Cabot Microelectronics Corporation
Third Fiscal Quarter 2013 Conference Call Script
July 30, 2013

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 third quarter of fiscal year 2013, which ended June 30. 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, 2012. 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 strong financial results for our third fiscal quarter of 2013. During the quarter, we achieved revenue of $110.0 million dollars, gross profit margin of 49.7 percent of revenue, and earnings per share of 65 cents, all of which are significantly higher than last quarter's results. Following relatively soft semiconductor industry conditions during the first half of our fiscal year, we saw strengthening in demand in our core business during our third quarter, as well as growth in demand for our QED products. This strengthening, coupled with our continued successful execution of our long-term strategies and our proven ability to manage our business over a range of industry conditions, contributed to our strong earnings performance this quarter. Bill Johnson will provide more detail on our financial performance later in the call.

Let me start this morning by providing some general comments on conditions within the semiconductor industry. As has been widely reported, the industry continues to experience a significant shift in demand from semiconductor devices for personal computers to those for mobile internet devices, which we have seen over the last several years. For example, during the period of 2009 through 2013, an industry report estimates the communications IC market will register a compound annual growth rate of 16 percent, compared to a compound annual growth rate of three percent, for the computer IC market during the same period of time. Demand for mobile devices is growing rapidly, but since these devices generally contain approximately half of the semiconductor content per device that PCs contain, overall industry demand has been somewhat muted.

The differing demand patterns for IC devices for the PC industry versus the mobile market mean that portions of the semiconductor industry supply chain that serve the mobile market are enjoying rapid growth, but those that serve the PC market are not. Since we serve the broad market, and sell our products to essentially every semiconductor manufacturer in the world, our growth has more closely tracked overall semiconductor industry activity.

Industry reports suggest that inventory levels are generally normal across device categories, with some accumulation of high-end ICs in preparation for specific product launches in the second half of the calendar year. IC manufacturers continue to cautiously manage inventory in the supply chain. That being said, the outlook of some of our strategic customers and industry analysts for the third calendar quarter calls for modest sequential growth.

Turning now to company-related matters, I am pleased to report our Pads business achieved sequential revenue growth of 14 percent for the quarter. While customers continue to enjoy the longer life afforded by our Pads, which is key to our value proposition, customer demand has returned to the levels we experienced during the first fiscal quarter of this year. Our pipeline of business opportunities remains healthy and we continue to partner with existing and new customers on product evaluations and qualifications. As a result of this collaboration, during the quarter we secured new business wins for both our D100 and D200 product platforms, for both leading edge and legacy Barrier and Tungsten applications.

Turning to our IC CMP slurry business, we achieved sequential revenue growth in all of our slurry business areas this quarter. During the quarter, we won new business across a range of applications, including Tungsten, Dielectrics, Barrier and Through-silicon Via, or TSV. Customers continue to actively sample our products for new opportunities and there are a number of evaluations underway, which we believe are evidence of our ability to provide innovative, reliable, high-quality solutions for leading edge applications. We believe these wins are a result of our consistent investments in technology and global infrastructure, which enhances our collaborations with our strategic customers to meet their demanding requirements and continue to enable the advancement of Moore’s law.

As the industry evolves and technology advances, our customers require greater customization of CMP solutions, and our ability to closely collaborate with them, with speed, is essential. Supporting our commitment to technology leadership, during recent years we have invested approximately 14 percent of our annual revenue in research and development activities. In order to get the greatest productivity from our significant investment in R and D, we are now focusing our R and D efforts on our most strategic customers. Our view is that as the industry continues to consolidate, a limited number of the largest semiconductor manufacturers will have greater and greater influence on the future of the industry. We are collaborating closely with technology leading customers, research scientist to research scientist, in our customers' time zones and languages, to assure that we are meeting the future needs of these important customers. We believe our global technology footprint is unmatched among CMP slurry and pad providers -- our technical capabilities in North America, Japan, Taiwan, Korea and Singapore enable real time collaboration as our scientists develop and deliver reliable, high-quality solutions with speed.

As technology advances, our customers' requirements for quality and consistency of our products continue to become more and more stringent. It is very important that we carefully manage our entire supply chain to assure absolute consistency of our products, especially for leading edge applications. We believe that our quality systems and supply chain management capabilities are world-class, and these represent a competitive advantage for us; and our focus on quality continues to demonstrate our commitment to developing high-quality solutions, while partnering with our customers.

Concluding my remarks this morning, we are convinced that our commitment to innovation, our global presence and our excellence in quality systems and supply chain management will continue to differentiate us from others in our space. The trends of advancing technology and greater mobile connectivity continue to introduce a number of technical challenges within the semiconductor industry, such as higher performance, new materials, expanding features and thinner form factors. We believe our company is uniquely positioned to overcome these challenges in collaboration with our strategic customers.

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

Thanks, Bill, and good morning everyone.

Revenue for the third quarter of fiscal 2013 was $110.0 million, which reflects strengthening in demand within the global semiconductor industry, following relatively soft conditions during the first half of the fiscal year, as well as growth in demand for our QED products. Revenue was down by 4.9 percent from the record revenue achieved in the same quarter last year and up 9.6 percent from the prior quarter. Year to date revenue of $316.9 million is essentially even with the prior year.

Drilling down into revenue by business area,
Tungsten slurries contributed 35.1 percent of total quarterly revenue, with revenue down 8.4 percent from the same quarter a year ago and up 4.9 percent sequentially. We believe the decline in demand for PCs, with the associated reduction in DRAM demand, which we have discussed in the past, accounts for our lower Tungsten business revenue compared to the same quarter last year.

Dielectrics slurries provided 27.8 percent of our revenue this quarter, with sales down 6.0 percent from the same quarter a year ago and up 2.8 percent sequentially. Within Dielectrics, year-to-date revenue from our Advanced Dielectrics business increased by approximately 26 percent compared to last year.

Sales of slurries for polishing other metals, including Copper, Aluminum and Barrier, represented 18.3 percent of our total revenue, and increased 12.4 percent from the same quarter last year and were up 17.9 percent sequentially. Year-to-date revenue from our Aluminum slurry business more than doubled compared to last year. Note that in the past we have referred to our “Copper” slurries as also including slurries for polishing Aluminum and Barrier. With development and changes within these various product lines we will now refer to this product family as slurries for polishing “Other Metals” to distinguish them from our Tungsten slurries.

Sales of our polishing pads represented 7.7 percent of our total revenue for the quarter and reflect a decrease of 6.5 percent from the same quarter last year and an increase of 14.2 percent sequentially. Year-to-date, our Pad revenue is up about 2 percent compared to last year.

Data Storage slurry products represented 4.8 percent of our quarterly revenue. This revenue was down 0.8 percent from the same quarter last year and down 2.8 percent sequentially.

Finally, revenue from our Engineered Surface Finishes business, which includes QED, generated 6.3 percent of our total sales, and was down by 20.6 percent from the record revenue achieved in the same quarter last year, and up 76.3 percent sequentially. Volatility in our QED revenue is expected, given that it is primarily a capital equipment oriented business.

Our gross profit this quarter represented 49.7 percent of revenue, which is up from 47.7 percent in the same quarter a year ago and 48.2 percent in the prior quarter. Compared to the year ago quarter, gross profit percentage increased primarily due to lower manufacturing costs and benefits associated with a weaker Japanese yen versus the U.S. dollar, partially offset by lower sales volume. The increase in gross profit percentage versus the previous quarter was primarily due to lower fixed manufacturing and logistics costs and the favorable impact of the weaker Japanese yen.

Year to date, gross profit represented 48.3 percent of revenue. In our fourth fiscal quarter we anticipate some gross margin headwind, as we expect higher costs on a short term basis associated with the transition to a new raw material supply contract with an existing supplier. We currently estimate this headwind will be around 150 basis points. Our full fiscal year gross profit guidance of 46 to 48 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 of $32.4 million were $1.2 million lower than in the third quarter of fiscal 2012. The decrease was primarily due to lower depreciation expense, clean room materials expense and staffing related expenses. Operating expenses were approximately $2.0 million lower than in the previous quarter, primarily due to lower staffing related costs.

Year to date, total operating expenses were $100.2 million, which is 3.9 percent lower than during the same period last year. We continue to expect our full year operating expenses to be within a range of $132 million to $136 million for fiscal 2013.

Diluted earnings per share were 65 cents this quarter, which includes a 5 cent benefit due to our recent election to permanently reinvest the earnings of our Japan subsidiaries, which lowered our effective tax rate. This is up from the 55 cents reported in the third quarter of fiscal 2012. Our EPS was up from 40 cents in the prior quarter, mainly due to higher revenue, a higher gross profit margin, lower operating expenses and a lower effective tax rate. Year to date, diluted earnings per share of $1.46 is up 17.7 percent compared to last year.

We now expect our effective tax rate for the full year to be between 32 and 34 percent, which is lower than our previous estimate of between 34 and 35 percent.

Turning now to cash and balance sheet related items, capital investments for the quarter were $4.7 million, and depreciation and amortization expense was $4.9 million. We now expect our capital spending for the full year to be approximately $18 million, which is lower than our previous estimate of $20 million. We purchased $10.0 million of our stock during the quarter. We ended the quarter with a cash balance of $201.6 million, which is $13.3 million higher than in the prior quarter, and we have $166.3 million of debt outstanding.

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

During the third fiscal quarter, we saw an increase in revenue for our CMP consumables products of approximately seven percent compared to the prior quarter. As we observe orders for our CMP consumables products received to date in July that we expect to ship by the end of the month, we see July orders trending approximately eight percent higher than the average rate in our third fiscal quarter. However, I would caution, as I always do, that four weeks of CMP related orders out of a quarter represent only a limited window on full quarter results. In particular, this increase in our July orders is higher than indications for sequential growth that we are hearing in the industry, and higher than what we have seen in terms of historical seasonality. So we would urge particular caution about extrapolating too much from this limited data point.

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