



Can We See the Light at the End of the Tunnel?

by Stephen Brennan

A big question on almost everyone's mind is how the September 11 terrorist attacks will change our world. When you're talking about the world of semiconductors, there are few specific impacts, but a very big general fallout. Even if defense and video conferencing grow and commercial aviation shrinks, semiconductors are so widespread that they don't stand to benefit from the ups or downs of any one economic sector. So the real question is: What will the impact be on the overall global economy and what does this mean for the fortunes of our industry?

UNHAPPY HOLIDAYS FOR CONSUMER ELECTRONICS

Prospects look pretty dismal at the moment for high-tech Christmas holiday sales. Whether you're talking PCs, cell phones or PDAs, there is little reason to expect strong sales. With new game systems hitting the market, these units may be the exception. Game systems, however, are simply not a large enough market to have a material impact on the semiconductor industry. The rising unemployment picture and lowering of consumer confidence do not bode well for the critical holiday season. Although generally misreported by the media, both gauges recorded huge drops prior to the impact of the attacks. In other words, we were already headed into a recession. Terrorist attacks, however, certainly do not help matters in the short term.

The recent huge layoffs in the aviation, tourism and hospitality sectors, for example, and the damage to confidence that goes beyond mere consumerism will, if anything, make this Christmas season worse than previously expected. In the third calendar quarter a lot of executives stated our industry was bouncing along a bottom. The expectation was that we would rise from it. Now, with debt-strapped corporations in no mood to spend, retreating consumer spending means we've likely started the final leg down to a real bottom. The good news is that Christmas will probably see a lot of bargains both on the retail racks and in the stock market. I expect that once the December pre-announcement season kicks in, we will see a rash of tax-loss selling that will drop equity stocks, including semiconductor stocks, to true bargain levels.

WHAT'S THE TIMING FOR THE UPTURN?

The big question remains the timing of the upturn. I'm going way out on a limb to say we'll see it in the third calendar quarter of 2002. But I fully expect the overall environment and consumer sentiment to worsen considerably before that point. In fact, I believe that when the upturn arrives, few will initially see it coming. So why expect a recovery in Q3 of 2002? The attack gave politicians and bureaucrats the political cover to take actions they should have taken already. The European Central Bank is now in a monetary easing mode, after stubbornly believing Europe could buck the negative global trends around the world. Japan looks to be finally enacting real banking reform. In the U.S., the mythical social security lockbox has been forgotten. Along with monetary easing that was not working by itself, we also are now pursuing expansionary fiscal policy.

Fiscal, monetary and regulatory actions all will take a while to have an impact. One should expect at least a six-month lag before the benefits of these stimuli packages are felt. "Because of this time lag, the stock market typically runs about six months ahead of the economy. Remember that semiconductor stocks began to slide in the second half of 2000, even as orders soared. Savvy investors could see the signs of the end: in the series of Fed rate hikes that began in September 1999, an inverted yield curve in 2000, a spike in oil prices during the winter at a level that proceeded eight of the last nine recessions, and the Fed's moves in early 2000 to dry up an oversupply of liquidity they created in Q4 1999 to fight a Y2K crisis that never materialized. Back then you could see the coming storm, even as the environment rose to heights no one imagined. Today, you can see the light at the end of the tunnel, even as the surroundings get darker. ■

About the Author

Stephen Brennan is an investor relations consultant with MCA, a leading Silicon Valley public relations firm. He may be reached at sbrennan@mcapr.com.