion remaining under authorization.

Also, as we previously outlined, we plan on repaying $300 million to $500 million of debt in 2020. This quarter, we intend to honor that commitment by retiring our $450 million January 2021 note. This will save $13 million of annual interest expense. We believe the stronger balance sheet provides us with flexibility to improve on our 100% free cash flow return and increase shareholder value over the long term through a combination of reinvestment in the business, continued dividend increases, greater and more consistent buybacks and entire aggregated acquisitions.

And now on to the fourth quarter outlook. Fourth quarter revenue is expected to be $1.44 billion, plus or minus $70 million. This outlook considers our current understanding of the impact related to the recent legislation enacted on Monday. It’s important to remember that this customer’s revenue has been significantly reduced over the last year to a low single-digit percent of total sales. We anticipate B2B revenue to decrease modestly for the third quarter. Strong growth in automotive as well as growth in industrial is more than offset by a decline in communications. This decline in communications is related to a slowdown of deployment as we forecasted in the last call and the limited impact from the recent legislation.

On a year-over-year basis, B2B revenue is forecasted to increase low to mid-single digits. We anticipate our operating margin to be approximately 42%, plus or minus 100 bps. We’re planning for the tax rate to be between 12% and 13%. And based on these inputs, adjusted EPS is expected to be $1.32, plus or minus $0.10.

So now I’ll close my remarks by stating that third quarter proved better than our expectations, largely driven by our conservative planning and aggressive execution. As we move through the integration planning process with Maxim, we remain fully committed to driving sustainable growth through cutting-edge innovation and a focus on our customer success.

I’m going to pass it back to Mike now to start our Q&A.

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**John William Pitzer** - *Crédit Suisse AG, Research Division - MD, Global Technology Strategist and Global Technology Sector Head*

Congratulations on the solid results. I just want to follow up on the recent Department of Commerce ruling. Am I to read into that, that you’ve embedded sort of 0 revenue coming from that one customer. And just given how strong China has been as a region, Vince, are you at all worried that there’s been pull forward? Or is that just a natural offshoot of that’s the geo where a lot of 5G deployment is happening?
Yes. Good question. Thanks, John. So we have pretty much discounted our top — what used to be our #1 customer in China to pretty much 0 in our long-term planning thinking. It has been a low single-digit customer over the past few quarters. So we have factored also, by the way, the latest regulatory upheaval into our numbers. So at this point in time, the largest 5G customer there in China that used to be is no longer part of the planning or the — either in the short term or the long term. I’d say as well what we’ve seen in terms of the strength in China that Prashanth referred to is really — is the fact that China was the first to go into the pandemic. First to come out. It’s an economy that’s growing very, very rapidly and has been up for several years now. So I think there’s been a very good balance, I believe, between supply and demand across all the sectors. I mean, we’ve seen growth in all markets with the exception of automotive. So I think what we’re seeing in terms of the strength in China is more about the match between the strength in our business and the economy than anything else.

Prashanth Mahendra-Rajah - Analog Devices, Inc. - Senior VP of Finance & CFO

Yes. Vivek, we’re going to split that. And let me take the first part of it. So to clarify, third quarter, we believe, did not see any pull-ins from Huawei. Fourth quarter outlook reflects the guidance we gave you, reflects the full impact for us of the Department of Commerce implications from earlier this week. So all of that is now baked in. In terms of the amount of decline that we are expecting in the communications business, this is a lumpy business. We’ve said that consistently. It’s growth measured in years and lumpy by quarter. We don’t give forward guidance on an end market basis by quarter anymore. We haven’t done that for a little bit of time. So we don’t want to start that now. But take it to understand that the movement in the communications business from third to fourth quarter was very much in normal operating lumpiness of the communications business is not exacerbated in any way by what happened on Monday or Tuesday’s announcement. And now I’ll pass back to Vince for your more challenging strategic question.

Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

Yes. So Vivek, I’ve been in this business a long, long time actually since 2 -- the inception of 2G, all those years ago back in the late 80s, early 90s and what I can tell you is that the patterns we’re seeing in 5G are no different to what we’ve seen in 2G, 3G or 4G. And if you look at 4G, specifically, just to give you a bit of perspective here, we grew, albeit a very, very lumpy business, as we always say, but we grew over the entire era of its build out by mid-single digits. We had more content than we had in the prior generations. We took more share. And we’re actually even better positioned in 5G because it’s a more complex radio problem fundamentally. We have a lot more technology to put into the space from microwave and RF, right down to the mixed signal. And now we’re attaching power also. So another factor that we’re beginning to see the emergence of. So today, 5G has really been about giving more bandwidth to the consumer, more throughput to the consumer. The future is about, I think, B2B more so than the consumer. And we’re beginning to see, I believe, the early adoption of 5G in the factory automation area. In fact, I have verified that with some of our industrial automation customers as well. So 3Q is definitely likely the highest revenue quarter this year, but there are lots of drivers at the secular level and the company level to keep us in good stead for growth over the long term.
Prashanth Mahendra-Rajah - Analog Devices, Inc. - Senior VP of Finance & CFO

Vivek, I’ll also add one thing to try to avoid the plethora of Huawei questions that I can tell are winding up. So we’ve given you a lot of context around that customer. We said they’re a mid-single-digit customer. The legislation put in place was we can ship for about half this quarter. So they’ll be lower this quarter than normal. And going forward, after that, our expectation should be, it goes to 0. So our outlook for 1Q would be down for communications because of that.

Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

The last couple of quarters have actually been low single digits. And as we’ve said now a couple of times, we are no longer factoring Huawei into our numbers.

Operator

Your next question comes from Tore Svanberg from Stifel.

Tore Egil Svanberg - Stifel, Nicolaus & Company, Incorporated, Research Division - MD

Congratulations, especially during these tough times. I had a question on sort of bookings linearity and backlog. I know last quarter, you obviously entered the quarter with pretty high backlog, and you were sort of discounting that. Are we sort of back to a more normal backlog level now for either you, Vince or Prashanth?

Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

Yes. So let’s -- maybe let me answer that by talking about the order patterns. So we saw strong May, some slowdown in June, which was expected. July was sort of a stable month-over-month, and that was better than we expected. Through August, relatively stable, and August is typically a lower seasonal month. So we have lower backlog in third quarter as we enter the quarter and a good balance between supply and demand. This quarter, as we look forward to our guide, we’ve got stronger coverage from backlog than we typically do. And if we converted -- if you recall, in the third quarter, we said that we had about $50 million of products that we couldn’t ship in the second quarter that we caught up with in the third quarter. That actually came in a little bit higher because we had fewer cancellations. So we probably had maybe $100 million all in of revenue in third quarter that really related to backlog from second quarter. So I think that through fourth quarter, we’re going to get supply and demand back in balance. Backlog has come down and will be more back to normal levels. As we have guided for the fourth quarter, we’ve taken into consideration the stronger backlog, but we’ve also taken into consideration that at an ADI level, our book-to-bill for the fourth quarter is now below parity.

Operator

And our next question comes from Ambrish Srivastava from BMO.

Ambrish Srivastava - BMO Capital Markets Equity Research - MD of Semiconductor Research & Senior Research Analyst

Vince, I wanted to pivot back to the strategic priorities, and thanks for articulating everything in context of the latest acquisition. This is a question I get a lot and I scratch my head on this, too, because of you bought Linear and then Maxim also on the power side. So the question -- and you did provide us with some details on Linear. A couple of questions tied to that. With respect to Hittite, you have given us the growth in Hittite versus what it used to grow and how you have been able to grow that versus prior to acquisition. So the question is, how has Linear done with respect to the core business? And I don’t expect you to answer it every quarter, but I think it’s a pertinent question in light of the Maxim acquisition. So kind of 2-part question. One, how has Linear done since you bought it?
And then this was the year that we were supposed to get revenue synergy. Now this is a very topsy-turvy year, so we all understand that. But should we expect revenue synergies to start showing up from Linear with all the efforts that have been going on?

Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

Yes. Thanks, Ambrish. So we have already seen the benefit of LTC in our growth numbers. I would say, at this point in time, we've put more than 100 basis points of growth on the base Linear growth rate to date. We have -- I think the greatest indicator for what things are likely to be in the future, I've said before that I believe that we can double the growth rate of LT over the longer term, and just given the markets in which we play and the design cycles, the product cycles, it takes 3 years minimum, and then you begin to see the real benefits, I think, after 5 years. So we're over 100 basis points of additive growth right now.

And if you look at our pipeline, I referred to it in the prepared remarks, we have got a design win pipeline of over $0.5 billion thus far. We have seen wins in communications, both on the wireless side as well as the data center side. Infotainment in automotive, infotainment, radar and, of course, BMS. We're seeing tremendous uptake for some of our more integrated products in areas like instrumentation tests using our micromodule technologies. And I'm quite pleased, given the turmoil in the global markets right now that we continue to see good traction on the design win rates, and I'm confident that we can get from 3% to 4% growth rates in the past to more -- a higher -- mid- to high single-digit level in the future and do it sustainably. So I think we have emerging evidence that we're on good track to do that.

Operator

And our next question comes from Toshiya Hari from Goldman Sachs.

Toshiya Hari - Goldman Sachs Group, Inc., Research Division - MD

Congrats on the strong results. Vince, I had a question on your automotive business. Curious, how are you thinking about the shape of the recovery in automotive over the next couple of quarters? Obviously, you've been impacted by your customer factory shutdowns and the demand situation post COVID. But curious, are you thinking it could be more of a V-shaped recovery, could it be more U-shaped? Any thoughts there would be super helpful. And if you can speak to your key applications within automotive. You gave great color on the July quarter, but if you can talk about BMS, A2B, some of the key growth drivers for October and beyond, that would be helpful.

Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

Okay. Thanks, Toshi. So yes, we're seeing a recovery in the market. Actually, our book-to-bill was greater than unity across all regions over the last month or so. And we believe that our third quarter represents the bottom of the cycle for us. So I think the near-term recovery and the demand that we're seeing relates to factories coming back online and also a slow improvement in SAAR. So I think the shape of the recovery really depends on the demand -- the end demand for cars and how SAAR actually grows. And we'll -- that will need -- we'll need to see continued vehicle demand to get back to the pre-COVID level. So it's not there yet. So factories are coming back online. Demand is slowly increasing. So hard to call the exact shape, but somewhere between a V and a U, I guess, or maybe already a U, and we're seeing the upsurge.

I would say electric vehicles in general have held up better in this market. As we said in the prepared remarks, there's a strong consumer preference for electric vehicles. It's the fastest-growing sector at this point in time. And we're continuing to gain share in the market. We've seen growth quarter-on-quarter in that space. And we're also very pleased with our performance. A2B actually grew about, I think it was 70% year-to-date. So the adoption, the design wins that we had gotten last year across most of the OEMs beginning to turn into serious revenue now. And on top of that, we're also overlaying this road noise cancellation technology that uses our digital signal processors, algorithmic technology and different analog support technologies on the input and output there. So those are the major areas. And I think, as I said, I believe we're in a slow recovery phase in automotive. And I think, in general, very hard to call the next quarter, the next 2 quarters, but my sense is '21 will be a growth year for the
industry and a growth year for ADI. And -- I mean that's how I viewed at this point in time. So we're seeing a gentle recovery in general across all our market spaces.

**Operator**

Our next question comes from Stacy Rasgon from Bernstein Research.

**Stacy Aaron Rasgon** - Sanford C. Bernstein & Co., LLC., Research Division - Senior Analyst

I'm a little bit confused. I know you've been saying we're entering into recovery, but how do I square that with a book-to-bill going forward that is less than 1? I mean is it just comm? Like how should I be thinking about book-to-bill by segment? And what does that imply for, like, the longer-term trajectory?

**Prashanth Mahendra-Rajah** - Analog Devices, Inc. - Senior VP of Finance & CFO

Yes. Great question, Stacy. The -- so I would say that certainly, the communications business is a piece of that. And I would also say that we -- when we look back at the demand activity over the last quarter or 2, we feel very good that, that was driven by very kind of real demand based on conversations with customers. But there was probably some level of inventory building that was going on in there given that the inventory levels at our end customers were so low. Coming into this pandemic, they had taken -- end customers really at the industrial level, had taken their inventory levels down pretty significantly in 2019. And then the pandemic hit. And so I think some of the strength that the industry is seeing now has a little bit of that renormalizing that. So as we kind of look forward into fourth quarter, there is a lot of opportunity for us. And I think that the new order activity remains good, overdues are declining. So it’s -- I think we'll have to let another quarter or 2 roll out. We don’t have enough visibility, I think, to tell you what the future portends. But we’re not seeing a sharp decline in order activity, but it is below 1.

**Stacy Aaron Rasgon** - Sanford C. Bernstein & Co., LLC., Research Division - Senior Analyst

Got it. But just to clarify -- I’m sorry?

**Michael C. Lucarelli** - Analog Devices, Inc. - Senior Director of IR

Stacy, we are guiding down sequentially. Our book-to-bill is slightly below 1. So it does go in tandem to what we’re saying. And you're right to think about the tele market. Comm is much below 1, auto is a bit above 1, industrials around 1. So it all lines up to what the guidance we gave and the range we have given.

**Operator**

And our next question comes from C.J. Muse, Evercore.

**Christopher James Muse** - Evercore ISI Institutional Equities, Research Division - Senior MD, Head of Global Semiconductor Research & Senior Equity Research Analyst

I guess, a cycle question. And if I look at your S-4 and you projected revenues in there for fiscal ’20, that roughly $170 million below what you’re actually looking to accomplish here. And so curious, versus what you put there in the S-4, what led to the upside there? And is that something that we should think can continue beyond the October quarter?
Prashanth Mahendra-Rajah - Analog Devices, Inc. - Senior VP of Finance & CFO

C.J., that was really around the timing of when we’re having those conversations. If you look back at the timing of when we were in those, the world looked very different to us. I think it looked differently to everyone back at that period when the pandemic looked like it was ranging at a pretty sharp pace across the globe. So our S-4 probably reflected more of the uncertainty that we had out there that has since been -- more clarity has been brought.

Michael C. Lucarelli - Analog Devices, Inc. - Senior Director of IR

We'll go to our last question, please.

Operator

Our last question comes from Craig Hettenbach from Morgan Stanley.

Craig Matthew Hettenbach - Morgan Stanley, Research Division - VP

Just a question for Vince on the industrial market and really about the composition maybe in the next couple of quarters. So certainly, medical has been strong, instrumentation. The more cyclically oriented factory automation has been weak. Do you expect any reversal in some of that kind of by subsegment performance as we move forward from here and the macro recovers?

Vincent T. Roche - Analog Devices, Inc. - President, CEO & Director

Yes. Well, we’ve seen -- I mean, energy is a couple of hundred million dollar business a year for ADI. That’s been doing well, and we’re getting a lot of new design wins. In renewables area, we’ve seen strong demand in our test business, supporting 5G build out and data centers in particular. And we’re seeing a little more weakness in instrumentation in areas that relate more to CapEx. If you look at aerospace and defense, which is an important part of our industrial story, obviously, there’s weakness in avionics that won’t be a huge surprise. But that’s a relatively small portion. The biggest portion of our aerospace and defense business is defense, and that business is holding up well as well as the space business, which continues to grow nicely.

I would say as well, automation is holding better than we had thought. But what really excites us there is the future as our customers rethink supply chains, onshoring, reshoring, and we’re going to see more and more automation used in general across the globe. So I think that unpacks the story for you. So I think we’re seeing strength pretty much across all the sectors or recovery across all the sectors in industrial right now.

Michael C. Lucarelli - Analog Devices, Inc. - Senior Director of IR

Thanks so much, Craig. And thanks, everyone, for joining us this morning. A copy of the transcript will be available on our website, and all reconciliations and additional information can also be found there. Thanks for joining us and your continued interest in Analog Devices.

Operator

This concludes today's Analog Devices conference call. You may now disconnect.
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