STMicroelectronics
Q2 Earnings Conference Call Remarks – Final
Tuesday, July 24, 2012
Carlo Bozotti, President and Chief Executive Officer

Thank you for joining us for our second quarter conference call.

(1. Key Points of Q2)

Let me share some **key points before going into a review of the quarter**:

First, net revenues and gross margin were in line with our guidance and we saw a significant improvement in our net results. However, in June, we did see a negative impact on our second quarter earnings as a result of the macro-driven changes in the market environment.

Second, we had an active quarter with respect to our product portfolio as you will hear from the level of new design wins and product ramps.

Third, we have set **three key priorities** with which we will manage the business during the second half of 2012 and beyond.

Priority number one is to gain market share – and we want it to be profitable market share gains. As part of this we want to continue to expand our customer base, which will also help reduce the risks in our business.

Priority number two is we are focused on moving our VLSI businesses, meaning our digital assets at ST, including ST-Ericsson, towards self-sustainability to drive improved financial performance.

Priority number three is we are focused on carefully managing our assets and investments and you can see this evidenced in our revised capex spending and in our net financial position remaining strong.

All these actions will enable us to improve our profitability and to enhance our flexibility to adjust to market changes.

(2. Q2 in detail)

Turning now to the **second quarter in detail**:

Revenues were up sequentially 6.5% to $2.15 billion and gross margin improved 470 basis points to 34.3%. We had expected the growth to be broad-based and it was, with all product segments reporting sequential growth even with the macro-driven change in customer demand in June.

Revenues from our wholly-owned businesses increased 4.4% on a sequential basis, with APG and AMM somewhat below our expectations while Digital and Power Discretes came in at or above our expectations.

AMM's second quarter net revenues increased 2.2% led by our analog and microcontroller applications.

Our automotive business grew sequentially 3.4%, driven by market share gains and growth in China, Japan and the US.

Digital revenues increased about 5% sequentially thanks to our set-top box products and despite a decrease in Imaging, due to the situation at specific customers, which has also significantly impacted the profitability of the Digital segment.

Power discrete saw 12.3% sequential growth in the quarter led by Power MOSFETs.

ST-Ericsson had been expecting low double-digit sales growth and came in higher at 19% as the NovaThor U8500 ModAp systems started to successfully ramp at major customers including Samsung and Sony Mobile Communications.

As I outlined at the start of the call, a key priority for the second half of the year is gaining market share – profitable market share growth. We had a number of new design wins in the quarter – healthcare and wellness, power management and energy savings, trust and security for instance. And we have a number of new product ramps during the second quarter.

We are winning for a number of reasons – breadth of our technology, internal manufacturing, lower power management capability – and others.
Let me begin with examples of our design wins in smart consumer applications.

On our MEMS and sensors business, I am proud to announce we ramped production of a new pressure sensor and an iNEMO module containing an integrated gyroscope and accelerometer for Samsung's latest and most advanced smartphone. Moreover, we have won many sockets for motion MEMS, temperature sensors and MEMS microphones.

We shipped in volume in the second quarter AMOLED drivers for smartphones and we have also enjoyed fast adoption of the new 40nm MPEG4 set-top box chips worldwide in Cable, Terrestrial, Satellite and IPTV markets.

In the trust and data-security marketplace, we announced that Wasion Group is using our NFC contactless interface and tamper-proof Secure Element in a smart meter that they will deploy in ChongQing, one of China's largest cities.

In the power-management and energy-saving sector, we started deployment of STarGRID Power Line Communication SoCs, in China, for new Smart Metering programs as well as collecting important design wins in the automotive marketplace for a range of body and powertrain applications in the US and in Europe.

Our discrete products also made progress: for example, our extra-low capacitance protection devices won sockets in high-speed applications with several leading smartphone and consumer-electronics manufacturers.

On top of new design wins, let me share important products that have now been launched:

First, we announced full production of our STM32 F0 microcontroller family at the beginning of the quarter and then a few weeks ago announced the new STM32 F3 family that combines exceptional analog peripheral integration with digital signal processing capability.

In MEMS, we also announced an accelerometer for safety applications and new gyros and gyro/accelerometer combos that are among the world's smallest. Small size and low power are consistent themes for ST; we also introduced a tiny antenna-sharing chip that will enable faster and more accurate location-based services while allowing Wi-Fi, Bluetooth and GPS receivers in a smartphone to share one antenna—saving space and reducing power consumption.

We also took an important step towards creating a unified processing platform, thanks to the recent combination of ST's strong, existing competences with those of the ST-Ericsson's application processor development team.

Turning now to our gross margin, our results were on track at 34.3%, improving 470 basis points sequentially, or 210 basis points excluding the one-time charge related to the NXP arbitration award last quarter. We benefited from a higher level of saturation, product mix and some currency benefits on the order of 30 basis points. We still are not optimally loaded, with about 70 basis points of unused capacity charges in the second quarter. And we are still running at less efficient levels from a manufacturing perspective.

Looking at our spending, overall operating expenses decreased by $34 million mainly driven by cost-realignment programs at ST-Ericsson. In combination with ST-Ericsson our goal is to deliver continuous improvement in spending levels throughout the remainder of 2012.

In the second quarter we saw a significant improvement in our net results, with a net loss of $75 million compared to a net loss of $176 million in the first quarter. Of course, substantial progress remains to be made. A critical component of our capability to improve our financial results is ST-Ericsson and the reduction of losses by two at ST-Ericsson, moving from Q1 to Q4 of this year, is on track.

(3. Review of key metrics)

At the beginning of my remarks I indicated that another key priority for the year is **careful management of our assets**. You may recall we started 2012 with the assumption of a much lower capex plan compared to 2011. In the first quarter we spent $125 million and in the second quarter $70 million. And last night we stated that with our current visibility we will reduce our capex plan by 25% this year compared to our original plan for 2012. Our focus will be on manufacturing improvements that bring productivity gains. So our spending will be in the range of $500 to $600 million for the full year 2012.

The careful management of our assets includes our cash, so with the reduction in capital expenditures, reduction in operating expenses, focus on profitable market share gains and moving our VLSI business to self-sustainability – all these steps should help us to substantially improve our free cash flow over time.

For 2012 our goal remains to be positive from a free cash flow perspective on a consolidated basis. In the first quarter we had a positive free cash flow, and in Q2 it was negative, including a large amount related to the NXP arbitration award payment. If you look at the first half in total it was a negative $31 million, however, it included the $60 million one-time payment to NXP. While we expect free cash flow to be negative in the third quarter we are on target to achieve our full year 2012 free cash flow goal.

(4. Market environment and Q3 outlook)

Now let me turn to the **market environment and our third quarter outlook**. If we look back, the first quarter was clearly the bottom of the inventory correction. In Q2 we started to see growth and our views on the third quarter when we spoke in April were based on strong bookings data. In May at our investor day in New York we indicated that bookings were still pretty good. At that point we continued to track solidly towards the mid-point of the Q2 sales range, if not even a little higher. Since then we have seen a change in customer sentiment and more volatility driven by macro-economic uncertainties.

Of course, trying to assess the potential impact of the macro environment on the third quarter is difficult as the uncertainty is high and visibility is more limited.

Nevertheless, we expect sequential revenue growth of about 2.5% at the mid-point, plus or minus 3 percentage points.

ST-Ericsson has indicated flat sequential revenues. Growth in the third quarter would be coming from ST's wholly-owned businesses with our new product momentum, notably in MEMS, Microcontrollers and Power MOSFET and IGBT.

We have a high level of confidence in our new products and the value they bring to customers.

With respect to the gross margin, we are expecting 35.3% plus or minus 1.5 percentage points including a similar level of unused capacity charges as in the second quarter.

(5. Conclusion)

To conclude, on the call today we have shared our key areas of focus: with respect to revenues, our objective is to deliver innovative designs and products in a timely fashion to gain market share in several strategic product families; to carefully manage our balance sheet during this expected market softness in the second half and to evaluate and be selective in our investments with the goal to exit the year with a net financial position similar to or better than at the end of 2011. And most importantly, we are focused – both at ST and at ST-Ericsson - on aligning our resources with the respective market opportunities. In the third quarter we expect to significantly reduce the level of operating expenses compared to the second quarter. Our goal is to become a much leaner company, better able to navigate the highs and lows of our industry, reduce our earnings volatility and significantly improve our financial performance.

My colleagues and I would now like to take your questions.