

IN DEPTH: TECHNOLOGY

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Chip industry headed for slow year, but Arizona should fare well

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The Business Journal

Thanks to a general lack of exciting new gadgetry to pack full of the latest semiconductors, 2005 looks to be a down year for the worldwide chip industry.

"We're dubbing this year the boring downturn," said Instat Senior Semiconductor Analyst Frank Dickson. "There's just no one gadget that everyone's talking about."

But in Arizona, the nation's No. 3 state for chip manufacturing jobs, the forecast looks brighter than what most analysts are expecting worldwide. Intel Corp.'s conversion of its Fab 12 in Chandler from 200mm to more efficient 300mm wafers is one example of how Arizona chip-makers may weather a slow 2005.

Industry analysts generally are calling for a single-digit decline in worldwide sales for 2005. This comes off a powerful 2004, when cell phones and laptop computer sales fueled 27 percent industry growth.

Analysts say that for at least this year, a lack of new innovations in cell phones, handheld devices and computers will slow sales and cause excess inventory.

On the bright side, that excess inventory could translate into cheaper consumer electronics for shoppers and the original equipment manufacturers who sell them.

Jim Feldhan, president of Semico Research in Phoenix, said he's predicting a 4.7 percent worldwide decline in chip sales for 2005. Worldwide sales were estimated at \$211 billion last year.

"The main reason behind this is that the end markets are going to slow down," he said. "Cellular phone and handheld device sales peaked last year."

Semico research showed that cell phone growth peaked at 26 percent last year but only is expected to grow about 6 percent this year.

"There's nothing new in the market today as far as gadgets go," Feldhan said. "The upgrade cycle has ended, and the second wave of it likely won't begin until 2006."

Dickson and Instat are predicting a 5.7 percent decline in worldwide sales this year for the semiconductor industry. That prediction is on the low end compared to most outlooks. He also cited oversupply as a major factor in the predicted downturn.

"The semiconductor industry is very sensitive to supply changes, and when capacity goes up, supply goes down," he said.

Feldhan and Dickson said the good news is that this likely won't have too profound of an affect on Arizona companies. Both said STMicroelectronics, Freescale Semiconductor Inc. and Microchip Technology Inc. likely would outperform worldwide sales because of where they're positioned in the chip industry.

Those companies do a good deal of business in consumer electronics and automotive products, two areas where growth in the chip industry still is expected in 2005.

Other hot pockets of chip growth, Feldhan said, should come in the areas of image sensors and flash memory, both of which are used in digital cameras. Flash also is used in MP3 players.

Phoenix-based ON Semiconductor, both analysts said, could have a rougher road in 2005. ON focuses heavily on more traditional semiconductors, an area where Feldhan said excess inventory will pose a problem.

If their interest in commenting on this story is any indication, both ON and Chandler's Microchip Technology may be bracing for an uncertain year. Both declined to share any insight into their plans for 2005 for this story.

Intel, however, could make waves when its Fab 12 plant opens late this year. That project could be a harbinger for things to come for the chip-maker's operations in Arizona.

"Fab 12 is the 'test' for conversion success," said company spokeswoman Jeanne Forbis. "Intel has never done this before."

Perhaps a successful Fab 12 conversion could mean more plant upgrades in Arizona.

"If the Fab 12 conversion is successful, Fab 22 would be a viable candidate for the next conversion -- when the corporation is ready to make that decision," Forbis said.

Intel made a \$2 billion investment to convert Fab 12, and a Fab 22 conversion likely would cost at least that much. The Fab 12 conversion won't add any new jobs to the Valley, but not shipping the jobs overseas is widely considered a success.

Feldhan said regardless of what happens in 2005, Intel should hold up fine. That's also good news for Arizona.

"We (Arizona) differentiate a little bit from the rest of the world because of Intel's large presence here," he said. "They tend to outperform the industry."

Dickson agreed Intel should have little trouble riding out 2005.

"Intel has a very long-term view of the semiconductor industry and they also are in a very high-end place within the industry," he said. "And in part because of Intel, overall, Arizona should weather this storm well."

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