ALTR-INTC Bombshell, MU Leaves Italy

Altera *(ALTR, $35.01 -0.34, Rated 'Not Compelling/Hold' on my latest Chip Investment Ideas)*
Using Intel as FGPA Foundry: ALTR announced after the close yesterday that it will be using Intel to manufacture next-generation FPGAs in advanced 14nm FinFET/3D transistor technology—but that it will also continue to partner with TSMC as it has for the last 20 years. I am a huge fan of ALTR the company, but apparently so are many other investors given its persistently less-than-favorable fundamental valuation, in my opinion.

In the near-term I consider this good news for ALTR and INTC at the expense of XLNX and TSMC, respectively: ALTR gets to leap-frog XLNX in their highly-competitive FPGA arena after a period of time when XLNX has been exercising bragging rights on 28nm ad nausea; and INTC gets to poke TSMC in the eye and encroach established business from a very-long-time customer due to its technology advantage.

However, longer-term I predict the ALTR-INTC relationship will likely prove to be a disappointment that ultimately does NOT prove to be any kind of significant competitive change for either ALTR or XLNX in the FPGA market nor TSMC or INTC in the wafer foundry market. Why? Because ultimately INTC's cost and margin structure and lack of customer sensitivity and flexibility will severely limit the scope of its supplier relationship with ALTR: at best it will plateau at a fairly insignificant level; and at worst it will deteriorate to hostilities and lawsuits. Not only will INTC be trying to compete with the biggest and best-est wafer foundry in the history of mankind, but it will doing that trying to satisfy the most established and loyal foundry customer in the history of the semiconductor industry (okay I'm exaggerating, but not . . . by . . . much). INTC is doomed, and I believe the best it can hope for is to learn how to be a foundry and not completely alienate itself from ALTR in the process. INTC will only make ALTR appreciate TSMC as a trusted and capable and loyal supplier even more than it already does—and I think TSMC knows it, as evidenced by the CEO quote in its counter-balancing press release.

The only mitigating factor in this case is that I give credit to ALTR for being aware of what kind of goo it may be stepping into, so it is hopefully keeping its expectations to a fairly low level which would basically entail the use of INTC for early-product-revision prototype quantities for however many months it takes for TSMC to catch-up to INTC's technology and deliver production quantities. Given new product gestation times for bleeding-edge technology offerings can easily extend a couple of years, ALTR's supplier-arbitration strategy might just work—at least for a while. ALTR will pay INTC's premium to buy time because it might be worth it, but not for volume since it probably won't be, in my opinion.

Micron *(MU, $7.93 -0.09, Buy, Target $15, FY13: ($0.74) on $7,887M, FY14: $0.67 on $9,175M)*
Sells Italian Fab: MU is off-loading its older 8-inch wafer fab in Avezzano, Italy to a German group called LFoundry for an undisclosed amount. This fab manufactures CMOS image sensors for MU-spin-out Aptina: MU owns just under 30% of Aptina and has been supporting it with $372M-worth of product at just around cost during FY12, although last quarter revenue dropped to $61M from $80M before that. I consider disposal of this albatross as good news for MU and remain positive on the shares primarily due to recent DRAM market price strength and its pending acquisition of DRAM competitor Elpida.

—Dan K. Scovel
Semiconductor Analyst

Tokeneke Research LLC
Rowayton, CT 06853
dscovel@tokenekeresearch.com
www.tokenekeresearch.com
203-554-4621

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