

**July is Strong, but 3Q Guidance is Soft
Risk Remains to the Downside**

The semiconductor industry continues to grow, but 3Q guidance is soft and sector share prices beat a retreat last month. While I have turned more cautious, I continue to recommend that investors pick individual stocks rather than trying to capture thematic trends in the current environment. Specifically, stocks with both favorable business situations and highly attractive share price valuation fundamentals to mitigate any potential downside risk.

July Strength: This year’s July up-tick was more pronounced than usual. Chip industry statistics for world-wide sales released by the Semiconductor Industry Association (SIA) reflected a three-month rolling average gain of +2.6% compared to average growth of +1.2% with a high of +5.4%, a low of -6.3%, and declines only five times over the last 23 years—including both of the last two. Japan rebounded to +7.9% after lagging with a decline the prior month, followed by The Americas with growth of +5.4%, Asia-Pacific at +1.2% and Europe at +0.3%.

Next month’s release of August data usually betters that of July. It has averaged a gain of +1.8% with a high of +5.2%, a low of -3.5%, and has declined only four times in the last 23 years—none in the last 11 years.

Weak 3Q Outlook: The 3Q outlook for growth is well below average based on management guidance during 2Q earnings season. The Tokeneke Universe is anticipating 3Q growth around +4% compared to the historical average just over +6%. Specifically, the weighted average based on management guidance during 2Q earnings season calls for growth of +4.4% with a range of +1.2% to +7.5%, while the average since 1990 is +6.3% with a high of +19.9%, a low of -11.7%, and has been negative only twice in 23 years.

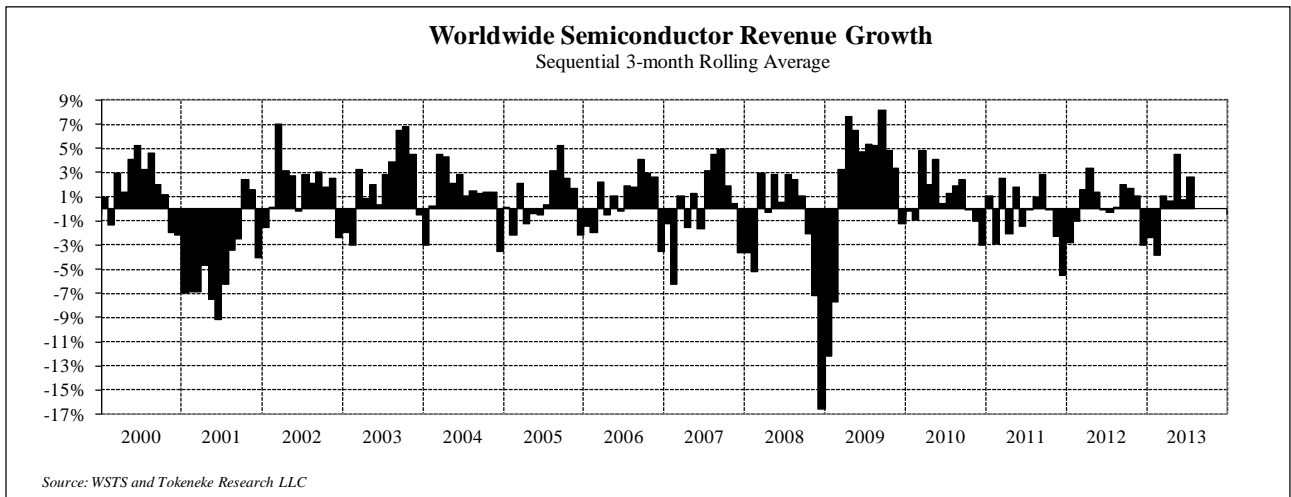
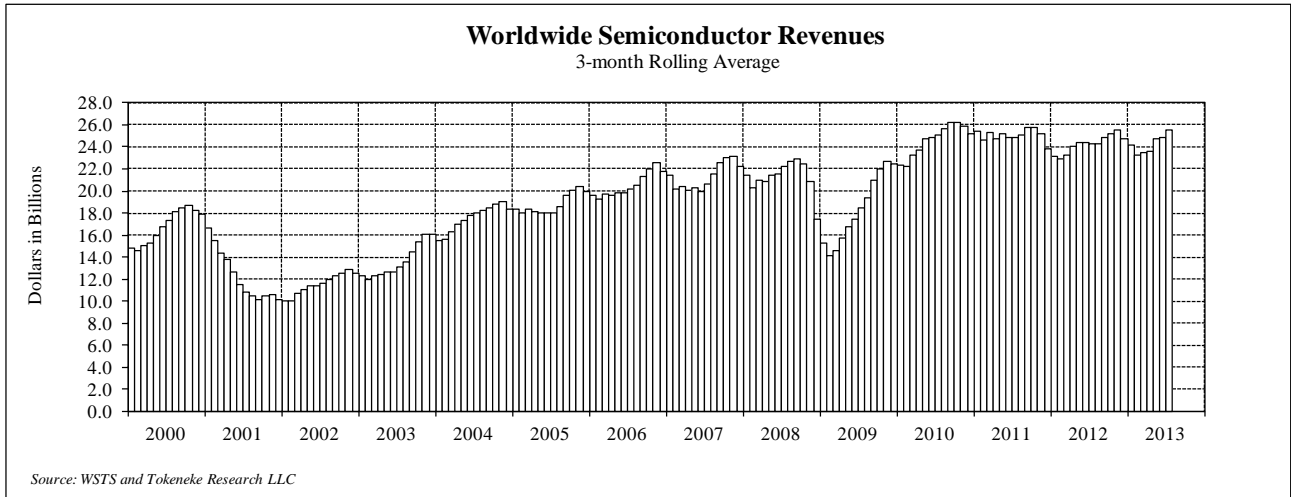
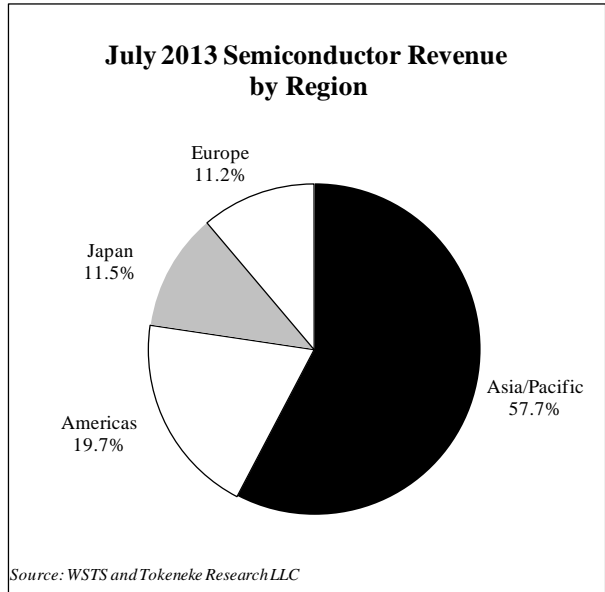
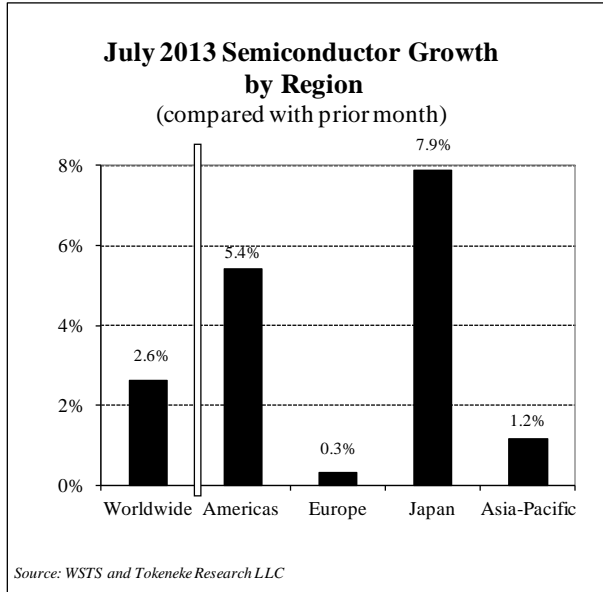
As I noted the last two months: the worldwide economy remains fragile; PC markets have deteriorated off of no-growth expectations; consumer markets are being cannibalized by smartphones (think digital cameras); and higher-growth expectations for both China (in general) and smartphones and tablets (in particular) have tempered. I expect 3Q sequential growth across the semiconductor industry to be supported by new video game platforms, continued strength from automotive and industrial markets, persistent inertia from smartphones and tablets, and possible incremental gains from communication infrastructure and PCs. Unfortunately it appears growth may fall short of seasonal norms largely due to weak macroeconomics and PC markets. Also, recall that most market researchers expect chip industry annual revenue growth in the low- to mid-single digit percentages.

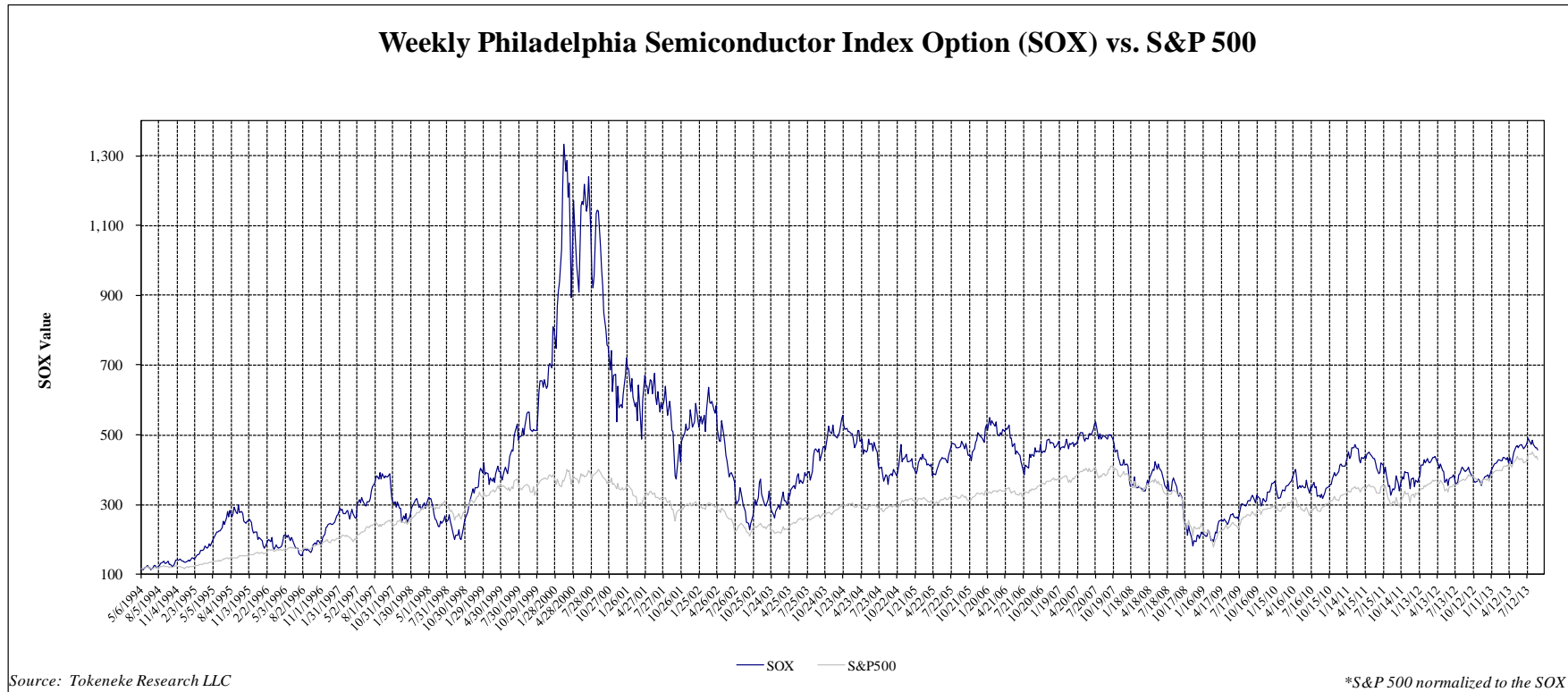
Share Prices Retreat: Semiconductor sector stocks both declined and underperformed broader equity markets during August. The Philadelphia Semiconductor Index Option (SOX) declined by -4.2% last month and the average stock in the Tokeneke Universe dropped by an even-worse -4.7% with only 25 out of 101 advancing. This compares to broader equity market softening in the NASDAQ, S&P500 and DOW of -1.0%, -3.1%, and -4.4%, respectively. Nevertheless, year-to-date the chip sector continues to outperform—albeit by a lesser margin: the SOX is up by +19.2% with the average stock in my Universe up by a similar +18.0% with 75 posting gains, compared to those same three indices with gains of +18.9%, +14.5% and +13.0%, respectively.

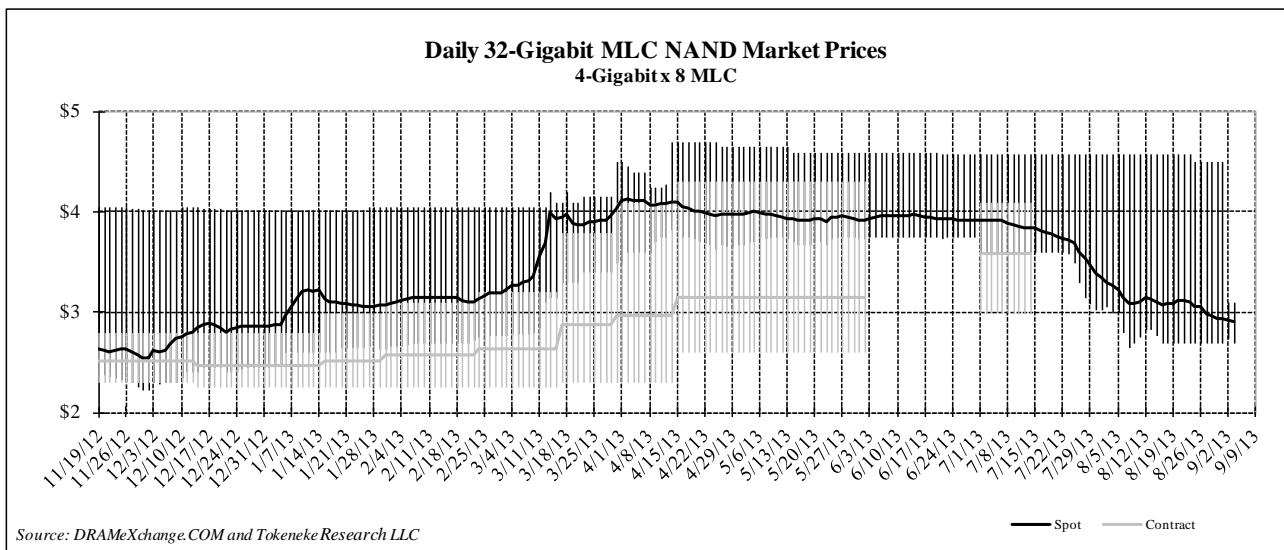
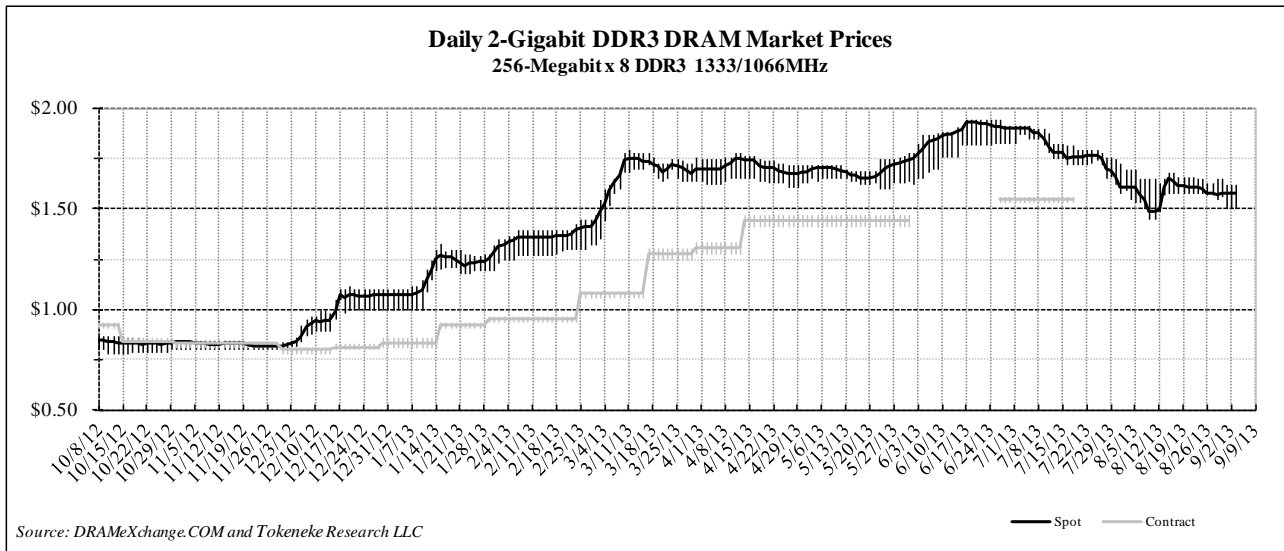
August		QTD (3Q)		YTD		Indices			
Winners (25/101)	Losers	Winners (51/101)	Losers	Winners (75/101)	Losers	Aug	QTD	YTD	
VLTR 52.1%	TXCC -42.3%	VLTR 62.6%	TXCC -31.1%	SPWR 282.4%	TXCC -59.3%	SOX	-4.2%	-2.3%	19.2%
MXL 21.5%	NPTN -27.1%	ISIL 32.9%	NPTN -26.4%	HIMX 152.9%	TSEM -46.3%	SMH	-3.7%	-1.5%	14.9%
MPWR 17.0%	SPWR -22.3%	SQNS 31.8%	BRCM -25.3%	MU 114.0%	GIG -42.3%	NASDAQ	-1.0%	5.5%	18.9%
CRUS 16.7%	IXYS -17.5%	CRUS 29.6%	DSPG -23.6%	SPRD 71.7%	MLNX -33.6%	S&P500	-3.1%	1.7%	14.5%
NXPI 13.8%	GIG -17.1%	POWI 28.5%	ADNC -20.8%	MXL 67.7%	MSPD -33.5%	DOW	-4.4%	-0.7%	13.0%
average stock -4.7%	SOX -4.2%	average stock +0.4%	SOX -2.3%	average stock +18.0%	SOX +19.2%				

Pick Stocks: The semiconductor industry continues to grow and the sector’s share prices have performed well so far this year, but growth is slowing and the rally appears to have rolled-over. The risk-reward trade-off has shifted unfavorably, in my opinion, although specific investment opportunities remain attractive as noted in my latest Chip Investment Ideas publication. I continue to recommend stocks with pronounced attractive fundamental valuations to mitigate potential downside risk—but only so much as discomfort will allow for your particular situation.

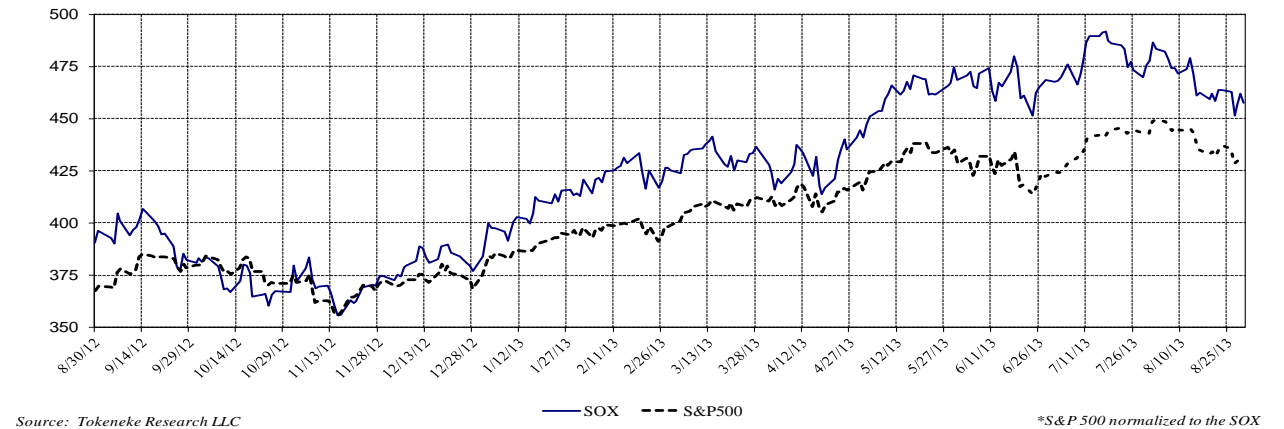
—Dan K. Scovel
Semiconductor Analyst







Daily Philadelphia Semiconductor Index Option (SOX) vs. S&P500 Daily Close, Trailing 12-months



The Company

Tokeneke Research is an independent research firm specializing in semiconductor industry business issues, providing fundamental research focused on US equities across all market capitalizations within the sector to investors. The company was founded in 2005 and is based in Connecticut.

The Offering

- *Monthly Newsletter:* A summarized review of noteworthy industry business developments, sales statistics, and sector equity market performance, as well as a near-term and annual outlook for sector business fundamentals and share prices. This report typically includes two pages of text and a handful of recurring charts and tables. It is intended for relatively broad-based distribution.
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My Background

I have an electrical engineering background, nearly 12 years of semiconductor industry experience, and was on Wall Street for nearly eight years where I was selected as the Best On The Street semiconductor analyst for 2002 by The Wall Street Journal, and third-rated Best of the Best across all sectors.

I obtained my undergraduate BS degree in electrical engineering from the University of Washington, and my MBA from Santa Clara University. My industry experience consists of nearly 12 years in various technical sales and marketing roles at four different semiconductor firms located in Silicon Valley beginning with Advanced Micro Devices in 1984, followed by two small start-up companies, and ending at Cirrus Logic where I supported the firm's Japanese market development. I joined Fahnstock & Co. as a senior semiconductor analyst in 1996 and was recruited by Needham & Co. in April 2000.

My formal coverage list as a sell-side analyst included the following equities: AMD, ALSC, ALTR, ARTI, ATML, CUBE, CY, ESST, GNSS, INTC, ISSI, LSI, MOSY, MU, OIIM, OVTI, RMTR, SIII, SMSC, STEC, SVTG, TDFX, TSRA, TXN, and ZRAN.

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