

# UBS Investment Research

## MEMC Electronic Materials

### Reduced Overhang From TPG's 63% Holding Upcoming

#### ■ Overhang from high ownership by TPG being reduced

Last night MEMC announced that it registered with the SEC for its largest shareholder, Texas Pacific Group, to sell up to 59.8M MEMC shares at a proposed price of \$11.97 (0.7% discount to yesterday's close). TPG owns 142M or 63% of MEMC's outstanding shares. Following completion of the sale, TPG would own only 40% (37% if the over-allotment is exercised).

#### ■ Expect improved independence going forward

Since TPG owns over 50% of MEMC, the company is considered "controlled" and is not required to have a majority of independent directors, a separate corporate governance committee, or an independent compensation committee. Following TPG's stock sale, MEMC will establish these required groups.

#### ■ Likely increase in management flexibility viewed positively

We believe MEMC could now consider more strategic moves, including acquisitions. We view MEMC as a successful turnaround story (25% OM, \$283M CFO in 2004) and look for increased traction in 300mm demand as a potential catalyst in 2H05.

#### ■ Valuation: Maintain N2 Rating; increasing PT from \$12 to \$14

Previously, we valued WFR applying an 8.5x multiple to our CY05 EBITDA estimate of \$347M. This multiple was a 10% discount to the 9.4x average at which its peer group traded in 2000 to reflect the TPG overhang. With the overhang reduced we increased our multiple to the peer avg. of 9.4x to arrive at our \$14 PT.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	781	1,028	1,101	1,165	-
EBIT	143	259	302	319	-
Net income (UBS)	117	224	231	247	-
EPS (UBS, US\$)	0.53	0.90	1.02	1.06	-
Net DPS (UBS, US\$)	0.00	0.00	0.00	0.00	-

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-3.7	25.2	27.4	27.3	-
ROIC (EBIT) %	-3.6	58.4	48.6	41.8	-
EV/EBITDA x	18.2	7.3	7.8	7.2	-
PE (UBS) x	-7.3	10.5	11.8	11.4	-
Dividend yield %	0.0	0.0	0.0	0.0	-

Source: UBS adjusted EPS is stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$12.05 on 03 Feb 2005

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## Global Equity Research

Americas

Electric Components & Equipment

Rating **Neutral 2**  
**Unchanged**

Price target **US\$14.00**  
**Prior: US\$12.00**

Price **US\$12.05**

RIC: WFR.N BBG: WFR US

4 February 2005

#### Trading data

52-wk. range	US\$13.25-7.39
Market cap.	US\$2.50bn
Shares o/s	208m
Free float	37%
Avg. daily volume ('000)	630
Avg. daily value (US\$m)	7.2

#### Balance sheet data 12/05E

Shareholders' equity	US\$0.67bn
P/BV (UBS)	4.1x
Net cash (debt)	US\$0.05bn

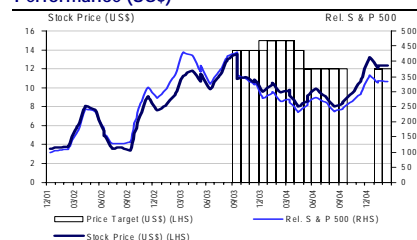
#### Forecast returns

Forecast price appreciation	+16.2%
Forecast dividend yield	0.0%
Forecast stock return	+16.2%
Market return assumption	8.3%
Forecast excess return	+7.9%

#### EPS (UBS, US\$)

	12/05E			12/04
	From	To	Cons.	Actual
Q1E	-	0.24	0.24	0.16
Q2E	-	0.24	0.25	0.20
Q3E	-	0.26	0.28	0.27
Q4E	-	0.28	0.30	0.26
12/05E	-	1.02	1.08	
12/06E	-	1.06	1.24	

#### Performance (US\$)



Source: UBS

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#### ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 4

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## TPG ownership to decline from 63% to 40%

- TPG currently owns 142 M shares of MEMC's 224M total outstanding shares (including 16M warrants). In the registration statement filed with the SEC, TPG is offering 52M MEMC shares, and up to 7.8M more to cover any over-allotments. Including the over-allotment option, the 59.8M share offering represents 27% of MEMC's market capitalization. The transaction is subject to SEC approval.
- After the completion of the transaction, TPG ownership will be reduced from 63% (142M shares) to 40% (90M shares), assuming the over-allotment option is not exercised (37% if exercised).
- The registration statement indicates a proposed maximum offering price of \$11.97 per share, a 1% discount to yesterday's \$12.05 close.
- The timing of the transaction is unknown at this time, but it is expected to take place following SEC approval.
- Following an initial period of market saturation, MEMC's stock should benefit from the proposed sale of MEMC shares held by TPG, because it will boost the liquidity of the shares.

**\$11.97 proposed maximum offering price**

**Share liquidity should improve**

**Table 1: Texas Pacific Group – Sales of MEMC shares**

Date of Stock Sale	May-03	Feb-04	Feb-05 to Mar-05 ?
# of shares sold	15.3 M	34.0 M	52 M to 59.8 M
Price shares sold at	\$10.00	\$9.70	\$11.97 (proposed)
Ending Share Balance	176.0 M	142.0 M	82.2 M to 90.0 M
% of shares owned	79%	63%	37% to 40%

Source: Company reports

## Increased Independence of the Board of Directors and Associated Committees Viewed Positively

In the company's prospectus filed last night, it was mentioned that under the New York Stock Exchange rules, a company is considered "controlled" when one shareholder holds over 50% of the company's equity, which is MEMC's case. Under these circumstances, a company is not required to have a majority of independent directors, a separate corporate governance committee, or an independent compensation committee. Once the sale of TPG shares is completed, MEMC will establish these required groups, which we believe will enhance corporate governance.

The company's prospectus also mentioned that Samsung and Texas Instruments each represented over 10% of the company's sales in the first 9 months of 2004.

In addition, the company's top 10 customers on a combined basis amounted to 61% of sales in the 9 months ending Sep 30, 2004.

### Price Target Increased to \$14; Look For Traction in 300mm Demand to be Potential Catalyst in 2H05

One of our concerns when we initiated coverage on MEMC was the high ownership by TPG and the likelihood of a sale in the near term. Our \$12 price target incorporated this overhang as we used an 8.5 multiple to our CY05 EBITDA estimate of \$347M. This 8.5 multiple was a 10% discount to the average 9.4x at which MEMC's peer group traded in 2000, a peak year for the group. With the TPG overhang now significantly reduced, we are now using the full 9.4x multiple and have increased our price target to \$14 from \$12.

Going forward, we look for evidence of increased traction in 300 mm wafer demand, which could become a catalyst for the shares in 2H-05.

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#### ■ MEMC Electronic Materials

MEMC, headquartered in St Peters, MO, is the world's only publicly traded pure-play silicon wafer manufacturer. The company produces and sells silicon wafers for the semiconductor industry, and is fourth in market share. MEMC sells its products to most semiconductor device manufacturers. Products include prime polished, epitaxial and test/monitor wafers in diameters ranging from 100mm to 300mm. The company operates nine plants that are strategically located close to the major semiconductor markets in the U.S., Europe, and Asia. Texas Pacific Group, a private equity company, controls MEMC.

#### ■ Statement of Risk

MEMC's business is subject to the cyclicalities of semiconductor demand, which can result in share price volatility. There is a risk of overcapacity of 300mm wafers in the future, which can result in price and margin erosion. In addition, continued investment in R&D and infrastructure are needed to ensure the long-term viability of the business which could limit EPS upside.

MEMC shares have low liquidity, as 63% are held by the company's controlling shareholder Texas Pacific Group (TPG). Potential share sales by TPG could increase the supply of shares in the market and limit appreciation in MEMC's share price. MEMC has historically used stock options to compensate its employees. As highlighted in our valuation section, we estimate that the company's potential stock option expense in CY06 is -\$0.04 or 4% of our official \$1.06 EPS estimate.

## ■ Analyst Certification

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### UBS Investment Research: Global Equity Ratings Definitions and Allocations

UBS rating	Definition	UBS rating	Definition	Rating category	Coverage <sup>1</sup>	IB services <sup>2</sup>
<b>Buy 1</b>	FSR is > 10% above the MRA, higher degree of predictability	<b>Buy 2</b>	FSR is > 10% above the MRA, lower degree of predictability	<b>Buy</b>	36%	32%
<b>Neutral 1</b>	FSR is between -10% and 10% of the MRA, higher degree of predictability	<b>Neutral 2</b>	FSR is between -10% and 10% of the MRA, lower degree of predictability	<b>Hold/Neutral</b>	53%	35%
<b>Reduce 1</b>	FSR is > 10% below the MRA, higher degree of predictability	<b>Reduce 2</b>	FSR is > 10% below the MRA, lower degree of predictability	<b>Sell</b>	11%	29%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 31 December 2004.

### KEY DEFINITIONS

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

**Predictability Level** The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

**Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

**Rating/Return Divergence (RRD)** This qualifier is automatically appended to the rating when stock price movement has caused the prevailing rating to differ from that which would be assigned according to the rating system and will be removed when there is no longer a divergence, either through market movement or analyst intervention.

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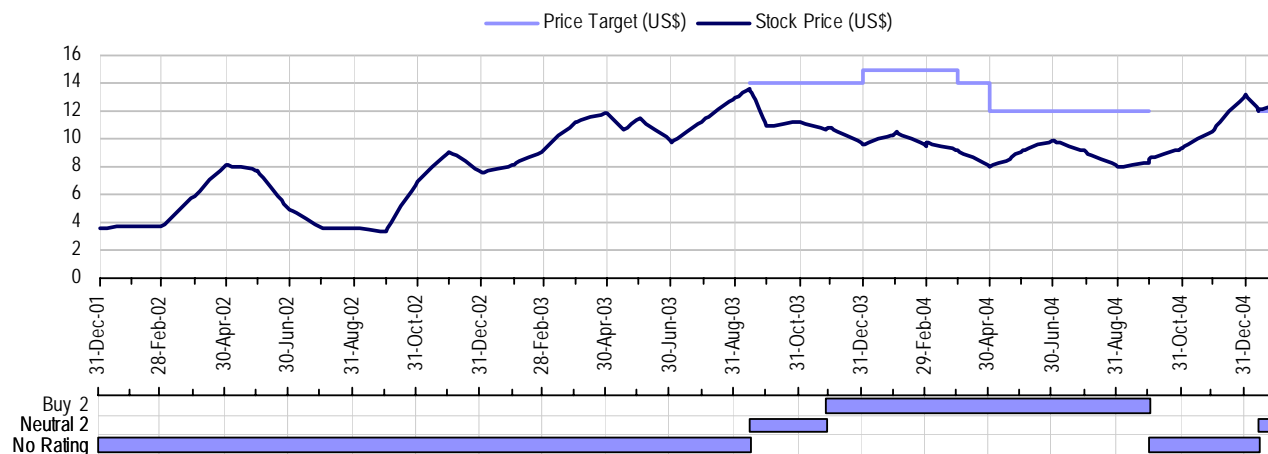
### Companies mentioned

Company Name	Reuters	Rating	Price
<b>MEMC Electronic</b> <sup>2,4,6,16</sup>	WFR.N	Neutral 2	US\$12.30

Price(s) as of 2 February 2005. Source: UBS.

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### MEMC Electronic Materials (US\$)



Source: UBS; as of 2 February 2005.

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