Cabot Microelectronics Corporation

2009 First Fiscal Quarter Earnings Report

January 22, 2009

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 2009, which ended December 31, 2008. A copy of our press release is available in the investor relations section of our website, cabotcmp.com, or by calling our investor relations office at 630-499-2600. Today's conference call is being recorded and will be archived for four weeks on our website. The script of this morning's formal comments will also be available there.

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, 2008. We assume no obligation to update any of this forward-looking information.

I will now turn the call over to Bill Noglows.

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

This morning we announced financial results for our first quarter of fiscal 2009, which we believe reflect the continuation and acceleration of softening demand for our products driven by the global economic downturn. As a result of sharply lower demand for our products, we reported a 30 percent decline in sequential quarterly revenue and approximately break-even net income performance for the first fiscal quarter.

The largest reduction in demand for our products came from the foundry segment, which represents a significant portion of our business, and we also experienced substantial declines in demand from memory and logic device producers. As we have discussed in the past, our revenue has historically tracked closely with the revenues reported by the largest foundries and this quarter was no exception. In general, we believe the decline in our revenue was consistent with the decrease in overall industry demand.

While we cannot change the economic environment in which we operate, we have taken actions to improve and optimize our operating effectiveness during the current downturn. In order to ensure alignment between production of our products and our customers' demand, we have shortened work schedules in our CMP consumables manufacturing operations globally. By adjusting work schedules, we retain the flexibility to ramp our production up or down to meet customer demand while managing our production costs.

Other actions taken to improve our operating effectiveness include a global hiring freeze, mandatory time off for employees, lower annual merit-based salary increases, restricted travel and the elimination of certain discretionary expenses. Our core CMP consumables business is not capital-intensive, but it is intellectually-intensive, so our initial cost management actions have been directed at minimizing expenses without incurring extensive layoffs. However, we are prepared to take more severe actions, as appropriate.

Notwithstanding our increased attention on reducing costs, we continue to invest in our business and execute on our two-pronged growth strategy of strengthening and growing our core CMP consumables business, and expanding into new areas through our Engineered Surface Finishes, or ESF business, so that we can emerge from this soft economic environment a stronger, and even more successful company. We believe this challenging business climate presents opportunities for strong companies with strong balance sheets, and we fully intend to take advantage of potential opportunities, as they arise.

A clear example of our continued investment in the company and execution of our strategy to strengthen and grow our core CMP consumables business, is our pending acquisition of Epoch Material Company, which we announced in December and expect to close during the quarter ending March 31, 2009, subject to regulatory approvals and customary closing conditions. Epoch is a Taiwan-based company specializing in the development, manufacture and sale of copper CMP slurries and CMP cleaning solutions to the semiconductor industry, and color filter slurries to the LCD industry.

With this acquisition, we expect to capitalize on Epoch's strong presence in Taiwan, the largest geographic region for CMP slurry demand, by leveraging Epoch's solid customer relationships and world-class facilities, which can be easily expanded for future growth. Additionally, we intend to utilize our global resources and infrastructure to expand the sales of Epoch branded products to the global semiconductor industry outside of Taiwan. We also expect to realize synergies from this transaction, which we anticipate will improve our overall cost structure, and allow us to support our customers more efficiently. This deal also enables us to continue to build and shift capabilities to the Asia Pacific region, closer to many of our customers.

Another example of the successful execution of our strategy to strengthen and grow our core CMP consumables business, even during the downturn, is the progress we continue to make in our CMP pad business. Although the current environment is generally resulting in fewer customer resources available to evaluate and qualify new products, we gained three new pad customers during the quarter. In addition, four other CMP slurry suppliers are now buying our pads for use in their slurry development activities. Use of our pads by our slurry competitors has the potential to accelerate the market acceptance of our pads and reinforces the credibility and performance of our product.

Another sign of progress in our pad business is our ongoing installation of on-site pad finishing capability within TSMC's facility in Taiwan, which continues on schedule. Construction and equipment installation is complete, product qualification is in process and we expect to begin high volume production by the end of March. In recognition of this innovative supply chain solution and our high performing, low cost of ownership products, we were honored with a supplier award by TSMC during its annual supplier day last November. Out of thousands of suppliers, TSMC granted awards to only six companies, and we are very pleased and proud of this special recognition.

We also continue to make progress on improving yields within our pad manufacturing operations. Even with significantly lower pad revenue this quarter, we achieved approximately break-even gross profit margin within our pad business.

In parallel with efforts in our core CMP consumables business, we are continuing to execute on our strategy to expand into new areas with our ESF business. Our focused efforts in research and development within QED has led to the introduction of a number of new products over the past year, including the recently released ASI metrology system for use with steeply aspherical optics. We believe this is an important enabling technology since the use of aspheres in optical systems design generally reduces the number of optics required which in turn, reduces the weight and size of an optical system, which is a key driver for many applications.

In summary, we are operating in challenging economic times, which are unprecedented for our industry and our company. We are taking actions to respond to this recessionary environment, while continuing to invest in our business for the long-term growth, and while attempting to minimize what we hope is a short-term dislocation. We have a seasoned and experienced management team that has successfully navigated businesses through difficult demand environments in the past. Ultimately, we believe our strong balance sheet with no debt, our solid cash flow, and the limited capital intensity required to run our core CMP business, afford us the flexibility to successfully sustain our business, maintain our CMP slurry leadership, and grow in new business areas.

And with that, I'll turn the call over to Bill Johnson. Bill?

Thanks, Bill, and good morning everyone.

Revenue for the first quarter of fiscal 2009 was $63 million, which was down by 32.5 percent from the first quarter of fiscal 2008 and down 30.1 percent from the previous quarter. Our reported revenue is consistent with the revenue outlook we provided on January 7th. We believe the decrease versus both comparator periods reflects a substantial and precipitous downturn in the semiconductor industry, driven by the current recessionary environment. Revenue declined in all of our major business areas, geographic regions and market segments. Despite the sharp reduction in our revenue, the average selling price for our slurries has remained relatively stable, and even increased from last quarter.

Drilling down into revenue by business area, Tungsten slurries contributed 41.4 percent of total quarterly revenue, with revenue down 32.6 percent from the same quarter a year ago and down 29.5 percent sequentially.

Sales of Copper slurries represented 14.1 percent of our total revenue, and decreased 37.6 percent from the same quarter last year and 29.3 percent sequentially. Although sales of copper slurries in total were down compared to last year, sales of copper slurries for barrier removal increased by 36.7 percent from the same quarter a year ago.

Dielectric slurries provided 31.1 percent of our revenue this quarter, with sales down 35.7 percent from the same quarter a year ago and down 31.7 percent sequentially. Included in this business is our advanced dielectrics product line, revenue from which was up nearly 40 percent from the same quarter last year.

Data Storage products represented 3.9 percent of our quarterly revenue; this revenue was down almost 50 percent from the same quarter last year and down 14.3 percent sequentially. We recently achieved an important new customer win for this business, but the additional demand generated by this new win did not offset the overall decrease in orders resulting from the challenging economic environment.

Sales of polishing pads represented 5.5 percent of our total revenue for the quarter; and increased 94.6 percent from the same quarter last year. We achieved several new customer wins this quarter, as Bill discussed; however, the total decrease in wafer starts by our existing pad customers was significant enough that we experienced a sequential revenue decrease of 36.9 percent.

Finally, revenue from our ESF business, which includes QED, generated 4.1 percent of our total sales, and our ESF revenue was down 24.0 percent from the same quarter last year and down 28.1 percent sequentially. As primarily a machine-oriented business, our QED business is subject to capital equipment cycles, and the current cycle has significantly adversely affected revenue in this area.

Our gross profit this quarter represented 45.6 percent of revenue, which was down from 47.9 percent in the same quarter last year and 46.6 percent in the previous quarter. Compared to both of these previous periods, the decrease in gross profit percentage this quarter was primarily due to lower utilization of our manufacturing capacity on the significantly lower level of sales, which was partially offset by higher manufacturing yields for both slurry and pads. Excluding our pad business, which operated at approximately break-even gross profit this quarter, total gross profit for the company as a percentage of revenue would have been 2.7 percentage points higher.

Our gross profit percentage guidance for full fiscal year 2009 remains unchanged at 46 to 48 percent of revenue. As a reminder, this guidance is for the full fiscal year and quarter to quarter our gross profit percentage may be above or below this range, such as we experienced this quarter. Current uncertainty in economic conditions makes it particularly difficult to predict full year results, and makes it more likely that actual results could differ from expectations. Consistent with our usual practice, we will re-evaluate our guidance on a quarterly basis and make updates, as necessary.

Now I'll turn to operating expenses, which include research, development and technical, selling and marketing, and general and administrative costs. Operating expenses of $29.4 million this quarter were higher than the $28.5 million reported in the year ago quarter, primarily due to increased costs for clean room materials and higher professional fees, partially offset by lower staffing related costs. Compared to the prior quarter, operating expenses were $2.3 million lower, mostly due to decreased staffing related costs.

Previously, we estimated full year operating expenses to be in the range of $120 to $125 million for fiscal 2009, which represented a flat to slightly lower outlook from fiscal 2008. As Bill mentioned earlier, we are currently taking a number of actions to reduce costs and improve our operating effectiveness during the current economic recession. Based on these actions, we now expect operating expenses to be lower and in the range of $110 to $115 million for full fiscal year 2009, excluding the effects of our pending acquisition of Epoch Material Company.

Diluted earnings per share were 1 cent this quarter, down from 51 cents reported in the first quarter of fiscal 2008 and 36 cents last quarter, primarily as a result of lower demand for our products resulting from the global economic downturn.

Turning now to cash and balance sheet related items, capital additions for the quarter were $2.5 million, which includes costs associated with the installation of pad finishing capacity on site at TSMC. Depreciation and amortization expense was $6.2 million in the first quarter, and share-based compensation expense was $4.2 million. We ended the quarter with $223.1 million in cash and short-term investments and no debt outstanding. Even upon closing of our pending acquisition of Epoch, which is being funded from our existing cash balance, we will still have a very strong cash position. Additionally, last October we renewed our revolving credit facility with attractive terms, despite the tight credit market, providing us with additional funding in this challenging economic environment.

I'll conclude my remarks with a few comments on our general outlook.

Examining order patterns during the three months of the first fiscal quarter, we saw a rapid softening in demand for our CMP consumables products as we recorded double-digit monthly sequential declines in each of the three months of the 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 significantly lower than the December level. We believe this reflects a further slowdown in orders as a number of our customers in Asia are planning extended production shutdowns around the Lunar New Year. 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 this morning and your interest in Cabot Microelectronics. We look forward to the next opportunity to speak with you. Goodbye.