

CABOT MICROELECTRONICS CORP  
Form 10-Q  
May 06, 2016  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended

March 31, 2016  
or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 000-30205

CABOT MICROELECTRONICS CORPORATION  
(Exact name of registrant as specified in its charter)

DELAWARE 36-4324765  
(State of Incorporation) (I.R.S. Employer Identification No.)

870 NORTH COMMONS DRIVE 60504  
AURORA, ILLINOIS (Zip Code)  
(Address of principal executive offices)

Registrant's telephone number, including area code: (630) 375-6631

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES X NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES X NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES  NO

As of April 30, 2016, the Company had 24,047,010 shares of Common Stock, par value \$0.001 per share, outstanding.

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## PART I. FINANCIAL INFORMATION

## ITEM 1.

CABOT MICROELECTRONICS CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited and in thousands, except per share amounts)

|   | Three Months<br>Ended March 31, |           | Six Months Ended<br>March 31, |           |
|---|---------------------------------|-----------|-------------------------------|-----------|
|   | 2016                            | 2015      | 2016                          | 2015      |
| Revenue                                     | \$99,244                        | \$104,858 | \$199,613                     | \$216,792 |
| Cost of goods sold                          | 52,348                          | 50,182    | 102,522                       | 105,142   |
| Gross profit                                | 46,896                          | 54,676    | 97,091                        | 111,650   |
| Operating expenses:                         |                                 |           |                               |           |
| Research, development and technical         | 14,934                          | 15,131    | 29,762                        | 30,149    |
| Selling and marketing                       | 6,668                           | 5,777     | 13,417                        | 13,416    |
| General and administrative                  | 12,990                          | 14,296    | 27,253                        | 26,047    |
| Total operating expenses                    | 34,592                          | 35,204    | 70,432                        | 69,612    |
| Operating income                            | 12,304                          | 19,472    | 26,659                        | 42,038    |
| Interest expense                            | 1,191                           | 1,059     | 2,358                         | 1,965     |
| Other income (expense), net                 | 452                             | (332 )    | 642                           | 725       |
| Income before income taxes                  | 11,565                          | 18,081    | 24,943                        | 40,798    |
| Provision for income taxes                  | 2,434                           | 4,270     | 4,503                         | 7,071     |
| Net income                                  | \$9,131                         | \$13,811  | \$20,440                      | \$33,727  |
| Basic earnings per share                    | \$0.38                          | \$0.57    | \$0.84                        | \$1.40    |
| Weighted average basic shares outstanding   | 24,061                          | 24,057    | 24,070                        | 23,845    |
| Diluted earnings per share                  | \$0.37                          | \$0.55    | \$0.83                        | \$1.36    |
| Weighted average diluted shares outstanding | 24,408                          | 24,693    | 24,444                        | 24,582    |
| Dividends per share                         | \$0.18                          | \$-       | \$0.18                        | \$-       |

The accompanying notes are an integral part of these consolidated financial statements.

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited and in thousands)

|  | Three Months<br>Ended March 31, |          | Six Months Ended<br>March 31, |          |
|--|---------------------------------|----------|-------------------------------|----------|
|  | 2016                            | 2015     | 2016                          | 2015     |
| Net income                                     | \$9,131                         | \$13,811 | \$20,440                      | \$33,727 |
| Other comprehensive income (loss), net of tax: |                                 |          |                               |          |
| Foreign currency translation adjustments       | 6,160                           | 48       | 6,357                         | (8,284)  |
| Minimum pension liability adjustment           | (85 )                           | -        | 287                           | -        |
| Net unrealized gain (loss) on cash flow hedges | (651 )                          | (443 )   | (92 )                         | (612 )   |
| Other comprehensive income (loss), net of tax  | 5,424                           | (395 )   | 6,552                         | (8,896 ) |
| Comprehensive income                           | \$14,555                        | \$13,416 | \$26,992                      | \$24,831 |

The accompanying notes are an integral part of these consolidated financial statements.

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## CABOT MICROELECTRONICS CORPORATION

## CONSOLIDATED BALANCE SHEETS

(Unaudited and in thousands, except share amounts)

|   | March 31,<br>2016 | September<br>30, 2015 |
|---|-------------------|-----------------------|
| <b>ASSETS</b>   |                   |                       |
| Current assets:   |                   |                       |
| Cash and cash equivalents   | \$226,388         | \$354,190             |
| Accounts receivable, less allowance for doubtful accounts of \$1,221 at March 31, 2016, and \$1,224 at September 30, 2015                                 | 52,087            | 49,405                |
| Inventories, net  | 76,325            | 70,678                |
| Prepaid expenses and other current assets   | 16,716            | 12,840                |
| Deferred income taxes   | -                 | 7,395                 |
| Total current assets  | 371,516           | 494,508               |
| Property, plant and equipment, net  | 104,315           | 93,743                |
| Goodwill  | 95,645            | 40,442                |
| Other intangible assets, net  | 61,657            | 4,565                 |
| Deferred income taxes   | 16,617            | 12,212                |
| Other long-term assets  | 14,836            | 15,004                |
| Total assets  | \$664,586         | \$660,474             |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                   |                       |
| Current liabilities:  |                   |                       |
| Accounts payable  | \$16,273          | \$15,448              |
| Accrued expenses, income taxes payable and other current liabilities  | 34,455            | 36,446                |
| Current portion of long-term debt   | 8,750             | 8,750                 |
| Total current liabilities   | 59,478            | 60,644                |
| Long-term debt, net of current portion  | 150,938           | 155,313               |
| Deferred income taxes   | 66                | 76                    |
| Other long-term liabilities   | 16,979            | 15,477                |
| Total liabilities   | 227,461           | 231,510               |
| Commitments and contingencies (Note 10)   |                   |                       |
| Stockholders' equity:   |                   |                       |
| Common Stock: Authorized: 200,000,000 shares, \$0.001 par value; Issued: 33,743,615 shares at March 31, 2016, and 33,489,181 shares at September 30, 2015 | 34                | 33                    |
| Capital in excess of par value of common stock  | 509,052           | 495,673               |
| Retained earnings   | 300,172           | 284,088               |
| Accumulated other comprehensive income (loss)   | 462               | (6,090 )              |
| Treasury stock at cost, 9,725,587 shares at March 31, 2016, and 9,041,678 shares at September 30, 2015  | (372,595)         | (344,740)             |
| Total stockholders' equity  | 437,125           | 428,964               |
| Total liabilities and stockholders' equity  | \$664,586         | \$660,474             |

The accompanying notes are an integral part of these consolidated financial statements.



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CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited and amounts in thousands)

|   | Six Months Ended<br>March 31, |           |
|---|-------------------------------|-----------|
|   | 2016                          | 2015      |
| Cash flows from operating activities:   |                               |           |
| Net income  | \$20,440                      | \$33,727  |
| Adjustments to reconcile net income to net cash provided by operating activities:                               |                               |           |
| Depreciation and amortization   | 12,495                        | 9,303     |
| Provision for doubtful accounts   | (14 )                         | (40 )     |
| Share-based compensation expense  | 8,202                         | 8,706     |
| Deferred income tax expense   | 574                           | 4,966     |
| Non-cash foreign exchange (gain) loss   | (288 )                        | 531       |
| (Gain) loss on disposal of property, plant and equipment  | 158                           | (100 )    |
| Impairment of long lived assets   | 79                            | -         |
| Other   | (78 )                         | (802 )    |
| Changes in operating assets and liabilities:  |                               |           |
| Accounts receivable   | 1,517                         | 2,747     |
| Inventories   | (2,157 )                      | (1,688 )  |
| Prepaid expenses and other assets   | (796 )                        | (11,480 ) |
| Accounts payable  | 93                            | 1,374     |
| Accrued expenses, income taxes payable and other liabilities  | (7,589 )                      | 1,426     |
| Net cash provided by operating activities   | 32,636                        | 48,670    |
| Cash flows from investing activities:   |                               |           |
| Additions to property, plant and equipment  | (10,330 )                     | (5,317 )  |
| Proceeds from the sale of property, plant and equipment   | 17                            | 175       |
| Acquisition of business, net of cash acquired   | (126,525)                     | -         |
| Net cash used in investing activities   | (136,838)                     | (5,142 )  |
| Cash flows from financing activities:   |                               |           |
| Repayment of long-term debt   | (4,375 )                      | (4,375 )  |
| Repurchases of common stock   | (27,855 )                     | (27,236 ) |
| Net proceeds from issuance of stock   | 4,695                         | 33,630    |
| Tax benefits associated with share-based compensation expense   | 666                           | 6,113     |
| Net cash used in financing activities   | (26,869 )                     | 8,132     |
| Effect of exchange rate changes on cash   | 3,269                         | (2,164 )  |
| Increase (decrease) in cash and cash equivalents  | (127,802)                     | 49,496    |
| Cash and cash equivalents at beginning of period  | 354,190                       | 284,155   |
| Cash and cash equivalents at end of period  | \$226,388                     | \$333,651 |
| Supplemental disclosure of non-cash investing and financing activities:   |                               |           |
| Purchases of property, plant and equipment in accrued liabilities and accounts payable at the end of the period | \$868                         | \$1,149   |

The accompanying notes are an integral part of these consolidated financial statements.





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CABOT MICROELECTRONICS CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited and in thousands, except share and per share amounts)

1. BACKGROUND AND BASIS OF PRESENTATION

Cabot Microelectronics Corporation ("Cabot Microelectronics", "the Company", "us", "we" or "our") supplies high-performance polishing slurries and pads used in the manufacture of advanced integrated circuit (IC) devices within the semiconductor industry, in a process called chemical mechanical planarization (CMP). CMP is a polishing process used by IC device manufacturers to planarize or flatten many of the multiple layers of material that are deposited upon silicon wafers in the production of advanced ICs. Our products play a critical role in the production of advanced IC devices, thereby enabling our customers to produce smaller, faster and more complex IC devices with fewer defects. We develop, produce and sell CMP slurries for polishing many of the conducting and insulating materials used in IC devices, and also for polishing the disk substrates and magnetic heads used in hard disk drives. We also develop, manufacture and sell CMP polishing pads, which are used in conjunction with slurries in the CMP process. We also pursue other demanding surface modification applications through our Engineered Surface Finishes (ESF) business where we believe we can leverage our expertise in CMP consumables for the semiconductor industry to develop products for demanding polishing applications in other industries. For additional information, refer to Part 1, Item 1, "Business", in our Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

The unaudited consolidated financial statements have been prepared by Cabot Microelectronics pursuant to the rules of the Securities and Exchange Commission (SEC) and accounting principles generally accepted in the United States of America (U.S. GAAP). In the opinion of management, these unaudited consolidated financial statements include all adjustments, consisting of normal recurring adjustments and preliminary purchase accounting adjustments discussed in Note 2, necessary for the fair statement of Cabot Microelectronics' financial position as of March 31, 2016, cash flows for the three and six months ended March 31, 2016, and March 31, 2015, and results of operations for the three months and six months ended March 31, 2016, and March 31, 2015. The consolidated balance sheet as of September 30, 2015 was derived from audited financial statements, but does not contain all of the footnote disclosures from the annual financial statements. The results of operations for the three and six months ended March 31, 2016 may not be indicative of results to be expected for future periods, including the fiscal year ending September 30, 2016. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes thereto included in Cabot Microelectronics' Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

The consolidated financial statements include the accounts of Cabot Microelectronics and its subsidiaries. All intercompany transactions and balances between the companies have been eliminated as of March 31, 2016.

2. BUSINESS COMBINATION

On October 22, 2015, the Company completed the acquisition of 100% of the outstanding stock of NexPlanar Corporation (NexPlanar), which was a privately held, U.S. based company that specialized in the development, manufacture and sale of advanced CMP pad solutions for the semiconductor industry. We acquired NexPlanar to expand our polishing pad portfolio by adding a complementary pad technology for which we believe we can leverage our global infrastructure to better serve customers on a global basis, including offering performance-advantaged slurry and pad consumable sets. We paid a total of \$126,455, including total purchase consideration of 141,716, less cash acquired of \$15,261. In addition, we paid \$605 in compensation expense related to certain unvested NexPlanar stock options settled in cash at the acquisition date. In the second quarter of fiscal 2016, we paid an additional \$ 70 for a post closing adjustment. We have included 100% of the NexPlanar revenue and earnings since October 22, 2015 in

our Consolidated Statement of Income. The net revenue in our Consolidated Statement of Income for the three and six months ended March 31, 2016, attributable to NexPlanar, was \$5,354 and \$9,380, respectively. The net loss included in our Consolidated Statement of Income for the three and six months ended March 31, 2016, attributable to NexPlanar, was \$2,004 and \$4,302, respectively.

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The following table summarizes the preliminary fair values of assets acquired and liabilities assumed as of the date of acquisition:

|  |            |
|--|------------|
| Total purchase consideration                   | \$ 141,786 |
| Cash   | \$ 15,261  |
| Accounts receivable                            | 3,060      |
| Inventories                                    | 2,768      |
| Prepaid expenses and other current assets      | 1,712      |
| Property, plant and equipment                  | 6,901      |
| Intangible assets                              | 61,000     |
| Deferred tax assets                            | 20,203     |
| Other long-term assets                         | 1,458      |
| Accounts payable                               | (1,057 )   |
| Accrued expenses and other current liabilities | (1,472 )   |
| Deferred tax liabilities                       | (22,453 )  |
| Total identifiable net assets                  | 87,381     |
| Goodwill                                       | 54,405     |
|  | \$ 141,786 |

The acquisition was accounted for using the acquisition method of accounting. Tangible and identifiable intangible assets acquired and liabilities assumed are recorded at fair value as of the acquisition date. The current fair values assigned to assets acquired and liabilities assumed are considered preliminary and are based on information available as of the date of the filing of this Form 10-Q. We believe that the information provides a reasonable basis for estimating the preliminary fair values of assets acquired and liabilities assumed, but certain items, such as deferred income taxes, may be subject to change as additional information is received. We expect to finalize the purchase price allocation as soon as practicable, but not later than one-year from the acquisition date of October 22, 2015.

In September 2015, the FASB issued Accounting Standards Update No. 2015-16, "Simplifying the Accounting for Measurement Period Adjustments" (Topic 805) (ASU 2015-16). The provisions of ASU 2015-16 require an acquirer to recognize adjustments to provisional amounts identified during the measurement period in the reporting period in which the adjustments are determined. We have elected the early adoption provision of this standard in the quarter ended March 31, 2016. During the quarter ended March 31, 2016, certain adjustments were made to the fair value estimates of property, plant and equipment. In accordance with the provisions of ASU 2015-16, we recorded the effect on the fair value of the assets as if the change had been completed as of the acquisition date, and we recorded the change in depreciation expense, which was not material, in earnings during the quarter ended March 31, 2016.

The fair values of identifiable assets and liabilities acquired were developed with the assistance of third party valuation experts. The fair value of acquired property, plant and equipment is valued at its "value-in-use" as there are no known plans to dispose of any assets. The fair value of acquired identifiable intangible assets was determined using the "income approach" on an individual asset basis. The key assumptions used in the calculation of the discounted cash flows include projected revenues, gross margin, and operating expenses. The valuations and the underlying assumptions have been deemed reasonable by Company management. There are inherent uncertainties and management judgment required in these determinations.

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The following table sets forth the components of identifiable intangible assets acquired and their estimated useful lives as of the date of acquisition:

|   | Preliminary<br>Fair Value | Useful<br>Life |
|---|---------------------------|----------------|
| Trade name                              | \$ 8,000                  | 7 years        |
| Customer relationships                  | 8,000                     | 11 years       |
| Developed technology - product family A | 25,000                    | 7 years        |
| Developed technology - product family B | 8,000                     | 8 years        |
| In-process technology                   | 12,000                    |                |
| Total preliminary intangible assets     | \$ 61,000                 |                |

The trade name represents the estimated fair value of the brand and name recognition associated with the marketing of NexPlanar's product offerings. Customer relationships represent the estimated fair value of the underlying relationships and agreements with NexPlanar customers. Developed technology represents the estimated fair value of NexPlanar's knowledge regarding its product offerings. In-process technology represents the fair value assigned to technology projects under development as of the acquisition date. The in-process technology assets are capitalized and accounted for as indefinite-lived intangible assets and will be subject to impairment testing until completion or abandonment of the projects. Upon successful completion of each project, we will make a determination of the appropriate useful life and the related amortization will be recorded as an expense over the estimated useful life based on the future expected cash flow stream. The intangible assets subject to amortization have a weighted average useful life of 7.8 years.

The excess of preliminary purchase consideration over the preliminary fair value of net assets acquired was recorded as goodwill, and is not deductible for income tax purposes. The goodwill is primarily attributable to anticipated revenue growth from the combination of our and NexPlanar pad technologies, expected synergies from the combined operations, and the assembled workforce of NexPlanar.

NexPlanar's results of operations have been included in our unaudited consolidated statements of income and comprehensive income from the date of acquisition. We incurred \$816 in professional fees related to the acquisition, \$526 of which were recorded as general and administrative expense during the fourth quarter of fiscal 2015, and \$290 of which were recorded as general and administrative expense during the first quarter of fiscal 2016. As previously discussed, we recorded \$605 in compensation expense during the quarter ended December 31, 2015, related to the cash settlement of certain unvested NexPlanar stock options. See Note 12 of this Form 10-Q for additional discussion of share-based compensation.

The following supplemental pro forma information summarizes the combined results of operations for Cabot Microelectronics and NexPlanar as if the acquisition had occurred on October 1, 2014.

|                              | Three Months<br>Ended March 31, |           | Six Months Ended<br>March 31, |           |
|------------------------------|---------------------------------|-----------|-------------------------------|-----------|
|                              | 2016                            | 2015      | 2016                          | 2015      |
| Revenues                     | \$99,244                        | \$110,758 | \$201,020                     | \$228,327 |
| Net income                   | 9,131                           | 12,201    | 21,503                        | 29,016    |
| Earnings per share - basic   | 0.38                            | 0.50      | 0.89                          | 1.20      |
| Earnings per share - diluted | \$0.37                          | \$0.49    | \$0.87                        | \$1.17    |

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The historical financial information has been adjusted to give effect to pro forma adjustments, which consist of amortization expense associated with intangible assets, and the elimination of interest expense on NexPlanar debt repaid prior to the acquisition. The proforma for the six months ended March 31, 2016 exclude the impact of \$605 in compensation expense related to unvested NexPlanar stock options settled in cash, and \$403 for the step-up of inventory as these items are assumed to have occurred during the quarter ended December 31, 2014 had the acquisition been completed on October 1, 2014. The pro forma adjustments are based on information currently available. Therefore, the pro forma consolidated results are not necessarily indicative of what the consolidated results actually would have been had the acquisition been completed on October 1, 2014. The pro forma consolidated results do not purport to project future results of combined operations, nor do they reflect the expected realization of any revenue or cost synergies associated with the acquisition.

## 3. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is defined as the price that would be received from the sale of an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The FASB established a three-level hierarchy for disclosure based on the extent and level of judgment used to estimate fair value. Level 1 inputs consist of valuations based on quoted market prices in active markets for identical assets or liabilities. Level 2 inputs consist of valuations based on quoted prices for similar assets or liabilities, quoted prices for identical assets or liabilities in an inactive market, or other observable inputs. Level 3 inputs consist of valuations based on unobservable inputs that are supported by little or no market activity.

The following table presents financial instruments, other than long-term debt, that we measured at fair value on a recurring basis at March 31, 2016 and September 30, 2015. See Note 8 for a detailed discussion of our long-term debt. We have classified the following assets and liabilities in accordance with the fair value hierarchy set forth in the applicable standards.

|                                  |           | Level   | Level | Total     |
|----------------------------------|-----------|---------|-------|-----------|
|                                  | Level 1   | 2       | 3     | Fair      |
| March 31, 2016                   |           |         |       | Value     |
| Assets:                          |           |         |       |           |
| Cash and cash equivalents        | \$226,388 | \$-     | \$ -  | \$226,388 |
| Other long-term investments      | 1,497     | -       | -     | 1,497     |
| Derivative financial instruments | -         | 169     | -     | 169       |
| Total assets                     | \$227,885 | \$169   | \$ -  | \$228,054 |
| Liabilities:                     |           |         |       |           |
| Derivative financial instruments | -         | 1,552   | -     | 1,552     |
| Total liabilities                | \$-       | \$1,552 | \$ -  | \$1,552   |

|                                  |           | Level | Level | Total     |
|----------------------------------|-----------|-------|-------|-----------|
|                                  | Level 1   | 2     | 3     | Fair      |
| September 30, 2015               |           |       |       | Value     |
| Assets:                          |           |       |       |           |
| Cash and cash equivalents        | \$354,190 | \$-   | \$ -  | \$354,190 |
| Other long-term investments      | 1,720     | -     | -     | 1,720     |
| Derivative financial instruments | -         | 14    | -     | 14        |
| Total assets                     | \$355,910 | \$14  | \$ -  | \$355,924 |

Liabilities:

|                                  |     |         |      |         |
|----------------------------------|-----|---------|------|---------|
| Derivative financial instruments | -   | 1,406   | -    | 1,406   |
| Total liabilities                | \$- | \$1,406 | \$ - | \$1,406 |

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Our cash and cash equivalents consist of various bank accounts used to support our operations and investments in institutional money-market funds which are traded in active markets. Our other long-term investments represent the fair value of investments under the Cabot Microelectronics Supplemental Employee Retirement Plan (SERP), which is a nonqualified supplemental savings plan, and these are included in other long-term assets on our Consolidated Balance Sheet. The fair value of the investments is determined through quoted market prices within actively traded markets. Although the investments are allocated to individual participants and investment decisions are made solely by those participants, the SERP is a nonqualified plan. Consequently, the Company owns the assets and the related offsetting liability for disbursement until such time a participant makes a qualifying withdrawal. The long-term asset was adjusted to \$1,497 in the second quarter of fiscal 2016 to reflect its fair value as of March 31, 2016.

In the first quarter of fiscal 2015, we entered into floating-to-fixed interest rate swap agreements to hedge the variability in LIBOR-based interest payments on a portion of our outstanding variable rate debt. These interest rate swaps represent our primary use of derivative financial instruments. The fair value of our derivative instruments is estimated using standard valuation models using market-based observable inputs over the contractual term, including one-month LIBOR-based yield curves, among others. We consider the risk of nonperformance, including counterparty credit risk, in the calculation of the fair value of derivative financial instruments. See Note 9 of this Form 10-Q for more information on our use of derivative financial instruments.

## 4. INVENTORIES, NET

Inventories, net consisted of the following:

|                 | March<br>31,<br>2016 | September<br>30, 2015 |
|-----------------|----------------------|-----------------------|
| Raw materials   | \$48,394             | \$ 42,603             |
| Work in process | 5,761                | 5,487                 |
| Finished goods  | 22,170               | 22,588                |
| Total           | \$76,325             | \$ 70,678             |

## 5. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill was \$95,645 as of March 31, 2016, and \$40,442 as of September 30, 2015. The increase in goodwill was due to \$54,405 in goodwill related to the acquisition of NexPlanar and \$798 in foreign exchange fluctuations of the New Taiwan dollar.



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The components of other intangible assets are as follows:

|   | March 31, 2016  |                          | September 30, 2015 |                          |
|---|-----------------|--------------------------|--------------------|--------------------------|
|   | Carrying Amount | Accumulated Amortization | Carrying Amount    | Accumulated Amortization |
| Other intangible assets subject to amortization:          |                 |                          |                    |                          |
| Product technology  | \$41,117        | \$ 10,010                | \$8,053            | \$ 7,490                 |
| Acquired patents and licenses                             | 8,270           | 8,000                    | 8,270              | 7,845                    |
| Trade secrets and know-how                                | 2,550           | 2,550                    | 2,550              | 2,550                    |
| Customer relationships, distribution rights and other     | 27,620          | 10,530                   | 11,392             | 9,005                    |
| Total other intangible assets subject to amortization     | 79,557          | 31,090                   | 30,265             | 26,890                   |
| In-process technology                                     | 12,000          |                          | -                  |                          |
| Other indefinite-lived intangibles*                       | 1,190           |                          | 1,190              |                          |
| Total other intangible assets not subject to amortization | 13,190          |                          | 1,190              |                          |
| Total other intangible assets                             | \$92,747        | \$ 31,090                | \$31,455           | \$ 26,890                |

\*Other indefinite-lived intangible assets not subject to amortization consist primarily of trade names.

As discussed in Note 2, we recorded \$61,000 of intangible assets related to our acquisition of NexPlanar. The allocation of that amount into the various categories of intangible assets, as well as the useful lives we have established, are discussed in Note 2.

Amortization expense on our other intangible assets was \$2,138 and \$3,954 for the three and six months ended March 31, 2016 respectively, and was \$582 and \$1,175 for the three and six months ended and March 31, 2015, respectively. Estimated future amortization expense for the five succeeding fiscal years is as follows:

| Fiscal Year       | Estimated Amortization Expense |
|-------------------|--------------------------------|
| Remainder of 2016 | \$ 4,024                       |
| 2017              | 7,529                          |
| 2018              | 6,870                          |
| 2019              | 6,453                          |
| 2020              | 6,448                          |

Goodwill and indefinite-lived intangible assets are tested for impairment annually in the fourth quarter of the fiscal year or more frequently if indicators of potential impairment exist, using a fair-value-based approach. The recoverability of goodwill is measured at the reporting unit level, which is defined as either an operating segment or one level below an operating segment. An entity has the option to assess the fair value of a reporting unit either using a qualitative analysis ("step zero") or a discounted cash flow analysis ("step one"). Similarly, an entity has the option to use a step zero or a step one approach to determine the recoverability of indefinite-lived intangible assets. In fiscal 2015, we chose to use a step one analysis for both goodwill impairment and for indefinite-lived intangible asset impairment.

We completed our annual impairment test during our fourth quarter of fiscal 2015 and concluded that no impairment existed. There were no indicators of potential impairment during the quarter ended March 31, 2016, so it was not

necessary to perform an impairment review for goodwill and indefinite-lived intangible assets during the quarter. There have been no cumulative impairment charges recorded on the goodwill for any of our reporting units.

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## 6. OTHER LONG-TERM ASSETS

Other long-term assets consisted of the following:

|                               | March<br>31,<br>2016 | September<br>30, 2015 |
|-------------------------------|----------------------|-----------------------|
| Auction rate securities (ARS) | \$5,694              | \$ 5,694              |
| Other long-term assets        | 4,120                | 3,595                 |
| Long-term contract asset      | 3,525                | 3,995                 |
| Other long-term investments   | 1,497                | 1,720                 |
| Total                         | \$14,836             | \$ 15,004             |

We classify our ARS investments as held-to-maturity and have recorded them at cost. Our ARS investments at March 31, 2016 consisted of two tax exempt municipal debt securities with a total par value of \$5,694, both of which have maturities greater than ten years. The ARS market began to experience illiquidity in early 2008, and this illiquidity continues. Despite this lack of liquidity, there have been no defaults in payment of the underlying securities and interest income on these holdings continues to be received on scheduled interest payment dates. Our ARS, when purchased, were issued by A-rated municipalities. Although the credit ratings of both municipalities have been downgraded since our original investment, one of the ARS is credit enhanced with bond insurance, and the other has become an obligation of the bond insurer. Both ARS currently carry a credit rating of AA- by Standard & Poor's.

The fair value of our ARS, determined using level 2 fair value inputs, was \$5,121 as of March 31, 2016. We have classified our ARS as held-to-maturity based on our intention and ability to hold the securities until maturity. We believe the gross unrecognized loss of \$573 is due to the illiquidity in the ARS market, rather than to credit loss. Although we believe these securities will ultimately be collected in full, we believe that it is not likely that we will be able to monetize the securities in our next business cycle (which for us is generally one year). We will continue to monitor our ARS for impairment indicators, which may require us to record an impairment charge that is deemed other-than-temporary.

In the third quarter of fiscal 2015, we amended a supply contract with an existing supplier. The amended agreement includes a fee of \$4,500, which provides us the option to purchase certain raw materials beyond calendar 2016. This fee was recorded as a long-term asset at its present value and is being amortized into cost of goods sold on a straight-line basis through December 31, 2019, the expiration date of the agreement. See Note 10 for more information regarding this contract.

Other long-term assets are comprised of the long-term portion of prepaid unamortized debt costs as well as miscellaneous deposits and prepayments on contracts extending beyond the next 12 months. As discussed in Note 3, we recorded a long-term asset and a corresponding long-term liability of \$1,497 representing the fair value of our SERP investments as of March 31, 2016.

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## 7. ACCRUED EXPENSES, INCOME TAXES PAYABLE AND OTHER CURRENT LIABILITIES

Accrued expenses, income taxes payable and other current liabilities consisted of the following:

|   | March<br>31,<br>2016 | September<br>30, 2015 |
|---|----------------------|-----------------------|
| Accrued compensation                          | \$13,981             | \$ 23,793             |
| Dividends payable                             | 4,355                | -                     |
| Goods and services received, not yet invoiced | 2,394                | 1,830                 |
| Deferred revenue and customer advances        | 465                  | 538                   |
| Warranty accrual                              | 211                  | 209                   |
| Income taxes payable                          | 7,335                | 4,276                 |
| Taxes, other than income taxes                | 1,404                | 975                   |
| Other accrued expenses                        | 4,310                | 4,825                 |
| Total   | \$34,455             | \$ 36,446             |

The dividends payable reflected in the table are excluded from the financing activities in the Consolidated Statement of Cash Flows as they were not paid as of March 31, 2016.

## 8. DEBT

On February 13, 2012, we entered into a credit agreement (the "Credit Agreement") among the Company, as Borrower, Bank of America, N.A., as administrative agent, swing line lender and an L/C issuer, Bank of America Merrill Lynch and J.P. Morgan Securities LLC, as joint lead arrangers and joint book managers, JPMorgan Chase Bank, N.A., as syndication agent, and Wells Fargo Bank, N.A. as documentation agent. The Credit Agreement provided us with a \$175,000 term loan (the "Term Loan"), which we drew on February 27, 2012 to fund approximately half of the special cash dividend we paid to our stockholders on March 1, 2012, and a \$100,000 revolving credit facility (the "Revolving Credit Facility"), which has never been drawn, with sub-limits for multicurrency borrowings, letters of credit and swing-line loans. The Term Loan and the Revolving Credit Facility are referred to as the "Credit Facilities." On June 27, 2014, we entered into an amendment (the "Amendment") to the Credit Agreement, which (i) increased term loan commitments by \$17,500, from \$157,500 to \$175,000, the same level as the original amount under the Credit Agreement at its inception in 2012; (ii) increased the uncommitted accordion feature on the Revolving Credit Facility from \$75,000 to \$100,000; (iii) extended the expiration date of the Credit Facilities from February 13, 2017 to June 27, 2019; (iv) relaxed the consolidated leverage ratio financial covenant; and (v) revised certain pricing terms and other terms within the Credit Agreement. On June 27, 2014, we drew the \$17,500 of increased term loan commitments, bringing the total outstanding commitments under the Term Loan to \$175,000.

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Borrowings under the amended Credit Facilities (other than in respect of swing-line loans) bear interest at a rate per annum equal to the "Applicable Rate" (as defined below) plus, at our option, either (1) a LIBOR rate determined by reference to the cost of funds for deposits in the relevant currency for the interest period relevant to such borrowing or (2) the "Base Rate", which is the highest of (x) the prime rate of Bank of America, N.A., (y) the federal funds rate plus 1/2 of 1.00% and (z) the one-month LIBOR rate plus 1.00%. The current Applicable Rate for borrowings under the Credit Facilities is 1.50% with respect to LIBOR borrowings and 0.25% with respect to Base Rate borrowings, with such Applicable Rate subject to adjustment based on our consolidated leverage ratio. Swing-line loans bear interest at the Base Rate plus the Applicable Rate for Base Rate loans under the Revolving Credit Facility. In addition to paying interest on outstanding principal under the Credit Agreement, we pay a commitment fee to the lenders under the Revolving Credit Facility in respect of the unutilized commitments thereunder. The fee ranges from 0.20% to 0.30%, based on our consolidated leverage ratio. Interest expense and commitment fees are paid according to the relevant interest period and no less frequently than at the end of each calendar quarter. We paid \$2,658 in arrangement fees, upfront fees and administration fees in February 2012 and we paid an additional \$550 in upfront fees and arrangement fees in June 2014, of which \$397 remains in prepaid expenses and other current assets and \$880 remains in other long-term assets on our Consolidated Balance Sheet as of March 31, 2016. We also pay letter of credit fees as necessary. The Term Loan has periodic scheduled repayments; however, we may voluntarily prepay the Credit Facilities without premium or penalty, subject to customary "breakage" fees and reemployment costs in the case of LIBOR borrowings. All obligations under the Credit Agreement are guaranteed by certain of our existing and future direct and indirect domestic subsidiaries. The obligations under the Credit Agreement and guarantees of those obligations are secured, subject to certain exceptions, by first priority liens and security interests in the assets of the Company and certain of its domestic subsidiaries.

In the first quarter of fiscal 2015, we entered into interest rate swap agreements that have the economic effect of converting fifty percent of our variable rate debt into fixed rate debt at a weighted average fixed rate of 1.5% plus the Applicable Rate defined above. See Notes 3 and 9 for additional information on the interest rate swap agreements.

The Credit Agreement contains covenants that restrict the ability of the Company and its subsidiaries to take certain actions, including, among other things and subject to certain significant exceptions: creating liens, incurring indebtedness, making investments, engaging in mergers, selling property, paying dividends or amending organizational documents. The Credit Agreement requires us to comply with certain financial ratio maintenance covenants. These include a maximum consolidated leverage ratio of 2.75 to 1.00 and a minimum consolidated fixed charge coverage ratio of 1.25 to 1.00 for the period January 1, 2016 through the expiration of the Credit Agreement. As of March 31, 2016, our consolidated leverage ratio was 1.61 to 1.00 and our consolidated fixed charge coverage ratio was 4.46 to 1.00. The Credit Agreement also contains customary affirmative covenants and events of default. We believe we are in compliance with these covenants.

At March 31, 2016, the fair value of the Term Loan, using level 2 inputs, approximates its carrying value of \$159,688 as the loan bears a floating market rate of interest. As of March 31, 2016, \$8,750 of the debt outstanding is classified as short-term.

Principal repayments of the Term Loan are generally made on the last calendar day of each quarter if that day is considered to be a business day. As of March 31, 2016, scheduled principal repayments of the Term Loan were as follows:

| Fiscal Year       | Principal Repayments |
|-------------------|----------------------|
| Remainder of 2016 | \$ 4,375             |
| 2017              | 7,656                |
| 2018              | 14,219               |
| 2019              | 133,438              |

Total \$ 159,688

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## 9. DERIVATIVE FINANCIAL INSTRUMENTS

We are exposed to various market risks, including interest rates and foreign currency exchange rates. We enter into certain derivative transactions to mitigate the volatility associated with these exposures. We have policies in place that define acceptable instrument types we may enter into and we have established controls to limit our market risk exposure. We do not use derivative financial instruments for trading or speculative purposes. In addition, all derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value on a gross basis.

Cash Flow Hedges – Interest Rate Swap Agreements

In the first quarter of fiscal 2015, we entered into floating-to-fixed interest rate swap agreements to hedge the variability in LIBOR-based interest payments on \$86,406 of our outstanding variable rate debt. The notional amount of the swaps decreases each quarter by an amount in proportion to our scheduled quarterly principal repayment of debt. The notional value of the swaps was \$79,844 as of March 31, 2016, and the swaps are scheduled to expire on June 27, 2019.

We have designated these swap agreements as cash flow hedges pursuant to ASC 815, "Derivatives and Hedging". As cash flow hedges, unrealized gains are recognized as assets and unrealized losses are recognized as liabilities. Unrealized gains and losses are designated as effective or ineffective based on a comparison of the changes in fair value of the interest rate swaps and the change in fair value of the underlying exposures being hedged. The effective portion is recorded as a component of accumulated other comprehensive income or loss, while the ineffective portion is recorded as a component of interest expense. Changes in the method by which we pay interest from one-month LIBOR to another rate of interest could create ineffectiveness in the swaps, and result in amounts being reclassified from other comprehensive income into net income. Hedge effectiveness is tested quarterly to determine if hedge treatment is appropriate.

Foreign Currency Contracts Not Designated as Hedges

Periodically we enter into forward foreign exchange contracts in an effort to mitigate the risks associated with currency fluctuations on certain foreign currency balance sheet exposures. Our foreign exchange contracts do not qualify for hedge accounting; therefore, the gains and losses resulting from the impact of currency exchange rate movements on our forward foreign exchange contracts are recognized as other income or expense in the accompanying consolidated income statements in the period in which the exchange rates change. As of March 31, 2016 and September 30, 2015, respectively, the notional amounts of the forward contracts we held to purchase U.S. dollars in exchange for other international currencies were \$1,098 and \$1,034, respectively, and the notional amounts of forward contracts we held to sell U.S. dollars in exchange for other international currencies were \$19,050 and \$18,690, respectively.

The fair value of our derivative instruments included in the Consolidated Balance Sheet, which was determined using level 2 inputs, was as follows:

| Balance Sheet Location                        | Asset<br>Derivatives |  | Liability<br>Derivatives |                       |
|---|----------------------|--|--------------------------|-----------------------|
|   | March<br>31,<br>2016 | September<br>30, 2015                          | March<br>31,<br>2016     | September<br>30, 2015 |
| Derivatives designated as hedging instruments |                      |  |                          |                       |
| Interest rate swap contracts                  |                      | Accrued expenses and other current liabilities | \$ -                     | \$ -                  |
|   |                      |  | \$ 716                   | \$ 885                |

|   |   |        |       |       |        |
|---|---|--------|-------|-------|--------|
| Other long-term liabilities                       |   | \$-    | \$ -  | \$824 | \$ 513 |
| Derivatives not designated as hedging instruments |   |        |       |       |        |
|   | Prepaid expenses and other current assets |        |       |       |        |
| Foreign exchange contracts                        |   | \$ 169 | \$ 14 | \$-   | \$ -   |
| Accrued expenses and other current liabilities    |   | \$-    | \$ -  | \$12  | \$ 8   |



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The following table summarizes the effect of our derivative instruments on our Consolidated Statement of Income for the three and six months ended March 31, 2016 and 2015:

| Statement of Income Location                      | Gain (Loss) Recognized in<br>Statement of Income |         |  |           |
|---|--|---------|--|-----------|
|   | Three Months<br>Ended<br>March 31,<br>2016       |         | Six Months<br>Ended<br>March 31,<br>2015 |           |
| Derivatives not designated as hedging instruments |  |         |  |           |
| Foreign exchange contracts                        |  |         |  |           |
| Other income (expense), net                       | \$ 698   | \$(344) | \$ 512                                   | \$(1,680) |

The interest rate swap agreements were deemed to be effective since inception, so there was no impact on our Consolidated Statement of Income. We recorded a \$92 unrealized loss in accumulated comprehensive income during the six months ended March 31, 2016 for these interest rate swaps. During the next 12 months, we expect approximately \$734 may be reclassified from accumulated other comprehensive income into interest expense related to our interest rate swaps based on projected rates of the LIBOR forward curve as of March 31, 2016.

## 10. COMMITMENTS AND CONTINGENCIES

## LEGAL PROCEEDINGS

While we are not involved in any legal proceedings that we believe will have a material impact on our consolidated financial position, results of operations or cash flows, we periodically become a party to legal proceedings in the ordinary course of business.

Refer to Note 17 of "Notes to the Consolidated Financial Statements" in Item 8 of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015, for additional information regarding commitments and contingencies.

## PRODUCT WARRANTIES

We maintain a warranty reserve that reflects management's best estimate of the cost to replace product that does not meet our specifications and customers' performance requirements, and costs related to such replacement. The warranty reserve is based upon a historical product replacement rate, adjusted for any specific known conditions or circumstances. Additions and deductions to the warranty reserve are recorded in cost of goods sold. Our warranty reserve activity during the first six months of fiscal 2016 was as follows:

|  |       |
|--|-------|
| Balance as of September 30, 2015                         | \$209 |
| Reserve for product warranty during the reporting period | 312   |
| Settlement of warranty                                   | (310) |
| Balance as of March 31, 2016                             | \$211 |

## POSTRETIREMENT OBLIGATIONS IN FOREIGN JURISDICTIONS

We have unfunded defined benefit plans covering employees in certain foreign jurisdictions as required by local law. Benefit costs, consisting primarily of service costs, are recorded as fringe benefit expense under cost of goods sold

and operating expenses in our Consolidated Statements of Income. The projected benefit obligations and accumulated benefit obligations under all such unfunded plans are updated annually during the fourth quarter of the fiscal year. Benefit payments under all such unfunded plans to be paid over the next 10 years are expected to be approximately \$2,188. For more information regarding these plans, refer to Note 17 of "Notes to the Consolidated Financial Statements" included in Item 8 of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

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## PURCHASE OBLIGATIONS

Purchase obligations include our take-or-pay arrangements with suppliers, and purchase orders and other obligations entered into in the normal course of business regarding the purchase of goods and services. We have been operating under a fumed silica supply agreement with Cabot Corporation, our former parent company which is not a related party, which had a termination date of December 31, 2016, which required us to purchase certain minimum quantities of fumed silica each year of the agreement, and to pay a shortfall if we purchased less than the minimum. This agreement was amended effective June 1, 2015 to, among other things, extend the term of the agreement through December 31, 2019, revise certain minimum purchase requirements through 2016, and provide us the option to purchase fumed silica for the remaining term of the agreement beyond calendar year 2016, for which we will pay a fee of \$1,500 in each of calendar years 2017, 2018 and 2019. This fee is included in other long-term liabilities at its present value of \$3,525 as of March 31, 2016. As of March 31, 2016, purchase obligations include \$12,924 of contractual commitments related to our Cabot Corporation supply agreement for fumed silica.

## 11. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The components of accumulated other comprehensive income (AOCI), including the reclassification adjustments for items that are reclassified from AOCI to net income, are shown below:

|   | Foreign<br>Currency<br>Translation | Cash<br>Flow<br>Hedges | Pension and<br>Other<br>Postretirement<br>Liabilities | Total      |
|---|------------------------------------|------------------------|---|------------|
| Balance at September 30, 2015   | \$ (4,011 )                        | \$ (901 )              | \$ (1,178 )   | \$ (6,090) |
| Foreign currency translation adjustment, net of tax of \$622                | 6,357                              | -                      | -   | 6,357      |
| Unrealized loss on cash flow hedges:  |                                    |                        |   |            |
| Change in fair value, net of tax of \$(71)                                  | -                                  | (127 )                 | -   | (127 )     |
| Reclassification adjustment into earnings, net of tax of \$20               | -                                  | 35                     | -   | 35         |
| Change in pension and other postretirement liabilities, net of tax of \$287 | -                                  | -                      | 287   | 287        |
| Balance at March 31, 2016   | \$ 2,346                           | \$ (993 )              | \$ (891 )   | \$ 462     |

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|  | Foreign<br>Currency<br>Translation | Cash<br>Flow<br>Hedges | Pension and<br>Other<br>Postretirement<br>Liabilities | Total   |
|--|------------------------------------|------------------------|---|---------|
| Balance at September 30, 2014  | \$ 10,115                          | \$ -                   | \$ (860 )   | \$9,255 |
| Foreign currency translation adjustment, net of tax \$(1,790)              | (8,284 )                           | -                      | -   | (8,284) |
| Unrealized loss on cash flow hedges:                                       |                                    |                        |   |         |
| Change in fair value, net of tax of tax \$(476)                            | -                                  | (863 )                 | -   | (863 )  |
| Reclassification adjustment into earnings, net of tax of \$138             | -                                  | 251                    | -   | 251     |
| Change in pension and other postretirement liabilities, net of tax of \$ 0 | -                                  | -                      | -   | -       |
| Balance at March 31, 2015  | \$ 1,831                           | \$ (612 )              | \$ (860 )   | \$ 359  |

The pretax amounts reclassified from OCI to net income during the six months ended March 31, 2016 and 2015, related to our cash flow hedges, were recorded as interest expense on our Consolidated Statement of Income.

## 12. SHARE-BASED COMPENSATION PLANS

We issue share-based awards under the following programs: our Cabot Microelectronics Corporation 2012 Omnibus Incentive Plan (OIP); our Cabot Microelectronics Corporation 2007 Employee Stock Purchase Plan, as Amended and Restated September 23, 2013 (ESPP); and pursuant to the OIP, our Directors' Deferred Compensation Plan, as amended September 23, 2008 (DDCP), and our 2001 Executive Officer Deposit Share Program (DSP). Prior to March 2012, when our stockholders approved the OIP, we issued share-based payments under our Second Amended and Restated Cabot Microelectronics Corporation 2000 Equity Incentive Plan, as amended and restated September 23, 2008 (EIP), our ESPP, and, pursuant to the EIP, the DDCP and DSP. For additional information regarding these programs, refer to Note 12 of "Notes to the Consolidated Financial Statements" included in Item 8 of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015. Other than the ESPP, all share-based payments granted beginning March 6, 2012 are made from the OIP, and since then, the EIP no longer has been available for any awards.

We record share-based compensation expense for all share-based awards, including stock option grants, restricted stock and restricted stock unit awards and employee stock purchase plan purchases. We calculate share-based compensation expense using the straight-line approach based on awards ultimately expected to vest, which requires the use of an estimated forfeiture rate. Our estimated forfeiture rate is primarily based on historical experience, but may be revised in future periods if actual forfeitures differ from the estimate. We use the Black-Scholes option-pricing model to estimate the grant date fair value of our stock options and employee stock purchase plan purchases. This model requires the input of highly subjective assumptions, including the price volatility of the underlying stock, the expected term of our stock options; expected dividend yield and the risk-free interest rate. We estimate the expected volatility of our stock options based on a combination of our stock's historical volatility and the implied volatilities from actively-traded options on our stock. We calculate the expected term of our stock options using historical stock option exercise data, and we add a slight premium to this expected term for employees who meet the definition of retirement-eligible pursuant to their grants during the contractual term of the grant. The expected dividend yield represents our annualized dividend in dollars divided by the stock price on the date of grant. The risk-free interest rate is derived from the U.S. Treasury yield curve in effect at the time of grant.

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Share-based compensation expense for the three and six months ended March 31, 2016, and 2015, was as follows:

|  | Three Months            |         | Six Months              |         |
|--|-------------------------|---------|-------------------------|---------|
|  | Ended March 31,<br>2016 | 2015    | Ended March 31,<br>2016 | 2015    |
| Cost of goods sold                                 | \$535                   | \$463   | \$1,069                 | \$961   |
| Research, development and technical                | 416                     | 384     | 834                     | 799     |
| Selling and marketing                              | 411                     | 248     | 815                     | 568     |
| General and administrative                         | 2,373                   | 4,204   | 6,089                   | 6,378   |
| Total share-based compensation expense             | 3,735                   | 5,299   | 8,807                   | 8,706   |
| Tax benefit  | (1,274)                 | (1,842) | (2,988)                 | (2,964) |
| Total share-based compensation expense, net of tax | \$2,461                 | \$3,457 | \$5,819                 | \$5,742 |

As discussed in Note 2, during the quarter ended December 31, 2015, we recorded \$605 in share-based compensation expense related to certain unvested NexPlanar incentive stock options (ISOs) settled in cash at the acquisition date. This amount represents the portion of the fair value of the original awards related to the post-acquisition period had these awards not been settled in cash at the acquisition date. U.S. GAAP prescribes that the portion of fair value of equity awards related to pre-acquisition service periods represents purchase consideration and the portion of fair value related to post-acquisition service periods represents compensation expense. Since the post-acquisition service requirement was eliminated through the cash settlement, the compensation expense was recorded immediately following the acquisition date. We also substituted certain NexPlanar ISOs with Cabot Microelectronics Corporation ISOs, preserving the intrinsic value, including the original vesting periods, of the original awards. We accelerated the vesting on the substitute awards made to certain individuals based on the terms of their employment agreements and recorded \$492 of share-based compensation expense related to this acceleration. The total \$1,097 of acquisition-related compensation is included in the table above as general and administrative expense.

Our non-employee directors received annual equity awards in March 2016, pursuant to the OIP. The award agreements provide for immediate vesting of the award at the time of termination of service for any reason other than by reason of Cause, Death, Disability or a Change in Control, as defined in the OIP, if at such time the non-employee director has completed an equivalent of at least two full terms as a director of the Company, as defined in the Company's bylaws. Five of the Company's non-employee directors had completed at least two full terms of service as of the date of the March 2016 award. Consequently, the requisite service period for the award has already been satisfied and we recorded the fair value of \$879 of the awards to these five directors to share-based compensation expense in the fiscal quarter ended March 31, 2016 rather than recording that expense over the one-year vesting period stated in the award agreement, as is done for the other non-employee directors who received an annual equity award in March 2016.

As discussed in our Quarterly Report on Form 10-Q for the quarter ended December 31, 2014, all unvested stock options and restricted stock held by our former President and Chief Executive Officer vested in full on December 31, 2015, in accordance with the terms of his employment letter with the Company dated December 12, 2014. We applied the accounting guidance under Accounting Standards Codification (ASC) Topic 718 "Stock Compensation" to determine the additional share-based compensation expense to be recorded as part of the modification of the outstanding equity. The original fair value of his unvested equity totaling \$5,033 was recorded ratably between the date of modification and December 31, 2015, rather than recording the expense over the original vesting period. During the quarter ended December 31, 2014, we recorded \$378 in share-based compensation expense related to this modification.

For additional information regarding the estimation of fair value, refer to Note 12 of "Notes to the Consolidated Financial Statements" included in Item 8 of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

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## 13. OTHER INCOME (EXPENSE), NET

Other income (expense), net, consisted of the following:

|                                   | Three Months<br>Ended March<br>31,<br>2016 |         | Six Months<br>Ended<br>March 31,<br>2015 |       |
|-----------------------------------|--|---------|--|-------|
| Interest income                   | \$178                                      | \$45    | \$387                                    | \$148 |
| Other income (expense)            | 274  | (377)   | 255                                      | 577   |
| Total other income (expense), net | \$452                                      | \$(332) | \$642                                    | \$725 |

Other income (expense) primarily represents gains and losses recorded on transactions denominated in foreign currencies. The increase in other income during the three months ended March 31, 2016 was primarily due to the impact of foreign currency fluctuations on monetary assets and liabilities denominated in currencies other than the functional currency, net of the gains and losses incurred on forward foreign exchange contracts discussed in Note 9, and a cash supplier award received this quarter.

## 14. INCOME TAXES

Our effective income tax rate was 21.0% and 18.1% for the three and six months ended March 31, 2016, respectively, compared to a 23.6% and 17.3 % effective income tax rate for the three and six months ended March 31, 2015, respectively. The increase in the effective tax rate during the first six months of fiscal 2016 was primarily due to the change in mix of earnings between foreign and domestic, including a scheduled reduction in the benefit available under our tax holiday in South Korea, as discussed below. This was partially offset by the absence of income taxes incurred during the first quarter of fiscal 2015 related to the restructuring of our operations in Taiwan.

The Company is currently operating under a tax holiday in South Korea in conjunction with our investment in research, development and manufacturing facilities there. This arrangement allows for a tax at 50% of the statutory rate in effect in South Korea for fiscal years 2016 and 2017, following a 0% tax rate in fiscal years 2013, 2014 and 2015. This tax holiday reduced our income tax provision by approximately \$1,797 and \$2,260 in the first six months of fiscal 2016 and 2015, respectively. This tax holiday increased our diluted earnings per share by approximately \$0.07 and \$0.09 during the first six months of fiscal 2016 and 2015, respectively.

In November 2015, the FASB issued ASU No. 2015-17, "Balance Sheet Classification of Deferred Taxes" (Topic 740). The provisions of ASU 2015-17 require that deferred tax assets and liabilities be classified as noncurrent in a classified statement of financial position. We elected the early adoption provision of this standard in the quarter ended December 31, 2015, and have prospectively classified all deferred tax assets and liabilities as noncurrent on our consolidated balance sheet in accordance with this standard. We have not retrospectively adjusted the deferred tax balances as of September 30, 2015.

## 15. EARNINGS PER SHARE

Basic earnings per share (EPS) is calculated by dividing net income available to common stockholders by the weighted-average number of common shares outstanding during the period, excluding the effects of unvested restricted stock awards that have a right to receive non-forfeitable dividends, which are considered participating securities as prescribed by the two-class method under ASC 260. Diluted EPS is calculated in a similar manner, but the weighted-average number of common shares outstanding during the period is increased to include the

weighted-average dilutive effect of "in-the-money" stock options and unvested restricted stock shares using the treasury stock method.

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The standards of accounting for earnings per share require companies to provide a reconciliation of the numerator and denominator of the basic and diluted earnings per share computations. Basic and diluted earnings per share were calculated as follows:

|   | Three Months Ended |            | Six Months Ended March |            |
|---|--------------------|------------|------------------------|------------|
|   | March 31,<br>2016  | 2015       | 31,<br>2016            | 2015       |
| Numerator:  |                    |            |                        |            |
| Net Income  | \$9,131            | \$13,811   | \$20,440               | 33,727     |
| Less: income attributable to participating securities                           | (41)               | (183)      | (160)                  | (330)      |
| Earnings available to common shares   | \$9,090            | \$13,628   | \$20,280               | 33,397     |
| Denominator:  |                    |            |                        |            |
| Weighted average common shares<br>(Denominator for basic calculation)           | 24,061,005         | 24,056,881 | 24,069,557             | 23,845,012 |
| Weighted average effect of dilutive securities:                                 |                    |            |                        |            |
| Share-based compensation  | 346,615            | 636,000    | 374,098                | 737,382    |
| Diluted weighted average common shares<br>(Denominator for diluted calculation) | 24,407,620         | 24,692,881 | 24,443,655             | 24,582,394 |
| Earnings per share:   |                    |            |                        |            |
| Basic   | \$0.38             | \$0.57     | \$0.84                 | 1.40       |
| Diluted   | \$0.37             | \$0.55     | \$0.83                 | 1.36       |

For the three and six months ended March 31, 2016 and 2015, approximately 1.2 million and 0.8 million shares, respectively, attributable to outstanding stock options were excluded from the calculation of diluted earnings per share because the exercise price of the options was greater than the average market price of our common stock and, therefore, their inclusion would have been anti-dilutive.

## 16. FINANCIAL INFORMATION BY INDUSTRY SEGMENT AND PRODUCT LINE

We operate predominantly in one reportable segment, as defined under ASC 280 – the development, manufacture, and sale of CMP consumables.

Revenue generated by product line for the three and six months ended March 31, 2016, and 2015, was as follows:

|                             | Three Months            |           | Six Months Ended  |           |
|-----------------------------|-------------------------|-----------|-------------------|-----------|
|                             | Ended March 31,<br>2016 | 2015      | March 31,<br>2016 | 2015      |
| Revenue:                    |                         |           |                   |           |
| Tungsten slurries           | \$43,885                | \$43,658  | \$88,297          | \$88,802  |
| Dielectric slurries         | 23,679                  | 23,882    | 46,697            | 52,065    |
| Other Metals slurries       | 14,180                  | 18,331    | 30,538            | 38,228    |
| Polishing pads              | 11,943                  | 8,841     | 22,452            | 17,603    |
| Engineered Surface Finishes | 3,743                   | 6,212     | 7,695             | 11,794    |
| Data Storage slurries       | 1,814                   | 3,934     | 3,934             | 8,300     |
| Total revenue               | \$99,244                | \$104,858 | \$199,613         | \$216,792 |



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17. NEW ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), an updated standard on revenue recognition. ASU 2014-09 provides enhancements to how revenue is reported and improves comparability in the financial statements of companies reporting using IFRS and US GAAP. The core principle of the new standard is for companies to recognize revenue for goods or services in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard is intended to enhance disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively, such as service revenue and contract modifications, and improve guidance for multiple-element arrangements. In August 2015, the FASB issued ASU No. 2015-14, "Deferral of Effective Date" (Topic 606). This standard officially defers the effective date of ASU 2014-09 by one year. ASU 2014-09 will be effective for us beginning October 1, 2018, and may be applied on a full retrospective or modified retrospective approach. Adoption is not permitted prior to the original effective date of the ASU, which for us is October 1, 2017. In March 2016, the FASB issued ASU No. 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)" (Topic 606). ASU 2016-08 provides clarification for the implementation guidance on principal versus agent considerations. We are currently evaluating the impact of implementation of these standards on our financial statements.

In June 2014, the FASB issued ASU No. 2014-12, "Accounting for Share-Based Payments When the Terms of an Award Provide that a Performance Target Could be Achieved after the Requisite Service Period" (Topic 718). ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant date fair value of an award, and compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved. The compensation cost should represent the amount attributable to the periods for which the requisite service has been rendered. ASU 2014-12 will be effective for us beginning October 1, 2016 and may be applied on a prospective or retrospective basis. We do not expect the implementation of this standard to have a material effect on our financial statements as we have not granted any awards with a performance condition.

In January 2015, the FASB issued ASU No. 2015-01, "Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items" (Subtopic 225-20). ASU 2015-01 eliminates the concept of extraordinary items from U.S. GAAP, so an entity no longer needs to consider whether an underlying event or transaction is extraordinary. ASU 2015-01 retains the prior presentation and disclosure guidance for items that are unusual in nature or occur infrequently and will expand the guidance to include items that are both unusual in nature and infrequently occurring. ASU 2015-01 will be effective for us beginning October 1, 2016. We do not expect the implementation of this standard to have a material effect on our financial statements as we have not had any events or transactions that were considered to be extraordinary.

In February 2015, the FASB issued ASU No. 2015-02, "Amendments to the Consolidation Analysis" (Topic 810). ASU 2015-02 amends the criteria for determining which entities are considered variable interest entities (VIEs), amends the criteria for determining if a service provider possesses a variable interest in a VIE and ends the deferral granted to investment companies for application of the VIE consolidation model. ASU 2015-02 will be effective for us beginning October 1, 2016. We do not expect the implementation of this standard to have a material effect on our financial statements as we have no interests in any entities that may be considered VIEs.

In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs" (Subtopic 835-30). The provisions of ASU 2015-03 require an entity to present the debt issuance costs related to a recognized debt liability in the balance sheet as a direct deduction to the carry amount of that debt liability. ASU 2015-03 will be effective for us beginning October 1, 2016, but early adoption is permitted. The implementation of this standard will require us to reclassify our debt issuance costs related to our term loan from their asset position on our balance sheet

to a liability position as an offset to the carrying amount of our outstanding debt. We do not expect the implementation of this standard to have a material effect on our financial statements.

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In April 2015, the FASB issued ASU No. 2015-05, "Customer Accounting for Fees Paid in a Cloud Computing Arrangement" (Subtopic 350-40). ASU 2015-05 provides guidance to entities on accounting for entering into a cloud computing arrangement with and without a software license. If an arrangement includes a software license, then the purchaser should account for the software license element of the arrangement consistent with the treatment of other software licenses. If an arrangement does not include a software license, it should be treated as a service contract. ASU 2015-05 will be effective for us beginning October 1, 2016, but early adoption is permitted. We are currently evaluating the impact of implementation of this standard on our financial statements.

In July 2015, the FASB issued ASU No. 2015-11, "Simplifying the Measurement of Inventory" (Topic 330). The provisions of ASU 2015-11 require an entity to measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. ASU 2015-11 will be effective for us beginning October 1, 2017, but early adoption is permitted. We do not believe the adoption of this standard will have a material effect on our financial statements.

In August 2015, the FASB issued ASU No. 2015-15, "Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements" (Subtopic 835-30). ASU 2015-15 provides guidance on the treatment of debt issuance cost related to line-of-credit arrangements based on comments provided by the SEC staff. The SEC staff stated that it would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance cost ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. ASU 2015-15 will be effective for us beginning October 1, 2016, but early adoption is permitted. We are currently evaluating the impact of implementation of this standard on our financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Recognition and Measurement of Financial Assets and Financial Liabilities" (Subtopic 825-10). The provision of ASU 2016-01 requires equity investments, other than those accounted for under the equity method of accounting or those that result in consolidation, to be measured at fair value with changes in fair value recognized in net income. ASU 2016-01 simplifies the impairment assessment of equity securities by permitting a qualitative assessment each reporting period, and makes changes to presentation and disclosure of certain classes of financial assets and liabilities. ASU 2016-01 will be effective for us beginning October 1, 2018, but early adoption is permitted. We are currently evaluating the impact of implementation of this standard on our financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842). The provisions of ASU 2016-02 require a dual approach for lessee accounting under which a lessee would recognize a right-of-use asset and a corresponding lease liability. Leases will be classified as either finance or operating leases. For finance leases, a lessee will recognize interest expense and amortization of the right-of-use asset, and for operating leases, the lessee will recognize a straight-line total lease expense. The guidance also requires qualitative and specific quantitative disclosures to supplement the amounts recorded in the financial statements, to afford better understanding of an entity's leasing activities, including any significant judgments and estimates. ASU 2016-01 will be effective for us beginning October 1, 2019, but early adoption is permitted. We are currently evaluating the impact of implementation of this standard on our financial statements.

In March 2016, the FASB issued ASU No. 2016-05, "Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships" (Topic 815). The provisions of ASU 2016-05 provide clarification that a change in a counterparty of a derivative instrument that has been designated as a hedging instrument does not require dedesignation of that hedging relationship, provided that all other hedge accounting criteria is met. ASU 2016-05 will be effective for us beginning October 1, 2018, but early adoption is permitted. We do not believe the adoption of this standard will have a material effect on our financial statements.

In March 2016, the FASB issued ASU No. 2016-07, "Simplifying the Transition to the Equity Method of Accounting" (Topic 323). The provisions of ASU 2016-07 require equity method investors to add the cost of acquiring additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method prospectively as of the date the investment qualifies for the equity method of accounting. ASU 2016-05 will be effective for us beginning October 1, 2018, but early adoption is permitted. We do not believe the adoption of this standard will have a material effect on our financial statements as we currently have no equity method investments.

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In March 2016, the FASB issued ASU No. 2016-09, "Improvements to Employee Share Based Payment Accounting" (Topic 718). The provisions of this standard involve several aspects of the accounting for share-based payments transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-07 will be effective for us beginning October 1, 2017, but early adoption is permitted. We are currently evaluating the impact of implementation of this standard on our financial statements.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following "Management's Discussion and Analysis of Financial Condition and Results of Operations", as well as disclosures included elsewhere in this Form 10-Q, include "forwardlooking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. This Act provides a safe harbor for forwardlooking statements to encourage companies to provide prospective information about themselves so long as they identify these statements as forwardlooking and provide meaningful cautionary statements identifying important factors that could cause actual results to differ from the projected results. All statements other than statements of historical fact we make in this Form 10-Q are forwardlooking. In particular, the statements herein regarding future sales and operating results; growth or contraction of, and trends in, the industry and markets in which the Company participates; the Company's management; various economic factors and international events; regulatory or legislative activity; product performance; the generation, protection and acquisition of intellectual property, and litigation related to such intellectual property; new product introductions; development of new products, technologies and markets; the Company's supply chain; natural disasters; the acquisition of or investment in other entities, including NexPlanar Corporation (NexPlanar); uses and investment of the Company's cash balance, including dividends and share repurchases, which may be suspended, terminated or modified at any time for any reason, based on a variety of factors; financing facilities and related debt, payment of principal and interest, and compliance with covenants and other terms; the Company's capital structure; the Company's current or future tax rate; the operation of facilities by the Company; and statements preceded by, followed by or that include the words "intends," "estimates," "plans," "believes," "expects," "anticipates," "should," "could" or similar expressions, are forwardlooking statements. Forwardlooking statements reflect our current expectations and are inherently uncertain. Our actual results may differ significantly from our expectations. We assume no obligation to update this forwardlooking information. The section entitled "Risk Factors" describes some, but not all, of the factors that could cause these differences.

This section, "Management's Discussion and Analysis of Financial Condition and Results of Operations" (MD&A), should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended September 30, 2015, including the consolidated financial statements and related notes thereto.

SECOND QUARTER OF FISCAL 2016 OVERVIEW

Our results in the second quarter of fiscal 2016 reflect continued soft demand conditions within the semiconductor industry, consistent with what we described in our Quarterly Report on Form 10-Q for the quarter ended December 31, 2015, and consistent with conditions we believe that other participants within the semiconductor industry have experienced. Looking forward, some industry reports and comments from other semiconductor industry participants forecast potential strengthening in demand beginning in our third fiscal quarter, driven by inventory replenishments, and in preparation for new product launches. We believe stronger semiconductor industry demand may lead to stronger demand for our consumables products in the second half of our fiscal year compared to the first half. Over the long-term, we continue to believe that semiconductor demand will continue to grow, fueled by demand for mobile internet devices (MIDs), as well as for electronics for automotive and industrial applications, accompanied by the continued advancement of semiconductor technology, including the introduction of more complex device architectures. However, there are many factors that make it difficult for us to predict future revenue trends for our business, including those discussed in Part II, Item 1A entitled "Risk Factors" in this Form 10-Q.

Revenue for our second fiscal quarter was \$99.2 million, which represented a decrease of 5.4% from the second quarter of fiscal 2015, driven by soft semiconductor industry conditions, including continued soft demand for personal computers (PCs), and competitive dynamics within data storage applications. Revenue from polishing pads increased 35.1% compared to the same quarter last year, including a full quarter benefit of our acquisition of NexPlanar Corporation (NexPlanar), which we completed on October 22, 2015. The overall decrease in revenue also reflects a



\$1.1 million adverse impact of foreign exchange rate changes, primarily due to the weaker Korean won versus the U.S. dollar. Revenue for the six months ended March 31, 2016 was \$199.6 million, including NexPlanar, which represented a decrease of 7.9% from the same period of fiscal 2015. The decrease reflects similar factors as noted in the quarter-over-quarter decrease, as well as competitive dynamics in certain dielectrics applications. The decrease in year-to-date revenue also reflects a \$2.5 million adverse impact of foreign exchange rate changes, primarily due to the weaker Korean won and Japanese yen versus the U.S. dollar.

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Gross profit for our second quarter of fiscal 2016, expressed as a percentage of revenue, was 47.3%, including a 110 basis point adverse impact of NexPlanar amortization expense. Gross profit was 52.1% for our second quarter of fiscal 2015. Other factors affecting our gross profit compared to last year include lower sales volume and higher fixed manufacturing costs, including other NexPlanar costs, partially offset by lower costs associated with our annual cash incentive program (Short Term Incentive Program, or STIP, and previously, our Annual Incentive Program, or AIP). Our gross profit was 48.6% on a year-to-date basis, including a 140 basis point adverse impact of acquisition-related costs and NexPlanar amortization expense, which decreased from 51.5% during the same period of fiscal 2015. We continue to expect our gross profit percentage for full fiscal year 2016 to be in the range of 49% to 51%, including NexPlanar. However, we may continue to experience fluctuations in our gross profit due to a number of factors, including the extent to which we utilize our manufacturing capacity and fluctuations in our product mix, which may cause our quarterly gross profit to be above or below this annual guidance range.

Operating expenses were \$34.6 million in our second quarter of fiscal 2016, including \$0.5 million of NexPlanar amortization expense, compared to \$35.2 million in the second quarter of fiscal 2015. The decrease in operating expenses from the comparable quarter of fiscal 2015 was primarily due to lower staffing-related costs, including costs associated with our STIP, and the absence of costs associated with last year's CEO transition, partially offset by NexPlanar costs. On a year-to-date basis, operating expenses were \$70.4 million, including \$2.1 million of acquisition-related costs and \$0.8 million of NexPlanar amortization expense, compared to \$69.6 million during the same period of fiscal 2015. We are lowering our guidance range for our full year fiscal 2016 operating expenses to \$139.0 million to \$143.0 million, including NexPlanar, which is \$2.0 million lower than our prior guidance range of \$141.0 million to \$145.0 million, and \$4.0 million lower than our original guidance range.

Diluted earnings per share for the second quarter of fiscal 2016 were \$0.37, including a \$0.04 adverse impact of NexPlanar amortization expense, compared to \$0.55 in the second quarter of fiscal 2015. The year-over-year decrease was primarily due to lower revenue and lower gross profit. Diluted earnings per share on a year-to-date basis in fiscal 2016 were \$0.83, including a \$0.15 adverse impact of acquisition-related costs and NexPlanar amortization expense, compared to \$1.36 in the same period of fiscal 2015. The year-to-date decrease was also primarily due to lower revenue and lower gross profit.

On January 7, 2016, we announced that our Board of Directors had authorized the initiation of a quarterly dividend program, and pursuant to it, declared our first quarterly cash dividend of \$0.18 per share, or approximately \$4.4 million, which we paid on April 15, 2016 to shareholders of record as of March 17, 2016. On January 7, 2016, we also announced that our Board of Directors authorized an increase in the Company's existing share repurchase program to \$150.0 million, from the approximately \$75.0 million that was available as of December 31, 2015. The dividend and share repurchase programs, which can be suspended, modified or terminated at any time for any reason, are part of our balanced capital allocation strategy, including funding organic investments, dividends, share repurchases, and acquisitions in closely related areas.

#### CRITICAL ACCOUNTING POLICIES AND ESTIMATES AND EFFECTS OF RECENT ACCOUNTING PRONOUNCEMENTS

We discuss our critical accounting estimates and effects of recent accounting pronouncements in "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in Item 7 of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015. There have been no material changes in our critical accounting estimates during the first six months of fiscal 2016. See Note 17 of the Notes to the Consolidated Financial Statements of this Form 10-Q for a discussion of new accounting pronouncements.



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RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2016, VERSUS THREE MONTHS ENDED MARCH 31, 2015

REVENUE

Revenue was \$99.2 million for the three months ended March 31, 2016, which represented a 5.4%, or \$5.6 million, decrease from the three months ended March 31, 2015. The decrease in revenue was driven by an \$8.1 million decrease due to lower sales volume, a \$1.1 million decrease due to foreign exchange fluctuations, primarily the weakening of the Korean won versus the U.S. dollar, and a \$0.7 million decrease due to price changes, partially offset by a \$4.3 million increase due to favorable product mix. The decrease in sales volume was consistent with continued soft demand conditions seen in the global semiconductor industry, continued soft demand for PCs, and competitive dynamics within data storage applications. Revenue from polishing pads increased 35.1% from the same quarter of fiscal 2015, and included \$5.4 million from our NexPlanar acquisition, revenue from tungsten slurries increased slightly, and revenue from all other major product areas decreased.

COST OF GOODS SOLD

Total cost of goods sold was \$52.3 million for the three months ended March 31, 2016, which represented an increase of 4.3%, or \$2.2 million, from the three months ended March 31, 2015. The increase in cost of goods sold was primarily due to \$3.1 million in higher fixed manufacturing costs, including \$1.1 million of NexPlanar amortization expense, partially offset by lower costs associated with our STIP, and a \$2.6 million increase in cost of goods sold due to product mix, partially offset by a \$2.2 million decrease due to lower sales volume.

Engineered abrasive particles are significant raw materials that we use in many of our CMP slurries. In an effort to mitigate our risk to rising raw material costs and to increase supply assurance and quality performance requirements, we have entered into multi-year supply agreements with a number of suppliers. For more information about our supply contracts, see "Tabular Disclosure of Contractual Obligations" in this Form 10-Q as well as in Item 7 of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

GROSS PROFIT

Our gross profit as a percentage of revenue was 47.3% for the three months ended March 31, 2016, compared to 52.1% for the three months ended March 31, 2015. The decrease in gross profit as a percentage of revenue was primarily due to lower sales volume and higher fixed manufacturing costs, including NexPlanar amortization expense and other NexPlanar fixed manufacturing costs, partially offset by lower costs associated with our STIP.

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RESEARCH, DEVELOPMENT AND TECHNICAL

Total research, development and technical expenses were \$14.9 million for the three months ended March 31, 2016, which represented a decrease of 1.3%, or \$0.2 million, from the three months ended March 31, 2015. The decrease was primarily due to \$0.3 million in lower staffing-related costs, including costs associated with our STIP, and a \$0.3 million decrease in clean room material costs, partially offset by \$0.2 million in higher professional fees, including costs of joint development arrangements.

Our research, development and technical efforts are focused on the following main areas:

- Research related to fundamental CMP technology;
- Development of new and enhanced CMP consumable products, including collaboration on joint development projects with technology-leading customers and suppliers;
- Process development to support rapid and effective commercialization of new products;
- Technical support of CMP products in our customers' research, development and manufacturing facilities; and,
- Evaluation and development of new polishing and metrology applications outside of the semiconductor industry.

SELLING AND MARKETING

Selling and marketing expenses were \$6.7 million for the three months ended March 31, 2016, which represented an increase of 15.4%, or \$0.9 million, from the three months ended March 31, 2015. The increase was primarily due to \$0.5 million of NexPlanar amortization expense, and \$0.3 million in higher staffing-related costs.

GENERAL AND ADMINISTRATIVE

General and administrative expenses were \$13.0 million for the three months ended March 31, 2016, which represented a decrease of 9.1%, or \$1.3 million, from the three months ended March 31, 2015. The decrease was primarily due to \$2.3 million in lower staffing-related costs, including share-based compensation costs associated with the fiscal 2015 executive officer transition and costs associated with our STIP, partially offset by \$0.5 million in higher professional fees, and \$0.3 million in higher information technology costs.

INTEREST EXPENSE

Interest expense was \$1.2 million for the three months ended March 31, 2016, slightly higher than \$1.1 million for the three months ended March 31, 2015.

OTHER INCOME (EXPENSE), NET

Other income was \$0.5 million for the three months ended March 31, 2016, compared to \$0.3 million of other expense during the three months ended March 31, 2015. The increase in other income included the impact of foreign currency fluctuations on monetary assets and liabilities denominated in currencies other than the functional currency, net of the gains and losses incurred on forward foreign exchange contracts discussed in Note 9 of the Notes to the Consolidated Financial Statements of this Form 10-Q.



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PROVISION FOR INCOME TAXES

Our effective income tax rate was 21.0% for the three months ended March 31, 2016 compared to 23.6% for the three months ended March 31, 2015. The decrease in the effective tax rate during the second quarter of fiscal 2016 was primarily due to the reinstatement of the U.S. research and experimentation tax credit in December 2015, partially offset by a change in mix of earnings between foreign and domestic, including a scheduled reduction in the benefit available under our tax holiday in South Korea from 100% to 50% of the statutory tax rate in effect in South Korea. We continue to expect our effective tax rate for full year fiscal 2016 to be within the range of 18% to 21%, including NexPlanar.

NET INCOME

Net income was \$9.1 million for the three months ended March 31, 2016, which represented a decrease of 33.9%, or \$4.7 million, from the three months ended March 31, 2015. The decrease was primarily due to lower revenue, a lower gross profit margin, and \$1.5 million in NexPlanar amortization expense.

SIX MONTHS ENDED MARCH 31, 2016, VERSUS SIX MONTHS ENDED MARCH 31, 2015

REVENUE

Revenue was \$199.6 million for the six months ended March 31, 2016, which represented a 7.9%, or \$17.2 million, decrease from the six months ended March 31, 2015. The decrease in revenue was driven by a \$21.5 million decrease due to lower sales volume, a \$2.5 million decrease due to foreign exchange fluctuations, primarily the weakening of the Korean won and Japanese yen versus the U.S. dollar, and a \$1.8 million decrease due to price changes, partially offset by an \$8.7 million increase due to favorable product mix. The decrease in sales volume was consistent with continued soft demand conditions seen in the global semiconductor industry, continued soft demand for PCs, and competitive dynamics within dielectrics and data storage applications. Revenue from polishing pads increased 27.5% from the same period of fiscal 2015, and included \$9.4 million from our NexPlanar acquisition. Revenue from all other major product areas decreased.

COST OF GOODS SOLD

Total cost of goods sold was \$102.5 million for the six months ended March 31, 2016, which represented a decrease of 2.5%, or \$2.6 million, from the six months ended March 31, 2015. The decrease in cost of goods sold was primarily due to a \$5.8 million decrease due to lower sales volume, a \$1.8 million decrease due to lower logistics costs, a \$1.8 million decrease due to foreign exchange fluctuations, and a \$0.9 million decrease due to lower costs related to raw material quality. These decreases were partially offset by a \$5.0 million increase in fixed manufacturing costs, including \$2.0 million of NexPlanar amortization expense and \$0.7 million of acquisition-related costs, and \$3.1 million due to product mix.

GROSS PROFIT

Our gross profit as a percentage of revenue was 48.6% for the six months ended March 31, 2016, as compared to 51.5% for the six months ended March 31, 2015. The decrease in gross profit as a percentage of revenue was primarily due to lower sales volume and higher fixed manufacturing costs, including NexPlanar amortization expense and other NexPlanar fixed manufacturing costs, partially offset by lower costs associated with STIP, lower logistics

costs, and a higher-valued product mix.

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RESEARCH, DEVELOPMENT AND TECHNICAL

Total research, development and technical expenses were \$29.8 million for the six months ended March 31, 2016, which represented a decrease of 1.3%, or \$0.4 million, from the six months ended March 31, 2015. The decrease was primarily due to \$0.7 million in lower staffing-related costs, including costs associated with our STIP, and a \$0.4 million decrease in clean room material costs, partially offset by \$0.5 million in higher professional fees, including costs in respect of joint development arrangements.

SELLING AND MARKETING

Selling and marketing expenses were \$13.4 million for the six months ended March 31, 2016, which was consistent with the six months ended March 31, 2015. Staffing-related costs decreased \$1.7 million from the comparable period of fiscal 2015, including the absence of \$1.2 million in the severance costs related to departing executive officers recorded in the first quarter of fiscal 2015. This decrease was offset by \$0.8 million of NexPlanar amortization expense, \$0.4 million in higher product sample costs, and a \$0.5 million increase in various other expenses.

GENERAL AND ADMINISTRATIVE

General and administrative expenses were \$27.3 million for the six months ended March 31, 2016, which represented an increase of 4.6%, or \$1.2 million, from the six months ended March 31, 2015. The increase was primarily due to \$1.8 million in acquisition-related costs recorded in the first quarter of fiscal 2016, partially offset by \$0.7 million in lower staffing-related costs, including lower costs associated with our STIP and lower costs associated with the fiscal 2015 executive officer transition.

INTEREST EXPENSE

Interest expense was \$2.4 million for the six months ended March 31, 2016 and increased \$0.4 million from the six months ended March 31, 2015. The increase was primarily due to the higher interest rate on the portion of our outstanding debt on which we have fixed the interest rate via interest rate swaps, implemented in the latter part of the first quarter of fiscal 2015, versus the variable interest rate on the rest of our outstanding debt.

OTHER INCOME (EXPENSE), NET

Other income was \$0.6 million and \$0.7 million for the six months ended March 31, 2016 and 2015, respectively.

PROVISION FOR INCOME TAXES

Our effective income tax rate was 18.1% for the six months ended March 31, 2016 compared to 17.3% for the six months ended March 31, 2015. The increase in the effective tax rate during the first six months of fiscal 2016 was primarily due to a change in the mix of earning between foreign and domestic, including the scheduled reduction in the benefit available under our tax holiday in South Korea from 100% to 50% of the statutory tax rate in effect in South Korea. This was partially offset by the absence of income taxes incurred in the first quarter of fiscal 2015 related to the restructuring of our operations in Taiwan.

NET INCOME

Net income was \$20.4 million for the six months ended March 31, 2016 which represented a decrease of 39.4%, or \$13.3 million, from the six months ended March 31, 2015. The decrease was primarily due to lower revenue, a lower gross profit margin, and \$5.6 million in costs related to the NexPlanar acquisition.

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## LIQUIDITY AND CAPITAL RESOURCES

We generated \$32.6 million in cash flows from operating activities in the first six months of fiscal 2016, compared to \$48.7 million in cash from operating activities in the first six months of fiscal 2015. Our cash provided by operating activities in the first six months of fiscal 2016 represented \$41.6 million in net income plus non-cash items and an \$8.9 million decrease in cash flow due to a net increase in working capital. The decrease in cash flows from operating activities compared to the first six months of fiscal 2015 was primarily due to a significant decrease in net income and changes in the timing and amount of accrued expense payments, including payments related to our annual cash incentive bonus program. The cash payment made in the first quarter of fiscal 2016 pursuant to our STIP, related to our performance in fiscal 2015, was \$6.4 million higher than the cash incentive payment made in the first quarter of fiscal 2015, related to our performance in fiscal 2014.

In the first six months of fiscal 2016, cash flows used in investing activities were \$136.8 million, representing \$126.5 million for the NexPlanar acquisition, net of \$15.2 million in cash acquired, and \$10.3 million for purchases of property, plant and equipment. In the first six months of fiscal 2015, cash flows used in investing activities were \$5.1 million, representing \$5.3 million for purchases of property, plant and equipment, partially offset by \$0.2 million received from other investing activities. We currently expect our total capital expenditures in fiscal 2016 will be in the range of \$17.0 million to \$20.0 million, including NexPlanar.

In the first six months of fiscal 2016, cash flows used in financing activities were \$26.9 million. We used \$25.0 million to repurchase common stock under our share repurchase program and \$2.9 million to repurchase common stock pursuant to the terms of our Second Amended and Restated Cabot Microelectronics Corporation 2000 Equity Incentive Plan (EIP) and our 2012 Omnibus Incentive Plan (OIP) for shares withheld from award recipients to cover payroll taxes on the vesting of restricted stock granted under these plans. We also used \$4.4 million to repay long-term debt. We received \$4.7 million from the issuance of common stock related to the exercise of stock options granted under our EIP and OIP and for the sale of shares to employees under our 2007 Employee Stock Purchase Plan, as amended and restated September 23, 2013 (ESPP), and we received \$0.7 million in tax benefits related to exercises of stock options and vesting of restricted stock granted under these plans. In the first six months of fiscal 2015, cash flows provided by financing activities were \$8.1 million. We received \$33.6 million from the issuance of common stock related to the exercise of stock options granted under our EIP and our OIP and for the sale of shares to employees under our ESPP, and we received \$6.1 million in tax benefits related to exercises of stock options and vesting of restricted stock granted under these plans. We used \$25.0 million to repurchase common stock under our share repurchase program and \$2.2 million to repurchase common stock pursuant to the terms of our EIP and OIP for shares withheld from award recipients to cover payroll taxes on the vesting of restricted stock granted under these plans. We also used \$4.4 million to repay long-term debt.

In January 2016, our Board of Directors authorized an increase in the amount available under our share repurchase program from the previously remaining \$75.0 million to \$150.0 million. Under this program, we repurchased 617,839 shares for \$25.0 million during the first six months of fiscal 2016 and we repurchased 531,559 shares for \$25.0 million during the first six months of fiscal 2015. As of March 31, 2016, approximately \$135.0 million remained outstanding under our share repurchase program. Share repurchases are made from time to time, depending on market conditions, in open market transactions, at management's discretion. The timing, manner, price and amounts of repurchases are determined at the Company's discretion, and the share repurchase program may be suspended, terminated or modified at any time for any reason. The repurchase program does not obligate the Company to acquire any specific number of shares. To date, we have funded share purchases under our share repurchase program from our available cash balance, and anticipate we will continue to do so. During fiscal 2015 and in fiscal 2016, we entered into "10b5-1" stock purchase plan agreements with independent brokers, which expired or will expire at various times,

to repurchase shares of our common stock in accordance with guidelines pursuant to Rule 10b5-1 of the Securities Exchange Act of 1934. A plan under Rule 10b5-1 allows a company to repurchase its shares at times when it otherwise might be prevented from doing so under insider trading laws or because of self-imposed trading blackout periods. Repurchases are subject to SEC regulations as well as certain conditions specified in the plan.

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As discussed above, on January 7, 2016, we announced that our Board of Directors authorized the initiation of a regular dividend program under which the Company intends to pay quarterly cash dividends on our common stock. Pursuant to this announcement, our Board of Directors declared our first quarterly cash dividend of \$0.18 per share, or approximately \$4.4 million, which we paid on April 15, 2016 to shareholders of record as of March 17, 2016. The declaration and payment of future dividends is subject to the discretion and determination of the Company's Board of Directors and management, based on a variety of factors, and the program may be suspended, terminated or modified at any time for any reason.

We entered into a Credit Agreement in February 2012, which provided us with a \$175.0 million Term Loan and a \$100.0 million Revolving Credit Facility, with sub-limits for multicurrency borrowings, letters of credit and swing-line loans. The Term Loan and Revolving Credit Facility are referred to as the "Credit Facilities". In June 2014, we entered into an amendment to the Credit Agreement (the "Amendment"), which provided for an additional \$17.5 million in Term Loan commitments to bring the total commitments to the same level as the original amount under the Credit Agreement at its inception in 2012, an extension of the maturity date of the Credit Facilities to June 27, 2019, and changes to certain pricing and other terms of the agreement, including a relaxed consolidated leverage ratio financial covenant. The Amendment also increased the uncommitted accordion feature that allows us to request the existing lenders or, if necessary, third-party financial institutions to provide additional capacity in the Revolving Credit Facility, from \$75.0 million to \$100.0 million. The Term Loan has periodic scheduled principal repayments; however, we may prepay the loan without penalty. The additional Term Loan commitments were drawn on June 27, 2014, and the Revolving Credit Facility remains undrawn. The Term Loan has \$159.7 million outstanding as of March 31, 2016. The Credit Agreement contains covenants that restrict the ability of the Company and its subsidiaries to take certain actions, including, among other things and subject to certain significant exceptions and according to certain terms: creating liens, incurring indebtedness, making investments, engaging in mergers, selling property, paying dividends or amending organizational documents. The Credit Agreement requires us to comply with certain financial ratio maintenance covenants. These include a maximum consolidated leverage ratio of 2.75 to 1.00 and a minimum consolidated fixed charge coverage ratio of 1.25 to 1.00 through the expiration of the Credit Agreement. As of March 31, 2016, our consolidated leverage ratio was 1.61 to 1.00 and our consolidated fixed charge coverage ratio was 4.46 to 1.00. The Credit Agreement also contains customary affirmative covenants and events of default. We believe we are in compliance with these covenants. See Note 8 of the Notes to the Consolidated Financial Statements of this Form 10-Q for additional information regarding the Credit Agreement.

As of March 31, 2016, we had \$226.4 million of cash and cash equivalents, \$131.4 million of which was held in foreign subsidiaries in Japan, the Netherlands, Singapore, South Korea and Taiwan where we have elected to permanently reinvest earnings rather than repatriate the earnings to the U.S. If we choose to repatriate these earnings in the future through dividends or loans to the U.S. parent company, the earnings could become subject to additional income tax expense.

We believe that our current balance of cash and long-term investments, cash generated by our operations and available borrowing capacity under our Credit Facilities will be sufficient to fund our operations, expected capital expenditures, merger and acquisition activities, dividend payments, and share repurchases for the foreseeable future. However, in order to further grow our business, we may need to raise additional funds in the future through equity or debt financing, strategic relationships or other arrangements. Depending on future conditions in the capital and credit markets, we could encounter difficulty securing additional financing in the type or amount necessary to pursue these objectives.

OFF-BALANCE SHEET ARRANGEMENTS

At March 31, 2016, and September 30, 2015, we did not have any unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which might have been established for the purpose of facilitating off-balance sheet arrangements.

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## TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

The following summarizes our contractual obligations at March 31, 2016, and the effect such obligations are expected to have on our liquidity and cash flow in future periods.

| CONTRACTUAL OBLIGATIONS                                |         | Less<br>Than<br>1<br>Year | 1-3<br>Years | 3-5<br>Years | After<br>5<br>Years |
|--|---------|---------------------------|--------------|--------------|---------------------|
| (In millions)  | Total   |                           |              |              |                     |
| Long-term debt   | \$159.7 | \$8.8                     | \$26.2       | \$124.7      | \$-                 |
| Interest expense and commitment fees on long-term debt | 11.2    | 3.9                       | 6.5          | 0.8          | -                   |
| Purchase obligations                                   | 29.0    | 25.5                      | 2.7          | 0.8          | -                   |
| Operating leases                                       | 11.6    | 2.6                       | 3.4          | 2.2          | 3.4                 |
| Severance agreements                                   | 0.6     | 0.6                       | -            | -            | -                   |
| Other long-term liabilities                            | 16.3    | 1.5                       | 4.3          | -            | 10.5                |
| Total contractual obligations                          | \$228.4 | \$42.9                    | \$43.1       | \$128.5      | \$13.9              |

We have been operating under a multi-year supply agreement with Cabot Corporation, our former parent company which is not a related party, for the purchase of fumed silica, which became effective January 1, 2013 and had a termination date of December 31, 2016. This agreement required us to purchase certain minimum quantities of fumed silica each year of the agreement, and to pay a shortfall if we purchased less than the minimum. This agreement was amended effective June 1, 2015 to, among other things, extend the term of the agreement through December 31, 2019, revise certain minimum purchase requirements through 2016, and provide us the option to purchase fumed silica for the remaining term of the agreement beyond calendar year 2016, for which we will pay a fee of \$1.5 million in each of calendar years 2017, 2018 and 2019. The purchase obligations in the table above reflect management's expectation that we will meet the minimum purchase quantities in calendar 2016. Purchase obligations include an aggregate amount of \$12.9 million of contractual commitments related to our Cabot Corporation supply agreement for fumed silica. The long-term fee is included in other long-term liabilities in the table above.

Interest payments on long-term debt reflect interest rates in effect at March 31, 2016. The interest payments reflect variable LIBOR-based rates currently in effect on \$79.8 million of our outstanding debt, and fixed interest rates on \$79.8 million of outstanding debt for which we have implemented interest rate swaps. Commitment fees are based on our estimated consolidated leverage ratio in future periods. See Note 8 of the Notes to the Consolidated Financial Statements of this Form 10-Q for additional information regarding our long-term debt.

Refer to Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" of Part II of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015, for additional information regarding our contractual obligations.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

EFFECT OF CURRENCY EXCHANGE RATES AND EXCHANGE RATE RISK MANAGEMENT

We conduct business operations outside of the United States through our foreign operations. Some of our foreign operations maintain their accounting records in their local currencies. Consequently, period to period comparability of results of operations is affected by fluctuations in exchange rates. The primary currencies to which we have exposure are the Japanese yen, the Korean won, and the New Taiwan dollar. Approximately 20% of our revenue is transacted in currencies other than the U.S. dollar. However, we also incur expenses in foreign countries that are transacted in currencies other than the U.S. dollar, which partially mitigates the exposure on the Consolidated Statement of Income. We periodically enter into forward contracts in an effort to manage foreign currency exchange exposure on our Consolidated Balance Sheet. However, we are unlikely to be able to hedge these exposures completely. We do not enter into forward exchange contracts or other derivative instruments for speculative or trading purposes.

The weakening of the Japanese yen and Korean won against the U.S. dollar in fiscal 2016 adversely affected our revenue. Additionally, the fluctuations of the yen, Korean won and New Taiwan dollar have had a significant impact on other comprehensive income on our Consolidated Balance Sheet. During the fiscal year ended September 30, 2015, we recorded \$8.1 million in currency translation losses, net of tax, that are included in other comprehensive income. During the six months ended March 31, 2016, we recorded \$6.4 million in currency translation gains, net of tax, that are included in other comprehensive income. These gains and losses primarily relate to changes in the U.S. dollar value of assets and liabilities denominated in foreign currencies when these asset and liability amounts are translated at month-end exchange rates.

MARKET RISK AND SENSITIVITY ANALYSIS RELATED TO FOREIGN EXCHANGE RATE RISK

We have performed a sensitivity analysis assuming a hypothetical 10% additional adverse movement in foreign exchange rates. As of March 31, 2016, the analysis demonstrated that such market movements would not have a material adverse effect on our consolidated financial position, results of operations or cash flows over a one-year period. Actual gains and losses in the future may differ materially from this analysis based on changes in the timing and amount of foreign currency rate movements and our actual exposures.

INTEREST RATE RISK

At March 31, 2016, we had \$159.7 million in long-term debt outstanding on our Term Loan. In the first quarter of fiscal 2015, we entered into interest rate swap agreements to hedge the variability in LIBOR-based interest rate payments on half of our outstanding debt. The notional amount of the swaps decreases each quarter by an amount in proportion to our scheduled quarterly principal repayment to maintain a fixed rate of interest on half of our outstanding debt. As of March 31, 2016, the fair value of this cash flow hedge is a liability of \$1.5 million. At March 31, 2016, we had \$79.8 million of outstanding debt at a variable rate of interest. Assuming a hypothetical 100 basis point increase in our current variable interest rate, our interest expense would increase by approximately \$0.2 million per quarter.

MARKET RISK RELATED TO INVESTMENTS IN AUCTION RATE SECURITIES

At March 31, 2016, we owned two auction rate securities (ARS) with a total estimated fair value of \$5.1 million and par value of \$5.7 million which were classified as other long-term assets on our Consolidated Balance Sheet. Beginning in 2008, general uncertainties in the global credit markets significantly reduced liquidity in the ARS market, and this illiquidity continues. For more information on our ARS, see Note 6 of the Notes to the Consolidated Financial Statements of this Form 10-Q.





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ITEM 4. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Our management, with the participation of our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), has conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of March 31, 2016. Based on that evaluation, our CEO and CFO have concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and to ensure that such information is accumulated and communicated to management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

While we believe the present design of our disclosure controls and procedures is effective enough to make known to our senior management in a timely fashion all material information concerning our business, we intend to continue to improve the design and effectiveness of our disclosure controls and procedures to the extent we believe necessary in the future to provide our senior management with timely access to such material information, and to correct deficiencies that we may discover in the future, as appropriate.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

We acquired NexPlanar Corporation (NexPlanar) on October 22, 2015. Subsequent to the acquisition, we applied certain corporate-level controls to elements of NexPlanar's internal control over financial reporting. We will report on our assessment of our combined operations within one year of the acquisition, as permitted by the Sarbanes-Oxley Act of 2002 and the applicable SEC rules and regulations concerning business combinations, but will exclude NexPlanar from management's assessment of internal control over financial reporting as of September 30, 2016. There were no changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

INHERENT LIMITATIONS ON EFFECTIVENESS OF CONTROLS

Because of inherent limitations, our disclosure controls or our internal control over financial reporting may not prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must take into account the benefits of controls relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include possible faulty judgment in decision making and breakdowns due to a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

While we are not involved in any legal proceedings that we believe will have a material impact on our consolidated financial position, results of operations or cash flows, we periodically become a party to legal proceedings in the ordinary course of business.

ITEM 1A. RISK FACTORS

We do not believe there have been any material changes in our risk factors since the filing of our Annual Report on Form 10-K for the fiscal year ended September 30, 2015. However, we may update our risk factors, including adding or deleting them, in our SEC filings from time to time for clarification purposes or to include additional information, at management's discretion, even when there have been no material changes.

RISKS RELATING TO OUR BUSINESS

DEMAND FOR OUR PRODUCTS FLUCTUATES AND OUR BUSINESS MAY BE ADVERSELY AFFECTED BY WORLDWIDE ECONOMIC AND INDUSTRY CONDITIONS

Our business is affected by economic and industry conditions and our revenue is primarily dependent upon semiconductor demand. Historically, semiconductor demand has fluctuated significantly due to economic and industry cycles and seasonal shifts in demand, which can dramatically affect our business, causing demand for our products to fluctuate. For example, during the second half of fiscal 2015, we experienced relatively soft demand conditions in the semiconductor industry, and these soft demand conditions continued through the second quarter of fiscal 2016. Furthermore, competitive dynamics within the semiconductor industry may impact our business. Our limited visibility to future customer orders makes it difficult for us to predict industry trends. If the global economy or the semiconductor industry weakens, whether in general or as a result of specific factors, such as macroeconomic factors, or unpredictable events such as natural disasters, we could experience material adverse impacts on our results of operations and financial condition.

Adverse global economic and industry conditions could have other negative effects on our Company. For instance, we could experience negative impacts on cash flows due to the inability of our customers to pay their obligations to us, or our production process could be harmed if our suppliers cannot fulfill their obligations to us. We also might have to reduce the carrying value of goodwill and other intangible assets, which could harm our financial position and results of operations.

Some additional factors that affect demand for our products include: the types of electronic devices that are in demand, such as mobile internet devices (MIDs) versus PCs; products that our customers may produce, such as logic IC devices versus memory devices or digital versus analog devices; the various technology nodes at which those products are manufactured; customers' efficiencies in the use of CMP consumables; customers' device architectures and specific manufacturing processes; the short order to delivery time for our products; quarter-to-quarter changes in customer order patterns; market share gains and losses; and pricing changes by us and our competitors.

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**WE HAVE A NARROW PRODUCT RANGE AND OUR PRODUCTS MAY BECOME OBSOLETE, OR TECHNOLOGICAL CHANGES MAY REDUCE OR LIMIT INCREASES IN THE CONSUMPTION OF CMP SLURRIES AND PADS**

Our business is substantially dependent on a single class of products, CMP slurries, which account for the majority of our revenue. We also continue to develop our business in CMP pads, and we acquired NexPlanar Corporation (NexPlanar), a supplier of advanced CMP pad solutions in the first quarter of fiscal 2016. Our business would suffer if these products became obsolete or if consumption of these products decreased. Our success depends on our ability to keep pace with technological changes and advances in the semiconductor industry and to adapt, improve and customize our products for advanced IC applications in response to evolving customer needs and industry trends. Since its inception, the semiconductor industry has experienced technological changes and advances in the design, manufacture, performance and application of IC devices. Our customers continually pursue lower cost of ownership and higher quality and performance of materials consumed in their manufacturing processes, including CMP slurries and pads, as a means to reduce costs, increase the yield in their manufacturing facilities, and achieve desired performance of the IC devices they produce. We expect these technological changes, and this drive toward lower costs, higher quality and performance and higher yields, will continue in the future. Potential technology developments in the semiconductor industry, as well as our customers' efforts to reduce consumption of CMP consumables, including through use of smaller quantities, could render our products less important to the IC device manufacturing process.

**A SIGNIFICANT AMOUNT OF OUR BUSINESS COMES FROM A LIMITED NUMBER OF LARGE CUSTOMERS AND OUR REVENUE AND PROFITS COULD DECREASE SIGNIFICANTLY IF WE LOST ONE OR MORE OF THESE CUSTOMERS**

Our CMP consumables customer base is concentrated among a limited number of large customers. The semiconductor industry has been consolidating as the larger semiconductor manufacturers have generally grown faster than the smaller ones, through business gains, mergers and acquisitions, and strategic alliances. Industry analysts predict that this trend will continue, which means the semiconductor industry will be comprised of fewer and larger participants in the future if their prediction is correct. One or more of these principal customers could stop buying CMP consumables from us or could substantially reduce the quantity of CMP consumables purchased from us. Our principal customers also hold considerable purchasing power, which can impact the pricing and terms of sale of our products. Any deferral or significant reduction in CMP consumables sold to these principal customers could seriously harm our business, financial condition and results of operations.

During the six months ended March 31, 2016 and 2015, our five largest customers accounted for approximately 54% and 55% of our revenue, respectively. During the six months ended March 31, 2016, Samsung and Taiwan Semiconductor Manufacturing Company (TSMC) were our largest customers accounting for approximately 17% and 15%, respectively, of our revenue. During the six months ended March 31, 2015, TSMC and Samsung were our largest customers accounting for approximately 20% and 14%, respectively, of our revenue. During full fiscal year 2015, our five largest customers accounted for approximately 58% of our revenue, with TSMC and Samsung accounting for approximately 18% and 15%, respectively.

**OUR BUSINESS COULD BE SERIOUSLY HARMED IF OUR COMPETITORS DEVELOP SUPERIOR CMP CONSUMABLES PRODUCTS, OFFER BETTER PRICING, SERVICE OR OTHER TERMS, OR OBTAIN CERTAIN INTELLECTUAL PROPERTY RIGHTS**

Competition from other CMP consumables manufacturers or any new entrants could seriously harm our business and results of operations, and this competition could continue to increase. Increased competition has and may continue to

impact the prices we are able to charge for our CMP consumables products, as well as our overall business. In addition, our competitors could have or obtain intellectual property rights that could restrict our ability to market our existing products and/or to innovate and develop new products.

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**ANY PROBLEM OR DISRUPTION IN OUR SUPPLY CHAIN, INCLUDING SUPPLY OF OUR MOST IMPORTANT RAW MATERIALS, OR IN OUR ABILITY TO MANUFACTURE AND DELIVER OUR PRODUCTS TO OUR CUSTOMERS, COULD ADVERSELY AFFECT OUR RESULTS OF OPERATIONS**

We depend on our supply chain to enable us to meet the demands of our customers. Our supply chain includes the raw materials we use to manufacture our products, our production operations and the means by which we deliver our products to our customers. Our business could be adversely affected by any problem or interruption in our supply of the key raw materials we use in our CMP slurries and pads, including raw materials that do not meet the stringent quality and consistency requirements of our customers, or any problem or interruption that may occur during production or delivery of our products, such as weather-related problems, natural disasters, or labor-related issues. For example, in our third quarter of fiscal 2015, we incurred significant costs associated with raw material that did not meet our material quality requirements. Our supply chain may also be negatively impacted by unanticipated price increases due to supply restrictions beyond the control of our Company or our raw materials suppliers.

We believe it would be difficult to promptly secure alternative sources of key raw materials in the event one of our suppliers becomes unable to supply us with sufficient quantities of raw materials that meet the quality and technical specifications required by us and our customers. In addition, new contract terms, contractual amendments to existing agreements with, or non-performance by, our suppliers, including any significant financial distress our suppliers may suffer, could adversely affect us. Also, if we change the supplier or type of key raw materials we use to make our CMP slurries or pads, or are required to purchase them from a different manufacturer or manufacturing facility or otherwise modify our products, in certain circumstances our customers might have to requalify our CMP slurries and pads for their manufacturing processes and products. The requalification process could take a significant amount of time and expense to complete and could occupy technical resources of our customers that might otherwise be used to evaluate our new products, thus delaying potential revenue growth, or motivate our customers to consider purchasing products from our competitors, possibly interrupting or reducing our sales of CMP consumables to these customers.

**WE ARE SUBJECT TO RISKS ASSOCIATED WITH OUR FOREIGN OPERATIONS**

We currently have operations and a large customer base outside of the United States. Approximately 86% of our revenue was generated by sales to customers outside of the United States for both the six months ended March 31, 2016 and full fiscal year ended September 30, 2015. We may encounter risks in doing business in certain foreign countries, including, but not limited to, adverse changes in economic and political conditions, fluctuation in exchange rates, compliance with a variety of foreign laws and regulations, as well as difficulty in enforcing business and customer contracts and agreements, including protection of intellectual property rights. We also may encounter the risks that we may not be able to repatriate earnings from our foreign operations, derive anticipated tax benefits of our foreign operations or recover the investments made in our foreign operations.

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**WE MAY PURSUE ACQUISITIONS OF, INVESTMENTS IN, AND MERGERS OR STRATEGIC ALLIANCES WITH OTHER ENTITIES, WHICH COULD DISRUPT OUR OPERATIONS AND HARM OUR OPERATING RESULTS IF THEY ARE UNSUCCESSFUL**

We expect to continue to make investments in technologies, assets and companies, either through acquisitions, mergers, investments or alliances, in order to supplement our internal growth and development efforts. Acquisitions, mergers, and investments, including our acquisition of NexPlanar, which we completed on October 22, 2015, involve numerous risks, including the following: difficulties and risks in integrating the operations, technologies, products and personnel of acquired companies; diversion of management's attention from normal daily operations of the business; increased risk associated with foreign operations; potential difficulties and risks in entering markets in which we have limited or no direct prior experience and where competitors in such markets have stronger market positions; potential difficulties in operating new businesses with different business models; potential difficulties with regulatory or contract compliance in areas in which we have limited experience; initial dependence on unfamiliar supply chains or relatively small supply partners; insufficient revenues to offset increased expenses associated with acquisitions; potential loss of key employees of the acquired companies; or inability to effectively cooperate and collaborate with our alliance partners.

Further, we may never realize the perceived or anticipated benefits of a business combination or merger with, or asset or other acquisition of, or investments in, other entities. Transactions such as these could have negative effects on our results of operations, in areas such as contingent liabilities, gross profit margins, amortization charges related to intangible assets and other effects of accounting for the purchases of other business entities. Investments in and acquisitions of technology-related companies or assets are inherently risky because these businesses or assets may never develop, and we may incur losses related to these investments. In addition, we may be required to impair the carrying value of these acquisitions or investments to reflect other than temporary declines in their value, which could harm our business and results of operations.

**BECAUSE WE RELY HEAVILY ON OUR INTELLECTUAL PROPERTY, OUR FAILURE TO ADEQUATELY OBTAIN OR PROTECT IT COULD SERIOUSLY HARM OUR BUSINESS**

Protection of intellectual property is particularly important in our industry because we develop complex technical formulas and processes for CMP products that are proprietary in nature and differentiate our products from those of our competitors. Our intellectual property is important to our success and ability to compete. We attempt to protect our intellectual property rights through a combination of patent, trademark, copyright and trade secret laws, as well as employee and third-party nondisclosure and assignment agreements. Due to our international operations, we pursue protection in different jurisdictions, which may provide varying degrees of protection, and we cannot provide assurance that we can obtain adequate protection in each such jurisdiction. Our failure to obtain or maintain adequate protection of our intellectual property rights for any reason, including through the patent prosecution process or in the event of litigation related to such intellectual property, could seriously harm our business. In addition, the costs of obtaining or protecting our intellectual property could negatively affect our operating results.

**BECAUSE WE HAVE LIMITED EXPERIENCE IN BUSINESS AREAS OUTSIDE OF CMP CONSUMABLES, EXPANSION OF OUR BUSINESS INTO OTHER PRODUCTS AND APPLICATIONS MAY NOT BE SUCCESSFUL**

An element of our strategy has been to leverage our current customer relationships, technological expertise and other capabilities to expand our business beyond CMP consumables into other areas, such as other electronic materials. Additionally, in our Engineered Surface Finishes business, we are pursuing other surface modification applications.

Expanding our business into new product areas could involve technologies, production processes and business models in which we have limited experience, and we may not be able to develop and produce products or provide services that satisfy customers' needs, or we may be unable to keep pace with technological or other developments. Also, our competitors may have or obtain intellectual property rights that could restrict our ability to market our existing products and/or to innovate and develop new products.

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**OUR INABILITY TO ATTRACT AND RETAIN KEY PERSONNEL COULD CAUSE OUR BUSINESS TO SUFFER**

If we fail to attract and retain the necessary managerial, technical and customer support personnel, our business and our ability to maintain existing and obtain new customers, develop new products and provide acceptable levels of customer service could suffer. We compete with other industry participants for qualified personnel, particularly those with significant experience in the semiconductor industry. The loss of services of key employees could harm our business and results of operations.

**RISKS RELATING TO THE MARKET FOR OUR COMMON STOCK**

**THE MARKET PRICE MAY FLUCTUATE SIGNIFICANTLY AND RAPIDLY**

The market price of our common stock has fluctuated and could continue to fluctuate significantly as a result of factors such as: economic and stock market conditions generally and specifically as they may impact participants in the semiconductor and related industries; changes in financial estimates and recommendations by securities analysts who follow our stock; earnings and other announcements by, and changes in market evaluations by securities analysts of, us or participants in the semiconductor and related industries; changes in business or regulatory conditions affecting us or participants in the semiconductor and related industries; announcements or implementation by us, our competitors, or our customers of technological innovations, new products or different business strategies; changes in our capital deployment strategy, or entering into a business combination; and trading volume of our common stock.

**ANTI-TAKEOVER PROVISIONS UNDER OUR CERTIFICATE OF INCORPORATION AND BYLAWS MAY DISCOURAGE THIRD PARTIES FROM MAKING AN UNSOLICITED BID FOR OUR COMPANY**

Our certificate of incorporation, our bylaws, and various provisions of the Delaware General Corporation Law may make it more difficult or expensive to effect a change in control of our Company. For instance, our amended and restated certificate of incorporation provides for the division of our Board of Directors into three classes as nearly equal in size as possible with staggered three-year terms.

We have adopted change in control arrangements covering our executive officers and other key employees. These arrangements provide for a cash severance payment, continued medical benefits and other ancillary payments and benefits upon termination of service of a covered employee's employment following a change in control, which may make it more expensive to acquire our Company.

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## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## ISSUER PURCHASES OF EQUITY SECURITIES

| Period                          | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price<br>Paid Per<br>Share | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Approximate<br>Dollar Value<br>of Shares<br>that May<br>Yet Be<br>Purchased<br>Under the<br>Plans or<br>Programs (in<br>thousands) |
|---------------------------------|---|---------------------------------------|--|--|
| Jan. 1 through<br>Jan. 31, 2016 | 125,150                                   | \$ 41.07                              | 122,014  | \$ 144,996   |
| Feb. 1 through<br>Feb. 29, 2016 | 125,713                                   | \$ 37.72                              | 125,713  | \$ 140,255   |
| Mar. 1 through<br>Mar. 31, 2016 | 132,497                                   | \$ 39.75                              | 132,497  | \$ 134,989   |
| Total                           | 383,360                                   | \$ 39.51                              | 380,224  | \$ 134,989   |

In January 2016, our Board of Directors authorized an increase in the amount available under our share repurchase program from the previously remaining \$75.0 million to \$150.0 million. Under this program, we repurchased 380,224 shares for \$15.0 million during the second quarter of fiscal 2016. As of March 31, 2016, \$135.0 million remained outstanding under our share repurchase program. The manner in which the Company repurchases its shares is discussed in Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, under the heading "Liquidity and Capital Resources", of this Form 10-Q. To date, we have funded share purchases under our share repurchase program from our available cash balance, and anticipate we will continue to do so.

Separate from this share repurchase program, a total of 3,136 shares were purchased during the second quarter of fiscal 2016 pursuant to the terms of our Second Amended and Restated Cabot Microelectronics Corporation 2000 Equity Incentive Plan (EIP) and our 2012 Omnibus Incentive Plan (OIP) as shares withheld from award recipients to cover payroll taxes on the vesting of shares of restricted stock granted under the EIP and OIP.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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ITEM 6. EXHIBITS

The exhibit numbers in the following list correspond to the number assigned to such exhibits in the Exhibit Table of Item 601 of Regulation S-K:

Exhibit

Number Description

- |      |   |
|------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |

101.INS XBRL Instance Document

101.SCH XBRL Taxonomy Extension Schema

101.CAL XBRL Taxonomy Extension Calculation Linkbase

101.DEF XBRL Taxonomy Extension Definition Linkbase

101.LAB XBRL Taxonomy Extension Label Linkbase

101.PRE XBRL Taxonomy Extension Presentation Linkbase

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CABOT MICROELECTRONICS CORPORATION  
[Registrant]

Date: May 6, 2016 By: /s/ WILLIAM S. JOHNSON  
William S. Johnson  
Executive Vice President and Chief Financial Officer  
[Principal Financial Officer]

Date: May 6, 2016 By: /s/ THOMAS S. ROMAN  
Thomas S. Roman  
Corporate Controller  
[Principal Accounting Officer]