

AIXTRON AG

Analyst Earnings Conference Call

First Half 2009 Results

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Prepared Remarks

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The spoken word applies

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Investor Relations  
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## **Operator**

- Good morning, ladies and gentlemen, and welcome to the AIXTRON H1/2009 results conference call.
- Today's call is being recorded and I would like to hand you over to Mr. Guido Pickert, Director of Investor Relations at AIXTRON, for opening remarks and introductions.

## **Slide 2 – Welcome [GP]**

- Good morning everyone and thank you for attending today's call.
- With us today are Paul Hyland, President and Chief Executive Officer of AIXTRON, and Wolfgang Breme, Executive Vice President and Chief Financial Officer of AIXTRON.
- As the operator indicated, this call is being recorded by AIXTRON and is considered copyright material. As such, it cannot be recorded or re-broadcast without express permission. Your participation in this call implies your consent to this taping.
- As at previous results conference calls, I trust that all participants have our results presentation slides, page two of which contains the usual Safe Harbor statement. I will therefore

not read it out, but would like to point out to you that it applies throughout this conference call.

- This call is not being immediately presented via Webcast or any other medium; however the Company reserves the right to place an audio file of the recording on its website at some point after the call.
- Let me now hand you over to Paul Hyland, AIXTRON's President & CEO, to start the actual presentation.
- Paul?

**Slide 2 – Welcome [PKH]**

- Thank you Guido.
- Ladies and gentlemen, good afternoon to those of you calling in from Europe, and good morning to those joining us from the US. I would like to welcome you, on behalf of AIXTRON's Executive Board, to our H1/2009 results presentation.
- As usual, let me start with some initial remarks on our current outlook.
- We have seen a remarkable improvement in outlook since we spoke to you in March of this year when we were not even able to offer a revenue guidance, beyond a projected break-even at €170m for the year.
- When I next spoke to you, during our Q1/2009 conference call in May, I was able to be more cautiously optimistic – following some more positive signals from our customers, to the point of being able to give you a revenue and profit guidance for 2009 of €200m to €220m revenues and 10 to 11% EBIT.
- Today, I am happy to tell you, that despite the ongoing recessionary effects on the general economy, our end customers seem to be gaining in confidence once more.

- That increase in customer confidence, that we first reported to you in May, has continued and been further confirmed in the form of increased order and quotation activities since.
- As a result of this increased activity, we feel able to raise our 2009 guidance to a new revenue range of EUR 230-250m and an EBIT range of 12-13%.
- I will get back to our current outlook later on in this presentation, when I will explain our guidance model to you.
- If we can now turn to slide 3 of our presentation ...I would like to talk you through the stages of the market recovery I believe we are experiencing now.....

**Slide 3 – Phases of Market Recovery [PKH]**

- We introduced this slide to you in May's Q1 presentation and used it to set out the 3 key stages of recovery that we were looking for.
- It is self-evident from the Q2 order intake we will talk about later, that Q1 did mark the bottom of a five quarter run of declining order intake following the industry's inventory de-stocking activities and consequently low utilization rates, starting back in 2008.
- Q2 not only marked the return of essential replenishment capital investments but was also notable for the specific investments being made by significant new investors, drawn in, we believe, by the increased strategic attraction of the LED market potential.
- We have, in effect, gone from incidents of 20% customer production utilization, as recently as in Q1 of this year, to 100% utilization, driven by demand, in a period of a little over 3 months.
- The final part of our market recovery model requires unequivocal evidence that the demand we are seeing now is

sustainable and at this point we firmly 'believe' it is, but must continue to gather evidence 'confirming' that it is.

- If you would now turn to slide 4; I would like to introduce a new slide here to try to scope the nature and volume of the LED backlighting market for TVs.

## Slide 4 – LED TV backlighting market development [PKH]

- With the rapid increase of LED TV shipments and the consequent rise in demand for high brightness LEDs, orders for AIXTRON LED manufacturing equipment have progressively gained momentum throughout this year.
- Consequently, I think it would be worthwhile trying today to put some detail into the volume and timing potential of this market.
- The numbers we will show you here are independent of any other backlighting applications and because of the very early stage of development this application is at, there is still a wide variety of opinion on this issue – but I will try to summarize the latest thinking on this area.
- First of all let's clarify what the LEDs are used for:
- The LED televisions that you can buy today are still LCD TVs. The difference is the light source that illuminates the image on the Liquid Crystal Display from behind the screen.
- LEDs will effectively replace the incumbent CCFL light source used previously, which can be likened to a fluorescent light source.

- I won't go into the many visual, environmental and power consumption benefits, but needless to say, the recent performance and cost of ownership improvements have triggered a huge interest in this new light source.
- There are two ways of delivering an LED solution for TVs;
- You can either have a strip array of LEDs around the edge of the TV frame in conjunction with an arrangement of light-guides delivering an effective and uniform backlight source.
- This is called 'Edge-lit backlighting' and we assume could employ c. 400-600 white LEDs, depending on the size of the television.
- A 40" LED Edge-lit Television for example contains about 450 LEDs.
- The alternative approach is, in effect, a matrix of either white or RGB (Red, Green & Blue) LED modules across the whole rear surface of the LCD screen, which has the benefit of more direct color lighting and the possibility to provide 'local dimming' and even higher contrast ratios.

- The two approaches to delivering an LED matrix backlight are either a 'Direct-lit' backlight or 'RGB backlit' and could use up to 1,200 LEDs in a 16:9 configuration on a 42" TV.
- There is speculation that 'RGB backlit' may be the eventual preferred approach for the 'premium' displays to be offered to consumers in the future.....This has yet to be proved.
- There are a variety of opinions as to how the split between 'Edge-lit' and 'Backlit' might develop – the most common speculation I hear; is 80:20 in favor of 'Edge-lit' TVs, which makes sense when you see the very high quality of the 'Edge-lit' TVs already being sold.
- I would now like to quantify the LCD TV market, i.e. the total addressable market or 'TAM':
- In 2008, depending on the source of information you use, between 85 and 103 million LCD TVs were shipped, with the 5 leading brands being Samsung, LG, Sony, Sharp and Philips.
- You can also see that the market share for LED backlit LCD TVs was estimated to be only about 2% in 2008.
- Canaccord Adams, the more optimistic of the three commentators we have used for this slide, expects the market

share of LED backlighting to climb to 5% in 2009, 10% in 2010 and as high as 35% by 2012.

- LEDinside's most recent report suggests a more cautious opinion of only 11% by 2012, but to be fair to LEDinside; their opinion was formed before the extraordinary increase in commitment we have seen over recent months.
- Nobody, as yet, has published a definitive opinion as to when a 100% penetration rate will be reached, but I've heard speculation that varies between 2015 and 2020.
- If we see the same rapid adoption surge that we are currently seeing in notebook backlighting, it could be possible that we see a date closer to 2015, rather than 2020. Time will tell.
- Let me now try to put some comparative scale to this opportunity.....
- A very rough "rule of thumb" market size comparison is that today about a billion mobile phones made each year consume about 10 billion LEDs.
- If, as projected by LEDinside, the LCD TV market grows to c. 175 million LCD units to be sold in 2012, and if the average number of LEDs used was say; 600, and we assume an

eventual 100% penetration, then 105 billion LEDs would be required to meet that eventual demand.

- However, as you can see, the opinions we are citing here vary on the likely penetration of LEDs by 2012 between 11-35%.
- Although we are at a very early stage of the development of LED TV backlighting, it is undoubtedly true that during Q2 we have seen a large number of branded and OEM manufacturers pushing power-saving LED-backlit LCD TVs with thinner form factors and a better picture quality, with equally strong marketing of the environmental and power saving benefits.
- While Samsung Electronics has clearly established a strong early position in the “LED TV” market by launching a range of LED TVs, its competitors; including Sony and LG Electronics have also been launching new LED TV models in Q2/2009.
- US TV maker VIZIO, the number 1 LCD TV brand in the US, has also recently announced that its first LED TVs would be available in September.
- We are already seeing evidence of aggressive pricing with the manufacturers’ aiming to increase their market share at this early ‘premium’ price stage.

- But what do all these positive end-market developments mean to us?
- To be truthful with you, there are so many variables in terms of chip size, number of LEDs required, yield, throughput, etc., that it is difficult to give you a precise number of systems that will be needed to serve this market, other than to say it is highly likely that we will have healthy demand, possibly for several years to come.
- A very recent and very comprehensive research report by Canaccord Adams has suggested that by 2012 the market could need an additional 300-650 MOCVD systems which confirms my point of how difficult it is to be precise at this stage.
- However, internally, we are in the process of planning to be able to cope with the most aggressive of the possible scenarios.
- For now, let's move to slide five, where I will touch on the highlights of our Q2 performance in sequential comparison to the previous quarter, namely Q1/2009.

**Slide 5 – Financial Highlights [PKH]**

- Our quarterly revenues increased by 23%, over the previous quarter to reach EUR 56.7m in Q2/2009.
- Thanks, principally to the increased sequential volume, the (“recurring”) quarterly absolute EBIT increased by 23% to EUR 4.7m or 8%.
- Although the absolute reported EBIT was 38% lower than in Q1, please remember, that there were two specific operational ‘events’ in Q1/2009 that positively contributed EUR 3.8m or 8% to the reported result then, which we have taken out here for comparison with Q2.
- Driven by recent increased investment demand for LED applications, we are pleased to report an increased order intake in Q2/2009 at EUR 57.9m, 85% higher than in Q1/2009 which was EUR 31.2m.
- This increased Q2 order intake and the positive outlook we are seeing in Q3, confirm our opinion that Q1 did indeed mark the low point in order demand.

- Order backlog now stands at EUR 109.4m, 9% up from the end of Q1.
- Free Cash Flow after the dividend payment is down to EUR 8.0m, a decrease by 23% compared to the EUR 10.4m of the previous quarter.
- Cash & Cash Equivalents, including cash deposits, is at EUR 84.4m, 3% up from the EUR 81.6m we had at the end of Q1 of 2009, despite the shareholder dividend payment in the quarter of EUR 8.2 million.
- Let me now walk you through slide 6, a summary comparison of the first half performances of 2009 and 2008.

**Slide 6 – Financial Highlights [PKH]**

- The total H1/2009 revenues were down 20% to EUR 102.9m from EUR 128.2m in H1/2008.
- Nevertheless, the gross margin significantly improved in the first half year period to 43%, 4pp up on H1/2008.
- H1/2009 EBIT came in lower at EUR 12.3m, with a 12% margin compared to EUR 17.6m and 14% margin in H1 2008.
- Our Net Result came out at EUR 8.8m, or EUR 0.10 per share, a decrease of 33% compared to the same period last year.
- Our Equipment Order Intake for H1/2009 was 44% lower than H1/2008 at EUR 89.1m.
- Our order backlog at the end of Q2 stood at EUR 109.4m, down 34% from the EUR 165.1m we saw in the first half of 2008.
- The ongoing negative memory market environment led to our silicon system order intake in H1/2009 being virtually zero.
- Consequently, 97% of our Order Backlog is for Compound Semiconductor systems, of which EUR 96m we believe will be converted into revenues within 2009.

- Liquidity remained high in the first half year, with the cash inflow from the sale of our building in Aachen in Q1 largely offsetting the dividend payment to shareholders in May.
- Free Cash Flow of EUR 18.4m (including changes in Cash Deposits) was up 12% on the H1/2008 Free Cash Flow figure of EUR 16.5m, by EUR 1.9m year on year.
- Finally, our Cash and Cash Equivalents position at June 30 remained very strong at EUR 84.4 million, 4% down year on year.
- Let us now move directly to Slide 7, and have a more detailed look at business developments in the end customer markets.

**Slide 7 – Business Development (PKH)**

- If we first look at our Compound system business in the left hand column ...
- Despite the weak first quarter and thanks to the recovering second quarter, our Compound Equipment revenues were only down 15% year on year at EUR 88.7m, and represent 86% of our total revenues.
- Our Compound Equipment order intake still decreased by 41% year on year to EUR 88.4m, but with some very strong signals that the speed of adoption of applications such as LED backlighting has increased significantly in the last 3 months and is likely to remain so for the remainder of the year.
- Additionally, albeit relatively small in comparison to backlighting, street lighting purchase orders of USD 120m, which we saw awarded to customers in Q2, in my view, mark the transition from a 'possible' new application to an 'emerging' application.
- But now let me turn to our other end market; systems serving Silicon Semiconductor producers.
- Total Silicon revenues were at a very low level of EUR 4.2m in the half year but the 58% reduction of Silicon Semiconductor

revenues year on year reduces in significance when looking at the development of total absolute revenues.

- Our Silicon Equipment order intake represents less than 1% of the total equipment order intake during H1/2009, due to the reduced demand of equipment for the memory market.
- Unfortunately, we believe that there is little evidence to suggest that this situation will improve during the course of this year and our current forecast reflects that.
- Separately, the development work being conducted on next-generation memory and logic equipment continues, with customer demonstrations and film development work being done within the company's research labs and at customers' facilities.
- This work, combined with the involvement of Sunnyvale staff in next generation Compound and other group nano-technology projects, means that the team in Sunnyvale continue to make a positive and valuable contribution to the group's objectives.
- The longer term strategic value of this combined group is more evident when you compare the evolving status and convergence of the two technologies.

- It is not difficult to imagine that the Compound 'new application' cyclicality will eventually become more 'technology node' / 'Moore's Law' driven, as is the case with Silicon applications, as the Compound applications reachable are of higher volume and mainstream in nature.
- Coupled with this market development and the inevitable Cost of Ownership focus, will come an increasing desire for a progression from Batch processing towards higher volume manufacturing processes.
- What this means is an eventual need for more standardized and integrated processes as well as a larger degree of automation. We have a wealth of experience in these areas within the Sunnyvale team.
- The influence and contribution of larger customers will also change and influence the nature and requirements of the market.
- These transitions are familiar challenges to the silicon team in Sunnyvale, which is why they are being increasingly used in Compound design and engineering projects.
- Finally, the convergence process works both ways: The 'Moore's Law' pressure I referred to earlier, is also drawing in

more complex compound material solutions into the Silicon arena as performance, shrinkage and cost pressures increase.

- I believe that we have the undisputed most experienced group of Compound material deposition experts in the industry, with more than 25 years of experience, which will become an increasingly valuable asset as this convergence process gains momentum.
- Let me now hand you over to Wolfgang Breme, our CFO, for a more detailed look at the first half year numbers.
- Wolfgang?

**Slide 8 - Group Income Statement [WB]**

- Thank you Paul and good afternoon and good morning to all of you.
- Before we go into the details of our H1/2009 and Q2/2009 Financials, just a short comment on our English report.
- Unfortunately, we had to correct a few numbers in the report we published this morning and you might have already downloaded it before we were able to publish the corrected version. If you look at the Q2 numbers in our Consolidated Income Statement it should read 1,566 in “Other operating income” instead of 4,568; 2,348 instead of 5,368 for “Other operating expense”; and the “Proceed from Disposals of Fixed Assets” in the Cash Flow Statement should read 7,910 instead of 5,410. Please make sure you have the latest version of the report.
- But let's get back to the presentation.
- Again, I'm able to present another set of strong financials despite the headwinds which had an impact on our H1 revenues in comparison to 2008.
- Slide 8 summarizes our H1 and Q2 income statement in a year-on-year comparison.

- As Paul mentioned already, our revenues are down by 20% in H1/2009 to EUR 102.9m from EUR 128.2m in H1/2008.
- Also the quarterly revenues decreased by 14% in Q2/2009 to EUR 56.7m from EUR 65.6m in Q2/2008.
- This development was expected by us and is in line with the guidance we gave earlier in the year.
- More importantly it is worthwhile to focus on the relative gross margins which improved in the first half of 2009 to 43% compared to 39% in H1/2008.
- This was principally due to a more favorable revenue mix with a higher percentage of final customer system acceptances, especially in the first quarter.
- It must also be said that our inherently flexible business model also played a major part in helping to keep the relative cost of sales figure lower, while revenues were decreasing.
- Due to our high degree of outsourcing of non-IP-critical operations, the majority of AIXTRON's costs of sales are direct cost which helps us to cope with significant fluctuations of our revenues – upwards and downwards of course.

- It is also true to say that the gross margin benefited from a stronger US-Dollar with an average exchange rate of USD 1.33 to the Euro in the first half year, compared to USD 1.53 during H1/2008.
- Even more importantly, I'm pleased to comment on another strong EBIT performance of the group.
- In H1/2009 we held EBIT at 12% despite the reduction of revenues compared to 14% EBIT in H1/2008. Also, the quarterly performance was in line with guidance and reached 8%.
- In comparison to 2008 I have to mention that in 2008 we benefited from significant income gains from our currency instruments as the US Dollar was extremely weak at this time. This was not the case in 2009 so far.
- Selling expenses were reduced significantly because of lower regional and volume related variable sales commissions.
- Administrative expenses remained stable year on year.
- If you do the maths, you will see a significant increase in research and development expenses.

- This largely reflects not only our planned investments in new products, but the EUR 16.9m R&D number in H1 was inflated by one specific project, which increased the R&D expenses by EUR 1.6m in the first quarter.
- Of course, as I'm sure you will understand in today's market environment, we had decreased interest income in the year which makes up the difference between EBIT and Result before taxes.
- The tax rate is, as expected, 31%, virtually the same as in the previous year.
- Net income stands at EUR 8.8m for H1/2009 and EUR 3.3m for Q2/2009 which relates to 10c per share and 4c per share, respectively.
- Let us now move on to Slide 9, our balance sheet slide.

**Slide 9 – Group Balance Sheet**

- AIXTRON's financial position is as strong as ever.
- The company recorded no bank borrowings as of June 30, 2009.
- The equity ratio increased to 74% as of June 30 from 68% as of December 31, 2008, principally due to higher retained earnings and lower inventories.
- This underlines the profitability of the group whereas the latter is an indicator for the reduced business volume growing through our facilities right now.
- Cash and Cash equivalents increased by 20% to EUR 84.4m compared to EUR 70.5m as of December 31, 2008.
- This indicates a positive cash generation ratio and includes of course the dividend payment to our shareholders in May 2009.
- The value of property, plant and equipment decreased to EUR 32.8m principally due to the sale of our Aachen headquarters building in January of this year.
- The increase in recorded goodwill from EUR 58.7m as of December 31, 2008 to EUR 59.1m as of June 30, 2009 resulted solely from currency translation.

- The value of other intangible assets decreased from EUR 10.3m in December to EUR 8.8m principally due to depreciation.
- Trade receivables decreased to EUR 26.0m in June in line with the reduced business volume.
- More importantly, this strong balance sheet leaves room for further growth in the future.
- On top of the operational funding, we have sufficient approvals from our shareholders to increase our share capital if the need would arise.
- AIXTRON is a growth business in the mid to long term view and the tools are in place to support this financially if necessary.
- Let us now move on to Slide 10 which shows the development of cash flows.

**Slide 10 – Group Cash Flow Statement**

- 82% of the cash flow from operating activities was turned to free cash flow.
- In addition, it is worth mentioning that the cash flow from investing activities contains EUR 7.0m in H1/2009 which is on deposits with a maturity exceeding 3 months as of June 30, 2009.
- This included, our change in cash and cash equivalents is EUR 13.9m compared to EUR 11.2m in H1/2008.
- We consider our cash position doesn't contain any excess bearing our future growth opportunities in mind.
- Let us now move on to Slide 11, our proven business development slide.

**Slide 11 – 24 Month Business Development [WB]**

- Our Order Intake, depicted on the top chart on this slide, had been declining steadily throughout the year 2008, and that continued in Q1/2009, which was no surprise.
- We are now happy to show you a substantial uptrend in order intake, confirming that Q1 did mark the bottom of the decreasing investment cycle of our customers.
- In Q2/2009 we have received various purchasing commitments of greater volume, higher than initially expected, which – as Paul said before – could mark the beginning of a period of stabilization in the markets.
- Nevertheless, thanks to our flexible setup, we are able to ramp-up our production with whatever speed market recovery may occur.
- As you can see in this slide, our Equipment Order Backlog, shown in the middle chart of this slide, peaked one to two quarters later than our Intake, towards the middle of last year and, consequently, dropped to a low point in the first quarter of this year.

- This build-up of Backlog in the early to mid point of last year, was mainly due to the fact, that the orders received in the prior period consisted of multiple and scheduled orders, leading to a more progressive development of revenues over several quarters peaking in Q4 of last year.
- The revenues shown at the bottom of slide 7 are also low compared to the 2008 quarters, but not unexpectedly.
- Not unexpectedly revenues picked up in Q2/2009 to EUR 56.7m already reaching the level of 2007 revenues prior to the last investment cycle in our industry.
- We see this trend continuing if the current more positive sentiment in our markets proofs sustainability,
- Allow me now to move on to Slide 12 and have a look at our Revenue Analysis.

**Slide 12 - Revenue Analysis [WB]**

- The breakdown of our revenues on slide 12 speaks for itself.
- Compound made up 86% of our revenues in H1/2009 with 4% revenues coming from Silicon revenues.
- It is important to mention that the silicon markets we are serving are significantly down year on year and the overall situation is extremely difficult for all equipment companies serving the Memory market, as you will have read in other recent company results.
- But we are nevertheless prepared for the next upturn of the memory markets and will bring our new technologies into the markets whenever the market rebounds.
- The remaining 10% of our revenues were spare part & service revenues.
- In terms of end applications, 73% of our systems are used to manufacture LEDs, for the backlighting of laptops, monitors, TVs and other devices.
- From our perspective the LED applications we see emerging are increasingly entering new markets and leave us in an

excellent position as the dominant equipment supplier for MOCVD equipment.

- 4% are used to manufacture parts for telecom/datacom applications such as mobile phones and 3% of our systems are used to produce consumer and optoelectronic devices such as lasers.
- The percentage of display related products was relatively high in H1 with 14%. This is principally because the total revenue of the Gen 3.5 large-area deposition Plastic Logic tool was recorded within Q1/2009.
- Geographically, the large majority of customers, namely 75% continue to operate in Asia. This was 12 percentage points below the 87% of H1/2008, mainly reflecting the inventory reduction which took place until Q1/2009. This process was particularly evident in Asia.
- The relatively high 19% European share of our revenues in the first half of 2009, reflects the Q1 revenue recognition of the Plastic Logic System I mentioned before.
- Ladies and gentlemen, thank you very much for your attention. You will find more financial information in the backup slide of

this presentation and in our half yearly report. Of course I will be happy to answer your questions in the Q&A session.

- But before that I will now hand you back to Paul for his concluding remarks.

**Slide 13 – Guidance [PKH]**

- Thank you Wolfgang.
- Let's move on now to slide 13, where you can see our revised guidance model.
- We enter the third quarter of the year with a much more positive customer sentiment, increasing momentum of LED technology demand, very high utilization rates, and an improved visibility of demand from LED manufacturers.
- This enables us to increase our guidance for fiscal year 2009:
- We believe that in 2009, AIXTRON can deliver revenues in the range of EUR 230-250m and an EBIT margin in the range of 12-13%.
- This guidance is based on the following assumptions:
- Actual revenues in H1/2009 came in at EUR 103m, represented by the light blue part of the pie chart.
- We anticipate approximately EUR 10m of additional spares & service revenues in the last six months of 2009, - which is the grey piece of the pie chart.
- Our Order Backlog stood at EUR 109m as per June 30, of which we believe, EUR 96m is convertible into revenues in the

remaining months of 2009, as represented by the dark blue color.

- As at June 30, we required EUR 21m more shippable purchase orders within Q3 to be able to reach the lower end of our revenue guidance, i.e. EUR 230m.
- In order to realize the upper end, i.e. EUR 250m, we needed an additional EUR 41m of order intake within Q3/2009.
- I would now like to finish up on Slide 14 with a few key 'take-aways' from this presentation.

**Slide 14 – Key Takeaways [PKH]**

- The new LED ventures that we spoke of in Q1 and the speed at which they have converted ‘intent’ into firm purchase orders illustrate the increased strategic interest and commitment in LED technology and markets that we have spoken of in earlier calls.
- The arrival of these strategically minded players has not only added momentum to this recovery cycle but in that they enter the market with substantial and sustainable balance sheets, they are more likely to maintain a longer term investment view and therefore significantly contribute towards the further development and critical mass of the LED industry.
- The effect of the substantial and focused investment moves made in the first half of this year, by the major TV manufacturers in particular, has created genuine demand from consumers and consequently spread to nearly all manufacturers which we believe will create the longer-term sustainability we are looking for as equipment suppliers.
- These are the main factors contributing to the rapid – and quicker than generally expected – market recovery we are enjoying today.

- We have spoken before of “potential government support for ‘green’ lighting applications” as a mid-term prospect. I think that it still remains ‘mid-term’ in reality, but developments in Q2 suggest that it may have edged nearer to the boundary with ‘short-term’ opportunities, with the recent commitments made by the Chinese government towards specific LED street lighting projects.
- The significance of ‘real’, rather than ‘token’ street lighting contracts being awarded is not in the absolute contract value, but in the emergence of yet another application, because it is the potential diversity of ‘real’ LED applications that will carry the industry forward when viewed in the long-term.
- Despite relatively fragile consumer confidence and, as yet, intangible economic recovery, we are in the fortunate position of benefiting from a growing industry trend, a strong business model, market & technology leadership and a very solid financial position.
- Financially; we have no debt and we do not anticipate needing to take on debt.
- We have sufficient cash for our anticipated capex needs, even after paying out our dividend in May.

- We continue to have a very flexible operating cost base, outsourcing c. 90% of our manufacturing whilst retaining most our key final assembly and test work internally.
- A comparison of the revenue levels and operating profits over the last three quarters provides strong evidence of the high operating leverage we have developed and demonstrates the financial benefits of that operational flexibility.
- We will continue to keep our R&D spending on a high level to further strengthen the foundation of our future business
- In summary.....
- We have seen clear indications of a strong market recovery for our LED business and we have been able to demonstrate profitable evidence of the benefits of having a flexible operational business model.
- I'm pleased to say that the outlook for the remainder of the year, and beyond, remains very positive.
- And securing our future; we continue to have a very active product development pipeline.

- Consequently, we feel that we are well positioned to be able to profit from the short, medium and long-term opportunities we see developing in the markets we serve.
- Thank you all very much for your attention.
- We will now be happy to answer any questions you may have to the best of our abilities, so I will pass you back to the operator.
- Operator?

## Operator

- Thank you gentlemen.
- Let me now open the conference call for the Q&A session.

### Operator

Thank you gentlemen. Let me now open the conference call for the Q&A session. [Operator Instructions] The first question comes from Sandeep Deshpande of JP Morgan. Go ahead with your question.

**<Q - Sandeep Deshpande>**: Hi, Paul. Congratulations.

**<A - Paul Hyland, President and Chief Executive Officer>**: Hi.

**<Q - Sandeep Deshpande>**: Just a couple of questions. I mean you have possibly seen some of the orders which have been indicated in the – for some of your competitors in the market. Would you have any comment on how the overall order outlook is looking in the current quarter and overall in the second half of the year? And I have one follow-up.

**<A - Paul Hyland, President and Chief Executive Officer>**: Good afternoon Sandeep.

I think you're referring to the fact that there was a reference made on Monday's call by Veeco, to orders taken in July?

I think you know that as a matter of policy we don't comment on order intake in the quarter.

But, what I would say is that we continue to see very positive discussions out there both in terms of order activities and quotations.

So I think the improving trend we've seen in Q2 we would expect to see a similar trend maybe even for the next couple of quarters.

**<Q - Sandeep Deshpande>**: And would you say that you will continue to maintain your – I mean share you had in the LED global – I mean there must be a dual market in 2009, in 2008?

**<A - Paul Hyland, President and Chief Executive Officer>**:

Well of course, as you know, market share is measured by revenue and I don't have any doubt that we'll continue to be the major player in that market.

I think it's important you talk about revenue market share rather than orders in the door.

You know that we have a strict internal policy: we only report orders for which we have a signed contract, whatever the agreed deposit is and a firm delivery date.

So we're very happy with our current position.

I don't see that anything significantly changed at any time in the last three months.

**<Q - Sandeep Deshpande>**: Thanks a lot.

### Operator

Next question comes from Jed Dorsheimer of Canaccord.

**<Q - Jed Dorsheimer>**: Hi. Thanks and congratulations on the solid quarter and outlook.

Couple of questions. I guess first, could you explain your – the criteria around your bookings in terms of what type of deposit and what timeframe it has to be shippable within for you to consider that a booked product?

**<A - Paul Hyland, President and Chief Executive Officer>**: I will try to answer that and maybe Wolfgang may want to add a comment to this but basically with all orders we like to start the customer discussions on the principle that we would receive a deposit with the order and up to 90% at point of shipment and typically 10% on the final acceptance on the customer's side.

We like to start those discussion with maybe a 50% deposit, 40% on shipment, 10% on final acceptance. We will of course discuss that level and negotiate with customers but generally speaking we're looking for a substantial portion of the figure at the point of shipment.

Now of course it will vary from customer to customer and we've already accepted that as the customer base becomes bigger that may change over time – as the size of customers increases then its likely that deposits may get less but nevertheless we're still able to command fairly significant deposits with orders and indeed you can see that, Jed, if you look at our balance sheet - you can see customer deposits is in there.

**<Q - Jed Dorsheimer>**: Great. And then [indiscernible] then we were yeah.

**<A - Paul Hyland, President and Chief Executive Officer>**:

An order. If we haven't received the signed contract, whatever the agreed deposit is and the firm delivery date, we will not record that as an order. So you can assume we have a 'gray' order book.

If for example, (whoever the customer is) if they ordered ten systems but only firmed up delivery for the first five systems, we would only tell you about an order intake for five and put five in the order backlog.

When eventually that customer either paid the additional deposit or agreed to the delivery date we would then report that further five.

So you can assume we already have orders for which we have not yet satisfied those criteria and that's been a policy we've had probably for about the last seven or eight years.

**<Q - Jed Dorsheimer>**: Great. Just trying to reconcile some differences there and that's quite helpful. Thank you.

Just looking at Slide 11, we're seeing a nice trend in uptick on the LED side and I know that your policy is not to comment on Q3 and not asking you to do that but would it be safe to assume that – should we assume that this ramp up is going to be relatively linear with that trend curve?

Or do you think that – or should we expect a step function difference?

Any qualitative commentary that you might be able to provide might be helpful.

**<A - Paul Hyland, President and Chief Executive Officer>**:

I think I said earlier on the call, whereas we could only see maybe one month in January, we're back to sort of two quarters.

I think for the next two quarters the outlook continues to look very positive.

We clearly know what sort of order levels we're talking about in Q3 but even the discussions for Q4 remain quite positive.

All I could say at this stage is that we will not be reporting order intake less than Q2 in Q3.

**<Q - Jed Dorsheimer>**: Great. And was wondering if you might be able to comment on the configuration of some of these tools that are being shipped without I guess maybe in – from a qualitative perspective would you say that the vast majority of the tools that are being ordered and shipped are being configured in a two inch, four inch or six inch configuration?

Could you give any commentary or colour on that?

**<A - Paul Hyland, President and Chief Executive Officer>**: Well I know that you already know from your own research – I read in your recent report which I thought was very good by the way I must say that Jed.

But the majority of people out there still are making LEDs using two inch wafers.

Although, there is definitely a trend amongst the volume manufacturers to move into three and four

Inch wafers.

We are currently shipping both; two and four inch wafer configuration systems.

You also asked about six inch wafers – you've probably seen an announcement from us recently where we had a press release on a project we had with SemiLEDs on six inch wafers but at the moment there is no significant six inch LED application systems yet going out, but there's quite a number of customers who are interested in that as the next step forward.

But nothing in the immediate future.

**<Q - Jed Dorsheimer>**: Great. And any I guess breakdown between Showerhead and Planetary?

**<A - Paul Hyland, President and Chief Executive Officer>**:

Well we don't give that breakdown, but probably last year it was fairly equal – with slightly more Planetary products in the field, but I mean we're in a very good position with what we can offer.

We actually ship common platform systems, which have the ability to deliver either planetary or showerhead technologies.

So the customer's choice of technology depends really what the customer's trying to do or in some cases what the customer's familiar with. But still both systems are making a significant contribution.

**<Q - Jed Dorsheimer>**: Great. And one last question and I'll get back in the queue. The EBIT guidance, the increased guidance that you've given for the year, what exchange rate are you assuming in that guidance?

**<A - Wolfgang Breme, Executive Vice President and Chief Financial Officer>**: Hi Jed.

**<Q - Jed Dorsheimer>**: Hello.

**<A - Paul Hyland, President and Chief Executive Officer>**: We're assuming for our budget and forecasting exercise it's \$140.

**<Q - Jed Dorsheimer>**: Great. I'll pass it on and Paul looking forward to seeing you in the U.S. here shortly.

**<A - Paul Hyland, President and Chief Executive Officer>**: Yes indeed, we will look forward to that.

**Operator**

At the moment there seem to be no further questions. [Operator Instructions] The next question comes from Bill Ong of Merriman.

**<Q - Bill Ong>**: Yes. Congratulations on a solid quarter, gentlemen.

**<A - Paul Hyland, President and Chief Executive Officer>**: Good morning, Bill.

**<A - Wolfgang Breme, Executive Vice President and Chief Financial Officer>**: Hi, Bill.

**<Q - Bill Ong>**: Good afternoon. What percentage of 2Q orders came from existing customers versus new customers that are entering or learning how to manufacture LEDs? My question is really centered around the new customers that are likely to over order more tools where their lack of experience to get best-in-class LED yields and thus will need to buy more tools to meet unit demand needs. As these new customers gain experience and improve yields to industry average, they will have "excess" capacity and thus less need purchase equipment near term. Is that a concern for Aixtron?

**<A - Paul Hyland, President and Chief Executive Officer>**:

Well, first of all, Bill, we're getting orders from both existing and new customers.

If we look back at the sort of mix of customers we had in Q1..... I don't think it's any secret to say that Taiwan suffered particularly badly in Q1 and many of those guys there saw a significant reduction in demand in Q1 in Taiwan.

And however we had a significant increase in customers coming in from Korea.....in Q2 we've seen both a resurgence of demand from Taiwan and it's continued from Korea.

We know that there are some fairly significant new players– many of whom are going through their own learning curve.

But it's too early to say what the relationship is between the systems going out and the likely forward demand.

Needless to say there's still a lot more potential market penetration to go before we're going to get to any sort of a full capacity for us. ..

**<Q - Bill Ong>**: My second question's more on the supply chain.

**<Q - Bill Ong>**: What's your current supply chain capacity levels? In other words how much revenue of systems are you able to ship before you start to need to expand your needs as well as your supply chain needs?

**<A - Paul Hyland, President and Chief Executive Officer>**: I don't see immediate need for any significant investment.

You have to remember nearly 90% of our manufacturing's already outsourced. We've been working at the business of outsourcing and supplier selection for probably six or seven years now. So it's not a new game to us.

We could see when we started to see that the initial investments for backlighting, back about 12 months ago - with the difficulty everybody has in projecting - we looked very closely at what could be the worst possible case.....what might we have to make to meet customer demand needs.

So we've been on the case now for probably six or nine months and looking at a variety of things, which includes increasing the supply base, reducing the manufacturing time internally.

At the moment we don't have any major obstacles that could prevent us meeting the needs of the market.

Now clearly in Q1 there was a sudden, very sudden, demand. I think probably everyone experienced the same issues. I know certainly that Veeco reported something similar, but I think we're through that now and we're working hard at trying to anticipate sort of the worst case scenario - but no significant show-stoppers have yet emerged.

**<Q - Bill Ong>**: Okay. So if I understand you it sounds like the supply chain has enough capacity head count in light of the current recession to expand the need to support this up tick in orders going forward for many quarters out.

**<A - Paul Hyland, President and Chief Executive Officer>**: As we stand here today, Bill; - Yes.

**<Q - Bill Ong>**: Great. Thank you very much.

**<A - Paul Hyland, President and Chief Executive Officer>**: Okay.

## **Operator**

Next question comes from Malte Schaumann [ph] from SES Research [ph].

**<Q - Malte Schaumann>**: Hi. Good afternoon, gentlemen.

**<A - Paul Hyland, President and Chief Executive Officer>**: Hi.

**<Q - Malte Schaumann>**: Just a short question on your development of the gross margins. I mean it was expected that you're going to see a margin growth from Q1 into Q2.

Do you expect that you are able, at the current exchange rate of \$140, slightly above, to be able to come back to gross margins of 42, 43% in quarters three and four?

**<A - Paul Hyland, President and Chief Executive Officer>**: Well, could be.

Hello, Herr Schaumann

It should be possible, yes.

But of course it's a combination of product mix per customer, final acceptances, etc. but of course we are targeting gross margins above the 40% mark.

That's what we are striving for, clearly.

**<Q - Malte Schaumann >**: Okay. And do you see a good chance that 41% maybe on the second quarter? What's kind of lowered you in the fiscal year?

**<A - Paul Hyland, President and Chief Executive Officer>**: Yes.

**<Q - Malte Schaumann >**: Okay. That's it for the moment. Thanks.

**<A - Paul Hyland, President and Chief Executive Officer>**: Thank you.  
**Operator**

We have another question of Sandeep Deshpande of JP Morgan.

**<Q - Sandeep Deshpande>**: Hi. Just a question on cost structure. I mean that given that your revenues are likely to increase substantially on the back of these – the ordering dates that you're seeing. How do you see your cost structure coming – particularly in terms of your operating costs having to scale to meet the revenue?

**<A - Wolfgang Breme, Executive Vice President and Chief Financial Officer>**: Sandeep, if you go back to last year think you get a pretty clear impression. Our operating expenses are not varying to a big extent. We will have increased selling costs because of - as I mentioned - the sales commission. If certain markets pick up where we work with partners, we will have, I believe, comparable research and development expenses in the first half and second half also. So this is more or less independent from the absolute revenue number. And I expect that, beside this, the S G and A expenses also should be relatively stable. So we don't see, currently, a big increase in costs moving forward with higher volume. Because if you see the guidance it is still way below last years, or even a Q4 level. So we don't see that we have to increase our costs in general.

**<Q - Sandeep Deshpande>**: Sorry to clarify, actually. If I say actually more than looking at least year, Wolfgang, I mean if you say that, I mean, looking with respect to your Slide Four, and I mean how the number of the machines could be required for a much larger penetration of LED in the TV backlighting. I mean if revenues are much larger than what people are teasing about, my question was would you say the R&D, you would increase the R&D or sales beyond – I mean sales commissions, etcetera.

**<A - Wolfgang Breme, Executive Vice President and Chief Financial Officer>**: It's quite a question of scale, what we are talking about. If we would have huge increases in volume going forward there will be increases in operating expenses, that's pretty sure and kind of a step function. But the leverage, the increased profitability on higher volumes should be significant. That's part of our business model. The operating expenses should not grow at the same percentage, at the same scale as the revenue line because with the increasing number of machines, also the standardization of the equipment we ship is increasing significantly. And so there shouldn't be increased requirements, for instance, to expand our research and development activities. Of course we are aware to increase something, for example our service activities. But service is included in our Cost of Sales and therefore Part of Gross Margin. Surely, we have to extend our service networks if the number of installed pieces of equipment is moving further up in the future. But as said, R&D or administration should be relatively stable going into the future.

**<Q - Sandeep Deshpande>**: And Paul, one last question on the new customers. I mean in terms of the new customers coming into this industry. I mean how do you see the ramp up of the orders? I mean they have been using VCR [ph] there could be

large numbers of orders coming through in the next 18 to 24 months. I mean have these new customers begun talking these big large numbers of you already? Or are you talking about a longer-term plan here?

**<A - Paul Hyland, President and Chief Executive Officer>:**

Well Sandeep, we wouldn't of course discuss conversations we're having with specific customers.

But you can be sure that all of the major names that are being talked about are actively engaged in looking at this market, not surprisingly.

Now I think you have to be very careful in reading all of the website news that comes out of Asia, because there are always one or two extra zeros in the numbers they predict.

But nevertheless most of the new people ..... that is the major new customers coming in, .....their balance sheets almost determine that they won't have short-term investment strategies. They don't come in and go out. Typically these guys are working on anything from 12 to 24 months development plans and they're unlikely to be phased by short-term changes.

So of course most of the discussions we have with those guys are based around long-term partnerships with them and will involve bigger quantities.

The biggest challenge many of the people face is just the speed at which they can access - or get access to - compound semiconductor skill-sets in order to ramp their current productions up.

At the moment, most of the discussions we're having are very positive.

**<Q - Sandeep Deshpande>:** Thank a lot.

**<A - Paul Hyland, President and Chief Executive Officer>:** You're welcome.

**Operator**

Your last question comes from Howard Abiera [ph] of One Investment [ph]. Please go ahead with your question.

**<Q - Howard Abiera>:** Good afternoon and congratulations. As first question, can you please remind us what is the time lag between the shipping and the final acceptance, please?

**<A - Paul Hyland, President and Chief Executive Officer>:** Yes, good afternoon.

Typically our lead times are in the range of four to six months. We've reduced them from a few years ago when it used to be nine to 12 months and today, four to six months is typically enough to be able to meet, I'd say, 99% of the customer delivery needs.

However, in Q1 of this year when we started to suddenly get very rapid orders, those lead times went out, but we're already beginning to see them now come back in.

A good clue to understanding the demand profile would be my comments about the order backlog: I said of the total Q2 order backlog of 109 million, 96 million of it is due out this year, and that sort of directly reflects what customers are asking for.

<Q - Howard Abiera >: Thank you.

<A - Paul Hyland, President and Chief Executive Officer>: You're welcome.  
Operator? Perhaps at this point unless there's any other questions?, operator?...

**Operator**

No further questions.

**Paul Hyland, President and Chief Executive Officer**

Okay. I would I first of all thank everyone for attending the call and of course we can follow up afterwards with any further answers to questions you may have, please feel free to call us. We'll be very happy to come back to you and trying to expand on anything you've heard here today.

But for the time being, thank you all very much indeed for your interest today..

Thank you and Good bye until next time.

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