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Infineon splitting its chips

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HENRY BECKER, Managing director, Infineon Technologies Richmond
Complexity, thrill and uncertainty in the computer chip industry make for a wild ride that Henry Becker enjoys.

The 43-year-old is managing director of Infineon Technologies Richmond, a 1.3 million-square-foot plant in eastern Henrico County that produces computer memory chips, those pieces that eventually find their ways into many types of consumer electronics.

The chips are made in an intricate process out of silicon, a material physicists refer to as a semiconductor.

"Next to God and my family, semiconductors are the most exciting aspect of my life," Becker said last week. "Where else can you compete in a global environment utilizing leading edge, state-of-the-art technology on a constantly changing landscape?"

That scene will change for Becker by July 1 when his facility and the rest of the Munich, Germany-based Infineon Technologies AG's global memory division -- representing about 40 percent of its total revenue -- separate from the company's two other units.

The move, executives say, will make more sense for both of Infineon's chipmaking operations.

"Our No. 1 challenge is to meet all of our customers' needs and expectations while going through the legal transition, and grow our business and produce positive revenues that make us attractive on the market," Becker said.

After this "strategic realignment" -- as the company's German supervisory board is calling the move -- Infineon can focus and improve profits at its two other divisions that make up its logic business.

That segment makes chips used in vehicles and security cards. The pieces can perform broader functions in mobile phones or communications networks than those memory chips made at the Henrico plant.

Some of the logic technology, for instance, uses chips to improve energy efficiencies in cars while other components are used by Microsoft Corp. for its Xbox 360 entertainment console.

Another reason for the separation is because factories in the past made computer memory chips used a more advanced technology than was needed for producing logic chips. As technology for memory advanced, its outdated production lines could be quickly converted to develop logic.

"What's happening now is the gap is widening, and some of the manufacturing processes [in memory] are different from the ones in logic," said Andrew Griffin, an analyst at London-based Merrill Lynch.

In addition, converting the plants will become more expensive and logic chips need their own manufacturing facilities.

At some point in the future -- the company won't say when -- Infineon likely will divest the memory business altogether with a public offering of its stock. Doing so will allow investors to target either the memory or logic companies, as opposed to Infineon as a whole.

Over the years, many semiconductor companies such as Texas Instruments Inc. and Toshiba Corp. have bailed out of the memory chip business, an industry subject to volatile price swings and constantly fluctuating supply and demand.

Infineon's plant in Henrico -- the size of 23 football fields -- has 2,300 employees who work in shifts around-the-clock to produce basic computer memory chips called DRAM, a key data-storage component in PCs, laptops and servers.

In the \$26 billion DRAM market, Infineon is ranked fourth worldwide among its rivals, according to market research firm iSuppli Corp. Samsung Electronics Co. Ltd. is the largest manufacturer with 30 percent share of the market, followed by Hynix Semiconductor Inc. and Micron Technology Inc., which has a plant in Manassas.

Price and demand last year for DRAM was down, hurting profit margins.

Infineon's memory division posted a 3.4 percent decrease in revenue and a 28 percent drop in operating profit in the fiscal year that ended Sept. 30, compared with the prior year.

The poor performance and market volatility helped frame the rationale to carve out the business, analysts said.

"Infineon had a very, very bad last year," Merrill Lynch's Griffin said.

The bad news continued into the company's fiscal first quarter, which ended Dec. 31. The logic business eked out a profit while executives blamed the "significant deterioration" of cash flow in the memory unit for Infineon's overall poor financial results.

Operating profit in the logic business was \$35.5 million versus a loss of \$139.8 million in the memory division for the first fiscal quarter.

"From a business standpoint, it's a very good decision" to separate the memory division, said Nam Hyung Kim, an analyst at California-based market research firm iSuppli.

However, he and others are skeptical on what kind of value would be created for shareholders if and when Infineon creates a publicly-traded company for its memory business.

"Where will the investors come from who are willing to buy one of the biggest memory companies still battling it out?," said Bob Merritt, who tracks the memory-chip industry at Phoenix, Ariz.-based Semico Research.

Going forward, keeping manufacturing costs for DRAM down will be essential because the chips are a commodity, and much like metals or oil, can be swapped with another company's product. The lower that Becker can keep his production costs, the greater his profit margins will be.

"Cost is king," he said.

Memory-chip production soared as computer sales exploded in the mid-1990s, followed by a downturn in 1998 -- just as Infineon's plant in Henrico was beginning to crank out chips -- and upswing the next two years.

Production for DRAM now grows at about half the pace it did in the 1990s, Semico Research's Merritt said. In addition, "the cost of producing those memory bits has been increasing at a phenomenal rate," he said.

Prices and demand for DRAM is rebounding, with "slow but solid growth for the next couple of years," Merritt said, which could bring relief to companies such as Infineon.

"Infineon is going to be a happier ship in a year's time than not," Griffin said.

The company is in the midst of a \$1.5 billion expansion to its Henrico plant, which will help it cut chip production costs by 30 percent.

The plant's addition here continues as the company prepares itself for that next upswing of the chip cycle.

One way to get a leg up on the competition in the DRAM business, Becker said, is to move away from its traditional use in PCs and jump into emerging markets such as portable devices, graphics applications and mobile communications.

After the dust settles on this year's realignment, the memory-chip company will employ 13,000 people worldwide.

In addition to business changes, Becker also looks ahead to a new era overseeing memory operations on this continent.

While the role that a memory chip plays will change over time, Becker said, "the need for it will always be there."

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