Q1FY15 Earnings Conference Call Remarks  
Carlo Bozotti, President and Chief Executive Officer, STMicroelectronics  
Thursday, April 30, 2015

Thank you for joining us this morning on our first quarter earnings conference call.

On the agenda today there is a review of the quarter, including our two product segments, the results and opportunities with the products introduced in 2014 and our new design wins. We will then turn to our second quarter outlook.

Let’s move to the first quarter results. The start of the year reflected the expected seasonal softness while a couple of other factors, that I will comment upon later, affected our revenue performance. Our gross margin was instead well aligned with our guidance, and despite seasonal factors, we generated again positive cash flow.

Turning to sales, on a sequential basis, our net revenues decreased 6.8%, slightly better than our historical seasonality. Revenues totaled $1.71 billion and were affected by a lower contribution from euro-denominated sales of about $19 million, mainly associated with distribution and impacting, in particular, our SP&A segment.
Specifically, we came in below our mid-point target because of lower sales of power supply components for PC-related applications.

Looking at our channel mix, about 30% of net revenues came through Distribution compared to 32% in the fourth quarter, with the lower percentage largely related to both currency and PC-related demand.

Turning to our gross margin, we delivered well in line with our outlook, coming in at 33.2%. On a sequential basis, this represents a decrease of 60 basis points, on normal beginning of the year pricing changes partially offset by currency benefits, net of hedging. The gross margin reflected about 110 basis points of unsaturation charges in the first quarter, in connection with our manufacturing capacity in digital technology.

At the operating expense level, combined R&D and SG&A were $591 million. On a sequential basis, operating expenses decreased about $20 million, reflecting a lower number of days in the quarter as well as favorable currency effects, net of hedging.
Therefore, taking into account about $35 million of R&D grants, net operating expenses were at the low end of our net operating expense range of $550 to $600 million, coming in at $555 million.

Restructuring costs during the first quarter were $29 million, principally in connection with the EPS cost reduction program and the finalization of the closing of our back-end plant in Longgang, China.

Operating income before impairment and restructuring was $10 million compared to $8 million in the year-ago quarter. First quarter operating margin was 0.6% and reflected the impact of 110 basis points of unused capacity. The benefit of today’s currency environment is still limited on our profitability due to outstanding hedges. Excluding existing hedging contracts, operating margin would have increased by over 300 basis points.

Free cash flow was $41 million in the first quarter, compared to a negative $51 million in the year-ago period, representing a $92 million positive swing. We benefited from a strong increase in net cash from operations.
During the quarter ST paid cash dividends totaling $82 million. As you may have noted, at our May 27\textsuperscript{th} annual general meeting, ST’s Supervisory Board is recommending the approval of a cash dividend of $0.40 per share to be distributed in quarterly installments of US$0.10 to shareholders of record, in each of the second, third and fourth quarters of 2015 and first quarter of 2016. We believe this is a clear sign of confidence in ST’s solid capital structure, today and moving forward.

Now let’s move to a summary of our segments’ performance. As a reminder, starting from the first quarter unused capacity charges are allocated directly to the product segments.

Looking first at SP&A, net revenues were $1.12 billion. SP&A operating margin, including unused capacity charges, decreased to 6.4\% in the 2015 first quarter, from 8.4\% in the fourth quarter reflecting lower revenues and not yet benefiting from favorable currency effects of about 2.9 points, due to hedging.

Within SP&A, let me begin with AMS. Revenues in the first quarter totaled $255 million, representing a sequential reduction of 4.3\%.
At the same time, our expansion into key customers and product diversification initiatives has started to re-gain momentum. This is visible in the latest smartphones and smart watches launched on the market – and in the most recent teardowns.

During the first quarter, we ramped production of our high-end touch-screen controller and pressure sensor for Samsung’s Galaxy S6. We also delivered our high-performance microphones in high volume to another leading smartphone brand.

Our latest ultra-low power, 6-axis motion sensor was chosen for another Samsung smartphone. This new motion sensor, which was awarded Product of the Year by Electronic Products and MEMS Industry Group, is gaining traction worldwide with important customers: in fact, during Q1 we ramped production for a global brand to use it in a wearable application, and we were also chosen by a top Chinese brand for their latest model.

Another important growth opportunity is linked to laptops and tablets–where our MEMS continue to help change human-computer interaction.
In March, we announced the adoption of our micro-mirrors and control devices by Intel for their Perceptual Computing initiatives. We have now started production for several end customers.

We also made advances in sensors for the automotive market, ramping production for a number of inertial sensors in car-navigation and telematics applications in Korea, Europe, and the US.

Turning now to APG, net revenues in the first quarter totaled $434 million, essentially stable with the fourth quarter despite an exposure to Euro-denominated revenues larger than the company’s average.

During the quarter we continued to build on the strength of our broad-based portfolio, recording wins across our strategic areas of focus:

• in car infotainment, we won a significant number of awards for our latest-generation car-radio processor with important manufacturers in Korea and Greater China: our Accordo platform is becoming a *de facto* standard of the car radio market. We also expanded our presence in Audio Amplifiers with additional design wins for our class D car-audio amplifier with a top Japanese brand and with a leading Korean maker for the European market.
- in 32-bit microcontrollers, we continued to expand our presence at major Tier 1’s with key wins in Europe and China in the areas of Body and Powertrain. We also gained in the mass market where, among other successes, we earned a design win from a market leader in the growing area of e-bike applications.
- in active safety, we earned additional sockets for a next-generation Advanced Driver Assistance System with a major European car-maker; and
- in Smart Power, we recorded a major design win with a European market leader in a Power Steering-related application using our proprietary BCD9 technology.

Turning to our Industrial and Power Discrete group, net revenues totaled $430 million. Sales decreased by 6.8% on a sequential basis, largely due to sales to power supply components for PC applications as well as exposure to Euro-denominated revenues.

During the quarter, we recorded a number of achievements across our focus areas.
In energy management for portable equipment, we ramped production of an AMOLED power supply chip for Samsung’s S6 and we continued to gain traction with RF Integrated Passive Devices for smartphones and Internet of Things applications with leading global brands.

In power transistors, we have one of the broadest product portfolios of the industry. Here we gained several design wins: to name a few, we were awarded low-voltage MOSFETs in a power supply for game-console applications; we landed a win for high-voltage IGBTs for an induction-heating application with a major Chinese customer and we won a design for high-voltage MOSFETs in ultra-HD display applications.

In power conversion, ST revealed—together with Flextronics—the world’s first plug-in charging platform for mobile devices with zero no-load power, based on our multi-mode power-management controller; we also captured wins for high-voltage power converters from several mass-market customers in Greater China.

Turning now to EPS, revenues were $581 million and continued to reflect mixed dynamics. On one hand, MMS revenues decreased 3.7% on a sequential basis, better than the Company average.
On the other, EPS revenues in total decreased 12% on a sequential basis mainly due to the decrease of ST-Ericsson legacy products and lower DPG sales for consumer and imaging products.

EPS had a negative operating margin of 11.1%, including unused capacity charges, improving from negative 13.1% in the year-ago quarter mainly due to lower operating expenses and higher R&D funding. And, of course, EPS is not benefiting yet from favorable currency effects of about 3.8 points, due to hedging.

Despite the new product introductions in DPG, the decline of legacy products - including entry-level set-top box, camera modules and former ST-Ericsson products - continued to outpace the ramp of new product revenues in the first quarter.

During the quarter we made progress in ramping new families of innovative products: among these, we began delivering the latest Ultra-HDp60 quad-core Cannes and Monaco-family systems-on-chip ICs to a European customer.
We are working to reduce costs, largely in DPG. In that regard we made progress during the first quarter; we also transferred over 90 employees in Asia to a leading software company and partner of ours. And, as expected, we will exit from the IBM Technology Development Alliance at the end of this second quarter.

Turning to MMS, the group had a solid quarter with net revenues of $374 million, posting a sequential decrease of 3.7% and growing 8% year-over-year, building on the strong performance already achieved in 2014. In general-purpose microcontrollers, the richness of our portfolio is a pillar of our product and market leadership and a driver of our year-over-year growth in this area: today, we offer over 600 STM32 part numbers. In the first quarter, we further extended our product range with the STM32L4, which allows designers to get higher performance and larger memory without trading power consumption. We also recorded important STM32 wins with major customers: for example, one for a wireless accessory for tablets for a global brand, one in Samsung’s Galaxy S6 as a sensor hub, and two in a high-end fitness band for another important mobile and wearable player.
We also made important steps in secure microcontrollers. We joined forces with the Austrian company ams to launch a breakthrough reference design for secure contactless NFC transactions and mobile payments in the smallest phones and wearable devices; and we captured an NFC Tag design in a next-generation headset at a major audio-equipment OEM.

Looking at our product portfolio moving forward, key products driving growth for the second quarter include filters and protection devices as well as power discrete from IPD, touchscreen controllers and 6-axis motion MEMS from AMS, microcontrollers from APG, STM32 microcontrollers and the secure element from MMS. On the other hand, a large volume socket within DPG has been very recently postponed, reducing our expected revenues for this product group in the second and the next quarters.

In the second quarter we expect to increase our revenues by about 3.5% sequentially, with most of our product groups contributing. This outlook incorporates an estimated top line currency impact of about $16 million.
Gross margin is anticipated to increase by about 60 basis points to 33.8%, including existing hedging contracts significantly mitigating the positive impact from currency.

Our firm objective in 2015 continues to be to achieve very significant year-over-year improvement in our operating performance as we move towards our financial model.

My colleagues and I would now be happy to take your questions.