THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

ESIO - Q4 2015 Electro Scientific Industries Inc Earnings Call

EVENT DATE/TIME: MAY 12, 2015 / 9:00PM GMT

CORPORATE PARTICIPANTS

Brian Smith *Electro Scientific Industries, Inc. - Director of IR*

Ed Grady *Electro Scientific Industries, Inc. - President & CEO*

Paul Oldham *Electro Scientific Industries, Inc. - CFO*

CONFERENCE CALL PARTICIPANTS

Jim Ricchiuti *Needham & Company - Analyst*

David Duley *Steelhead Securities LLP - Analyst*

Tom Diffely *D.A. Davidson & Co. - Analyst*

Mark Miller *Noble Financial Group - Analyst*

Pete Enderlin *MAZ Partners - Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the ESI FY15 Fourth-Quarter Earnings Call. My name is Bethany, and I will be your operator for today. At this time all participants are in listen-only mode. We will conduct a question-and-answer session toward the end of this conference.

(Operator Instructions)

As a reminder, this call is being recorded for replay purposes.

I would now like to turn the conference over to your host for today, Mr. Brian Smith. You may proceed.

Brian Smith - *Electro Scientific Industries, Inc. - Director of IR*

Thank you Bethany, and good afternoon, everyone. My name is Brian Smith, Director of Investor Relations for ESI. With me today are Ed Grady, our CEO; and Paul Oldham, our Chief Financial Officer. This call will cover our FY15 fourth-quarter results.

Before we go into the details of the call, I would like to remind you that some of what we say on this call will include forward-looking statements concerning customer orders, shipments, revenue, gross margins, expenses, and earnings. These statements are subject to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. The statements include a number of risks and uncertainties that are discussed in more detail in today's press release and our filings with the SEC. Actual results may differ materially from those forward-looking statements.

This call also contains time-sensitive information that we believe to be accurate as of today, May 12, 2015, and which could change in the future. This call is the property of ESI.

Now I'll the call over to Ed.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Thanks, Brian. Good afternoon, and welcome to our fourth quarter conference call.

Overall Q4 was a quarter of solid execution for ESI, as we introduced new key products, closed our Topwin acquisition, initiated site consolidation to increase efficiency, strengthened our sales force, and focused all our efforts on resources to grow the Company going forward.

Revenues for the quarter were in line with our expectations. Gross margin was strong for this level of revenue. The result was an adjusted net loss per share of $0.21, better than our guided range. Looking at some of our key end markets, flex via drilling was stronger than we had expected, with good bookings, and great customer response to our new GemStone flex via drilling system. GemStone expands our via drilling portfolio by adding a system that incorporates our proprietary laser technology. Combined with ESI's patented beam positioning technology, the system delivers the best cost of ownership and manufacturing quality in the flex and rigid flex market.

Looking forward, growth in the flex market is expected to be solid, driven by expanding mobile and wearable device markets. Expansion of our flex product portfolio reinforces our customers' confidence that ESI is the partner of choice.

In January, we introduced the CornerStone ICP platform, which is a high-performance via drilling system for IC packages. We are re-entering this market segment after about ten years of under-investment.

The CornerStone ICP platform responds to the expressed needs of customers for lower cost of ownership, coupled with product extendibility in a market segment that is growing rapidly as semiconductor companies move top-level interconnect from the silicon into the package, lowering overall cost and consumer devices. As customers transition to this new architecture, their initial reactions to CornerStone have been positive; however, qualifications take time to convert bookings to revenue. We shipped our first beta unit this month, and expect to gain plan-of-record approval by Q3 this fiscal year. Additional beta units will ship to key customers in Q2 and Q3.

Business levels in micro-machining business were disappointing, as our largest customer continued to move to a re-use and reconfiguration policy, rather than large volume orders of new tools. We did, however, see investment in some very advanced applications, but at much lower unit volume. We expect this policy to continue; however, we also expect new applications focused on quality and manufacturing yields to emerge, coupled with broader market applications.

The team is executing on several growth fronts, including the integration of Topwin, the development of third-party sales channels, engagement with new contract manufacturers, and the development of another new low-cost micro-machining platform to greatly expand the applications we can address, especially within China and Asia. We made good progress on all these fronts during Q4, and there are good opportunities for growth.

We closed on the acquisition of Topwin during Q4, and as mentioned, the integration effort is in full swing. The Topwin team is working with our Shanghai Center for Advanced Development on programs that combine the key competencies of both Topwin and ESI to develop a flexible, lower-cost platform that will enable us to respond quickly to a wider range of laser micro-machining opportunities in the China market. This program is key to our China strategy, and is on track to deliver beta units to customers this quarter.

We took several other important actions in Q4 to move our corporate revitalization effort forward. First, we announced the closure of our development center and assembly plant located in Chelmsford, Massachusetts. This facility originated from our acquisition of the semi systems business of GSI about two years ago. Now is the time to fold the business into the existing ESI footprint, in order to streamline operations and increase efficiency, as we leverage ESI common platforms to reduce costs, improve margins, and expand the product offerings in this key sensor-driven market.

Second, we completed the actions to secure a line of credit, which will give the Company greater financial flexibility as we look forward and begin to see growth in revenues. Finally, the Board took action to adopt a couple of governance best practices for the Company by declassifying our Board and eliminating our poison pill. These governance changes will make us more responsible to shareholders and other constituents.

Turning to our outlook for the future, we just completed our FY15, which was an investment and foundational year, setting the stage for growth across our product portfolio in existing and near-adjacent markets. We are executing by leveraging our core competencies in fiber lasers, accuracy, precision, and speed that differentiate us in these target markets. We have delivered on the key milestones outlined in our strategy in new product development, channel expansion, marketing investment, and operational efficiency to position ourselves to expand into target adjacent markets.

As we look to FY16, our goal is to build on this foundation and begin to see the returns on our investments, with growth in revenue focused initially on reaching break-even, followed by sustained profitable growth. There's still work to do as we qualify our new products, enter new markets, and leverage our sales channel to engage with and penetrate new customers, and exercise more market-based product development approach.

We are re-making ESI to adapt to the realities of the real and growing markets we now serve. I am very pleased with the progress we have made this last fiscal year to position ourselves for success. Although this will not be a linear transition, we are committed as a team to taking the right steps on both the top line and cost structure to turn around ESI and put it on a long-term growth path. With that, I will turn the call over to Paul for an overview of our financial results.

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Thank you Ed, and good afternoon, everyone. The following information includes results from our fourth quarter and fiscal year ending March 28, 2015. To improve comparability, we are also providing the earnings per share and related income statement results on a non-GAAP or adjusted basis, excluding the impact of purchase accounting, equity compensation, restructuring, asset write-offs, and other items.

Bookings for the quarter were $40 million, about flat with last quarter, but up 26% from $31.7 million a year ago. Bookings in our interconnect and micro-fabrication business were up slightly from last quarter. Flex via drilling was better than expected, down slightly from strong results in Q3, but up significantly year over year.

The results were driven by improvements in Korea, where we saw early demand for some HDI applications in memory, and from strong customer reception for our next-generation GemStone via drilling tool, where we received a large multi-unit order. The GemStone system represents our second introduction of an internally developed laser application this year. Looking forward, we see additional opportunities to utilize our laser technology to expand our capability and lower cost.

As Ed mentioned, advanced micro-machining orders were low this quarter, as key opportunities did not materialize or pushed out of the quarter. However, we saw our first orders from Topwin, and have had good engagement and interest in our new low-cost platform. We expect to see improvements in this business over time as we strengthen our position and introduce low-cost platforms in the China market.

Bookings in our semiconductor business were down sequentially, on seasonally lower circuit trim and service bookings. Also in our third quarter, we received an initial order for our semiconductor scribing system, which shipped this quarter, but has not completed the acceptance process. Orders from component test increased on solid systems demand. After more than a year of little activity, we are beginning to see some capacity additions, particularly in China and Japan.

Shipments were $41.7 million. Backlog was $36.5 million, and is up significantly from last year, giving us a relatively stronger footing moving into FY16. Our booked-to-bill ratio was 0.96. Remember, our booked-to-bill ratio compares orders to shipments, not to revenues. Revenue for the quarter was $37.6 million, with solid revenues in interconnect and micro-machining, and growth in components.

GAAP gross margin was 37.1%, and included about $400,000 of purchase accounting and equity compensation in cost of sales. We also took a $950,000 charge against inventory, as we discontinued certain low-volume products associated with the consolidation of our manufacturing locations. On a non-GAAP basis, gross margin was 40.7%, compared to 36.9% last quarter. The higher gross margin was primarily due to improved other cost of sales, including warranty, freight, and reductions in material costs on some key products. Looking forward to next quarter, we expect adjusted gross margins to be roughly flat.

GAAP operating expenses were $25.2 million, including $1 million of equity compensation and purchase accounting, plus $465,000 of acquisition costs related to Topwin. We also took a $2.1-million charge related to the closure of our facility in Chelmsford, Massachusetts.

On a non-GAAP basis, operating expenses in Q4 were $21.7 million, up from last quarter as we had projected. The increase was due to the added cost of Topwin and higher product launch costs associate with GemStone another new products. Looking forward, we expect operating expenses to continue roughly in this same range.

On a GAAP basis operating loss was $11.3 million. Non-GAAP operating loss was $6.4 million, compared to a loss of $4 million in the prior quarter. On a non-GAAP basis, income tax was $150,000, an improvement from Q3, primarily on timing of foreign income. We expect Q1 tax expense to normalize back to around $300,000 to $400,000, and to continue in that range each quarter throughout FY16.

GAAP net loss was $15.1 million, or $0.48 per share, compared to a loss of $0.21 per share last quarter. Contributing to the GAAP loss was the previously announced $4.3-million, non-cash write-down of our minority equity investment, partially offset by a $600,000 currency gain on the closure of our former Beijing R&D facility. Adjusted net loss was $6.5 million, or $0.21 per share, on lower revenues, compared to a loss of $4.7 million, or $0.15 per share, last quarter.

Turning now to the balance sheet, cash and investments were $58 million at quarter end. We used approximately $11 million in operating cash during the quarter. In addition, we spent approximately $9 million for the acquisition of Topwin. Operating cash flow was impacted by our net loss, adjusted for non-cash items of $7.3 million and working capital uses of $3.7 million. Accounts receivable increased by $5.4 million to $46 million, primarily related to the timing and level of shipments, and the addition of Topwin. DSO on lower sales increased to 112 days.

Inventories decreased by $2.8 million, and inventory turns were approximately 1.6 times. In addition, accounts payable declined, mostly on timing of inventory receipts and payments. Looking forward, we would expect to see our cash used from operations to narrow significantly, on improved operating income, normalization of timing for accounts receivable and payables, and continued improvements in inventory.

Capital expenditures were $1.8 million, up from last quarter, primarily on costs to ramp productions of our internally developed lasers. Depreciation and amortization, excluding purchase accounting, was $1.9 million. Finally in March, we closed on the three-year revolving line of credit of up to $30 million through Silicon Valley Bank. As we stated last quarter, this facility will give us more financial flexibility through this transition as we drive our growth initiatives.

As we look forward to our new fiscal year, we have put a lot of the building blocks for growth in place. In addition, we will continue to invest in new products for known adjacent markets, and our improving efficiency in our business. Overall, we expect to see good growth year over year, but will continue to see some volatility in our results until our new products are fully adopted in the market, which will be later in the year.

As a result, we expect our first quarter revenues to be in the $40-million range. Adjusted loss per share is expected to be between $0.15 and $0.20. Although we are not giving specific guidance for FY16, we are generally comfortable with the current consensus, and continue to expect to achieve break-even during the year.

Now I will give the call back to Ed for a brief summary.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Thanks, Paul.

In summary, we've made substantial changes in who we are as a Company. During this quarter we took several steps forward in our turn-around effort as we introduced new products and closed an acquisition that will drive growth in the future. After a FY15 devoted to making the investments that set the stage for growth, we see FY16 as the year we see those investments begin to pay off. All of us as a team are driving to make that pay-off begin as soon as possible, and putting us on a long-term growth path.

This concludes our prepared remarks. At this time I would be pleased to take your questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

James Ricchiuti, Needham & Company.

Jim Ricchiuti - *Needham & Company - Analyst*

Thank you, good afternoon. I wonder -- Ed, maybe you can talk a little bit more about the new products, and generally how satisfied you are with the initial market reception? You highlighted GemStone, CornerStone, but I wonder if you could talk in maybe a little bit more detail as to how you think these products should contribute in FY16?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Sure, Jim. I'd say the biggest opportunity is, as we -- we've got to get the products into the market. We shipped our first CornerStone beta unit this quarter. We had the large order for the GemStone product. GemStone is clearly going to contribute revenue and growth in the flex market -- flex and rigid flex throughout the year.

I would expect more contribution from the CornerStone ICP product in the latter half of the year. I suspect that the lower-cost programs we have going in China, one of those units will ship to a beta customer this quarter. Again, I would expect those to begin to see revenue generated in the Q2 through Q4 time frame. With that, I think other than some other products we haven't yet announced, we see a lot of strong demand.

I'd say the biggest thing we're seeing from customers, Jim, is exactly as we said, we're driving cost of ownership. The markets we're selling to and in the PCB space are very cost sensitive and productivity sensitive. When we go to a customer that's running on 14%, 15% gross margins, and we can show them a way to get better productivity in their factory, they're quite interested in talking to us. I would say of the top ten customers, we get traction with pretty much all of them as we introduce the product. We're getting no push-back. We're getting actually pull, as I indicated last quarter. We're getting pull, and pretty dramatic pull, to get the products in as beta units for testing. Does that help?

Jim Ricchiuti - *Needham & Company - Analyst*

It does. Also, speaking of margins, your margins were a bit better than expected. Paul, maybe you could talk a little bit about that. Was it mix related? You seem to suggest that margins can be at these levels in Q1. Any sense as to how we might think about gross margins as we go through the year, obviously off a function of revenue?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

This -- clearly revenue has an impact, but we did see better margins this quarter. A lot of those were on items that would just in general better execution. We've been getting in front of some of warranties, so warranties coming down. We'd expect to see that trend continue. We've made some good progress in our products around material cost, and saw some one-time benefit of that as we caught up the inventory value there. But also, we'll see ongoing benefit of lower material costs on a couple of key products.

Although a lot of the items this quarter where other cost of sale items -- I think several of those will persist into next quarter. As we get a couple of these new products out, that should help our mix of gross margin, as well. We feel comfortable at least in this next quarter that we ought to see margins, gross margin percentage, in this same range. As we see volumes begin to grow, that will help us absorb more of the fixed cost, which will give us a little more of the floor under that, as well.

Jim Ricchiuti - *Needham & Company - Analyst*

Got it. One other question and I'll jump back in the queue. I think you've talked in the past, at least last call, about Topwin being able to generate somewhere in the neighborhood of $7 million to $10 million of revenue this year. Is that something you are still targeting?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Absolutely, yes. We don't see any indication that that's not going to happen, Jim.

Jim Ricchiuti - *Needham & Company - Analyst*

Ed, do you see some upside to that, or is that a good number to be looking at here?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I would say it's a good number to look at. I will tell you, however, that we have looked at how we can take their product lines as they exist today outside of China, something that was historically not in our forecast. I can't really comment on whether we've got traction yet with that, but early indications are that if anything, it will make sure we hit the target as specified. But yes, there's some potential up side. But I would say the up side is outside of China, not necessarily in China.

Jim Ricchiuti - *Needham & Company - Analyst*

Okay. Thanks very much.

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

I would add to that, that the other benefit we are seeing from Topwin is the lower-cost platform. We've gotten a lot of good customer engagement as we look at our existing set of customers for how we can leverage that was some of our technologies as we go forward. Ed mentioned that a little bit in his script, but we have seen a lot of customer engagement relative to that, that the platforming capability they bring beyond their own external sales.

Jim Ricchiuti - *Needham & Company - Analyst*

Thanks, Paul.

Operator

David Duley, Steelhead.

David Duley - *Steelhead Securities LLP - Analyst*

Yes, thanks for taking my question. As far as FY16 goes, do you think it will be your current set of products recovering, or new products that will be the primary driver of growth?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I'd say it's the new products, David, that are going to be the biggest driver of growth. I'm going to lump a couple things together. Clearly, Topwin is a definition of new products. CornerStone, as we talked about, is a new products, which is clearly something we are counting on. GemStone is a new product which we are counting on. Largely those three, plus a couple other things in the queue, the new low-cost platform in China. I think those are going to be the key drivers in revenue expansion. Obviously there are some smaller pieces that add up, if you put them together in the core markets, but largely those are going to be the big contributors.

David Duley - *Steelhead Securities LLP - Analyst*

Okay. As far as the CornerStone product, you already have a big order, so that will be layering into revenue this year -- this fiscal year. You mentioned GemStone revenue later in this fiscal year, or calendar year? I was a little confused.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I think you got them -- they're switched. GemStone we already have an order. Paul mentioned we had a large-unit volume order in Q4, and we're continuing to see incremental demand. CornerStone ICP is focused at the integrated circuit package market, and we shipped our beta unit this quarter -- this month, I should say -- not this quarter, this month. Again, that's going to go through qualification, but the interesting part about that is that there's such a pull for that product from the customer base that we're really -- I would say doing more running and running fast to keep up with demand in that product line.

David Duley - *Steelhead Securities LLP - Analyst*

Can you remind us of the relative market size that each one of these products address?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Paul, I don't know if you want to --

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Yes, the flex market in general, the way we've talked about that is that's a $100-million to $150-million market, of which we have a large share. The IC package market we think of about -- as another $150-million market. Then an adjacent market to that would be the HDI market, which would be a much larger market. That's how we see those markets. Entering into HDI roughly doubles or more than doubles the addressable market for PCB drilling applications for us. The new tool, the GemStone tool, while it's a flex drilling tool, it's very versatile and very capable tool, so it does bleed over a couple of the applications.

David Duley - *Steelhead Securities LLP - Analyst*

As far as the ICP product, or the one for the ICP packaging, why is it that you think you're getting so much pull all of a sudden? Is it the current technologies aren't very good at addressing what they're doing, or is there a new technology coming that's behind a sense of urgency from your customers?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

There's a couple things, David, there going on. First is there's a push in the device market to change the form factor of what gets put in these mobile devices and wearables. People are looking at both the X and Y and the Z format of what goes in. It's thinner printed circuit boards, it's smaller chip sizes, packed more closely together. All of those drive the need for smaller via sizes. Also it drives the need for higher density, more vias in a given area.

With that, what our customers see is our ability to do that, with again leveraging the core capabilities of ESI, which are the precision, the accuracy, and the speed at which we can do these drilling applications. Then if you couple that with about a 40% footprint reduction on the fab floor, it's a big deal to these people, because they take existing fab space, and without building a new building, can re-purpose the fab space and get more productivity out of the current floor space.

David Duley - *Steelhead Securities LLP - Analyst*

Okay, and then final question for me is, as far as the micro-machining segment goes, do you think your growth there, or rekindling growth there, is dependent upon a new product, or do you think that some of the older products might actually start to have some rekindling of ordering again -- or applications, however you want to look at it?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I would say we will continue to see a dribble of some of the older products, but this market is heavily driven by contract manufacturers and by low-cost tools. If anything, the positioning we need to have is supported by the Topwin acquisition. It's supported by the Topwin platform, where we put some of our advanced positioning and placement capability on those tools, to again provide a little bit higher-value tool.

As I said in my remarks, some of the customers have moved to more re-purpose and reconfiguring of their install base. But, we are extremely well-positioned with our large -- with what has been our largest customer. We've got a great relationship with them, and we continue to see a pipeline. It's just we're not seeing the pipeline like in the past that we had seen. It's just a little different dynamic today. We feel good about where we are with that customer and a broader base of customers. That's the key point is there are now people jumping into the fray of other applications using laser micro-machining. That's about it, David.

David Duley - *Steelhead Securities LLP - Analyst*

Thank you.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Sure.

Operator

Tom Diffely, D.A. Davidson.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Yes, good afternoon, thanks. First Paul, when you look at the different new products that have come out, between the two new releases and the Chinese-based products, is there a big difference in the actual margin structure of those products?

THOMSON REUTERS

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

There is -- I would say there is not a large difference. They have very different cost structures, because they are designed for different markets. Certainly, building on our standard platform for the GemStone tool and utilizing our own laser technology has given us capability in the market, which allows us to have an attractive product with good cost of ownership and good margins for us. Leveraging the Topwin base or platform in the China market, while, it's a much lower cost tool, also gives us a much lower cost platform to play from. In general, I think we would see somewhat lower gross margins, but not significantly such, once we have the platforms fully in place across those different products.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. Are you able to talk about an incremental gross margin for the Company on a go-forward basis, or is it going to be too mix dependent?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

I think that what we've talked about is we would expect it to be the low 40%s to mid 40%s as volumes come back up. Certainly, we've been running under a critical mass from a volume, and that's impacted us the last couple of quarters. We're seeing some recovery of that as some of these new products and material cost reductions have come in. We would expect in general to run in that low to mid-40%s, depending on the volume.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. Then when you look at the restructuring, is most of the cost already been accounted for in the March quarter?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Yes, in general they have been, Tom, for everything we can. As you recall, though, the 8-K release we did a month or so ago, and we announced the restructuring, we noted that some of those costs have to get recognized as incurred. We would expect about another $3 million to $3.5 million, probably about mid-year, related to future facility obligations, which we'll of course be trying to mitigate, but I think you'll see another charge then related to that.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. You mentioned you closed the Beijing facility, the R&D facility. Is that because you put everything into the Topwin facility?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

This was something we did almost three years ago, 2.5 years ago --

---

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Oh, okay.

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

-- as part of having a more focused approach to our laser development. This is basically the final winding up of that subsidiary, and being able to then withdraw the capital that has contributed there. Essentially we have had a currency gain over that period of time such that we were able to recognize that gain, and get more cash back when we repatriated that cash this last quarter.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. Was there a meaningful FX impact to the business in the last quarter?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

No. In general, we don't have a lot of ongoing FX impact, because most of our sales are in US dollars. We don't see a lot there. We had a little bit of a benefit in some regions from an expense perspective, but I wouldn't say it's been meaningful in our business.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. When you look at the new set of tools, the products out there, and the markets they address, is there a different sense of seasonality that you would expect to see on a go-forward basis? Is it going to be a little bit more second- and third-quarter weighted, like a lot of the more consumer-driven products are?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Yes, I think we've seen in the last few years a heavy weighting because of our large customer to the first and second quarter. I think over time as we have a more diversified set of products that the other markets -- we won't see as heavy of swings from quarter to quarter, because it does sell into a broader set of markets. I think there will still be some general seasonality towards our first and second quarters, just because of the natural back-to-school and Christmas seasons. But I think the seasonality over time will -- it will be mitigated on a quarter-to-quarter basis from what we've seen historically.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. Finally, when you look at the component strength in the quarter, do you expect that to continue? Are we entering a new buying cycle for the component guys?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

I probably wouldn't go quite that far. I think we've seen some broader expansion of the smaller chips, not general capacity additions. We think that will continue, but it will probably be in small pieces, not in a big recovery.

Tom Diffely - *D.A. Davidson & Co. - Analyst*

Okay. All right, thank you for your time.

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Thank you.

Operator

Mark Miller, Benchmark Company.

Mark Miller - *Noble Financial Group - Analyst*

Good afternoon.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Hi, Mark.

Mark Miller - *Noble Financial Group - Analyst*

A couple of firms have recently mentioned they've seen a pick-up in their outlook for business for equipment related through silicon via has picked up. Are you being influenced by that? Are you seeing anything like that?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I'm trying to understand the question, Mark. You mean the via drilling companies have seen their business pick up, or other tooling companies?

Mark Miller - *Noble Financial Group - Analyst*

This was specifically Ultratech, which is lithography-type application.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I think we're in different spaces. They're doing some obviously photolith-type applications for some of the packaging technology. Our business in this space is largely driven by devices, mobile devices in the flex circuit area, and the printed circuit business.

I guess the best answer I can give you is that what we're seeing is, I think I said earlier, that the demand for smaller packages, meaning smaller chips and tighter spacing of the chips both X and Y and Z making thinner devices, is requiring a tooling set that can make smaller holes, vias, and make these -- the printed circuit boards more compactly. That's right up our alley in terms of precision, accuracy, and speed. What we're seeing is the market demand is moving towards our specific strength as a Company.

Mark Miller - *Noble Financial Group - Analyst*

Okay. Break-even still looks like to be around $50 million, is that for next year? Is that your break-even level, you still feel?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Yes, that's our target. I'd say we're probably running a little bit ahead of -- a little higher than that number right now, but it's very margin dependent. If we can stay on our margin model, then that -- then it's around that $50-million range.

Mark Miller - *Noble Financial Group - Analyst*

I apologize if I missed this. Did you give the backlog, quarter ending?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

We did. It's $36.5 million.

Mark Miller - *Noble Financial Group - Analyst*

Thank you.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Mark, backlog is up from a year ago.

Operator

Pete Enderlin, MAZ Partners.

Pete Enderlin - *MAZ Partners - Analyst*

Thank you. You added 40-plus employees in the fourth quarter. Was that largely Topwin?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Yes.

Pete Enderlin - *MAZ Partners - Analyst*

Okay. Now you're going to have cuts from closing Chelmsford. Then in addition to that, another $3 million to $3.5 million of charges. About how many people beyond Chelmsford would the additional charges represent?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

The charges I discussed are related to the facility costs. That's just beyond -- the way the accounting works is you can't take that as an up-front charge any more, you have to take it as you go. Once we exit the facility about mid fiscal year, then we'll start to -- we will incur those costs.

Pete Enderlin - *MAZ Partners - Analyst*

Okay, it's not necessarily a lot more people at this point.

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

At this point that's right. Obviously, we will have some ongoing adjustments to our business, but we have not announced any other restructuring in that regard.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

I would say the -- Peter, just to be fully transparent, the up in Topwin, will ultimately, if you just looked at head count will be offset by the reduction in Chelmsford. It's a net zero on it from a head count perspective.

Pete Enderlin - *MAZ Partners - Analyst*

Right.

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Also, there is a timing difference, because Chelmsford is a transition that will happen so that we can transfer the products. It will happen over time, over a couple of quarters.

Pete Enderlin - *MAZ Partners - Analyst*

Sure. What's your general sense about the Chinese economy? Is there a potential effect from a slow-down in device sales in China? Are you seeing any of that?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Not so far. I would say a lot of the products set that we're delivering tools into are the high-end tool sets. So far, we are actually seeing pretty strong demand in China, continued strong demand in China, both in the PC board side, as well as in the micro-machining side. I guess the other piece I would add is we're seeing demand throughout other parts of southeast Asia increase, as customers look for lower-cost regions to expand to.

Pete Enderlin - *MAZ Partners - Analyst*

Okay. What's your -- what was your thinking behind eliminating the staggered Board, and the early termination of the rights plan? That's a commendable thing to do, but was there anything specifically that prompted it, or what brought it about?

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

There was nothing really that brought it about. I think as we look at -- I think Rick Wills came on to our Board as our new Chairman. We've re-assigned some of the committee chairs. Our nominating governance committee looked at this and said what is the current best practices in the industry? We found that we were not consistent with best practices, and we're trying to move to being best practices in the industry across not only governance, but everything we do. That was the key driver.

Pete Enderlin - *MAZ Partners - Analyst*

Okay, thank you very much.

Operator

Jim Ricchiuti, Needham & Company.

Jim Ricchiuti - *Needham & Company - Analyst*

Paul, we'll see this in the 10-K, but was your large customer, is it going to show up again in the K, in terms of customer concentration?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

Yes, actually it will turn out this year that we won't have a greater-than-10% customer, but we have two customers that were just under the 10%, just barely under the 10% threshold.

Jim Ricchiuti - *Needham & Company - Analyst*

Okay. I don't know if you're willing to comment on this, but if we were to exclude the revenues in FY14 from your large customer in FY15, can you give us a sense as to how the revenues would have looked, in terms of the rate of change?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

In general, Jim, when we take a look at that analysis, our base business or our other business would be up slightly year over year.

Jim Ricchiuti - *Needham & Company - Analyst*

Okay. One final question, just with respect to the recovery that you did see in flex in Korea, is your sense that that is sustainable? I'm curious if in talking with your customers there, if that is basically just improvement that you're seeing as a result of the active roll-out of Samsung with its new products?

Paul Oldham - *Electro Scientific Industries, Inc. - CFO*

I would say that it wasn't a large recovery, that we definitely started to see some tool sales. At this point I'd probably say it's more technology buys than it was capacity coming back on line. It was mainly driven -- or was driven in part by packaging applications, as it related to strong memory activity. This was for via drilling for packages, not so much a big recovery in terms of Korea and capacity. Certainly if Samsung performs better, that capacity in Korea will become more fully utilized, and we could see some capacity improvement over the course of this coming year, as well. But at this point it was more technology buys, I'd say.

Jim Ricchiuti - *Needham & Company - Analyst*

Got it. Thanks very much.

Operator

I would now like to turn the call over back to Ed Grady. You may proceed.

Ed Grady - *Electro Scientific Industries, Inc. - President & CEO*

Thank you very much for joining us. You're welcome to call Paul, Brian, or me if you have any further questions. Thanks for attending our call today.

Operator

Ladies and gentlemen, that concludes today's conference. Thank you for your participation, and you may now disconnect. Have a great day.

THOMSON REUTERS