

Energy Alternative Sources

Company Update Estimate Change

Rating: BUY
Price: \$14.54
Price Target: \$21.00

Bloomberg: NASDAQ: ESLR

Market Data

52-Week Range: \$17.50-\$4.68
Total Entprs. Value (MM): \$900.1
Insider Ownership: 14.0%
Institutional Ownership: 48.0%
Shares Out. (MM): 63.5
Market Cap. (MM): \$923.3
Float (MM): 50.2
Float (%): NA
Avg. Daily Vol.: 3,044,007

Financial Summary

Net Debt (MM): (\$23.20)
Net Debt/Capital: (10%)

USD	2005A	2006E	2007E	2008E
Rev. (MM)	43.6	97.3	183.7	409.6
Prev. Rev.	--	98.0	184.7	--
EV/Rev.	20.6x	9.3x	4.9x	2.2x
EPS				
Mar	(0.06)	(0.13)A	—	—
Prev.	--	0.00	--	--
Jun	(0.07)	(0.13)	—	—
Prev.	--	0.00	--	--
Sep	(0.07)	(0.08)	—	—
Prev.	--	0.00	--	--
Dec	(0.08)	(0.05)	—	—
Prev.	--	0.00	--	--
FY Dec	(0.29)	(0.42)	(0.15)	0.45
Prev. FY	--	(0.34)	0.00	--
FY P/E	NM	NM	NM	32.3x
Consensus	(0.29)	(0.20)	0.05	—

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Evergreen Solar (NASDAQ: ESLR)

Solid Results; Ramp in EverQ Progressing

Investment Summary

We continue to recommend the purchase of the shares as improvements in manufacturing operations provide increased confidence in the company's ability to execute in its current facility and its EverQ JV.

Event

ESLR reported a loss of \$0.13/sh. in 1Q06, including 2 cents of FAS-123 expense. On a comparable basis, ESLR reported a loss of \$0.11/sh., 2 cents better than our forecast and 3 cents better than consensus.

Key Points

- **EverQ Facility on Track or Even Ahead of Schedule.** ESLR produced its first modules out of the EverQ facility, which is on track or slightly ahead of schedule. We expect a significant ramp in revenues from \$9.5M in 2Q06 to \$18M in 3Q06 and \$23M in 4Q06. The recent production and full employment of the facility gives us confidence that ESLR should be able to achieve these targets.
- **Silicon Supply Secure.** Renewable Energy Corporation (REC) accelerated silicon supply to Evergreen in the wake of MEMC's decision to break its supply contract with Evergreen. Additionally, the company demonstrated its ability to use chunk silicon in addition to granular silicon. We believe this could provide Evergreen with additional flexibility to source from multiple suppliers after the silicon shortage abates, which is a net positive.
- **Thin Wafers Progressing Ahead of Schedule.** ESLR converted its Marlboro facility to thin wafers at an industry best 150 microns. The resultant silicon use also declined to 6 g/watt, which is half the silicon usage of the industry average. Throughout 2006, ESLR expects to expand the program to the EverQ facility. If the company is successful at meeting its goal of thin wafers by the end of 2006, it would be roughly a year ahead of our forecast.
- **Better than Expected Quarter; Changing Estimates to Reflect FAS-123 Expense.** Excluding FAS-123 expense, ESLR reported a loss of \$0.11/ sh. versus our estimate for a loss of \$0.13/sh. and consensus for a loss of \$0.14/sh. The better than anticipated results were due to higher revenues. The company decided to include FAS-123 expenses in its reported numbers, which negatively impacted EPS by 2 cents/sh. Therefore, we decided to adjust our model to reflect the change in options accounting. Should the consensus also move toward the new methodology, it would have the effect of lowering consensus estimates by 8-10 cents/sh. in 2006. Importantly, on the same basis, we are increasing our 2006 EPS estimate to reflect the better than anticipated results in 1Q06.

Valuation/Risks

Long-Term Prospects Drive Valuation Call. Due to strong industry demand, capacity expansions, and ESLR's proprietary technology, we expect EPS in FY08-10 to go from \$0.45 to \$1.48. We are valuing the shares based on a 0.80x PEG ratio on the industry's growth rate of 30%, and discounting this back at a 15% discount rate, which results in our near-term price objective of \$21/sh.

EverQ Facility Progressing as Planned. ESLR announced during the quarter that most of the machines have been installed in the new EverQ facility and that the plant had produced its first solar module. The company has hired over 200 workers and is in the process of training them on the machines. The company indicated that it is on track for production in 2Q06 with a ramp to full production by 4Q06. While the company did not detail future expansion plans beyond the initial 30 MW, we expect that the company to make additional announcements after the start of production in the second quarter.

Thin Wafers Progressing Ahead of Schedule. During the quarter, the company was able to produce thin wafers (150 microns) and convert them into cells at the Marlboro facility. This is roughly one quarter ahead of schedule. The company expects to convert the EverQ facility to thin wafers by the end of FY06. The company is currently producing solar modules using 9 grams of silicon per watt of output at EverQ, but at only 6 grams of silicon per watt at Marlboro. This compares to an industry average above 10g/watt. Importantly, this figure includes all breakage. The company believes it can further reduce silicon usage to 5g/watt, or more than 50% better silicon usage than the industry average.

ESLR Improved Efficiencies Again. A common argument against investing in the shares of ESLR is its relatively low efficiency relative to some competitors. We do not think this is a valid concern; in fact, we believe that ESLR may have more room to improve efficiencies with its technology versus other more mature solar cell technologies. Efficiency is simply the amount of light energy that is successfully converted into electricity (higher is better). ESLR is currently at 14.0%-14.5% efficiency versus an industry average of around 15-16%. However, in the last 2 quarters, the company improved its efficiency by an average of 100 bps. In effect, this serves to increase output by 8% and also revenues by 8% without any additional costs to manufacture. The company indicated that it already has plans to increase the efficiency to around 15% over the coming year. Given the limited resources devoted to string ribbon technology versus the industry, we believe that ESLR still has ample opportunity to improve efficiency before approaching physical limitations of 23-25% efficiency. Importantly, we have not built into our model improvements in the underlying efficiency.

Quad Ribbon Could Provide Upside. The company is also making progress on its Quad ribbon furnace. Currently the company uses a dual ribbon furnace that requires manned operation to run. The Quad ribbon furnace grow four ribbons simultaneously instead of two and, perhaps most importantly, is semi-automated, requiring manual input only every 3-4 days. We estimate that the quad furnace could increase margins 300-500 basis points versus a similarly equipped dual ribbon furnace. The company purchased and installed five furnaces during the quarter, with another three on order. If the trial run is successful then the company will roll out the quad furnaces to the EverQ facility as well.

New Order Again. The company announced another new order in the quarter from Solartecnik. This is the fourth order in the last six months and follows previous orders from Global Resource Options, Inc. (GRO), Powerlight Corporation and S.A.G. Solarstrom. The cumulative orders amount to over \$380 million over the next four years. These four orders amount to more than our revenue assumption for all of 2006 and 2007 and represent more than two years worth of backlog.

1Q06 Results:

Excluding FAS-123 expenses, Evergreen reported a loss of \$0.11/sh. in 1Q06 versus our estimate for a loss of \$0.13/sh. and consensus of a loss of \$0.14/sh. The reported EPS in the quarter was (\$0.13) as the company started to expense its options liability. This compares to a year ago loss of \$0.06/sh. The variance versus year ago levels was due to increased costs associated with the EverQ JV startup. The variance versus our estimate and consensus estimates was due to better than anticipated revenues from the Marlboro facility.

Record Revenues Drive Earnings Outperformance. The company reported record quarterly revenues of \$11.9 million versus our estimate of \$11.5 million and consensus of \$11.0 million. The better than anticipated revenues were due to increased productivity from the switch to thinner wafers and higher efficiency cells. Assuming a market price of \$3.20/watt, the company produced near full capacity at 14.5 MW annual run rate in the quarter. The higher revenues also resulted in record gross margin of 8.9% (9.8% excluding stock expense) at the Marlboro facility, which was in-line with our forecast. Overall margins were at -9.5%, as the company recorded \$2.5 million in expenses from the EverQ startup, but did not record any revenues from the JV. We expect margin improvement throughout the year as EverQ ramps production.

Higher Costs Supported By Results. The company increased spending on both SGA and R&D versus our estimates. However, the variance versus our estimate was due to the company's decision to expense options. ESLR reported

SGA expense of \$4.4 million versus our estimate of \$4.0 million, with \$700K of incremental expense for FAS 123 compliance. Similarly, the company spent \$4.5 million on R&D versus our estimate of \$3.5 million, with \$300K for option expense. We believe that the increased SGA expenses are justified by the early returns, which include over \$380 million in new orders generated in the last six months. Additionally, the R&D spending yielded better efficiencies out of the solar modules, which serve to increase revenues. The company indicated that it is on track to increase efficiencies another 50-100 bps, which should improve the profitability further.

Strong Balance Sheet Allows for Additional Expansion. Evergreen ended the quarter with \$114 million in cash and investments on hand. The only major debt is a \$90M convertible debt offering that is significantly above its strike price (~\$8/sh.) that will likely be converted into shares. We believe this affords the company with ample opportunity to expand either the EverQ facility or internally without accessing the capital markets. We believe the company and the board of directors are evaluating the performance at the EverQ facility and will likely make additional expansion announcements in 2Q06 following production startup at EverQ.

Company Description

Evergreen Solar is a manufacturer of polysilicon wafers (13 patents), cells (5 patents) and modules (8 patents) for the generation of electricity through photovoltaic processes. They currently account for less than 1% of the global photovoltaic market, but are in the process of ramping production significantly (11x in 5 years - Jefco Estimate). Because of its proprietary string ribbon technology to produce wafers, Evergreen is potentially the low-cost manufacturer of solar panels. Currently, nearly 70% of total sales are into Germany. Evergreen's main manufacturing platform will initially be the joint venture with Qcells (the fastest growing and 5th largest solar module manufacturer), which should add expertise to the cell and module manufacturing process. The basis for the company's potential as a low-cost provider rests with its proprietary string ribbon technology to manufacture wafers with 35% less silicon than its competitors.

Evergreen Solar	FY	FY	FY	FY	March	June	Sept	Dec	FY	FY	FY
Income Statement (\$ in millions)	2002	2003	2004	2005	1Q	2QE	3QE	4QE	2006E	2007	2008
Product Revenues	5.3	7.7	22.2	43.6	11.6	21.0	30.1	34.7	97.3	183.7	409.6
<i>Growth</i>	243%	46%	187%	96.2%	12.4%	96.3%	171.2%	200.1%	123.1%	88.7%	123.0%
Research Revenues	1.4	1.6	1.3	0.4	0.3	0.3	0.3	0.3	1.1	1.0	1.2
Net sales	6.7	9.3	23.5	44.0	11.9	21.2	30.3	35.0	98.4	184.7	410.8
<i>Growth</i>	172%	38.1%	152.8%	87.1%	13.0%	98.6%	171.1%	200.3%	123.5%	87.7%	122.5%
COGS	12.4	15.4	29.7	40.0	13.0	22.1	24.9	25.7	85.7	130.9	269.3
GROSS PROFIT	(5.7)	(6.1)	(6.2)	4.1	(1.1)	(0.9)	5.4	9.3	12.7	53.8	141.5
<i>% margin</i>	(83.9%)	(65.2%)	(26.3%)	9.3%	(9.5%)	(4.1%)	17.9%	26.5%	12.9%	29.1%	34.4%
Selling and administrative expenses	4.5	5.3	7.8	12.3	4.4	5.0	5.1	5.3	19.80	24.3	40.0
<i>% of sales</i>	67.0%	57.3%	33.1%	27.9%	37.0%	23.6%	16.8%	15.2%	20.1%	13.2%	9.7%
Research and Development	3.7	3.8	4.9	11.5	4.5	4.6	4.5	4.5	18.12	18.3	23.0
<i>% of sales</i>	54.8%	40.7%	21%	26%	38.0%	21.7%	14.8%	12.9%	18.4%	9.9%	5.6%
Depreciation	1.97	2.01	3.46	3.87	1.10	1.10	1.35	1.35	4.90	7.2	9.2
<i>% of sales</i>	29.2%	21.5%	14.7%	8.8%	9.3%	5.2%	4.5%	3.9%	5.0%	3.9%	2.2%
OPERATING INCOME	(13.9)	(15.2)	(18.909)	(19.7)	(10.0)	(10.5)	(4.2)	(0.5)	(25.2)	11.2	78.5
<i>% margin</i>	(205.7%)	(163.2%)	(80.3%)	(44.6%)	(84.5%)	(49.4%)	(13.8%)	(1.5%)	(25.6%)	6.1%	19.1%
Interest Income	0.7	0.0	0.1	0.2	0.0	1.0	1.0	1.0	3.04	2.7	1.2
Interest Expense	0.0	0.0	0.0	0.0	0.0	(1.0)	(1.0)	(1.0)	(2.95)	(3.9)	(10.0)
Other Income	0.0	0.2	-0.5	1.0	0.4	0.4	0.3	0.3	1.42	0.0	0.0
Foreign exchange gains	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.00	0.0	0.0
PRETAX INCOME	(13.2)	(15.0)	(19.363)	(18.5)	(9.6)	(10.1)	(3.8)	(0.2)	(23.7)	10.0	69.7
<i>% margin</i>	(195.7%)	(160.8%)	(82.3%)	(42.0%)	(80.9%)	(47.6%)	(12.6%)	(0.5%)	(24.1%)	5.4%	17.0%
Income taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.7	1.9	2.6	12.0	24.2
<i>Tax rate</i>	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	(18.0%)	(1092.6%)	(11.0%)	120.6%	34.7%
Minority Interest Paid				(1.2)	(1.5)	(1.4)	0.5	1.3	-1.1	8.0	16.1
NET INCOME	(\$13.199)	(\$14.974)	(\$19.363)	(\$17.3)	(\$8.1)	(\$8.7)	(\$5.0)	(\$3.4)	(\$27.5)	(\$10.1)	\$29.4
<i>% margin</i>	(195.7%)	(160.8%)	(82.3%)	(39.3%)	(68.5%)	(41.1%)	(16.4%)	(9.7%)	(27.9%)	(5.5%)	7.2%
EARNINGS PER SHARE	(\$1.16)	(\$1.26)	(\$0.58)	(\$0.29)	(\$0.13)	(\$0.13)	(\$0.08)	(\$0.05)	(\$0.42)	(\$0.15)	\$0.45
Fas-123 Impact	0.0	-13.5	-2.9	0.0	1.20	1.75	1.75	1.75	6.45	7.00	8.00
Net Income Reported	(\$13.192)	(\$28.472)	(\$22.267)	(\$17.3)	(\$6.9)	(\$7.0)	(\$3.2)	(\$1.6)	(\$21.0)	(\$3.1)	\$37.4
EARNINGS PER SHARE (ex Fas123)	(\$1.16)	(\$2.39)	(\$0.67)	(\$0.29)	(\$0.11)	(\$0.11)	(\$0.05)	(\$0.03)	(\$0.32)	(\$0.05)	\$0.57

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Jefferies makes a market in Evergreen Solar.

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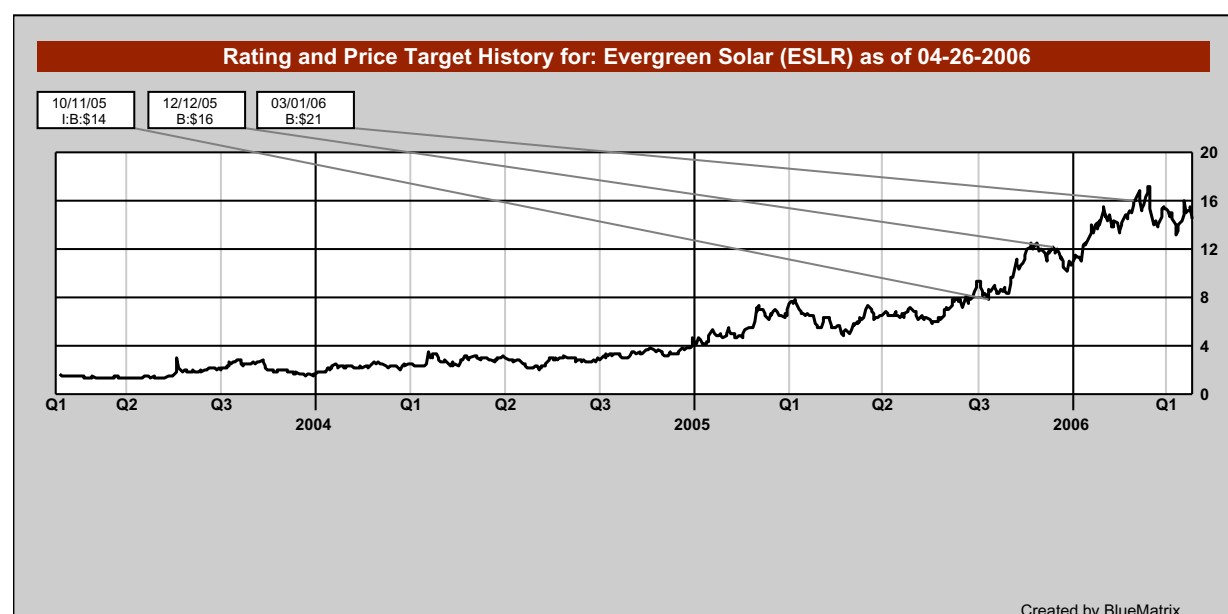
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Distribution of Ratings

Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [BUY/SB]	419	52.97	74	17.66
HOLD [HOLD]	346	43.74	32	9.25
SELL [UNPF/SU]	26	3.29	2	7.69

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