

U.S. Top 25 Stock List

Adding Applied Materials (AMAT), removing Cypress (CY)

- Following WMR IT analyst Bob Faulkner's latest rating changes, we are adding **Applied Materials (AMAT)** and removing Cypress Semiconductor (CY).
- The key investor debate for Applied Materials is whether or not the semiconductor capital equipment spending cycle will peak in 2011. We believe the cycle will be stronger both in magnitude and in length.
- The market appears quite skeptical. Current consensus expectations assume flat revenues and earnings for AMAT in 2012. At a P/E of under 10 times forward earnings, near its 5-year low, we see a compelling risk-reward trade-off. Its 2.1% dividend yield is also attractive compared to its technology sector peers.

Prior under-investment to drive a stronger, longer spending cycle

Applied Materials is the largest global provider of equipment, services and software used to manufacture semiconductors, flat panel displays and solar photovoltaic products. Simply put, we believe that the market is overly conservative regarding the semiconductor capital spending cycle and, as such, Applied Materials' earnings for 2012 and beyond are likely to positively surprise current consensus estimates.

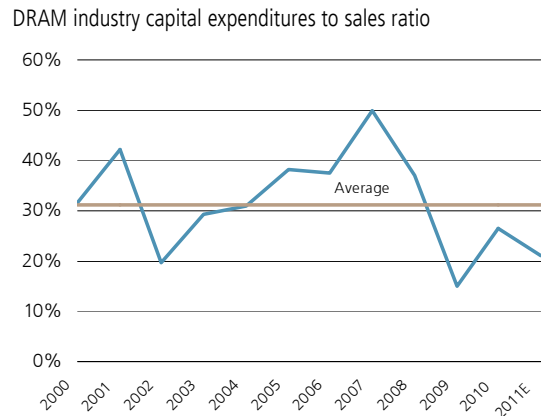
As WMR Technology analyst Bob Faulkner notes in his report, "Applied Materials – Upgrade to Outperform" (14 March 2011), industry capital spending is set to increase as DRAM memory capacity has not kept up with demand (see Fig. 1).

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Figure 1: Industry capacity additions have lagged, suggesting spending to pick up



Source: Company reports and UBS WMR, as of 14 March 2011.

Figure 2: UBS WMR U.S. Top 25 Stock List

Adobe Systems (ADBE)	Coca-Cola (KO)	Halliburton (HAL)	Lear Corp (LEA)	Schlumberger (SLB)
Ameriprise (AMP)	Colgate-Palmolive (CL)	Hewlett-Packard (HPQ)	McDonald's (MCD)	Staples (SPLS)
Apple (AAPL)	Dow Chemical (DOW)	Illinois Tool Works (ITW)	McKesson (MCK)	Teva Pharmaceuticals (TEVA)
Applied Materials (AMAT)	FedEx (FDX)	Interpublic Group (IPG)	MetLife (MET)	Thermo Fisher Sci (TMO)+
Broadcom (BRCM)	General Mills (GIS)	Intercontinental Exchange (ICE)	National Grid (NGG)+	US Bancorp (USB)

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Source: UBS WMR, as of 14 March 2011.

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Further upside potential from foundries

While ARM-based processors dominate the handset market, Intel is aggressively attempting to enter the space. Should Intel's efforts be successful, ARM-based processors will need to improve both their speed and power consumption, which will require more advanced, leading-edge wafer technology. This has the potential to drive another leg of spending on equipment by the foundries (foundries are companies that operate semiconductor fabrication plants for the designs of other companies).

Valuation looks attractive

Applied Materials' stock has pulled back 11% since 3 March 2011, leaving its current P/E ratio at just 9.8 times consensus forward 12-month earnings estimates. While we recognize that consensus earnings already reflect a level of earnings that is above its 2007 peak, a stronger earnings cycle should support a higher absolute valuation for the semiconductor capital equipment industry leader.

Removing Cypress Semiconductor (CY)

WMR IT analyst Bob Faulkner removed Cypress Semiconductor from his Technology sector Outperform list on 14 March 2011. The stock has rallied significantly over the past six months – up 56% – leaving its valuation less compelling at 15.8 times consensus forward 12-month earnings estimates. Additionally, while Bob still views Cypress as a fundamentally sound story, the stock appears increasingly vulnerable to a potential near-term inventory correction should several of the new entrants in the tablet market ultimately fail.

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Term / Abbreviation	Description / Definition
1H, 2H, etc. or 1H07, 2H07, etc.	First half, second half, etc. or first half 2007, second half 2007, etc.
1Q, 2Q, etc. or 1Q07, 2Q07, etc.	First quarter, second quarter, etc. or first quarter 2007, second quarter 2007, etc.
2007E, 2008E, etc.	2007 estimate, 2008 estimate, etc.
ADR	American depositary receipt
AUM	Assets under management = total value of own and third-party assets managed
bn	Billion (10 ⁹)
bp or bps	Basis point or basis points (100 bps = 1 percentage point)
BVPS	Book value per share = shareholders' equity divided by the number of shares
CAGR	Compound annual growth rate
Capex	Capital expenditures
CFO	1) Cash flow from operations; 2) Chief financial officer
CFPS	Cash flow per share
Cost/Inc Ratio (%)	Costs as a percentage of income
CPI	Consumer price index
CR	Combined ratio = ratio of claims and expenses as a percentage of premiums (for insurance companies)
CY	Calendar year
DCF	Discounted cash flow
DDM	Dividend discount model
Dividend Yield (%)	Dividend per share divided by price per share
DPS	Dividend per share
EBIT	Earnings before interest and taxes
EBIT Margin (%)	EBIT divided by revenues
EBIT(D)A	Earnings before interest, taxes, (depreciation) and amortization
EBITDA Margin (%)	EBITDA divided by revenues
EBITDA/Net Interest	EBITDA divided by net interest expense
EBITDAR	Earnings before interest, taxes, depreciation, amortization and rental expense
EFVR	Estimated fair value range
EmV	Embedded value = net asset value + present value of forecasted future profits (for life insurers)
EPS	Earnings per share
Equity Ratio (%)	Shareholders' equity divided by total assets
EV	Enterprise value = market value of equity, preferred equity, outstanding net debt and minorities
FCF	Free cash flow = cash a company generates above outlays required to maintain/expand its asset base
FCF Yield (%)	Free cash flow divided by market capitalization
FFO	Funds from operations
FY	Fiscal year / financial year
GDP	Gross domestic product
GF	Grandfathered status
Gross Margin (%)	Gross profit divided by revenues
h/h	Half-year over half-year; half on half

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Interbank Ratio	Interbank deposits due from banks divided by interbank deposits due to banks
Interest Coverage	Ratio that expresses the number of times interest expenses are covered by earnings
Interest exp	Interest expense
ISIN	International securities identification number
LLP/Net Int Inc (%)	Loan loss provisions divided by net interest income
LLR/Gross Loans (%)	Loan loss reserves divided by gross loans
m/m	Month-over-month; month on month
mn	Million (10 ⁶)
n.a. or NA	Not available or not applicable
NAV	Net asset value
Net Debt	Short- and long-term interest-bearing debt minus cash and cash equivalents
Net Int Margin (%)	Net interest income divided by average interest-bearing assets
Net Margin (%)	Net income divided by revenues
n.m. or NM	Not meaningful
NPL	Non-performing loans
Op Margin (%)	Operating income divided by revenues
p.a.	Per annum (per year)
P/BV	Price to book value
P/CFPS	Price/Cash flow per share
P/E	Price to earnings
P/E Relative	P/E relative to the market
P/EmV	Price to embedded value
PEG Ratio	P/E ratio divided by earnings growth
PPI	Producer price index
Prim Bal/Cur Rev (%)	Primary balance divided by current revenue (total revenue minus capital revenue)
Profit Margin (%)	Net income divided by revenues
q/q	Quarter-over-quarter; quarter on quarter
ROA (%)	Return on assets
ROCE (%)	Return on capital employed = EBIT divided by difference between total assets & current liabilities
ROE (%)	Return on equity
ROAE (%)	Return on average equity
ROIC (%)	Return on invested capital
Solvency Ratio (%)	Ratio of shareholders' equity to net premiums written (for insurance companies)
Tier 1 Ratio (%)	Tier 1 capital divided by risk-weighted assets; describes a bank's capital adequacy
tn	Trillion (10 ¹²)
WACC	Weighted average cost of capital
UBS WMR	UBS Wealth Management Research
y/y	Year-over-year; year on year
YTD	Year-to-date

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Statement of Risk

Equity markets are difficult to forecast because of fluctuations in the economy, investor psychology, geopolitical conditions, and other important variables.

Description and Methodology

To be added to the WMR U.S. Top 25, stocks must have a market capitalization of at least USD 2 billion and:

1. be listed on either the Sector Outperform or Sector Marketperform List from Wealth Management Research (WMR), or
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The list of 25 stocks represents our top absolute return ideas from a risk/reward perspective over the next 12 months. Stocks are chosen for inclusion on the list combining top-down analysis of anticipated investment themes and bottom-up company analysis emphasizing valuation relative to estimated secular earnings growth. Changes to the list will occur when other stocks are judged to offer more attractive risk/reward tradeoffs.

The indicated performance is based on capital appreciation plus dividends of an equal weight portfolio, but does not include transaction costs, such as commissions, fees, margin interest, and interest charges. Actual transactions adjusted for such transaction costs will result in reduced total returns. Prices of stocks in this performance reflect closing prices one trading day after the addition or deletion to ensure that changes to the list are announced in a manner that allows clients to match the list's performance.

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Name	Ticker	Sector	Price (3/14/2011)
Interpublic Group	IPG	Consumer Discretionary	\$12.43
Lear Corp	LEA	Consumer Discretionary	\$100.80
McDonald's	MCD	Consumer Discretionary	\$75.67
Staples	SPLS	Consumer Discretionary	\$20.22
Coca-Cola	KO	Consumer Staples	\$63.94
Colgate-Palmolive	CL	Consumer Staples	\$78.27
General Mills	GIS	Consumer Staples	\$36.92
Halliburton	HAL	Energy	\$45.06
Schlumberger	SLB	Energy	\$85.36
Ameriprise	AMP	Financials	\$61.56
Intercontinental Exchange	ICE	Financials	\$124.79
MetLife	MET	Financials	\$44.74
U.S. Bancorp	USB	Financials	\$26.87
McKesson	MCK	Health Care	\$77.26
Teva	TEVA	Health Care	\$49.21
Thermo Fisher Scientific	TMO	Health Care	\$54.68
FedEx Corp.	FDX	Industrials	\$88.63
Illinois Tool Works	ITW	Industrials	\$54.36
Applied Materials	AMAT	Information Technology	\$14.96
Adobe Systems	ADBE	Information Technology	\$34.08
Apple	AAPL	Information Technology	\$353.56
Broadcom	BRCM	Information Technology	\$40.56
Cypress Semiconductor	CY	Information Technology	\$18.88
Hewlett-Packard	HPQ	Information Technology	\$41.49
Dow Chemical	DOW	Materials	\$36.61
National Grid	NGG	Utilities	\$45.41

Source: Bloomberg

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Stock Recommendation System

Wealth Management Research

Analysts provide a relative rating, which is based on the stock's total return potential against the total estimated return of the appropriate sector benchmark over the next 12 months.

Industry Sector Relative Stock View

Outperform (OUT)	Expected to outperform the sector benchmark over the next 12 months.
Marketperform (MKT)	Expected to perform in line with the sector benchmark over the next 12 months.
Underperform (UND)	Expected to underperform the sector benchmark over the next 12 months.

Under review

Upon special events that require further analysis, the stock rating may be flagged as "Under review" by the analyst.

Suspended

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UBS 12-Month Rating	Definition
Buy	FSR is > 6% above the MRA.
Neutral	FSR is between -6% and 6% of the MRA.
Sell	FSR is > 6% below the MRA.

Key Definitions

Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

Market Return Assumption (MRA) is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

Under Review (UR) Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

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