ON SEMICONDUCTOR CORPORATION

SCRIPT FOR
CLOSE OF FAIRCHILD ACQUISITION CONFERENCE CALL

Parag Agarwal

Thank you, <operator> and good afternoon everyone.

Welcome to ON Semiconductor Corporation's conference call to discuss the close of the transaction for our acquisition of Fairchild Semiconductor. Joining me today are Keith Jackson, our President and CEO, and Bernard Gutmann, our Chief Financial Officer.

Earlier today we distributed a press release announcing the close of the transaction to acquire Fairchild Semiconductor, a leader in energy-efficient power and analog semiconductor solutions. The press release and the supplemental presentation slides summarizing the transaction are available in the "Investor Relations" section of ON Semiconductor's website at www.onsemi.com. This call is being webcast on the "Investor Relations" section of our website. It will also be archived for approximately a year in the "Investor Relations" section of our website.

During the course of this conference call, we will make projections or other forward-looking statements regarding future events or the future financial performance of the company. The words "believe," "estimate," "project," "anticipate," "intend," "may," "expect," "will," "plan," "position", "should" or similar expressions are intended to identify forward-looking statements. We wish to caution that such statements are subject to risks and uncertainties that could cause actual events or results to differ materially from projections. Important factors which can affect our business, including factors that could cause actual results to differ from our forward-looking statements, are described in our Form 10-Ks, Form 10-Qs and other filings with the Securities and Exchange Commission.

Our estimates may change, and the company assumes no obligation to update forward-looking statements to reflect actual results, changed assumptions, or other factors, except as required by law.

As we are in quite period for the third quarter of 2016, we will not be able to answer questions related to current business trends for the company, current industry environment, and outlook for the fourth quarter of 2016.

For all synergy related discussions on this call, we have used Fairchild's 2015 results as the base for all comparisons.

Now, let me turn it over to Keith Jackson, who will provide details on strategic implications of the transaction. Keith?

Keith Jackson

Thank you, Parag, and good afternoon everyone. Let me start by welcoming the employees of Fairchild Semiconductor to the ON Semiconductor family. I am confident that the immense talent and dedication of our newest employees will accelerate our progress towards building a world class power management company with industry leading profitability.

We are very excited about the strategic opportunities and financial benefits our acquisition of Fairchild Semiconductor will create for us going forward. The combination of ON Semiconductor creates a new leader in power semiconductors with annual revenue of approximately $5 billion. Fairchild's strength in medium and high voltage power management, coupled with our leadership in low-voltage power management and analog control devices, propels us to a leadership position in the power management market with a broad portfolio of products across the complete voltage spectrum for automotive, industrial, and communications end-markets.

The acquisition of Fairchild Semiconductor provides us a platform to aggressively expand our profitability in a highly competitive industry. With an expanded revenue base and the addition of Fairchild's manufacturing network, we expect that our industry leading cost structure will improve further, and we expect this cost structure to accelerate our margin expansion towards our target margins, which we announced at our analyst day in February 2015. We expect that the combination of the two companies should generate significant shareholder value from incremental free cash flow resulting from synergies between the two companies. We expect annual synergies run rate of approximately $225 million annually as we exit 2019 and incremental free cash flow of approximately $235 million from the acquisition in 2019. Free cash flow is defined as cash flow from operations less capital expenditure. As indicated earlier, our target of $225 million of annual synergies is based on Fairchild's 2015 results. Bernard will provide additional details on synergies in his prepared remarks.

As we have indicated earlier, our acquisition of Fairchild is highly complementary, and the revenue overlap between ON Semiconductor and Fairchild is small. Fairchild significantly boosts our capabilities in mid to high voltage power management, which is highly complementary to ON Semiconductor's strong presence in low voltage power management and analog control devices. The addition of medium to high voltage products and technologies to our portfolio significantly expands our capabilities in the automotive, industrial and communications end-markets.

In terms of end-market exposure, our exposure to our strategic end-markets of automotive, industrial and communications remain unchanged at approximately 75 percent. However, the customer overlap between the two companies is small, and given the highly complementary nature of products of the two companies, there is a potential for revenue synergies resulting from the combination of the two companies. The small customer overlap between the two companies helps in driving further diversification of our customer base. While the number one customers of the two companies contribute approximately 5 percent and 8 percent of revenue in 2015, the top customer of the combined company would have contributed 4 percent of revenue based on 2015 revenue of the two companies. Despite being highly diversified, we expect to grow at a rate higher than that of the overall semiconductor industry. Given our approximately 75 percent exposure to automotive, industrial, and communications markets and leadership in growth areas such as ADAS, vehicle electrification, LED lighting in automotive, quick charging solutions for mobile devices, and industrial motor control, we expect to continue to outgrow the semiconductor industry.

Now, I will provide additional details on the complementary capabilities that Fairchild provides us in various end-markets. As I indicated earlier, the revenue overlap between the product portfolios is small. Even in areas of overlap, the overlapping products are optimized for different operating parameters, such as current and voltage.

In the automotive end-market, Fairchild significantly enhances ON Semiconductor's capabilities in the rapidly emerging electric vehicle and hybrid electric vehicle market. The combination of Fairchild's automotive qualified medium voltage and high voltage MOSFETs with ON Semiconductor's extensive portfolio of automotive qualified power management solutions positions the company as an unrivaled supplier of power solutions for traditional internal combustion engine vehicles as well as the fast growing EV/HEV vehicles. As automotive manufacturers turn to next generation semiconductor materials to improve power density and efficiency in hybrid and electric vehicles, Fairchild's 1200V silicon carbide power devices coupled with ON Semiconductor's 650V gallium nitride power devices provide market leading solutions.

In the industrial end-market, Fairchild is an established market leader in industrial motor control power solutions with its discrete and power module product portfolio. Combining these products with ON Semiconductor's BLDC motor control ICs and IPMs provides our industrial customers with comprehensive solutions for the extensive range of motor-based systems.

The combination of ON Semiconductor's and Fairchild's AC to DC, DC to DC and power discrete portfolios creates an industry leader in high performance power conversion serving a broad range of applications traversing the high, medium and low voltage spectrum. Fairchild's super-junction MOSFETs and ON Semiconductor's GaN power switches enable significantly improved power density and efficiency for industrial variable speed drives, as well as uninterruptable power supplies used in networking, telecom and data center applications. In addition, Fairchild has an established footprint in cloud power solutions that includes networking equipment and data center servers.

In the communication end-market, with the addition of Fairchild's portfolio, ON Semiconductor's addressable content per device increases to $11 from $9. The combined company is now a market leader in wall-to-battery power solutions and USB Type C peripheral connectivity. Fairchild Semiconductor has a leading position in fast charging AC to DC power adapters with support for multiple industry protocols. Fairchild's strength in power adapters is now augmented by ON Semiconductor's growing portfolio of power adapter products. In addition, ON Semiconductor offers complementary magnetic resonance wireless charging products to provide our customers a broad portfolio of wired and wireless charging solutions. Bringing together the low power portfolios creates a comprehensive catalog of DC to DC and battery management solutions for applications ranging from smartphones to AR/VR glasses.

Our business has evolved over the last several years, and we have moved away from being just a supplier of standard products to being a provider of highly differentiated power management and analog solutions. With a vastly improved product profile and a larger revenue base resulting from the acquisition, we have reorganized our business into three business segments – Power Solutions Group or PSG, Analog Solutions Group or ASG, and Image Solutions Group or ISG. Personnel, assets and resources of Systems Solutions Group or SSG have been reallocated among PSG, ASG and, to a lesser extent, ISG.

PSG focuses on semiconductor components for multiple applications and functions, including power switching, signal conditioning, circuit protection, signal amplification and voltage reference. PSG is headed by Bill Hall. ASG focuses on analog, mixed-signal and advanced logic ASIC and ASSP solutions for a broad base of applications in the automotive, industrial, communications, medical, military and aerospace markets. ASG is headed by Bob Klosterboer. ISG focuses on CMOS and CCD image sensors, proximity sensors and image signal processors for automotive, industrial, medical, military and aerospace markets. ISG is headed by Taner Ozcelik.

With that, let me now turn the call over to Bernard, who will provide an update on financial details of Fairchild acquisition. Bernard?

Bernard Gutmann

Thank you, Keith and good afternoon everyone.

Let me start with the discussion of our target model we provided at our last Analyst day in February of 2015. Our target model calls for non-GAAP gross margin of 40 percent and non-GAAP operating margin in range of 17 to 19 percent on revenue of $4 billion. Our progress towards the margins detailed in our target financial model has been hampered in large part by the current macroeconomic environment and semiconductor industry conditions. However, we believe that the acquisition of Fairchild should accelerate our progress towards the margin targets detailed in our target model, despite a modest revenue growth assumption of two percent per year. We will provide additional updates on the target financial model for the combined company at our next analyst day in spring of 2017.

Moving on to the synergies target we provided in November of last year. We now expect that total synergies resulting from the combination of ON Semiconductor and Fairchild Semiconductor to be approximately $225 million annually as we exit 2019, as compared to $150 million exiting 2017 that we announced in November of last year. The increase of $75 million in annual synergies is expected to come from manufacturing and operational improvements of the combined company and from insourcing of production. Apart from cost savings from elimination of redundancies, we expect to benefit from operating leverage and efficiencies resulting from our significantly expanded scale. As indicated earlier, for purposes of our discussion of synergy targets, we have used ON Semiconductor's and Fairchild's 2015 results as the baseline.

On the manufacturing front, we intend to leverage Fairchild's 8 inch manufacturing capacity to improve cost structure of the combined manufacturing network. Also, given that manufacturing networks of the two companies have been running below optimal utilization, there is room for savings from consolidation of facilities. Further savings are expected to come from insourcing of production, especially for Fairchild's back-end operations. As a reminder, ON Semiconductor has one of the most efficient back-end operations in the industry and our back-end cost structure is significantly superior to that of contract manufacturing houses. Additional scale from Fairchild should help in further improving our front-end and back-end manufacturing cost structure. With substantially improved scale, transition to 8 inch front-end manufacturing, and insourcing of production, we feel confident in our ability to achieve our target non-GAAP gross margin of 40 percent for the combined company.

Moving on to operating expenses. As a matter of policy and in the best interest of our shareholders, we are committed to retaining the best talent from both the companies, and decisions to curtail functions and programs will be taken solely based on business considerations. In research and development, both companies have been investing in similar areas and we expect savings as we curtail or redirect our R&D investments. In sales, general and administrative, we expect savings through elimination of duplicate corporate functions. Also, a significantly larger revenue base of the combined company should drive operating expenses leverage, which in turn should drive operating margin expansion. Based on our early assessment of Fairchild's operations, we feel comfortable in achieving our non-GAAP operating margin target of 17 percent to 19 percent for the combined company.

In terms of timeline, in keeping with our previous announcements, we expect a synergies run rate of $75 million after first six months of close of transaction. We expect to exit 2017 with a synergies run rate of approximately $160 million. Approximately $130 million of the synergies in the first eighteen months are expected to come from operating expenses, and the remaining $30 million of synergies are expected to come from cost of goods sold. We expect to exit 2018 and 2019 with annual synergies run rate of $200 million and $225 million, respectively. Synergies in 2018 and 2019 are expected to come from consolidation of manufacturing facilities and insourcing of production. Given that our visibility has improved significantly from integration preparation activities since the announcement of the transaction, our confidence in achieving these synergies has improved meaningfully.

Moving on to accretion targets. The acquisition is expected to be accretive on a GAAP EPS basis in the latter half of 2017 and immediately accretive on a non-GAAP basis. Non-GAAP EPS excludes such items as step-up valuation of acquired inventory, amortization of intangibles, restructuring expenses, non-cash interest expenses and one-time items. We expect Fairchild to contribute approximately $0.20 to our non-GAAP EPS in 2017, which is lower than our initial estimate as it took longer than expected to receive all necessary regulatory approvals. The accretion is expected to be approximately $0.38 in 2018 and $0.43 in 2019.

We expect robust free cash flow contribution from Fairchild, starting with approximately $100 million in 2017. The $100m incremental cash flow includes approximately $25 million in restructuring cash costs and approximately $110 million of incremental interest related to the acquisition. In 2018, we expect incremental free cash flow of approximately $200 million, which includes approximately $100 million of acquisition related incremental interest expense. In 2019, we expect incremental free cash flow of approximately $235 million from Fairchild. Acquisition related interest expense is expected to be approximately $90 million in 2019. Our previous experience indicates that free cash flow during any year tends to be weighted towards the second half of the year.

With the acquisition of Fairchild, ON is now one of the most diversified companies in the semiconductor industry, not only in terms of end-market exposure but also in terms of customer concentration. While the number one customers of the two companies contribute approximately 5% and 8% of revenue in 2015, the top customer of the combined company would have contributed 4% of revenue based on 2015 revenues of the two companies. We believe that a diversified customer base, coupled with a diversified exposure to attractive end-markets and a vastly improved scale, should result in a company that can deliver highly stable results on sustained basis.

Moving on to use of capital, we intend to aggressively de-lever the company in the first two years with the aim of achieving net leverage of two times adjusted EBITDA by the end of 2018. Following de-levering the company by late 2018, we plan to re-initiate our shareholder capital return program. We will also explore the possibility of divesting certain non-strategic assets in order to raise capital to aggressively de-lever our balance sheet.

With that, let me now turn the call over to Keith. Keith….

Keith Jackson

Thanks Bernard. We are very excited about the expected benefits that the combination of ON Semiconductor and Fairchild will bring to our customers, shareholder and employees. I also take this opportunity to thank the leadership and staff of Fairchild Semiconductor for their efforts in ensuring the close of this transaction. This concludes our prepared remarks and we will now take your questions.

<Operator>, please open up the line for questions.

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