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Chu: We have to work harder and look for more customers

THE explosion in merger and acquisition (M&A) activity in the global semiconductor industry last year was nothing short of incredible. In the first half of 2015 alone, announced semiconductor acquisition agreements had a combined value of US\$72.6 billion (RM290 billion) (see bar chart), nearly six times the annual average for M&A deals struck during the five previous years.



Singaporean chipmaker Avago Technologies Ltd announced a deal to acquire California-based wireless chipmaker Broadcom Corp for about US\$37 billion — the biggest technology acquisition ever.

Dutch chipmaker NXP Semiconductors NV also announced that it bought Texas-based microchip manufacturer Freescale Semiconductor Inc for US\$11.8 billion (see Table 1).

TABLE 1

Major mergers and acquisitions in 2015				
ANNOUNCED	BEING SOLD OR ACQUISITION TARGET	BUYER	PURCHASE PRICE (US\$ MIL)	TYPE OF TRANSACTION
January	Silicon Image (US)	Lattice (US)	607	cash
February	Lantiq (Germany)	Intel (US)	NA	NA
February	Entropic Communications (US)	MaxLinear (US)	287	cash and stock
March	Freescale (US)	NXP (Netherlands)	11,800	cash and stock
March	Vitesse (US)	Microsemi (US)	389	cash
March	ISSI (US)	Uphill Investment (China)	731	cash
April	Omnivision (US)	Hua Capital (China)	1,900	cash
May	Micrel (US)	Microchip (US)	839	cash and stock
May	Broadcom (US)	Avago (Singapore)	37,000	cash and stock
May	NXP RF power unit (Netherlands)	JAC Capital (China)	1,800	cash
June	Altera (US)	Intel (US)	16,700	cash
June	Cypress touchscreen ICs (US)	Parade Technologies (Taiwan)	100	cash
July	Micron (US)	Tsinghua Unigroup (China)	23,000	cash
July	MACOM automotive unit (US)	Autoliv (Sweden)	100	cash
July	NXP CMOS sensor unit (Netherlands)	AMS (Austria)	NA	NA
September	Atmel (US)	Dialog (UK)	4,600	cash and stock

Other mega M&A last year include German chipmaker Infineon Technologies AG's acquisition of US-based power semiconductor rival International Rectifier Corp for US\$3 billion, and IBM's sale of its microelectronics business to semiconductor foundry GlobalFoundries.

The flurry of deals took place as major semiconductor firms, faced with declining sales, needed to broaden their portfolios to stay in investors' favour.

Calling the 2015 events "a perfect storm", semiconductor market researcher IC Insights in a September 2015 note says, "In addition to the monstrous M&A wave currently taking place, trends such as the lack of any new entry points for start-up IC (integrated circuit) manufacturers, the strong movement to the fab-lite business model and the declining capex (capital expenditure) as a percentage of sales ratio, all promise to dramatically reshape the semiconductor industry landscape over the next five years."

Closer to home, investors are still digesting the impact of the "merger tsunami" on local players. Some quarters believe that with more giants on the global scene, local companies may see more sales orders coming in. However, others worry that the local companies may lose clients with fewer global players in the market.

Basically, Malaysian semiconductor firms are involved in the lower end of the value chain, serving the foreign semiconductor manufacturers, brand owners, IC developers and fabricators. They can be divided into two groups. The first are outsourced semiconductor assembly and test (OSAT) companies such as Unisem (M) Bhd, Globetronics Technology Bhd, Inari Amertron Bhd and Malaysian Pacific Industries Bhd (MPI), which provide outsourced services, including assembly, packaging, fabrication and testing.

The second are test equipment suppliers like JF Technology Bhd, ViTrox Corp Bhd, Aemulus Holdings Bhd, MMS Ventures Bhd and Elsoft Research Bhd, which serve the OSAT companies and other multinational semiconductor manufacturers.

Commenting on the huge wave of semiconductor M&A occurring since last year, JF Technology managing director and CEO Datuk Foong Wei Kuong says he expects more positives than negatives for the local semiconductor players.

"The good news is that our sales orders will grow. For example, some local companies are net positive beneficiaries of [the] Avago-Broadcom [deal] because they indirectly inherit more businesses. Theoretically, if you are dealing with an existing customer and it is acquiring another company, the enlarged entity may increase orders and your customer base will expand," he tells The Edge.

Foong, however, cautions that if the enlarged entity has an excess capacity post-acquisition, its operation may have to be scaled down. In that scenario, the local players may not benefit from the merger. "Bear in mind that industry consolidation is [to achieve] economies of scale, so a lot of duplication work has to be cut," he says.

ACE Market-listed JF Technology is a home-grown high-performance test contacting solution provider whose customers include semiconductor assembly and test service provider Unisem, turnkey packaging and test service provider Carssem (M) Sdn Bhd and integrated circuit test handler supplier SRM Integration (M) Sdn Bhd.

Asked if the semiconductor "merger mania" would translate into higher sales for local firms, Unisem chairman and group managing director John Chia Sin Tet says he has seen the impact already, albeit marginally.

"Some of our customers have amalgamated and we have benefited from them. Basically, yes, I think there are more advantages than disadvantages from the industry consolidation, but it should be noted that there are also M&A that don't work," he says.

Chia, however, acknowledges that the surge in global M&A is generally good for the semiconductor industry and he expects the trend to continue. "Moving forward, there will be a lot of capex requirements and you have to achieve a certain size. The possibility of being marginalised will be there if you remain as a small player," he adds.

ViTrox co-founder and president Chu Jenn Weng says it is important that the players themselves expand their customer base and not be overly reliant on one region, industry or client.

"We have to work harder and look for more customers. We have to make sure that our products are so good that even if our customers are acquired by another company, the acquirer will still buy our products," he says, noting that

ViTrox has yet to see an increase in orders.

Chu, for one, would rather put in more effort, time and resources to develop new products to ensure that ViTrox is well positioned to capture market opportunities.

"After all, M&A activity is all about gaining market share and becoming more competitive. So, if we can remain competitive, we will still have a good chance of being their supplier," he says.

It is worth noting that year to date, ViTrox, Unisem and MMS Ventures are among the local semiconductor stocks with positive total returns. Most are trading at mid-to-high teen price-earnings multiples, Bloomberg data shows.

TABLE 2

Valuation comparison of semiconductor stocks										
COMPANY	MARKET CAP (RM MIL)	PRICE (AUG 18)	CONSENSUS TARGET PRICE (RM)	UPSIDE POTENTIAL (%)	52-WEEK LOW (RM)	52-WEEK HIGH (RM)	P/E (TIMES)	P/B (TIMES)	YIELD (%)	TOTAL RETURN YTD (%)
Inari Amertron Bhd	2947.5	3.08	3.17	2.9	2.33	3.96	19.1	4.5	2.4	-15
Unisem (M) Bhd	1863.9	2.54	2.76	8.7	1.65	2.77	10.8	1.4	4.7	10.2
Malaysia Pacific Industries Bhd	1589.2	7.99	7.95	-0.5	6.12	10.70	9.5	1.6	3	-12.4
ViTrox Corp Bhd	923.0	3.92	3.85	-1.8	2.70	4.00	16.6	4.1	1.8	15.1
Globetronics Technology Bhd	817.5	2.90	3.29	13.4	2.75	6.91	17.6	2.9	4.7	-53.9
Elssoft Research Bhd	334.7	1.85	1.85	0	1.20	2.10	14.7	4	0	0
Aemulus Holdings Bhd	120.7	0.27	0.25	-7.4	0.27	0.62	10.5	1.7	0	-47.1
MMS Ventures Bhd	113.6	0.70	NA	NA	0.45	0.77	13.7	3.2	0	21
JF Technology Bhd	69.3	0.55	NA	NA	0.53	0.86	39.9	2.9	0	-28.9

<http://www.theedgemarkets.com/my/article/facing-challenges-semiconductor-merger-mania?type=Corporate>