

THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

inTEST Corporation (INTT)



ROBERT E. MATTHIESSEN has served as inTEST Corporation's Chief Executive Officer since August 1998 and President since February 1997. Mr. Matthiessen also served as Chief Operating Officer from December 1997 to August 1998. Prior to that, Mr. Matthiessen served as Executive Vice President after joining inTEST in October 1984. Mr. Matthiessen has served as a Director since February 1997. The inTEST board of directors believes that Mr. Matthiessen's education and experience in the fields of mechanical and electrical engineering, his experience in the ATE industry throughout his more than 40-year career, and his extensive network of contacts and relationships in this industry, in addition to his more than 25 years of experience at the company, are the attributes, skills, experiences and qualifications that uniquely qualify him to execute the company's strategies and make valuable contributions as one of its Directors.

SECTOR — SEMICONDUCTORS

TWST: Please begin with a brief overview of inTEST Corporation.

Mr. Matthiessen: inTEST designs, manufactures and markets products that are primarily used by semiconductor manufacturers to test their integrated circuits and wafer products. Our product lines include test head manipulators, docking hardware, tester interfaces and thermal test systems. And as a matter of fact, we are 30 years old this year. We were founded in 1981 and conducted our IPO in 1997. Since 1997, we've made five acquisitions, three significant ones. We have traditionally participated in the back-end test segment in the semiconductor business, so we supply capital equipment to the test areas of semiconductor manufacturers. This equipment is not the testers themselves nor the handling equipment itself, but those components that make it possible for the testers to be connected to the handling equipment, which ultimately makes our equipment mission critical. In addition, in recent years we've diversified our product suite into markets outside of semiconductors to help mitigate the semiconductor capital equipment curve. These markets include new growth industries, such as aerospace/defense, automotive, telecommunications and medical/pharmaceutical.

TWST: What would you say constitutes the biggest part of inTEST's business?

Mr. Matthiessen: Presently it's still the traditional businesses that we started in; and that would be the test head manipulators and docking hardware, which are used to connect testers to handlers and wafer probers, in addition to thermal conditioning equipment that's used on the test floor.

TWST: How do your products support the current marketplace?

Mr. Matthiessen: Change drives this industry. There's been a broad switch to mobile computing and the creation of dynamic new consumer products that require more capabilities in ever-smaller packages. With technological advances shrinking the size of individual Integrated Circuits, the number of ICs on a silicon wafer has continually increased. Today some wafers carry thousands of ICs, each of which has to be tested. This has translated into considerable opportunity for inTEST. As ICs become more complex and testing takes on increasing importance, semiconductor manufacturers turn to inTEST to help them test their products more efficiently, maximize yields and reduce their manufacturing cost. Go back to "change" a moment. Our success is driven by change in the industry. Any change related to package types, wafer sizes, pin counts, etc., results in a need for new advanced inTEST products. We also make equipment that's used in the product development areas of our customers; and so as they develop a product, if they're using our equipment in the development of those products, it makes it much easier to migrate that equipment into their capacity build situations.

TWST: Are there still issues of cyclicity or seasonality that have been synonymous with the industry? How has your company addressed those types of issues?

Mr. Matthiessen: Yes, the cyclicity is still here; that's what makes it so exciting and that's why we love it so much. And seasonality is here to some extent. If there were no other influences, I would say that typically second quarter is the strongest quarter, as people begin to build up their capital equipment to test parts that will be eventually sold in the

Christmas season, and fourth quarter is generally the weakest quarter. Although, those issues can sometimes be impacted by some macroeconomic condition that we were not aware was going to come, so sometimes you see those trends and sometimes you don't. Our strategy to deal with issues such as this is to strategically outsource manufacturing where it makes sense to do so. For example, as you know, the industry experienced a severe downturn a couple of years ago. Like many companies, we restructured and lowered our breakeven line quite a bit and began outsourcing at that time to a great extent. The end result is we have a very elastic situation at inTEST facilities, where we do mostly assembling rather than manufacturing, therefore it's easy for us to expand and contract with the cyclicity.

TWST: Looking at the semiconductor industry and particularly the segment you're in, what do you see as the dominant or prevalent trends over the next two to three years? What are the positive trends and what are the negative or cautionary aspects of those trends?

Mr. Matthiessen: One trend is there's going to be more and more parts being tested. We're relatively agnostic to the type of parts that are being tested because we're not actually making the tester itself. But the quantity of parts is important to us, and we see that as an ever-increasing number. Another thing that's happening is ASPs are being lowered, which is a negative aspect to us. Although the number of parts are going up, the lower ASPs mean that money gets tighter and tighter and so the pressure comes all the way down the chain, all the way down to us little guys who are supplying equipment to the test floor. So that becomes a challenge for us.

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The other negative is the attempts by the IC manufacturers themselves to reduce their respective need for test. The engineers that design these parts spend a great deal of their time trying to make them with as little test as possible because test is not seen as a value-added situation by them. And so the more success they have, the less they feel they need extra equipment. Fortunately, they've not been very successful at that because the parts keep getting bigger and bigger, microprocessors keep growing and so test has not shrunk as a result of that, but has actually increased. Another trend is consolidation both at the customer level and the supplier level. For example, Texas Instruments and National Semiconductor have announced their intention to combine. We see that as a positive influence to inTEST, because TI has been a very strong customer of inTEST, whereas National has not been so strong. But TI is the lead dog in this merger and as such, we would expect that perhaps National will become a stronger inTEST customer. We also see consolidation at our level, in the companies that are in our space, and so that's a trend that's probably positive because we have less competition at that point.

TWST: How would you quantify inTEST's value proposition? When comparing your products to that of the competition, what continues to differentiate inTEST within that competitive landscape?

Mr. Matthiessen: We have a very clear difference between our competitors in each of the areas in which we compete, and we offer a more capable high-end product in each area. For instance, test head manipulators range in ASPs all the way from approximately \$4,000 or \$5,000 up to the \$50,000 to \$60,000 range. We tend to participate in the upper end of that range because our margins are better. We also build higher-end equipment because we're aiming at the end user more than at the OEM customer. The OEM customer's interest is basically in low price, whereas the end user, the guy that's going to end up with the equipment, is interested more in functionality and how it's going to help him. So we are the guys that sell primarily to the end user and as such, we typically operate at the high end.

TWST: From your perspective, how robust is the competition and what are the decision points for customers in choosing their suppliers?

Mr. Matthiessen: We participate in three areas, and I've alluded to them but not really defined them as such. We participate in mechanical, electrical and thermal areas of the test floor. The mechanical area is where we make test head manipulators and docking hardware. In the docking hardware, we are the most robust supplier in the market. We invented the standard that's used on test floors today, and we have 50% or better of that market. In the manipulator market, as I said, we compete at the high end, but the low-end guys build a lot of manipulators, and so they are fairly robust.

Although during the downturn, one of those competitors went out of business and another one seems to be having considerable trouble, so we seem to have been one of the stronger ones coming through that.

In the electrical business, we make tester interfaces. That's the electrical connection between a tester and a wafer prober, and we are probably the most robust of the independent manufacturers. Now the tester manufacturers themselves also build that equipment, and in fact we build it on an OEM basis many times for them. In the thermal business, we are the leader of the pack in the basic unit that's used in the semiconductor business, which is called Thermostream. We probably have 60% of that business, and that's growing.

TWST: What are some of the opportunities that inTEST may have in terms of future mergers, acquisitions, joint ventures or strategic alliances? Do you see any specific market functions or perhaps technology that may need to be filled in or filled out?

Mr. Matthiessen: Within our traditional markets in the semiconductor business, I think we've identified pretty much everything that's there and we know where we fit. The opportunities for further growth there other than the organic growth of business itself are rather limited. However, I alluded before to the fact that we are doing some business outside of semiconductor. We call it non-semi business, and we see that as the avenue to our future growth because there are many areas out there that we've never addressed, specifically in the thermal area. Our thermal products used in semiconductor test actually could be used

in any kind of electrical test outside of semiconductor because they are rather generic products when you get right down to it. What they do is supply temperature-controlled environment for whatever you want to test, whether it be a single semiconductor at a semi test manufacturer or an entire assembly at a company that builds circuit boards or the like. So we see a need for thermal equipment that's been developed for the semiconductor industry to be migrated into the general electronics industry where they normally don't see such sophisticated products at such a reasonable price — and that's where our targets are.

TWST: How strong financially is inTEST at this point? What items are you focused on for improvement? Are you as well positioned as you would like to be as far as your balance sheet?

Mr. Matthiessen: I'm not sure anybody is as well positioned as they want to be. We'd like more cash and in fact we are in a cash-building situation, which is a critical component for a company of our size. But we do have a healthy balance sheet and carry no debt. We consider that essential and we try to keep it that way. If there is any debt, we keep it to a minimum just for a specific use and then retire it as soon as possible.

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TWST: Would you speak to your expectations in the next year or two as far as the rate of gain and sales?

Mr. Matthiessen: In the semi business, we are going to grow and contract in tandem with the semi cycle. There is not much more that we could do than that because we're riding on the same ocean as they are — and so in this past year, the semi business grew somewhere between 15% and 20%, and we rode that wave. It probably will not grow as much next year, but on average I would say that our annual growth will be something in the neighborhood of whatever the semi industry is doing, and maybe a mature industry like that is something like 8% or 9% a year now. So we are not expecting more than that, but we like it when it is more than that. For the areas outside of our traditional semi business, that may be different and if we involve ourselves in M&A, then we make step functions in growth. And that is actually where our targets are.

TWST: What about risk? Besides the overall economy, is there anything that keeps you up at night?

Mr. Matthiessen: Supply chain interruptions. I mean look at what just happened in Japan. I don't think we felt that directly yet, but Japan is 20% of the economy of the world, and it's hard to believe that we are not going to feel that impact someplace downstream. It happens that at inTEST we don't have any direct parts that are threatened by that. The only parts that we have from Japan that are critical are available in pretty good supply at the moment; they either weren't impacted by that specific event or there is enough in the warehouses to carry us over. Another risk is cheap, low-priced competition. We are an established company. As I said, we've been around for 30 years, we have a sales and distribution and service network that circles the globe. If you're in one specific geographical area that builds semiconductors, you're always afraid that some guy in a garage shop is going to start building or copying your equipment

and his overhead is going to be near zero. So that is something we always have to keep our eyes on, especially given that we operate extensively in Southeast Asia, where you always have to keep your eyes peeled for that sort of thing.

But when that happens, you have to convince your customer of the advantages of working with a global company where we can not only supply your factory in Taiwan, but we can supply your factory in Japan, and we can supply your factory in Korea or Southeast Asia and have everything work together. So it's the value proposition that we have to sell at that point.

TWST: Introduce us and assess the current top-level management team at inTEST. Do you have the horsepower for the run ahead?

Mr. Matthiessen: We have a great management team, and the experience for the old guys like me goes back before the 30 years, start of this company. The original management team, which includes me and our Chairman and Founder Alyn Holt, followed by Dan Graham, who is Senior Vice President and General Manager of two of

our groups, all go back to the early days of the semiconductor business. I always like to tell people that one of my first visits to a semiconductor company was to Intel on Bowers Avenue in Santa Clara, and at the time they were still in trailers.

Of course, some of the people I tell that to weren't even born yet. We've had management positions in a company called Computest going back many years, and then many of us worked at Siemens Corporation in the United States up until around 1980 when we branched out. That's when Alyn Holt started inTEST. I went out and started my own business for a few years, and then we got back together in 1985 at inTEST. Our CFO has been with the company for 15 years and is a driving force in our fiscal discipline. We have people who are younger than us who are coming up through the ranks. The fellow that runs our thermal division has strong management background and is doing a wonderful job with that group. So we have a solid level of experience in the management team without being overbuilt and having too much overhead in that area.

TWST: For a long-term investor looking at the financial statements and inTEST's annual reports, what would you suggest are the one or two items that the investor should focus on over time to get added insight into what the company is doing and where it's going?

Mr. Matthiessen: I'm one of the longer-term investors and, in fact, one of the longest-term investors, including those others of us that were here for the IPO, and I'll tell you what we look at. We're in a cyclical business. In a cyclical business if you run high debt, you have a good chance of not being here next week, and so we keep an eye on the debt level. And as I said, it's at zero right now. The only time when you'll see any debt on our balance sheet is something to do with an acquisition, and we retire that in short order, which we did recently in our last acquisition. The other thing we look at is our book-to-bill ratio that tells

us where we've been and where we're going. Right now book-to-bill is about parity. It's been running above parity for the past few quarters, and it'll probably oscillate a little bit below parity. Because we sold so much in the past few quarters, we expect it to slow down a little bit, but it's always a good indicator of what's going to happen. So those are the two things I would look at.

TWST: How could the investment community improve its understanding of inTEST? Are there any misunderstandings, any misperceptions there, or perhaps lack of insight? What kind of questions are you hearing from investors and analysts?

Mr. Matthiessen: It's a confusing business and it can be very difficult to define what we do to the nontechnical investor. So for many investors, it's a pretty difficult thing to understand. I think the important point is the equipment we make that's used on the test floors is mission critical — this is not something people buy just to pretty the place up. If they have testers and if they have wafer probers or device handlers, they must buy the type of equipment that we supply to make them work. So they may have \$1 million worth of tester and \$200,000 worth of handling equipment that have to be joined together; in order to do that they're going to need our equipment. So I think the biggest misconception is in what we actually do. My neighbors think that we make computers because to them everything to do with electronics must relate to computers. Many of the investors think we either make the testers or make the handlers, and we make neither — we make what goes in between the two. So it's a difficult thing to readily understand, but if I get an investor nailed down in a room with me, I guarantee you by the time he leaves he'll know what we do.

TWST: What would have been the recent dialogs or coverage from analysts?

Mr. Matthiessen: The only coverage we have right now is from Zacks, which happens to be paid coverage. We utilized their services so that we can get on First Call. We've gotten fairly positive coverage from Zacks, but our goal right now is to expand that coverage to non-paid coverage, and we're doing that by presenting our story to the various sell-side houses as well as to institutions. We've been on the road a great deal this year, and we have more plans to continue on this path. And I think we're having some success, so we'll see.

TWST: What are some of the challenges in getting the investment community's attention at this point?

Mr. Matthiessen: I think first and foremost, we are a small- or micro-cap company, and it is challenging to get the attention of Wall Street — not impossible, but challenging. While we are diligent in getting our story out to investors via conferences, marketing trips in the cities where most investors are, etc., we are very focused on securing sell-side coverage. The investment community is a tough community to get to, and there is nothing like a research report to keep investors influenced and abreast of what we're doing. So as far as getting to the investors, we are indeed on an aggressive program of attending conferences and doing one-on-ones in all the financial cities across the country, and in addition, trying to get that coverage that will be in front of them on a routine basis.

TWST: What do you see, if any, as competitive weaknesses for inTEST? How are you addressing those possible weaknesses over the next two to three years?

Mr. Matthiessen: Our biggest weakness is the fact that most, or in fact all of our competitors, are non-public. Obviously there are

considerable costs associated with being public that go directly to our bottom line, and this overhead is simply part of being a public company. I think we do a very good job of it, and if you can keep your productivity up, you can do that because there are also advantages to being a public company. The other disadvantage of being public is everything we do is completely transparent to the world outside of us. I can't with absolute certainty tell you what the sales level of my competitors are because they're not public. There are many things they know about us that we'd rather they didn't know, but as a public company we must make the information available to our investors — so that's probably our biggest weakness.

TWST: What would be your summary statement to investors? What are the four or five strengths, highlights and advantages that inTEST offers as an investment today?

Mr. Matthiessen: We talked about the management team before, that's a very big strength here. We have an experienced team — a very successful management team whose success can be measured in the fact that we made it through the largest downturn this industry has ever seen in the past couple of years. We call it the nuclear winter. We not only survived, we've come through a stronger and more efficient company. We could not have done this without the dedication and outright intelligence of our management team and every employee. In addition to that, we supply leading-edge products and have extensive intellectual property — something on the order of 50 patents today — which is a barrier to entry and is also a declaration to the industry that we are the leaders in these products. From a financial standpoint, we have a healthy balance sheet, carry no debt, we are profitable, are generating cash and we have a specific growth strategy. We have a goal of growing this company to \$100 million in three years, and we plan to do that through M&A in the non-semi business to mitigate the semi capital equipment curve.

TWST: Is there anything we've missed here, anything we've overlooked that you'd like to add?

Mr. Matthiessen: No, I think you've covered it pretty well. We appreciate the opportunity to present the inTEST story to your audience.

TWST: Thank you. (KL)

ROBERT E. MATTHIESSEN
CEO, President & Director
inTEST Corporation
804 East Gate Drive
Suite 200
Mount Laurel, NJ 08054
(856) 505-8800
(856) 505-8801 — FAX
www.intest.com
e-mail: info@intest.com

Investor Relations Contact:
Laura J. Guerrant-Oiye
Principal
Guerrant Associates
Phone: (808) 882-1467
Email: lguerrant@guerrantir.com