

UBS Investment Research

MEMC Electronic Materials

Misses 1Q, But 2H05 Looks Solid

■ Misses 1Q revenue and EPS

MEMC reported sales of \$258M and proforma EPS of \$0.23, versus consensus expectations of \$268M and \$0.24. The shortfall was primarily due to issues at two of its customers. However, we believe this integration issue has been resolved and sales to those customers will likely increase in 2Q05.

■ Expect average selling prices (ASPs) to improve in 2H05

Despite a 4% q/q revenue decline MEMC's gross margin was down only 40 bps q/q. Had it not been for the two customer-specific issues, which resulted in a poorer mix (lower sales of higher-price, higher-margin 300mm wafers), blended pricing and gross margin would have been higher in 1Q05. We expect blended ASPs and margins to improve in 2H05 on better pricing and mix.

■ Maintaining EPS estimates

We view the company's 2Q revenue guidance for growth of 2-5% q/q as conservative. With semiconductor inventories cleared, we estimate wafer demand to continue to improve (up 6-7% YOY), which should drive higher utilization rates and pricing (up 3% YOY). In addition, we expect a richer mix of 300mm wafers and continued polysilicon shortages to contribute to stronger pricing in 2H05.

■ Valuation: Maintain Buy 2, \$17 target price

Our target price is based on applying a 13x multiple to our CY06 EPS estimate of \$1.34.

Highlights (US\$m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	781	1,028	1,108	1,256	-
EBIT	143	259	302	399	-
Net income (UBS)	117	225	272	312	-
EPS (UBS, US\$)	0.53	0.90	1.10	1.34	-
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	27.3	31.8	-
ROIC (EBIT) %	-3.6	58.4	48.9	52.7	-
EV/EBITDA x	18.2	7.3	7.5	5.6	-
PE (UBS) x	-7.3	10.5	10.6	8.6	-
Dividend yield %	0.0	0.0	0.0	0.0	-

Source: Company accounts, Thomson Financial, UBS estimates. 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\$11.62 on 28 Apr 2005 19:35 EDT

Stephen Chin

Analyst
stephen.chin@ubs.com
+1-212-713 4111

Marisa Hernandez, CFA

Associate Analyst
marisa.hernandez@ubs.com
+1-212-713 4086

Global Equity Research

Americas

Electric Components & Equipment

Rating **Buy 2**
Unchanged

Price target **US\$17.00**
Unchanged

Price **US\$11.62**

RIC: WFR.N BBG: WFR US

29 April 2005

Trading data

52-wk. range	US\$14.56-7.39
Market cap.	US\$2.43bn
Shares o/s	209m
Free float	37%
Avg. daily volume ('000)	1,674
Avg. daily value (US\$m)	21.2

Balance sheet data 12/05E

Shareholders' equity	US\$0.71bn
P/BV (UBS)	3.7x
Net cash (debt)	US\$0.07bn

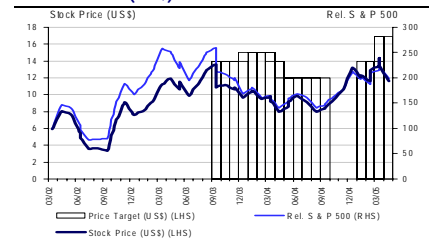
Forecast returns

Forecast price appreciation	+46.3%
Forecast dividend yield	0.0%
Forecast stock return	+46.3%
Market return assumption	8.6%
Forecast excess return	+37.7%

EPS (UBS, US\$)

	From	12/05E To	Cons.	12/04 Actual
Q1	0.24	0.23	0.24	0.16
Q2E	0.26	0.25	0.26	0.20
Q3E	0.29	0.29	0.30	0.27
Q4E	0.31	0.32	0.32	0.27
12/05E	1.10	1.10	1.13	
12/06E	1.34	1.34	1.30	

Performance (US\$)



Source: UBS

www.ubs.com/investmentresearch

This report has been prepared by UBS Securities LLC

ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 5

UBS does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. Customers of UBS in the United States can receive independent, third-party research on the company or companies covered in this report, at no cost to them, where such research is available. Customers can access this independent research at www.ubs.com/independentresearch or may call +1 877-208-5700 to request a copy of this research.

Misses 1Q revenue and EPS

MEMC reported sales of \$258M and proforma EPS of \$0.23, versus consensus expectations of \$268M and \$0.24. The shortfall was primarily due to issues at two of its customers, and to a lesser extent, a continued soft wafer start environment and pricing pressure during the quarter.

GAAP EPS was reported at \$0.34 because of a tax credit.

Table 1: MEMC – Quarterly Results from Operations (\$'s in millions)

	1Q 04	2Q 04	3Q 04	4Q 04	1Q 05	2Q 05E Guidance
Sales	\$229	\$256	\$275	\$268	\$258	\$263M to \$271M
Sequential Growth	12%	12%	8%	-3%	-4%	2% to 5%
Gross Margin \$'s	\$73	\$87	\$111	\$98	\$93	
Gross Margin %	32%	34%	40%	37%	36%	Flat to up Slightly
SG&A	-\$17	-\$18	-\$18	-\$19	-\$18	
R&D	-\$9	-\$9	-\$9	-\$10	-\$11	
Operating Income \$	\$47	\$60	\$84	\$69	\$64	
Operating Income %	21%	23%	30%	26%	25%	Flat to up Slightly
EBITDA \$'s	\$57	\$70	\$95	\$80	\$77	
EBITDA Margin %	25%	28%	35%	30%	30%	
Proforma EPS	\$0.16	\$0.20	\$0.27	\$0.27	\$0.23	
Shares	222	221	223	222	224	

Source: Company reports

Issues at customers have been resolved

We believe the issues at the two customers have been resolved, and expect sales to those customers to increase in 2Q05. At one customer, MEMC said there was a “false alarm”: there were yield issues in a new line which the customer originally thought were related to MEMC’s wafers. That turned out not to be the case, but MEMC’s sales to that customer suffered as a result. At another customer, there were wafer integration issues in a new line. MEMC has figured out how to fix this problem for the customer, and sales to that client are expected to increase. While the two issues have been addressed and resolved, the second quarter could also be slightly hurt as it will likely take some time to ramp up sales to those customers to their prior levels. The impact on revenues from the issues with those two customers amounted to \$10M in foregone sales in 1Q05, which equates to the quarter’s sales shortfall versus guidance of \$268 M.

2Q guidance looks conservative; solid outlook for 2H-05

We view the company’s 2Q revenue guidance for growth of 2-5% q/q and flat to slightly higher margins as conservative. With semiconductor inventories cleared, we estimate wafer demand to continue to improve (up 6-7% YOY), which should drive higher utilization rates and pricing (up 3% YOY). In addition, we

expect a richer mix of 300mm wafers and continued polysilicon shortages to contribute to stronger pricing in 2H05.

Pricing pressure reported in 1Q; should be less in 2Q

Management indicated that pricing pressure in 1Q05 was in the “low single digits”, and that it was worse for smaller (less than 300mm) diameter wafers. For 2Q05, management also expects some pricing pressure (but less than in 1Q05), but believes it will be able to offset its impact through cost reductions and lower operating expenses.

Capacity utilization rate in the mid-80s

MEMC indicated that its capacity utilization rate was in the mid-80s in 1Q-05, with 300mm wafer capacity utilization being above that average. The company expects capacity utilization to improve in 2Q05 and beyond, as wafer starts improve, particularly since semiconductor inventories appear to have cleared.

300mm expansion plans on track

MEMC reported that it achieved 300 mm capacity of 150,000 wafer starts per month in 1Q05, as expected. In addition, the company said it is on track to achieve 200,000 wafer starts per month in the summer of 2005.

Expect pricing and margins to improve

Despite a 4% q/q revenue decline MEMC’s gross margin was down only 40 bps q/q. Had it not been for the two customer-specific issues, which resulted in a poorer mix (lower sales of higher-price, higher-margin 300mm wafers), blended pricing and gross margin would have been higher in 1Q05. We expect blended ASPs and margins to improve in 2H05 on better pricing and mix.

Potential polysilicon shortages could provide further pricing power

We believe potential polysilicon shortages could enhance MEMC’s ability to negotiate wafer prices with customers in the second half of the year. Management indicated that, as of yet, it has not seen wafer shortages in the industry due to raw material (polysilicon) shortages. However, it added that this could be the case later in the year, as wafer demand increases and solar panel demand of polysilicon continues to increase.

In addition, MEMC is analyzing alternatives on how to best benefit from potential polysilicon shortages. We believe those alternatives may include a project to increase the company’s involvement with the solar panel industry.

Balance sheet continues to improve

MEMC continues to generate solid cash from operations. During 1Q05, the cash balance increased by \$24M to \$116M, and debt decreased by \$4M to \$136M,

for a net debt position of \$20M, or \$0.09 per share (down from \$0.22 per share in the prior quarter).

Days receivables decreased by 1 to 46 days during the quarter, as account receivables declined more than revenues. Days inventories increased by 7 to 74 days in the first quarter, on a \$7M increase in inventories.

Table 2: MEMC – Selected Balance Sheet Metrics (\$'s in millions)

	1Q 04	2Q 04	3Q 04	4Q 04	1Q 05
Cash and Equivalents	\$141	\$129	\$103	\$92	\$116
Debt	\$272	\$242	\$203	\$140	\$136
Net Debt	\$132	\$112	\$99	\$48	\$20
Net Debt Per Share	\$0.59	\$0.51	\$0.44	\$0.22	\$0.09
Cash From Operations	\$48	\$82	\$46	\$212	\$73
Capex	\$26	\$46	\$26	\$52	\$54
Free Cash Flow	\$21	\$36	\$20	\$161	\$19
Accounts Receivable	\$119	\$139	\$152	\$141	\$131
AR DSO's	47	49	50	47	46
Inventory	\$123	\$113	\$120	\$128	\$135
Inventory Days	71	60	66	67	74

Source: Company reports

■ 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 cyclical nature 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 are 34% owned by the 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.

■ Analyst Certification

Each research analyst primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.

Required Disclosures

This report has been prepared by UBS Securities LLC, an affiliate of UBS AG (UBS).

For information on the ways in which UBS manages conflicts and maintains independence of its research product; historical performance information; and certain additional disclosures concerning UBS research recommendations, please visit www.ubs.com/disclosures.

UBS Investment Research: Global Equity Ratings Definitions and Allocations

UBS rating	Definition	UBS rating	Definition	Rating category	Coverage ¹	IB services ²
Buy 1	FSR is > 10% above the MRA, higher degree of predictability	Buy 2	FSR is > 10% above the MRA, lower degree of predictability	Buy	37%	30%
Neutral 1	FSR is between -10% and 10% of the MRA, higher degree of predictability	Neutral 2	FSR is between -10% and 10% of the MRA, lower degree of predictability	Hold/Neutral	52%	32%
Reduce 1	FSR is > 10% below the MRA, higher degree of predictability	Reduce 2	FSR is > 10% below the MRA, lower degree of predictability	Sell	11%	25%

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 March 2005.

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.

EXCEPTIONS AND SPECIAL CASES

US Closed-End Fund ratings and definitions are: Buy: Higher stability of principal and higher stability of dividends; Neutral: Potential loss of principal, stability of dividend; Reduce: High potential for loss of principal and dividend risk.

UK and European Investment Fund ratings and definitions are: Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Reduce: Negative on factors such as structure, management, performance record, discount.

Core Banding Exceptions (CBE): Exceptions to the standard +/-10% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Companies Mentioned table in the relevant research piece.

Companies mentioned

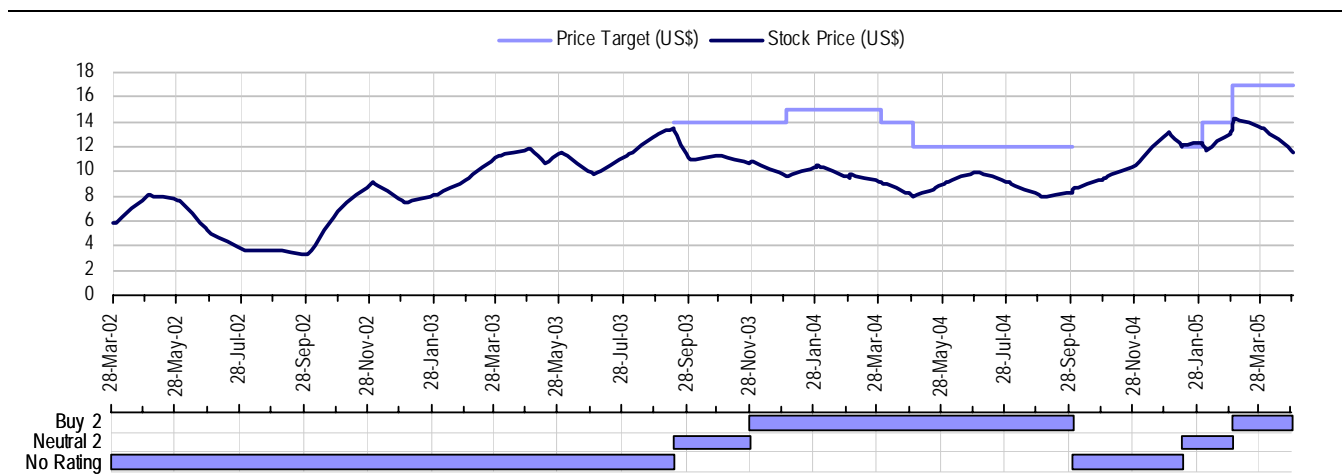
Company Name	Reuters	Rating	Price	Price date/time
MEMC Electronic ^{2,4,5,16}	WFR.N	Buy 2	US\$11.62	28 Apr 2005 19:35 EDT

Source: UBS. EDT: Eastern daylight time.

2. UBS AG, its affiliates or subsidiaries has acted as manager/co-manager in the underwriting or placement of securities of this company or one of its affiliates within the past three years.
4. Within the past three years, UBS AG, its affiliates or subsidiaries has received compensation for investment banking services from this company/entity.
5. UBS AG, its affiliates or subsidiaries expect to receive or intend to seek compensation for investment banking services from this company within the next three months.
16. UBS Securities LLC and/or UBS Capital Markets LP makes a market in the securities and/or ADRs of this company.

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

MEMC Electronic Materials (US\$)



Source: UBS; as of 28 April 2005.

Note: On October 13, 2003, UBS adopted new definition criteria for its rating system. (See 'UBS Investment Research: Global Equity Ratings Definitions and Allocations' table for details.) Between January 11 and October 12, 2003, the UBS ratings and their definitions were: Buy 1: Excess return potential > 15%, smaller range around price target; Buy 2: Excess return potential > 15%, larger range around price target; Neutral 1: Excess return potential between -15% and 15%, smaller range around price target; Neutral 2: Excess return potential between -15% and 15%, larger range around price target; Reduce 1: Excess return potential < -15%, smaller range around price target; Reduce 2: Excess return potential < -15%, larger range around price target. Prior to January 11, 2003, the UBS ratings and definitions were: Strong Buy: Greater than 20% excess return potential, high degree of confidence; Buy: Positive excess return potential; Hold: Low excess return potential, low degree of confidence; Reduce: Negative excess return potential; Sell: Greater than 20% negative excess return potential, high degree of confidence. Under both ratings systems, excess return is defined as the difference between the FSR and the one-year local market interest rate.

Global Disclaimer

This report has been prepared by UBS Securities LLC, an affiliate of UBS AG (UBS).

Head Office: UBS Limited, 1 Finsbury Avenue, London, EC2M 2PP, UK Phone: +44-20-7567 8000

Local Office: UBS Securities LLC, 1285 Avenue of the Americas, New York, NY 10019 Phone: +1-212-713 2000

This report has been prepared by UBS AG or an affiliate thereof ("UBS"). In certain countries UBS AG is referred to as UBS SA.

This report is for distribution only under such circumstances as may be permitted by applicable law. It has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein, except with respect to information concerning UBS AG, its subsidiaries and affiliates, nor is it intended to be a complete statement or summary of the securities, markets or developments referred to in the report. The report should not be regarded by recipients as a substitute for the exercise of their own judgement. Any opinions expressed in this report are subject to change without notice and may differ or be contrary to opinions expressed by other business areas or groups of UBS as a result of using different assumptions and criteria. UBS is under no obligation to update or keep current the information contained herein. UBS, its directors, officers and employees (excluding the US broker-dealer unless specifically disclosed under required disclosures) or clients may have or have had interests or long or short positions in the securities or other financial instruments referred to herein, and may at any time make purchases and/or sales in them as principal or agent. UBS (excluding the US broker-dealer unless specifically disclosed under Required Disclosures) may act or have acted as market-maker in the securities or other financial instruments discussed in this report, and may have or have had a relationship with or may provide or has provided investment banking, capital markets and/or other financial services to the relevant companies. Employees of UBS may serve or have served as officers or directors of the relevant companies. UBS may rely on information barriers, such as "Chinese Walls," to control the flow of information contained in one or more areas within UBS, into other areas, units, groups or affiliates of UBS.

The securities described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. Options, derivative products and futures are not suitable for all investors, and trading in these instruments is considered risky. Past performance is not necessarily indicative of future results. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related instrument mentioned in this report. For investment advice, trade execution or other enquiries, clients should contact their local sales representative. Neither UBS nor any of its affiliates, nor any of UBS' or any of its affiliates, directors, employees or agents accepts any liability for any loss or damage arising out of the use of all or any part of this report. **Additional information will be made available upon request.**

United Kingdom and rest of Europe: Except as otherwise specified herein, this material is communicated by UBS Limited, a subsidiary of UBS AG, to persons who are market counterparties or intermediate customers (as detailed in the FSA Rules) and is only available to such persons. The information contained herein does not apply to, and should not be relied upon by, private customers. **Switzerland:** Distributed by UBS AG to persons who are institutional investors only. **Italy:** Should persons receiving this research in Italy require additional information or wish to effect transactions in the relevant securities, they should contact Giubergia UBS SIM SpA, an associate of UBS SA, in Milan. **South Africa:** UBS South Africa (Pty) Ltd (incorporating J.D. Anderson & Co.) is a member of the JSE Securities Exchange SA. **United States:** Distributed to US persons by either UBS Securities LLC or by UBS Financial Services Inc., subsidiaries of UBS AG; or by a group, subsidiary or affiliate of UBS AG that is not registered as a US broker-dealer (a "non-US affiliate"), to major US institutional investors only. UBS Securities LLC or UBS Financial Services Inc. accepts responsibility for the content of a report prepared by another non-US affiliate when distributed to US persons by UBS Securities LLC or UBS Financial Services Inc. All transactions by a US person in the securities mentioned in this report must be effected through UBS Securities LLC or UBS Financial Services Inc., and not through a non-US affiliate. **Canada:** Distributed by UBS Securities Canada Inc., a subsidiary of UBS AG and a member of the principal Canadian stock exchanges & CIPF. A statement of its financial condition and a list of its directors and senior officers will be provided upon request. **Hong Kong:** Distributed by UBS Securities Asia Limited. **Singapore:** Distributed by UBS Securities Singapore Pte. Ltd. **Japan:** Distributed by UBS Securities Japan Ltd to institutional investors only. **Australia:** Distributed by UBS AG (Holder of Australian Financial Services Licence No. 231087) and UBS Securities Australia Ltd (Holder of Australian Financial Services Licence No. 231098) only to "Wholesale" clients as defined by s761G of the Corporations Act 2001. **New Zealand:** Distributed by UBS New Zealand Ltd.

© 2005 UBS. All rights reserved. This report may not be reproduced or redistributed, in whole or in part, without the written permission of UBS and UBS accepts no liability whatsoever for the actions of third parties in this respect.

