Cabot Microelectronics Corporation
First Fiscal Quarter 2012 Conference Call Script
January 26, 2012

Good morning. With me today are Bill Noglows, Chairman and CEO, and Bill Johnson, Chief Financial Officer.

This morning we reported results for our first quarter of fiscal year 2012, which ended December 31. A copy of our earnings release is available in the investor relations section of our website, cabotcmp.com, or by calling our investor relations office at 630-499-2600. A webcast of today's conference call and the script of this morning's formal comments will also be available on our website.

Please remember that our discussions today may include "forward-looking statements" that involve a number of risks, uncertainties and other factors that could cause actual results to differ materially from these forward-looking statements. These risk factors are discussed in our SEC filings, including our report filed on Form 10-K for the fiscal year ended September 30, 2011. We assume no obligation to update any of this forward-looking information.

I will now turn the call over to Bill Noglows.

Thanks, Trisha. Good morning, everyone, and thanks for joining us.

This morning we announced solid financial results for our first fiscal quarter of 2012. During the quarter, we achieved revenue of $102.1 million, gross profit margin of 48.3 percent of revenue, and earnings per share of 45 cents, which includes an adverse effect of approximately 7 cents from professional fees related to our previously announced proposed leveraged recapitalization and special cash dividend. Our financial performance this quarter was impacted by continued softness within the industry. We believe this is consistent with our characterization of industry and business conditions when we announced results for our fourth quarter of fiscal 2011 last October, and also during our conference call to announce our new capital management initiative on December 13. The December quarter is typically a seasonally soft quarter for us; however, our results reflect somewhat greater softness than typical seasonality. While we expect current industry conditions to persist in the near term, we are managing our business activities and discretionary costs accordingly, as reflected by our solid financial performance this quarter.

Let me start this morning with our view on the current industry environment. Some industry analysts indicate that overall holiday spending on electronics was in line with expectations. Demand for smart phones and tablets appears to have been relatively strong, but orders for PCs, TVs and gaming devices appear to have been weaker than anticipated, with the exception of emerging markets such as China, India and Africa. As a result, DRAM inventory levels appear to be higher than normal. However, on a positive note, industry reports indicate that IC inventories, excluding DRAM, have returned to normal levels.

Some industry analysts predict that the soft industry demand environment will continue through the March quarter; however, they are also generally forecasting stronger IC unit growth in calendar 2012 when compared to 2011. This would suggest some anticipated strengthening in demand during the calendar year. Remember that demand for our CMP consumables products is ultimately driven by demand for end-use products such as smart phones, tablets and other electronic devices. As a result, semiconductor unit growth, or wafer starts, is the biggest driver of our revenue. According to IC Insights and World Semiconductor Trade Statistics, growth forecasts for calendar 2012 range from 3 to 7 percent on a unit basis. This is an increase from their 2 to 3 percent unit growth estimates for calendar 2011. Additionally, it appears that the hard disk drive industry is beginning to recover from the impact of the flooding in Thailand in late 2011.

Based on what we are seeing in the market, we are planning for continued softness in industry demand through the March quarter, and some strengthening in the second half of our fiscal year. However, we acknowledge that we have very limited visibility into near term demand, and so we continue to remain cautious.

Turning now to company-related matters, we announced a new capital management initiative this past December that we expect will provide additional value to our shareholders. We are very pleased with the positive reaction to this announcement. The initiative includes a proposed leveraged recapitalization of our company with a special cash dividend of $15 per share, or approximately $345 million in aggregate, and an increase in authority under our share repurchase program to $150 million. We expect to declare and pay the proposed special cash dividend during our second fiscal quarter of 2012, contingent upon arranging financing that is acceptable to us. To reiterate what we discussed on the December call, we believe this new capital management initiative represents a more efficient approach to capital allocation for our company that will provide significant value to our shareholders.

Although this capital management initiative is a departure from our historical capital allocation approach, our long-term growth and investment strategies remain unchanged. Our primary strategies continue to be strengthening and growing our core CMP consumables business and continuing to advance our Engineered Surface Finishes business. We intend to continue to execute our business strategies and manage our company for profitable growth. We will continue to invest in organic growth, pursue growth through acquisitions, and also consider opportunities to provide additional value to shareholders on an ongoing basis. Bill Johnson will provide more on our proposed leveraged recapitalization later in the call.

Turning to our core CMP consumables business, we continue our efforts to collaborate with our customers as a trusted industry partner through new product development and joint development programs. As I have discussed in the past, periods of industry softness sometimes provide greater opportunity for us to work more closely with our customers to evaluate new products on their tools, which may be underutilized during these times. Our technical staffs around the world are currently very busy, with a high level of interactions with customers on a wide range of potential future business opportunities. More specifically, during the quarter, our collaborative efforts and the investments we have made in high quality, high performing new products were rewarded with customer adoptions of our slurry products for a new Copper application and a new Data Storage application.

We are also leveraging our customer collaboration and investments in CMP polishing pads to earn additional business in our CMP Pad business. During the quarter, a customer who previously selected our next generation D200 pad for an advanced node Tungsten buff application also selected our D200 pad for an advanced node Shallow Trench Isolation buff application. In addition, a second existing customer adopted our D200 pad for an advanced node Aluminum application, while also expanding its utilization of our D100 pad products for another advanced node application. On a combined basis, we continue to have more than 50 opportunities for our D100 and D200 pad products around the world in various stages of evaluation or qualification. These wins are two examples of our ability to transform these opportunities into product adoptions. While we are excited about these wins, I would emphasize that meaningful revenue for this new business is still several quarters away.

We have also experienced greater collaboration and interest from our customers in South Korea during the quarter. Sales this quarter continued to be especially strong in South Korea, where our revenue increased approximately 11 percent compared to last quarter and 26 percent versus the first quarter of last year. We believe our technical capabilities at our new facility in South Korea have strengthened our ability to serve our customers within the country. Our customers have responded positively to our local presence and are actively engaged in real time collaboration with us to develop and qualify products. We have several products currently under evaluation at this facility with our customers and we look forward to translating these opportunities into commercial sales during this fiscal year.

The increased collaboration in South Korea is a great example of the benefits we can realize from making investments close to our customers. It is also representative of the broader investment strategy we have been implementing over time within the Asia Pacific region to strengthen and grow our business.

Concluding my remarks today, we are encouraged by our customers' continued interest in our CMP consumables products. During this period of near term industry softness and macroeconomic uncertainty, we will continue to monitor industry trends and manage our business appropriately. Given the significant investments we have made in facilities and capabilities over the last several years, particularly in the Asia Pacific region, we believe we are well positioned for profitable growth when industry demand strengthens.

And with that, I will turn the call over to Bill.

Thanks, Bill, and good morning everyone.

Revenue for the first quarter of fiscal 2012 was $102.1 million, which was down by 10.6 percent from the first quarter of last year and down by 6.9 percent from the prior quarter. We believe these decreases in revenue primarily reflect soft demand within the global semiconductor industry. Compared to the prior quarter, revenue decreased within each of our business areas.

Drilling down into revenue by business area, Tungsten slurries contributed 39.9 percent of total quarterly revenue, with revenue down 2.9 percent from the same quarter a year ago and down 0.7 percent sequentially.

Sales of Copper products represented 15.7 percent of our total revenue, and decreased 21.8 percent from the same quarter last year and decreased 0.8 percent sequentially. The year over year decrease in revenue is primarily a result of reduced demand from some of our foundry customers, similar to what we experienced last quarter.

Dielectric slurries provided 27.4 percent of our revenue this quarter, with sales down 10.2 percent from the same quarter a year ago and down 5.4 percent sequentially.

Data Storage slurry products represented 4.9 percent of our quarterly revenue; this revenue was down 30.0 percent from the same quarter last year, and down 27.2 percent sequentially. The decrease in our Data Storage revenue is largely due to the slowdown in the hard disk drive industry related to the recent severe flooding in Thailand.

Sales of our polishing pads represented 6.8 percent of our total revenue for the quarter; and decreased 17.1 percent from the same quarter last year and 6.3 percent sequentially.

Finally, revenue from our Engineered Surfaces Finishes business, which includes QED, generated 5.3 percent of our total sales, and was up 6.9 percent from the same quarter last year and down 37.5 percent sequentially. Volatility in our QED revenue is not surprising, given that it is primarily a capital equipment oriented business.

Our gross profit this quarter represented 48.3 percent of revenue, which is slightly above our guidance range of 46 to 48 percent of revenue for full fiscal year 2012. This is down from 50.3 percent in the same quarter a year ago and up from 46.4 percent in the prior quarter. Compared to the year ago quarter, our gross profit percentage decreased primarily due to lower production volumes and selective price reductions, partially offset by lower variable manufacturing costs. The increase in gross profit percentage versus the previous quarter was primarily due to lower variable and fixed manufacturing costs, and a higher valued product mix, partially offset by the adverse impact of lower production volumes.

Now I'll turn to operating expenses, which include research, development and technical, selling and marketing, and general and administrative costs. Operating expenses this quarter of $34.0 million were $1.0 million higher than the $33.0 million reported in the first quarter of fiscal 2011. The increase was primarily driven by professional fees of approximately $2.4 million related to our proposed leveraged recapitalization and special cash dividend, and as such, should not represent an ongoing cost at this level. These costs were partially offset by lower staffing related expenses. Operating expenses were approximately $100,000 lower than the $34.1 million reported in the previous quarter.

Diluted earnings per share were 45 cents this quarter, which reflect an adverse effect of approximately 7 cents per share from professional fees associated with our proposed leveraged recapitalization and special cash dividend. This is down from 71 cents reported in the first quarter of fiscal 2011 on lower revenue and lower gross profit margin. Compared to the previous quarter, diluted EPS was up from 40 cents, due to a lower effective tax rate, a higher gross profit margin and foreign exchange gains included in other income, partially offset by the adverse effect of lower revenue.

Turning now to cash and balance sheet related items, capital additions for the quarter were $3.9 million, depreciation and amortization expense was $6.0 million and share-based compensation expense was $3.4 million. In addition, we purchased $13.0 million of our stock during the quarter under our share repurchase program. We ended the quarter with a cash balance of approximately $294 million.

Earlier, Bill discussed our proposed leveraged recapitalization and special cash dividend. At this time, we expect to declare and pay the proposed special cash dividend during our second fiscal quarter of 2012. Before doing so, we need to finalize terms on the associated financing. In recent weeks, we have made progress on arranging the financing; we have selected our lead banks and are working with them to syndicate the credit facility. We are negotiating a $275 million credit facility, which we expect will include a $175 million term loan with a 5 year maturity, as well as a $100 million revolving credit facility that we expect will be initially undrawn. We believe our company represents an attractive credit to prospective lenders, and this financing opportunity has been met with strong interest.

I'll conclude my remarks with a few comments on recent sales and order patterns.

Examining revenue patterns within the three months of our first fiscal quarter, we saw demand for our CMP consumables products relatively constant during the quarter, and at a level approximately 4 percent below last quarter. As we observe orders for our CMP consumables products received to date in January that we expect to ship by the end of the month, we see January results trending in line with the average rate in our first fiscal quarter. We typically experience lower demand around the Lunar New Year, which began on January 23rd. However, I would caution, as I always do, that several weeks of CMP related orders out of a quarter represent only a limited window on full quarter results.

Thank you for your time and your interest in Cabot Microelectronics.