

No signs of 2H recovery for ICs, equipment, says analyst

Posted: Apr 20 2005

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This article was printed from Electronic Engineering Times - Asia located at:

http://www.eetasia.com/article/article_content.php3?article_id=8800364458

Contrary to popular belief, there are no signs of a recovery for the semiconductor and chip-equipment industries in the second half of 2005, according to an analyst with Adams Harkness Inc. Several researchers, including Semico Research Corp., believe that the overall chip industry is set to rebound in the second half of 2005 and should enjoy strong growth through 2007 (see April 8 story).

Avinash Kant, an analyst with investment banking firm Adams Harkness, disagrees based on current economic indicators. "We see weaker consumer demand in H2:05 due to rising interest rates and higher gas prices," Kant said.

The IC-equipment market looks especially dismal. This week alone, chip-equipment vendors Nova Measuring Instruments Ltd and Therma-Wave Inc. separately announced workforce reductions, while ASML Holding NV and Lam Research Corp. posted lackluster results in their respective quarters.

"Based on our channel checks, we have made the argument that contrary to the conventional belief of a second-half recovery, orders (for semiconductor-production equipment) in the second half of 2005 would likely be worse than in the first half," Kant said.

"Given weakening fundamentals and the fact that equipment orders have been more first half loaded, however, we expect these numbers to be revised down meaningfully as companies get more visibility into the second half," he said. "Our channel checks at various subsystems suppliers (to equipment companies) indicate no improvement in their internal forecast over the next few months."

The chips are down

There are also ominous signs for chip makers and OEMs as well. "Fairchild Semiconductor, Sun Microsystems and IBM have also announced weaker-than-expected quarters," he said. "During the Texas Instruments conference call, there was some talk that wireless could be below seasonal norm in the second quarter."

On the chip side, Advanced Micro Devices Inc. (AMD) this week reported a loss in Q1 due to deficits in its flash-memory unit (see April 13 story). Spansion LLC, the flash memory venture of AMD and Fujitsu, has filed for an IPO with the Securities and Exchange Commission, likely indicating AMD is jettisoning its unprofitable memory unit (see April 13 story).

Analysts praised AMD's move to spin-out Spansion. "AMD will be able to reduce its debt load, as Spansion will accept roughly \$775 million in debt, leaving AMD proper with roughly \$900 million, much lower than its 1Q05 level of \$1.65 billion," said Richard Shannon, an analyst with Piper Jaffray & Co. (Minneapolis, Minn).

Shannon upgraded AMD's shares to an "outperform" status. "Our upgrade is based on two factors: 1) continued excellent performance from its microprocessor business, and 2) the impending spin-out of its flash business, which will highlight a profitable processor business and remove the requirement to fund a very capital-intensive flash memory business over the next few years," he said.

Not all is doom-and-gloom in flash memory, especially for NAND specialist SanDisk Corp., which will shortly report its results. "We expect SanDisk to best our Q1 revenue and EPS estimates of \$454

million and \$0.30, which are below consensus estimates of \$467 and \$0.31," according to a new report from RBC Capital Markets Inc. (San Francisco).

"Based on our checks, we believe there is EPS upside due to benign pricing, better 90nm yields, and less non-captive outsourcing," according to the report. "We estimate Q1 ASPs to be down in the 5 percent range, vs. the company's expectation of down 15 percent."

It's a mixed bag for the chip-equipment market. Etch specialist Lam, for example, reported revenue of \$349 million in the March quarter, which "was in-line with our \$348 million estimate," said Bill Ong, an analyst with American Technology Research Inc. in San Francisco.

"Pro forma EPS of \$0.44 was better than our \$0.42 estimate," he said. "June quarter revenue is expected to stay flat at \$350 million, plus or minus \$10 million."

Lam reported March quarter orders at \$315 million, down 19 percent sequentially - or "at the low end of guidance versus our midpoint expectation of \$320 million, or down 17 percent," Ong said. "June quarter orders are expected to be sequentially flat, reflecting the stabilization of the business. Management continues to cite limited business visibility beyond the June quarter; however, the key to order growth is dependent on a foundry spending recovery."

Shares of lithography-light source firm Cymer Inc. this week fell following disappointing Q1 results and Q2 order guidance from its largest customer: ASML.

"ASML reported disappointing Q1 results and disappointing Q2 order guidance, pointing to a digestion period at its memory customers, continued weakness in foundry demand and a U-shaped rather than a V-shaped recovery," said Cristina Osmena, an analyst with Jefferies & Co. Inc.

"However, we believe that Cymer, though vulnerable to weaker demand at its largest customer, may not see a commensurate impact on its business," Osmena said. "Cymer enjoys higher exposure to end customers continuing to spend in 2005, including Intel, Elpida and Toshiba."

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