

# **Cabot Microelectronics Corporation**

## **First Quarter Fiscal Year 2014 Conference Call Script**

### **January 23, 2014**

Good morning. With me today are Bill Noglows Chairman and CEO, and Bill Johnson, Executive Vice President and CFO.

This morning we reported results for our first quarter of fiscal year 2014, which ended December 31. A copy of our earnings release is available in the investor relations section of our website, [cabotcmp.com](http://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, 2013. 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 2014. Our results reflect the soft industry conditions, including traditional seasonal weakness, that we referenced last October when we reported results for our previous fiscal quarter. Even within this environment, however, our gross margins improved on lower revenue when compared to the same quarter last year, and when combined with lower operating costs, helped to mitigate the impact of soft demand conditions, on our earnings. During the quarter, we achieved revenue of \$100.5 million dollars, gross profit margin of 47.5 percent of revenue, a 50 basis point improvement year-over-year, and earnings per share of 45 cents. Bill Johnson will provide more detail on our financial results later in the call.

Let me start this morning with our views on the semiconductor industry. Industry reports generally indicate that the holiday sales of technology products were solid, driven primarily by demand for smartphones and tablets. Gartner announced that demand for PCs continued to be weak during the fourth quarter of 2013 and worldwide PC shipments declined for the seventh consecutive quarter, registering a decrease of approximately seven percent, year over year. However, on a positive note, some recent industry reports suggest that a variety of new form factors, such as thinner and lighter hybrid notebooks, may encourage PC replacement, and certain industry analysts are forecasting modest growth for the PC market in 2014. This would represent an important shift from the contraction that has beset the PC market over the past two years, and an incremental positive benefit to our industry.

Due to the level of semiconductor sales relative to semiconductor device production, analysts believe that most IC inventories decreased during the December quarter and returned to more normal levels. Earlier this month, the Semiconductor Industry Association reported that worldwide sales of semiconductors in November increased for the ninth consecutive month. The report indicated solid momentum across all geographic regions and most product categories, and suggested that the industry is well-positioned heading into the New Year. In addition, some IC manufacturers are now

reportedly seeing a pull-in of orders from chip customers for delivery during the March quarter, and as a result fab utilization rates now appear to be improving.

Last week several of our executives attended SEMI's Industry Strategy Symposium, or ISS conference, in California. This is an annual event hosted by SEMI early in the calendar year, and represents a great opportunity to network and compare views with other industry participants. The theme of the conference this year was Pervasive Computing, highlighting the future opportunities of even greater mobility, connectivity and what is being called the "internet of things". Our participants came away from the event energized about the long term future opportunities for our company, given emerging technologies such as FinFet and 3d NAND, and the increasing role that highly engineered materials, like our CMP solutions and formulated products are likely to play in the continued growth, development and advancement of the semiconductor industry.

Looking forward, based on these recent reports from a number of industry analysts and public statements from some of our strategic customers, as well as historical trends within similar seasonal demand patterns, we expect strengthening in overall semiconductor industry demand during the fiscal year. Having successfully navigated periods of both strong and soft industry demand environments, we believe these industry trends, coupled with the continued successful execution of our strategic initiatives, positions us well as we work to deliver another year of solid business performance in fiscal 2014.

Let me now turn to our core IC CMP consumables business. During the quarter we continued to pursue our long term strategic business initiatives related to technology leadership, collaborating with our customers, and supply chain excellence. We continue to focus our R and D efforts on innovating for leading edge applications for technology leading customers. We are encouraged by some early indications from our new product development focus and R&D realignment, and expect accelerating new product introductions and business wins in the future.

Our business and technical teams around the world are collaborating with customers on a wide range of new business opportunities, and during the quarter we won new business with our CMP products for Tungsten, Copper, Aluminum, TSV, and Pads applications.

We continue to believe that our global supply chain management and quality systems are unmatched within the industry. This capability gives our customers the confidence to trust that the high-performing and reliable solutions we provide for them will have the consistency and lack of variability that they demand in their fab operations. As our customers' quality requirements continue to tighten and narrow, we are able to respond quickly and effectively by leveraging our entire supply chain and integrating our strategic suppliers in the process to consistently meet or exceed our customers' requirements.

One specific example of our success in combining our capabilities in technology leadership, collaborating with customers and supply chain excellence is our earning Western Digital Media's Supplier of the Year Award. This award recognizes our performance in quality, product development and business support in fiscal 2013. Similar to many other customer awards we have earned, we believe this recognition demonstrates our commitment to being a long term trusted partner, delivering high-performing, high-quality and reliable products and solutions.

Concluding my remarks today, with the continuation of positive trends in mobile connectivity, and some recovery within the PC market, we expect long term growth in demand for our CMP consumables products. We believe our global footprint, and our depth and breadth of product offerings differentiate us from our competitors, and in particular, our supply chain capabilities and

quality systems represent a competitive advantage for us. We continue to pursue our business objective of being the leading CMP solutions provider to the overall semiconductor industry.

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

Thanks, Bill, and good morning everyone.

Revenue for the first quarter of fiscal 2014 was \$100.5 million, which was down by 5.6 percent from the first quarter of last year and down by 13.5 percent from the record revenue we achieved in the prior quarter. We believe the decrease in revenue, compared to the same quarter last year, primarily reflects softer demand due to lower utilization at some fabs, and continued soft demand for PCs. Compared to the previous quarter, we believe the decrease in revenue primarily reflects soft demand within the global semiconductor industry, including traditional seasonal weakness, that we began to experience late last fiscal year and referenced last October when we reported results for our previous fiscal quarter. Revenues were also adversely impacted by customary fluctuations in our QED business, primarily capital equipment oriented, which also achieved record revenue in the prior quarter. Excluding the adverse impact of lower QED revenue, our CMP consumables revenue decreased by nine percent sequentially.

Drilling down into revenue by business area, Tungsten slurries contributed 37.2 percent of our total quarterly revenue, with revenue down 8.2 percent from the same quarter a year ago and down 6.0 percent sequentially. We believe lower utilization at some fabs and the continued soft demand for PCs primarily accounts for our lower Tungsten business revenue this quarter.

Dielectrics slurries provided 29.8 percent of our revenue this quarter, with sales down 1.4 percent from the same quarter a year ago and down 7.9 percent sequentially.

Sales of slurries for polishing metals other than Tungsten, including Copper, Aluminum and Barrier, represented 17.7 percent of our total revenue, and decreased 1.0 percent from the same quarter last year and 16.1 percent sequentially. Recall that we achieved a record revenue level for our Aluminum slurry products in the prior quarter.

Sales of our polishing pads represented 7.4 percent of our total revenue for the quarter, and decreased 12.4 percent from the same quarter last year and 14.6 percent sequentially. Compared to the same quarter last year, we believe the revenue decrease is partially due to competitive pricing pressure as well as customer efficiency gains in use of our pads, which we have discussed in the past, and lower utilization at some fabs. We believe the sequential revenue decrease is primarily due to soft industry conditions, particularly at certain foundries.

Data Storage products represented 5.0 percent of our quarterly revenue; this revenue was down 1.6 percent from the same quarter last year, and up 1.1 percent sequentially.

Finally, revenue from our Engineered Surface Finishes business, which includes QED, generated 3.0 percent of our total sales, and was down 24 percent from the same quarter last year and down 67 percent sequentially. Recall that our QED business achieved record revenue in the prior quarter and volatility in our QED revenue is expected, given that it is primarily a capital equipment oriented business. I would point out, that similar to the first quarter of fiscal 2014, our QED business enters the second quarter with a very limited equipment order backlog.

Our gross profit this quarter represented 47.5 percent of revenue. This is up from 47.0 percent in the same quarter a year ago and down from 50.9 percent in the prior quarter. Compared to the year ago quarter, gross profit percentage increased primarily due to benefits associated with a weaker

Japanese yen versus the U.S. dollar and higher manufacturing yields, partially offset by lower sales volume and higher variable manufacturing costs, including higher raw material costs. The decrease in gross profit percentage versus the previous quarter was primarily due to lower sales volume and higher variable manufacturing costs, including higher raw material costs, partially offset by lower fixed manufacturing costs, including incentive compensation. Our full fiscal year 2014 guidance range of 48 to 50 percent of revenue remains unchanged.

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 were \$32.0 million, or \$1.4 million less than the \$33.4 million reported in the same quarter a year ago, primarily due to lower clean room materials expense and depreciation expense. Operating expenses were \$3.5 million lower than the \$35.5 million reported in the previous quarter, primarily due to lower staffing related costs, including incentive compensation.

Recall that there is typically a noticeable increase in our operating expenses in the March quarter due to certain annual factors such as merit salary increases, higher payroll taxes beginning with the new calendar year and costs around our annual meeting in March. We continue to expect our operating expenses for full fiscal year 2014 to be in the range of \$131 million to \$135 million.

Diluted earnings per share were 45 cents this quarter. This is up from 41 cents reported in the first quarter of fiscal 2013 and down from 69 cents reported in the previous quarter. Compared to the same quarter last year, earnings per share increased primarily due to lower tax expense on our foreign earnings resulting from our election to permanently reinvest the earnings of certain foreign subsidiaries. The first quarter of fiscal 2013 also included an adverse foreign tax adjustment that reduced our EPS by approximately seven cents. Compared to the prior quarter, earnings per share decreased mainly due to lower revenue and a lower gross profit margin, partially offset by lower operating expenses.

Turning now to cash and balance sheet related items, capital investments for the quarter were \$3.7 million, and depreciation and amortization expense was \$5.0 million. In addition, we purchased \$8.0 million of our stock during the quarter under our share repurchase program, leaving approximately \$82.0 million remaining in share repurchase authorization. We ended the quarter with a cash balance of \$246.5 million and have \$159.7 million of debt outstanding.

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

During the first fiscal quarter, we saw a decrease in demand for our CMP consumables products of approximately nine percent compared to the prior quarter, generally consistent with what we were seeing in the first few weeks of October when we last spoke to you. 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 approximately five percent lower than the average rate in our first fiscal quarter. Recall as we approach the Lunar New Year, which begins on January 31<sup>st</sup> that we typically experience some order fluctuation around this holiday period. 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.