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China SMIC Sees Strong China Chip Market Through 2008

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SAN JOSE -- The head of China's largest contract chipmaker said a projected global downturn in the chip industry is unlikely to affect his company because of fast growth in its domestic market.

"From now to 2008, in China, we don't see any weakening in the market," said Richard Chang, president of Semiconductor Manufacturing International Corp. (SMI) during a speech at the Taiwan + China Semiconductor Industry Outlook 2004 conference in San Jose, California.

He also said that while a glut in older production technology has formed globally, "for advanced technology, we don't see oversupply."

Higher end technology chips normally command better prices for contract chipmakers, which could help mitigate the effect of any downturn in the global chip industry next year.

Chang predicted global chip revenue would likely be flat in 2005. That echoed a Semiconductor Industry Association forecast of 2005 chip revenue remaining at US\$214 billion, after growing a projected 29% to an all-time high this year.

If Chang is right, his company's fast revenue and profit growth could remain on track due to rising demand from China.

SMIC reported a net profit US\$39.3 million on revenue of US\$274.9 million in the third quarter, up from a loss of US\$8.5 million in the year-earlier period, on revenue of US\$107.1 million.

But several analysts warn global semiconductor industry revenue growth could be down slightly in 2005 - partly because too many new factories have been built during a strong 2004, and the excess supply could hurt prices - particularly in computer memory chips.

Memory Chip Segment Could Prove A Drag

The SIA warned the memory chip segment could "be the major factor in dampening industry expansion next year."

The chip industry group projects memory chip market revenue could drop 15% to \$23 billion in 2005 after growing 61% to US\$26.9 billion this year.

That could spell trouble for SMIC, which has invested in an expensive new memory chip plant in Beijing. The plant, a leading-edge 12-inch factory built in partnership with two of the biggest memory chip firms in the world, Germany's Infineon Technologies AG (IFX) and Elpida Memory Inc. (6665.TO) of Japan, began operations just a few months ago.

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But a number of other 12-inch memory chip plants have recently begun turning out new chips, and more are slated to come on line early next year.

Slower chip revenue could hurt SMIC's ability to make good on the new factory. The advanced plants cost as much as US\$2.2 billion fully equipped, and unless SMIC can churn out chips fast, the depreciation costs alone could hurt its balance sheet.

Computer memory chip prices are already falling. The price of the most widely used computer memory chips, 256-megabit double data rate chips that run at 400 megahertz, or DDR-400, closed trading at US\$3.83 each Tuesday, down about 15% over the past month.

The memory chip partnership does have benefits for SMIC, however. It propelled the company to the leading position in China in terms of technology, and positioned it to compete with the leading contract chipmakers.

SMIC has said it will produce chips using the most advanced production technology, 90-nanometer technology for memory chip products as well as other kinds of chips made for mobile phone chip giant Texas Instruments Inc. (TXN).

At the conference Tuesday, Chang said SMIC developed its 90-nanometer technology without help.

"It's in-house technology," he said, adding the company started developing a production process last year using equipment obtained from Dutch Giant ASML Holding NV (ASML).

SMIC Says No Connection With Military

The rapid leap in technology surprised most observers and drew some complaints. The cutting-edge tools necessary for SMIC to produce 90-nanometer chips used to be banned from export to China under international treaties, due to their possible dual-use in producing chips for missiles and other weapons.

But Chang indicated his firm had no trouble obtaining the equipment, and that it wouldn't be used for military purposes.

"As far as the military is concerned, SMIC has no connection," he said.

China's military has "never" tried to contact us, he said. He also welcomed "legitimate agencies to inspect us at any time" to see if SMIC is making chips for military purposes, and added that one fail-safe already in place is the large number of U.S. and Taiwanese workers in SMIC's plants.

"There are so many foreigners in our fabs - too many not to notice" if chips are being made for the Chinese military, he said.

In the past, the U.S. tried to remain three generations ahead of China in production technology, and the far larger 250-nanometer production technology was a perceived limit.

SMIC's 90-nanometer technology leaps across 180-nanometer, 150-nanometer and 130-nanometer sizes to the leading edge - and puts China nearly on par with U.S. chip technology.

Considering SMIC hadn't produced a single semiconductor until 2001, it is moving fast by any measure.

The Cayman Islands-incorporated chipmaker began mass producing semiconductors November 2001. Since then, it has grown at a brisk pace, and could edge out Singapore's Chartered

Semiconductor Manufacturing Ltd. (CHRT) to become the world's third-largest contract chipmaker this year, behind only Taiwan Semiconductor Manufacturing Co. (TSM) and United Microelectronics Corp. (UMC).

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