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## Price war appears inevitable between Intel and AMD

Jack Robertson  
 (04/20/2001 1:57 PM EDT)  
 URL: <http://www.eetimes.com/showArticle.jhtml?articleID=2911729>

Rivals on several fronts, Intel Corp. and Advanced Micro Devices Inc. are partners in financial pain.

And with neither company clear on whether the PC market is nearing recovery, another heated pricing war looks likely as AMD tries to wrest market share away from its much larger competitor.

AMD chairman and chief executive Jerry Sanders fairly gloated this week as he reported that first-quarter sales held steady with the previous period, compared with Intel's 23% sequential drop in quarterly revenue.

Touting the desktop Athlon and upcoming successor, the Palomino, which is launching this quarter initially for notebook PCs, Sanders said AMD is prepared to go head-to-head with its rival on processor pricing.

"We'll buttress ourselves against any foolish moves by our competitor. We'll match them [in price] clock cycle by clock cycle," he said.

Although both are banking on new-generation processors as a buffer against stormy business conditions, the promise of a price war between the two could end up in steeply eroded margins, analysts said.

Though choosing to blame weak overall demand over pricing competition, Intel said its gross margin could drop another 3 percentage points, to 49%, in the current period, after nose-diving to 51.7% last quarter from 63% at the end of last year.

Citing a "lack of visibility" concerning the current quarter's sales, Intel chief financial officer Andy Bryant said revenue could range from a 7% drop, to \$6.2 billion, to a slight gain over last quarter's \$6.68 billion.

AMD did not report earnings estimates, but said second-quarter revenue will be anywhere from flat to down 10%, from \$1.19 billion in the first quarter.

Key to the immediate financial fate of both companies are second-quarter microprocessor sales.

Although it didn't confirm analysts' projections of a 50% price cut, Intel acknowledged this month that it will slash Pentium 4 tags to propel the new processor into the market, a move that will likely be met by similar cuts from AMD.

Intel is also said to be struggling to deliver its 1GHz Pentium III processors for notebook PCs in any volume, with shipments delayed up to a month or more. Analysts said the company's 933MHz Pentium III will hold the fort as it is still considerably faster than anything AMD offers in the notebook market.

"The really savvy consumer might [notice the speed difference]," said Dean McCarron, an analyst at Mercury Research Inc., Scottsdale, Ariz. "There are certain applications where you would. If you're playing a demanding action game or working with video, you might notice a slight difference."

AMD's first-quarter net earnings of \$124.8 million dropped 30% sequentially and 34% year over year. The company increased its share of processor unit shipments to 21%, from 17% in the previous period, Sanders said.

AMD is "on plan" to continue increasing its processor market share, but is unlikely to reach its previously announced goal of 30% by year's end, he added.

Athlon chips will continue to be made on Fab 25's aluminum interconnect line in Austin, Texas, Sanders said. As Athlon migrates to higher frequencies requiring copper interconnects, production will be centered at Fab 30 in Dresden, Germany, which will be operating at 100% capacity by year's end.

AMD will shrink top-end processor dice by starting 0.13-micron production in Dresden in the fourth quarter. The company plans to convert the Austin fab to flash memory, which is now made solely in Japan via a joint venture with Fujitsu Ltd., Sanders said.

AMD said it is holding to its previously announced \$1 billion capital spending plan, up \$200 million from last year. More than half the budget is earmarked for expanding capacity in Dresden and transitioning to 0.13 micron.

AMD and Intel both conceded that flash memory chip sales will remain down. AMD, which is suing flash customer Alcatel for breach of contract, said it has no such problems with its other 25 long-term flash contracts.

At Intel, where first-quarter net earnings of \$485 million represented a drop of 82% year over year and 78% sequentially, the company also is maintaining its capital spending schedule. Intel will allocate \$7.5 billion to capital improvements this year, and spent \$2.6 billion in the first quarter, according to Bryant.

During last week's conference call, Bryant said he saw no quick market turnaround that would resurrect Intel's networking and communications businesses. The company disclosed that these, along with all other non-PC-related business, suffered a \$1.06 billion operating loss in the first quarter.

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