

On the Way Up? Or Down?

By Jeff Chappell -- 1/12/2005

Electronic News

<http://www.reed-electronics.com/electronicnews/article/CA495611?text=semico>

HALF MOON BAY, Calif.--The market researchers held court here Tuesday afternoon, and by all accounts, no one expects 2005 to be a particularly tough year for equipment and materials suppliers.

Not a great year, but not a particularly bad year – revenues might contract, or there might be single digit growth for equipment vendors, depending on whom one asks. But generally, forecasters at VLSI Research, Advanced Forecasting, Gartner Inc., IC Insights and Semico Research agreed 2005 is shaping up to be a mild year, compared to say, 2001.

While analysts gave a sneak peak of their forecasts on Monday, on Tuesday they went more in depth, delving into the reasoning behind their prognostications.

According to Semico Research, the industry still has a few quarters to go before it hits the bottom of the current down cycle in Q3, with a recovery ensuing in 2006. Furthermore, he said that the most recent replacement cycle for cell phones and PCs is drawing to a close.

While the industry reacted rather quickly to overcapacity in the latter half of 2004, macroeconomic factors: namely oil prices, the U.S. deficit, the ongoing U.S. war in Iraq, and the weak U.S. dollar, as well as world gross domestic product (GDP), will temper end markets in 2005, Jim Feldhan, Semico president, suggested.

World GDP was a common thread running through the analysts' presentations. After a big year in 2004, with the world GDP growth reaching 4.7 percent – the average is 3.5 percent – Feldhan said Semico forecast that growth to slow to 2.2 percent in 2005.

IC Insights' Bill McClean also cited a slowing of world GDP this year, although his company forecast growth contracting not nearly as much, to 3.2 percent. While GDP may be in good shape this year, the other triggers of a chip industry downturn: overcapacity, inventory burn and a slow down of electronic system sales, are all in place, McClean, IC Insights president, said.

Electronic system sales peaked last year with 13 percent growth, having seen 10 percent year-over-year growth in 2003, according to IC Insights.

However, by Q3, IC Insights forecast a return to sequential growth for the chip industry. As for 2006, the second year following a cyclical peak, has always been a growth year, McClean noted.

Gartner Inc.'s Dataquest unit is also forecasting that the recovery will begin this year and continue into the next. In fact, while 2005 will still be lackluster for equipment suppliers, sustainable, sequential quarterly growth will return for tool vendors by the end of the year and continue in 2006, said Klaus-Dieter Rinnen, VP of semiconductors at Gartner.

"We believe this downturn will be short and shallow," Rinnen said. He also noted that industry fundamentals are stronger than many realize, according to Dataquest's market data. Device unit growth may have slowed but it doesn't appear to go negative, as the oversupply situation that developed last year was not extreme.

"It's a different situation from what we had in 2000/2001," Rinnen said.

In fact, VLSI Research's Dan Hutcheson suggested that the industry fundamentals are actually in pretty good shape. Revenue measured in terms of square inches of silicon shipped is actually increasing, Hutcheson, VLSI Research's president and CEO. In November of last year, it was at \$41 per square inch, and had been rising since March. While it turned down in December, revenue per square inch typically dips at the end of the year, according to VLSI's data.

Spot prices were flat through the holidays, indicating that the inventory correction has been made. Chip average selling prices are actually beginning to rise now, and there never was a price collapse related to over supply, Hutcheson said. "We're not seeing the classic signs of a downturn," he added.

While VLSI Research does see growth slowing down next year -- Hutcheson characterized it as a flattish year -- it sees chips still growing 8.8 percent last year, while equipment will grow 3.8 percent. They were the only presenters at ISS among the market researchers Tuesday to forecast positive revenue growth for equipment suppliers in 2005.

While the other forecasters were predicting a return to sequential growth for equipment vendors by the end of the year, Moshe Handelsman, president and CEO of Advanced Forecasting, said the industry is still heading down to an inflection point in Q3 of this year. But on the other hand, he said the industry hasn't overheated, and characterized the ensuing downturn as relatively mild.

"It is not as bad as 2001. I don't even believe it will be as bad as 1996," Handelsman said. The slowdown in the equipment market that began toward the end of last year corresponds with IC revenues, he said.