

# Tower Semiconductor's (TSEM) CEO Russell Ellwanger on Q1 2014 Results - Earnings Call Transcript

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## Executives

Russell Ellwanger - Chief Executive Officer

Oren Shirazi - Chief Financial Officer

Noit Levi – Director of Investor Relations

## Analysts

Cody Acree - Ascendant Capital Markets

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Tower Semiconductor Ltd. ([TSEM](#)) Q1 2014 Earnings Conference Call May 15, 2014 10:00 AM ET

## Operator

Ladies and gentlemen, thank you for standing by. Welcome to the TowerJazz First Quarter 2014 Results Conference Call. (Operator Instructions) As a reminder, this conference is being recorded, May 15, 2014.

Joining us today are Mr. Russell Ellwanger, TowerJazz's CEO; and Mr. Oren Shirazi, CFO. I would now like to turn the conference over to Ms. Noit Levi, Director of Investor Relations and Public Communications. Ms. Levi, please go ahead.

## Noit Levi

Thank you. Before we begin, I would like to remind you that some statements made during this call may be forward-looking and are subject to uncertainties and risk factors that could cause actual results to be different from those currently expected. These uncertainties and risk factors are fully disclosed in our Forms 20-F, F-4, F-3 and 6-K filed with the Securities and Exchange Commission, as well as filing with the Israeli Securities Authority. They are also available on our website. TowerJazz assumes no obligation to update any such forward-looking statements.

Now, I'd like to turn the call to our CEO, Mr. Russell Ellwanger. Russell, please go ahead.

## Russell Ellwanger

Thank you, Noit, and welcome to our Q1 2014 quarterly release. I'll begin with the Q1 financial highlights focusing on a few major achievements which of course Oren Shirazi, our CFO will later provide a detailed financial summary of.

To begin with, revenues were \$132.7 million. EBITDA, \$27.1 million and we realized a GAAP net profit of \$39 million. The \$132.7 million revenue is an 18% increase as compared with the 112.6 in the quarter of 2013 against the pure plate foundry market weighted average growth of 10%. And very significant, if we eliminate the Micron revenue from the Q1 2013 and from the Q1 2014, the organic growth was 27%.

The EBITDA was \$27 million, 21% of revenues, substantial increase as compared to the \$15 million or 30% of revenues in Q1 2013. The GAAP net profit of \$39 million for which Oren will provide much more detail, I wanted to very importantly note that this is a result of the very high value created by our majority stake in

the TowerJazz Panasonic Semiconductor Company. This value can drive over \$600 million of strong annual revenues into the company.

Cash closing balance was \$183 million, compared with \$123 million as of Q4 2013.

I wanted to talk a little bit about customer and market vectors. If we look at Q1 2014, our top five customers, and compared the revenue of those top five customers in Q1 2013, there was a 48% growth with only two customers exceeding 4%, the biggest one being 12%. If we look at the top 10 customers of Q1 2014, and compare that to Q1 2013, there was a 59% growth. We forecast continuous growth throughout the year and these 10 customers are well represented by all five business units. I wanted then to talk a little bit about what is happening in those business units that's driving this type of an organic growth.

For the mixed signal CMOS business unit, one of the focuses is the internet of things applications, which require low leakage and mature technology nodes of 0.18-micron down to 0.11-micron. Here we expanded our technology offering with new devices for superior area efficiency for multiple voltages, low power standard cell libraries. For the analogue switch market, we developed a new technology using a hybrid of a 4.1 volt IO embedded into our 1.8 volt, 0.18-micron platform, providing optimal operational conditions to minimize power consumption and area and also demonstrating excellent speed performance.

Looking at our RF and high precision analogue business units, we continue to show a strong increase in orders from both the mobile and optical fiber segments for both handsets and 4G LTE infrastructure build outs. Growth in the mobile segment is primarily driven by our frontend module technology with our industry leading RF SOI platform used for switching and tuning functions in mobile devices. RF SOI revenue continues to grow at a strong pace quarter over quarter and we are now sampling a next generation process with our lead customer which is expected to continue this growth trend well into 2015 and beyond.

We also continued to gain design traction for our silicon germanium power amplifier technology for use in both Wi-Fi and cellular markets. Growth in the infrastructure segment is primarily driven by the use of our silicon germanium technology and optical fiber links, which are experiencing strong growth due to China's 4G LTE infrastructure build out. Our silicon germanium technology is highly differentiated and optimized for fiber optic links and thus we have won a large share of this market. To maintain our lead in this area, we are currently working with a lead customer on a low power version of our SiGe process, planned for initial product tape out around mid-2014. Our advanced SiGe technology has also been adopted for demonstrations of future higher frequency systems such as the proposed 5G wireless handset standard and advanced security imaging systems.

This quarter we announced with the University of California Irvine the demonstration of the World's most sophisticated W band 7,510 gigahertz imaging integrated circuits. These are for applications such as for example next-generation through clothing airport security systems.

Our power management business unit is another in which we see consistent growth and design wins tape outs and revenue driven by the adoption of both our 0.18-micron BCD technology serving power management, audio and display driver products for consumer and enterprise markets as well as our 700 volt technology serving commercial LED lighting and motor driver markets. This past quarter we released new technologies in both of these market segments. For a 0.18-micron BCD process, we released a new process capable of shrinking power used by the devices by more than 15% without any performance penalty, which

results in a corresponding dye cost saving for our customers. This has helped to win some major US customer accounts that we expect will begin to contribute to revenue growth starting in 2015.

For our 700 volt process, we announced a major new 8-inch technology capable of combining high voltage drivers with dense CMOS and nonvolatile memory in a unique modular platform which can be used not only for simple LED drivers, but also for more sophisticated products and incorporate dimming and other effects in a single chip versus the more expensive multichip solutions used today. Preliminary design kits for this process have been released and we expect multiple customers to tape out product designs in the next few months.

The CMOS image sensor business continues to grow in all fronts, namely high-end broadcasting and cinematography, industrial camera, medical x-ray sensors and gesture control. We see high demand for current products, higher than our forecast from the beginning of the year and an increase in new product tape outs. As we previously stated, we expect strong wafer based strong revenue growth starting Q4 this year and wrapping through 2015 in the gesture control application.

In our U.S aerospace and defense business unit, we continue to see revenue growth. In part this is due to increased R&D spending from our customers. An example was announced this quarter with a multimillion dollar award to TowerJazz from the US Air Force Research Laboratory towards a program directed at the manufacture of advanced read-out ICs which are used in many commercial and military sensors, detectors and imaging systems. We continue to build out more capacity and progress with our customer partner in our annex for the manufacture of commercial infrared sensors. We expect to see these turn to very strong wafer based revenue over the next years.

In terms of our top business units, IDM transfer revenues continued to grow quarter over quarter. We do continue to expand our existing relationships and transfers with existing customers as well as new customers, including joint development programs for next-generation products. For both the CMOS image sensor and TOPS group, there's major activity and success using new specialized capabilities and offerings of the TowerJazz Panasonic Semiconductor Company, which I will introduce a little bit later.

As a predictor of continuous growth, if we look at the customer map sets entering our foundries, and as previously stated from the time that the map set enters into the foundry, it takes between three to four quarters to start a strong ramp. The ramp lasts for maybe three quarters and then a stable ramp revenue will be available for four to six quarters before it's replaced by new products. In Q1 2012 we had a 117 maps entering into our factories, Q1 2013, 131 and in Q1 2014, 168, so Q1 2014 over Q1 2013, a 28% growth. The organic growth that is being seen from Q1 2014 over 2013 is 27% is result predominantly of the increase of maps that's entering the factories in the latter part of 2012 and the beginning of 2013. The fact of the 28% increase in the map sets that have entered into the factories in Q1 should be a strong indicator of continued organic growth in the 2015 through 2016 timeframe.

I'll now talk a bit about our new venture, TowerJazz Panasonic Semiconductor Company. To begin with, it really is a revolutionary foundry concept. There are integrated device makers and there's maybe a few system companies that also offer foundry services, Samsung being one system company that offers foundry services within its semiconductor group. But I think that this activity is unique in the fact of having a very successful and large system company Panasonic. Presently I think \$80 billion to \$85 billion revenue that has spun off its semiconductor operations to join into a partnership to create a pure play foundry. Now the

beauty of this isn't just the capacity, it's the fact for a foundry offering of having multiple specialized flows that have been tailored not just to make specialty chips, but analog chips that have been proven to work in analog components and in systems. And this becomes something very major within this venture.

On April 1, we announced that we completed the venture and kicked off the venture with Panasonic Corporation, the name of the company being TowerJazz Panasonic Semiconductor Company. And that this company would be enabling at least \$1 billion of annual revenue run rates in the 2015 time frame. What are the highlights of the deal? TowerJazz holds 51% of the Panasonic Semiconductor or TowerJazz Panasonic Semiconductor Company or TPSC. We appointed the CEO, CFO and one of the two VP of sales for external foundry. Panasonic nominated the COO, CTO and the other VP of sales for the Panasonic internal sales. This venture provides TowerJazz with incremental annual revenues of approximately \$400 million initially and growing from there as we develop the foundry business within these factories. This initial revenue from Panasonic customer can vary quarterly from approximately \$90 million to \$105 million.

Panasonic utilization is approximately 55% of the capacity of TowerJazz Panasonic Semiconductor Company which provides the venture a profitable model from day one. With this 50% utilization, there is substantial capacity for additional foundry business. Total available capacity of this company is 1 million wafer per year's 8 inch equivalent, over three manufacturing facilities in Japan. So at 50% utilization, 500,000 wafers per years are available for foundry capabilities. Panasonic committed to acquisition its products from TPSC for a period of at least 5 years of volume production. Now one of the beauties of this venture with Panasonic is that the products that are made for Panasonic are used by Panasonic for its components or possibly ultimate systems. And there is no direction or need for Panasonic to stop using these products. Hence the contract is a very stable contract over the 5 years and we expect that when the 5 years is completed, that there's no reason that it should not extend for whatever indefinite period of time after that.

This venture expands TowerJazz leadership to include a state of the art, 300 millimeter analog technology Fab including best of class, 65 nanometer CMOS image sensor, dark current and quantum efficiency performance and an additional 45 nanometer digital technology. All of this was had for a \$7.5 million purchase price. Because the value comes into growing the foundry capabilities for which Panasonic and analog system leader saw us as an analog foundry leader than can increase the utilization of the factories to the benefit of all parties.

If we look at the corporate ownership holding structure, you have TowerJazz Semiconductor with two factories in Israel, Fab 1 and Fab 2, 100% ownership of Jazz Semiconductor Fab 3 in the United States, 51% ownership of TowerJazz Panasonic with three factories in Japan, and 100% ownership of Nishiwaki Fab4 in Japan. At the time that we announce on April 1, the completion of the deal, the creation of TowerJazz Panasonic Semiconductor Company. We also announced that we would be ceasing the operation of the Nishiwaki factory by the end of 2014. I wanted to talk to that for a minute. TPSC provides more available CMOS capacity for foundry service than the Nishiwaki in its entirety.

TPSC comes with a strong and long-term supply agreement with Panasonic. Hence the consolidation of the non-micron Nishiwaki activities into a factory or the three factories inside of this venture made tremendous sense, mainly for the reason that the ceasing of the Nishiwaki operations will reduce \$130 million of annualized fixed cost. All continuing business deals are being transferred to existing TowerJazz facilities or most all deals or the TowerJazz Panasonic Semiconductor Company. If we look at ceasing the Nishiwaki operations, from Q4 14 on a quarterly basis, there will be a \$32 million reduction in fixed cost to the

company. But from the present run rate, again about a \$30 million revenue reduction for Micron. The Micron contract that we signed when we acquired the Nishiwaki factory ends as of June 2, this year. So our targets is to continue our organic growth to fully replace Micron's revenue in order to achieve net profit at a lower revenue level than before for the fact that we have taken out then on a quarterly basis \$32 million of fixed cost.

The Q1 GAAP net profit was enabled and Oren will talk in detail through the high value of the asset that we acquired through our stake in the TowerJazz Panasonic Semiconductor Company. The Q2 GAAP net profit should go back to the levels that I was in Q4. Q3 we'll see possibly some benefit from the cessation of operations of Nishiwaki. And in Q4, we'll see the full benefit of the cessation of operation, and that will carry out the throughout in 2015. As we continue the organic growth within the existing factories, the target of GAAP net profit becomes realizable and our target certainly is to achieve that as we've said before in Q4. If it's achieved or not, it will certainly be very close with the market difference between previous years of operation.

Just quickly to talk about the TowerJazz Panasonic plant overview, there's three factories Tonami factory a 200 millimeter factory. 48,000 wafer start per month, 0.15 micron to 0.35 micron. The products that it is making are mainly in the power area BCD, Sets and IGBT. Nonvolatile memory and CCD image sensors.

In Uozu, we have a state-of-the art 300 millimeter facility with 22,000 wafer start per month, 8 inch equivalents, 45 nanometer to 65 nanometer. Products are 45 to 65 low power CMOS, 65 nanometer RF CMOS and 65 nanometer CMOS image sensors. And Arai, we have a 15,000 wafer start per month, 0.11 micron to 0.13 micron copper line where the products are 110 nanometer analog ICs and CMOS image sensors.

Also in the Arai factory, is a thick copper RDL line that we believe we will have great use for as we continue to develop and sell it to our customers the capabilities within these factories. There's a very large and strong offering within these factories serving many device applications. Various technologies including power devices with a variety of 1.2 to 600 dry voltages. Within these factories is for example strong discrete capabilities, IGBT capabilities. I believe that we will probably be the only foundry in the world with an IGBT foundry offering as a function of the capabilities that have been transferred into this venture from the Panasonic flows. In the case of the Uozu factory, as I've mentioned, it's very, very high-end best of breed CMOS image sensor capability quantum efficiency and low dark current. The factories have served a variety of devices, MCU, LSI, DSP, image sensors, power devices, power management ICs, system LSI, with these devices having been successfully tailored to meet a variety of N system integration applications, which is audio visual, mobile communication, automotive, PC peripheral, security, healthcare appliances. All of this knowledge, all of this product and flow tailoring is now available through a foundry offering to the variety of our customers worldwide and we believe will attract many new customers.

There's a variety of areas where our capabilities overlap, but what that allows is a for a stronger, richer feature portfolio within the existing TowerJazz factories as well as within this TowerJazz Panasonic semiconductor company where we incorporate the best feature of both platforms for both cost benefit as well as for performance benefit. There's several areas of joint development, for example high voltage CMOS that we are doing within these factories because of equipment and technology capabilities, and there's incremental capabilities that were not had at all within TowerJazz existing factories as far as the 65 nanometer, 45 nanometer, 300 millimeter capabilities in logic, mixed signal RF, SOI CMOS, and CIS CCD.

If we look at progress that has been made so far on the foundry side of this venture and the CMOS image sensor business unit, we have made major steps forwards through the TowerJazz Panasonic deal. As we already mentioned last quarter, Panasonic, now TPSC, does have this worldwide leading CIS technology at 65 nanometer 300 millimeter wafers. This, combined with the reputation TowerJazz has in the image sensor business, allowed us to engage with several customers already on markets that were not accessible to TowerJazz until now such as very high-end cellphone camera markets and high-end digital SOI markets. We have prepared with our partners at TPSC, a foundry match PDK for 1.12-micron state of the art pixel technology and it's now released to selected customers who already started their designs.

In parallel, we are preparing a unified CIS PDK that will be our mainstream PDK for the CIS 65 nanometer process and already includes 20% photo mask reduction against the present flow. This process design kit is targeted for all pixels having dimensions larger than 1.35 micron for many types of applications, including obviously the digital SOI market. This design kit is going to be released to our customers by middle of next month and we have already many inquiries for data on this process for specific products by a variety of customers. Hence TowerJazz Panasonic Semiconductor Company allows us not only to increase our market share within our customer base by allowing them to get into new markets and applications, but also allows us to acquire new customers.

As far as the TOPS business unit, IDM transfer products for one of our customers, is already in this new enterprise. In addition, we recently won a new customer project was planned to be manufactured at the TPS site and several other transfers are in advanced stages of negotiation. We will soon offer customers advanced CMOS and RF CMOS automotive qualified at 65 nanometer, 45 nanometer technology nodes running on 300 millimeter wafers. This technology is ideal for applications such as portable devices, cellular phones, Wi-Fi and WiMAX.

So what was the big benefit of this joint venture? Why does it make sense for both companies? They truly are complementary capabilities, creating excellent synergy. For TowerJazz, the well-known and highly reputable name of Panasonic will be extremely valuable in acquiring Japanese customers. If we look at our Nishiwaki factory, we had good success bringing customers into that factory. And as mentioned, the customers that we brought there outside of the Micron deal are being moved, almost all customers are being moved to other factories within TowerJazz. But we did not have extremely fast or great traction within the Japanese market. Part of that was that the previous owner of the company was Micron who is not a Japanese company. TowerJazz also not a very well-known Japanese name, hence within the business culture, the amount of time it takes to build trust before actual ramps would begin is quite tedious and quite long. In the case of the Panasonic factories, Panasonic being such a reputable company, there is no issue there as far as the trust coming into the company from the Japanese customers and we've seen that already.

Lastly, to talk about our guidance, Q2 2014 guidance is \$230 million with a range of 5% above or 5% below.

Now I would like to turn the call over to Oren.

### **Oren Shirazi**

Thank you, Russell. Welcome everyone and thank you for joining us today. I will start by providing our P&L results highlights for the first quarter of 2014, then discuss our balance sheet. I will also give details regarding the implications of the Panasonic transaction and business and structuring in Japan on our balance sheet and P&L line item.

Firstly it is important to note that excluding all those one time effects from the Panasonic transaction and the business's structure in Japan, we had a good quarter on an organic basis in which we increased our revenue year-over-year by \$20 million, increased our EBITDA by \$13 million and improved our balance sheet ratio and P&L margins as I will detail.

Our revenues for the quarter were \$133 million, \$20 million higher than \$113 million in the first quarter of 2013, an increase of 18% overall which includes an organic growth rate, which excludes the Micron long-term contract revenue of 27%.

We recorded net profit for the first quarter of 2014 amounting to \$39 million, which included three one-time elements. A, \$150 million in onetime net acquisition gains derived from the increased value of the TowerJazz Panasonic Semiconductor Company which we named TPSC, which is the new company established in Japan. This net gain is mainly as a result of an appreciation to fair market value of the equipment of the three fabs acquired in Japan, which was done in accordance with GAAP and based on a third party appraisal opinion and this amount is net after deferred tax liability accrual. We also -- B, we also reported a onetime noncash allowance of \$71 million resulting from our decision to fill the Nishiwaki fab operation in Japan, reflecting mainly noncash fixed asset impairment. This \$71 million allowance includes all expected adjustments to tangible and intangible impairment net values and considering all anticipated costs associated mainly with employee and other liabilities. C, finally we reported an additional onetime cost, which was a noncash charge of \$7 million net, resulting from the restructuring of the Jazz bonds.

The non-GAAP statement we provided exclude all these onetime items, as well as depreciation and amortization and show that on a non-GAAP basis, our gross profit for the quarter was \$45 million, an increase of 32% compared to the \$34 million reported in the first quarter of 2013.

On a non-GAAP basis, our operating profit for the quarter was approximately \$28 million, an increase of 84% as compared to \$15 million in the first quarter of last year. And the operating margins improved from 13% in the first quarter of 2013 to 21% in the first quarter of 2014. Net profit is on non GAAP basis for the quarter worth approximately \$20 million which is \$13 million better than in the first quarter of last year. The net margin increased from 6% of revenues in the first quarter of 2013 to 15% in the current quarter on a non GAAP basis.

As compared to the prior quarter, we achieved similar growth and operating non GAAP margins of 34% and 21% respectively and improved the net margin from 14% to 15%. This is all very impressive given that seasonally the first quarter trend tends to be weaker than the fourth quarter.

Our EBITDA for the quarter was \$28 million significantly higher than the \$15 million in the first quarter of 2013. On a GAAP basis, we achieved \$39 million in net profit representing \$0.81 basic earnings per share and \$0.59 earnings per share on a fully diluted basis.

On a GAAP basis, financing expenses net includes in the first quarter of 2014, a onetime non-cash cost of \$10 million which I discussed before resulting from the Jazz bonds exchange deal which we completed in March 2014. And for the first quarter of 2013, financing expenses include one-time net cash – one time non cash income of \$6.5 million resulting from the events extension contract signed during March 2013.

I will now discuss and analyze our balance sheet as of the end of the first quarter 2014. The main changes in the balance sheet are a result of the first time consolidation of TPSC which is the Panasonic related

transaction new company comprised of the following main items, A, Assets, which include \$58 million of cash, \$37 million of inventory and \$240 million of property and equipment. B, liabilities which include \$85 million loan from Panasonic which we expect will be replaced by our Japanese bank 5 year loan shortly and \$85 million of differed tax liability resulting directly from the property and equipment appreciation to fair market value. C, \$15 million of shareholder's equity; and D, \$150 million of net gain from the Panasonic transaction as explained earlier in my review. The main other changes in the balance sheet are as a result of the Nishiwaki fab cessation of operations due to the classification of assets and liabilities from long term to short term, which is mainly its property and equipment and its employees retirement allowance.

As we announced in March 2014, we signed agreements with certain of our U.S. bond orders which strengthened our balance sheet, reducing our net debt through June 2015 by approximately \$50 million and extended maturity to December 2018. This transaction was following the definitive contract signed with Wells Fargo, Capital Finance Bank providing us with a credit line of up to \$70 million maturing in December 2018. This credit line extension together with the bonds transaction has significantly improved our balance sheet and financial position, enabling us to continue to execute our strategic growth plan.

Overall, refinancing of our debt as well as the transaction with Panasonic has strongly enhanced our balance sheet and financial ratios as of March 31, 2014 as follows. Our shareholder's equity was \$200 million at the end of this quarter as compared to \$141 million at the end of 2013.

As of the end of this quarter, our issued and outstanding ordinary share count was \$49 million worth 49 million ordinary shares similar to that number in December 31, 2013 in terms of quantity of shares. Out of which 18 million ordinary shares were held by Israel Corporation.

Cash, short term deposits and designated deposits as of March 31, 2014 were \$183 million, an increase of \$60 million when compared with \$123 million as of December 2013. During the quarter, we generated \$25 million positive cash flow from operations excluding interest payment. And increased our consolidated cash balance by \$68 million as a result of the TPSC venture.

On the other hand, we invested \$9 million net of CapEx in fixed assets. We repaid net \$7 million of debt and paid \$6 million of interest payments to our debt holders. Our current assets increased significantly from \$290 million at December 31, 2013 to \$433 million on March 31, 2014.

And our net current assets which are the current assets, net of current liabilities increased from \$141 million on March 31, 2013 and from \$159 million on December 31, 2013 to be \$187 million on March 31, 2014. This ends my financial review and I will be happy to accept questions at the end of the conference call.

And now I wish to turn the call to Mrs. Noit Levi-Karoubi. Noit?

#### **Noit Levi**

Thank you, Oren. Before we open up the call for the Q&A session, I would like now to add the general and legal statement to our results in regards to statements made and to be made during this call.

Please note that the first quarter of 2014 financial results has been prepared in accordance with U.S. GAAP and the financial tables in today's earning release includes financial information that may be considered non-GAAP financial measures under regulation G and related reporting requirements as established by the Securities and Exchange Commission as they apply to our company. Namely these results represented financial data which is reconciled as indicated by the footnote below the table on a non-GAAP basis after



deducting one, depreciation and amortization. Two, compensation expenses in respect to options, grants. And three, finance expenses net other than interest accrued such that's non-GAAP financial expenses net include only interest accrued during the reported period.

Non-GAAP financial measures should be evaluated in conjunction with and are not a substitute for a GAAP financial measures. The table also contains the comparable GAAP financial measures to the non-GAAP financial measure, as well as the reconciliation between the non GAAP financial measures and the most comparable GAAP financial measures. EBITDA is presented is defined in our quarterly financial release. EBITDA is not required GAAP financial measure and may not be comparable to a similarly title measure employed by other companies. EBITDA and the non-GAAP financial information presented herein should not be considered in isolation or as a substitute for operating income, net income or loss, cash flows provided by operating, investing and financing activities, per share data or other income or cash flow statement data prepared in accordance with GAAP and is not necessarily consistent with the non-GAAP data presented in previous filings.

I would now like to turn the call over to the operator. Operator?

### **Question-and-Answer Session**

#### **Operator**

Thank you. (Operator Instructions) the first question is from Cody Acree of Ascendant Capital. Please go ahead.

**Cody Acree** - Ascendant Capital Markets

Thanks for taking my questions and congrats on the progress. Oren, could you help us with gross margin expectations for the June quarter and how you would expect those to track through rest of the year?

**Oren Shirazi**

Yes, thank you. So basically we did not yet announce the official date that we will fill the operation in Nishiwaki. Following that date, of course we will have significant improvement. Recent we didn't get enough, because we don't yet receive the final date, timing of the orders from the customer. So we're trying of course to do the best we can. But we announced that from the quarter after we cease the operations, actually we will be able to save \$130 million annual run rate which will improve the margins. Of course the Panasonic transaction does not have any negative margin or something like that so we just should be in incremental upside. And until then for Q2, you should actually look at the Q1. And if you look at Q1 margins and extrapolate to Q2 you just need to exclude the three one item – the three one-time item which I mentioned the \$150 million of Panasonic the \$71 million of Nishiwaki and \$7 million net of the bond.

**Cody Acree** - Ascendant Capital Markets

So, Oren, just to be clear, you are saying that the Panasonic gross margin is net neutral to the corporate average?

**Oren Shirazi**

No. I did not say, I did not indicate anything about the -- because we don't give this internal information about the exact amount of margin or exact percentage of margin of the Panasonic incremental contribution. I just said that it is not negative.

**Cody Acree** - Ascendant Capital Markets

Okay, thank you. And on the OpEx side, can you also kind of help us work through that through the year? For the June quarter, obviously, you will have some Panasonic expenses coming in and then how you expect those to trend and track through the year.

**Oren Shirazi**

What? Sorry, I did not understand the question.

**Cody Acree** - Ascendant Capital Markets

Sorry. On the spending side, on the operating expenses, can you just help us with the June quarter and then how those track through the year?

**Oren Shirazi**

Again for Q2 2014, the margins are expected to be the same like Q1 2014, because – I mean not the same. The same if you exclude those three onetime items and then you should add the margins are expected from Panasonic and we obviously did not discuss that publicly.

**Cody Acree** - Ascendant Capital Markets

No, I'm sorry. I guess what I was trying to get to is your R&D and your G&A (inaudible) for the year.

**Oren Shirazi**

Okay. In regards to the SG&A, sorry the line is not so good here. So in regards to the SG&A, expected to be about the same level. It could be a very slight increase during Q2, Q3 because of the inclusion of Panasonic. On the other hand there will be a reduction from the quarter that we will cease operations of Nishiwaki. We did not announce which quarter is that, but if you assume it is Q3 so from Q4, if you assume it is Q2 so from Q3, okay? But from that point in time there will be a reduction because of the stopping to include the Nishiwaki cost.

**Cody Acree** - Ascendant Capital Markets

Then with the \$130 million you expect in savings, if you look at it from a cash flow standpoint, do you expect that to flow -- how much of that really flows through the earnings, or is there a portion of that that you expect to be redeployed into other investments?

**Oren Shirazi**

No. We don't expect anything of that to deploy to the other investments. Of course when you reduce the \$130 million of cost, also we will have a reduction of the Micron revenue because that contract is expiring in that public domain that in June 2. So in the 2nd of June, so still again like I said in the beginning we did not announce and not necessarily that we want to announce because it is a Micron deal until when exactly. They will continue to order although contract expires -- the committed contract expires in June 2. But from the time that the orders will stop and will cease operations, there will be a reduction in revenue and a reduction in the variable costs that are associated with that revenue and this \$130 million fixed cost. So for illustration point of view, if Micron revenue are X, the value of the cost associated with that should be between a third to a half of this X and then on top of that you have the \$130 million fixed cost reduction.

**Cody Acree** - Ascendant Capital Markets

And then lastly -- thanks for taking this many questions. But on the CapEx side, what does that look like for the remainder of the year and maybe into 2015 as you look at the available capacity you have at Panasonic?

**Oren Shirazi**

So it's basically the same answer like the answer about the SG&A. It's related to all the fixed costs and also the CapEx that you asked. So basically for Q2 and until the moment we will cease operation in Nishiwaki, you should expect a slight increase in the CapEx because of the fact that we are including now, consolidating in full Panasonic venture. And from the moment, like you mentioned like 2015 for sure, and also in 2014 and the end of 2014 from whenever we will cease the operations, you will see actually a reduction in the CapEx of Nishiwaki and overall CapEx after those two transactions. So CapEx in 2015 should be not too high, not higher or lower in a significant manner than the CapEx run rate which existed so far.

#### **Operator**

The next question is from Jay Srivatsa of Chardan Capital Markets.

#### **Jay Srivatsa** - Chardan Capital Markets

Thanks for taking my questions and congrats on achieving GAAP profitability. Russell, when you look at the JV beyond the Panasonic business, are you sensing that there will be more opportunities from other Japanese or Asian customers as you look at setting up the fab going forward?

#### **Russell Ellwanger**

Definitely, the answer is yes. We have already Asian customers that we are engaging with. One specifically that's at I believe very end stages of signing a contract and others that we're engaged with in Asia. In Japan I think the answer is yes as well. There's one company in Japan already that is very desirous to go into the TowerJazz Panasonic Company and the activity has not yet began, but has expressed desire that was not previously for that flow working with the company. As mentioned before, we did not have necessarily a very difficult [inaudible 00:01:54] to move into the Nishiwaki factory. There's always the latency. There's a lot of noise in the line. There's always the latency from the time that you've started engagement until the time that you ramp, until the time that you reach volume. And then over the past month when we saw that the contract was getting very strong with Panasonic to -- there's somebody on the line that's very, very loud.

At any rate we stopped trying to bring new customers and stopped moving even the existing customers with new activities when we thought that there was a chance that we would stop the operations there. But that being said, the name of Panasonic itself is so strong and so reputable that whatever initial barrier there is to develop a relationship and to develop the trust with a Japanese company and it's very, very trust based business there, I think that that barrier will be greatly reduced through the fact of that this is still more or less half owned by Panasonic. And that the operations have been a Panasonic factory, the manpower for the most part on the operational side is the Panasonic workforce augmented a bit by TowerJazz workforce.

So the ability to bring additional Japanese customers to the factory I think will be much easier than it was to go into Nishiwaki. But in general Asian customers really like to work in Japan. They believe very strongly in the quality of Japanese factories and certainly these three factories that we have are the best of the best in quality. The 300 millimeter factory to my knowledge is the only factory in the world that has virtual metrology. With so much activity, so much work there that I don't know that it's zero metrology in the fab, but there's very close to zero because all of the output parameters are so well dialed into understanding the impact of the next processing steps. So the quality coming out of these factories is amazing.

So I hope that I answered your question. It was a very, very long answer but I hope that it did answer the question, Jay.

#### **Jay Srivatsa** - Chardan Capital Markets

You did, and apologies for the noise in the background. The next question then is at a higher level, do you sense that Panasonic and integrated fab company looking to go into kind of a JV with you, the foundry company, is indicative of a macro trend or more and more integrated analog companies will likely look at similar ops?

**Russell Ellwanger**

If it will become a worldwide trend, that I couldn't say. Do I think that there's more opportunities for such activities in Japan? I definitely do. It's not just that I believe that there's more opportunities in Japan. We've actually been approached for another opportunity in Japan that at this point is maybe too early for us to want to get involved in as we have this present venture to work on and make successful. So the fact that we were approached certainly there's others that see the model that we did with Panasonic who's truly been a phenomenal partner in this. And I think that it can make very good sense for them. But for the rest of the world, I really don't know. I couldn't say.

**Jay Srivatsa** - Chardan Capital Markets

Okay. And then last question for me on the India opportunity. Could you give us an update on where things are and what is the next step in terms of progression in that project?

**Russell Ellwanger**

Sure. As we stated in the March timeframe, there were cabinet minutes that two consortia were given a letter of intent from the government. Our consortia is one of those, which is JP, IBM and ourselves. We're now in the process of responding to the LOI. According to the cabinet minutes, as they had been published, they were going to then award financial contracts within this year, I believe in the third quarter from the way that it was published. However, there is a new government coming in place and how much the previous cabinet's minutes are binding for the new cabinet, that I really can't express. But from everything that we see, it's moving forward and we're responding to the LOI. So from where we sit everything is progressing.

**Jay Srivatsa** - Chardan Capital Markets

Okay, last question for me. Oren, on the net income, given some of the costs that you expect to incur in the next quarter, is it realistic to expect that you would be able to achieve GAAP profitability one more time? Or do you expect that to be able to -- do you expect to be able to see that later in the year again?

**Oren Shirazi**

So we do not give forecast for net profit and we can voice a lot of things. One of them increasing the revenue, the other, all kinds of things affecting the cost and expenses and financing expenses and all that. We can always say what we have said before, that after we cease operations of Nishiwaki -- before we cease operations in Nishiwaki we are bound to the previous model and everybody can calculate the net profit excluding the Panasonic and Nishiwaki one-time items in the profit and loss. And after that, we'll have our benefit. But we're not in a position to guide these benefits together with the forecast the revenues increase when will it be converted into bottom line of net profit.

**Operator**

There are no further questions at this time. Mr. Ellwanger, would you like to make your concluding statement?

**Russell Ellwanger**

Definitely. Thank you. So as always I think those that participate in the call or those that will later listen to the call for the interest you have in the company. I believe that where we're at now is a very pivotal point in

the company, maybe one of the most exciting that we've been in in years. We've moved our run rate from the \$500 million to \$650 million to presently a run rate of upwards of \$900 million, with an existing capacity capability that can bring the revenues of the company to \$1.2 billion. And that becomes our target. That becomes our challenge. That becomes our activity now to take the capacity that we have within the existing TowerJazz facilities to continue this organic growth trajectory that we've had to come to full utilization of our specialty products and the trajectory is very strong in all the factories right now.

And then through this TowerJazz-Panasonic venture, to move forward to continue to grow the revenue there from beyond the circa \$400 million from the Panasonic revenues and grow it to well above \$600 million and achieve this \$1.2 billion run rate. The trajectories in the company right now show us in the fourth quarter of this year really being extremely high utilization through all the three Fab 1, Fab 2, Fab 3 TowerJazz facilities and actually increasing capacity in two of the facilities, that being Fab 2 with Migdal Haemek and Fab 3 in Newport Beach. And the customer traction presently shows that we'll be able to grow the foundry portion, the available 50% capacity of the three factories of the TowerJazz-Panasonic semi-company over the next years.

From the first contract that we have where the customer has already started the transfer, the IDM transfer into one of the venture companies or factories, we expect to start seeing wafer revenue in the fourth quarter of this year. And that will wrap in throughout next year the other activities. We believe that we'll start seeing a very nice ramp of the foundry portion of the TPSC throughout 2015 and we target to have it full in 2016, 2017, 2018. So that being said, the \$1.2 billion I think is certainly an achievable target over the coming years. The associated bottom line performance will be in hand very nicely as that has occurred. On top of it, there's always incremental models, new things that are being looked at, things that can be happening. Jay had asked about the India project.

That's not part of our multiyear plan. It's not part of any commitments, but providing that does happen, that's incremental, very, very high margin business for us, without any investment from us into the creation of the company other than the potential or other than an equity investment in the company. So there's always new things happening that can grow us nicely beyond the \$1.2 billion. But we do right now have existing capacity capability of achieving \$1.2 billion annual revenues and we're very, very excited over the next years to update you as we progress and to continue on the trajectory that we're now on.

As a last note, next week on May 21 we will be presenting at the B. Riley Conference and we'll be very excited to see you there, very happy to meet with you on one on ones, any of you that would wish to set that up or to just talk with you at the presentation itself. So I thank you very, very much for your time, for your attention, for your interest in the company and wish you the best. Thank you.

#### **Operator**

Thank you. This concludes the TowerJazz First Quarter 2014 Results Conference Call. Thank you for your participation. You may go ahead and disconnect.

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