More deals ahead? China fund buys Silicon Valley chip maker

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China's aggressive new policy to expand its semiconductor industry is worrying U.S. chipmakers, many of which are based in Silicon Valley, and raising potential national security concerns as it begins to acquire U.S. tech companies.

The world's largest market for integrated circuits, China is expected to spend up to $100 billion on both domestic investments and acquisitions abroad to grow its semiconductor industry by more than 20 percent annually over the next five years.

"Clearly their ambition is to transition from being a technology follower to a leader," said Jonathan Davis, vice president of the semiconductor equipment maker trade group SEMI.

The Chinese growth plan, which was announced last year and is still unfolding, comes from a country awash in money and looking to grow its own information technology industry from the bottom up, experts say.

"The goal is total control end-to-end on their technology - hardware and software," said semiconductor industry analyst Pat Moorhead of Moor Insights and Strategy in Austin, Texas.

In one of the first signs of its interest, a new Chinese investment group with connections to the government made a $1.64 billion offer in September to buy OmniVision Technologies of Santa Clara. The company has about 30 percent of the market for digital image sensors.

Little has been heard about the deal since then, prompting speculation it may have run into trouble with the secretive interagency Committee on Foreign Investment in the U.S. That panel reviews foreign acquisitions of U.S. tech companies for competitive and national security concerns, and OmniVision's image sensors, which can be use for surveillance and security systems, may have caught its attention. A spokesman for the agency said it does not comment on "specific cases."

Then in March, a Chinese consortium led by investment funds in Shanghai and Beijing offered to buy Milpitas-based Integrated Silicon Solution Inc., or ISSI, for $639 million. ISSI designs and sells specialty memory chips globally, including to U.S. companies that supply the aerospace industry and military. The deal is still pending and likely will be reviewed by the foreign investment panel.

The OmniVision offer may have been shelved when the political landscape wasn't shaping up favorably for the deal, said China expert Derek Scissors, who noted that it would have taken place as U.S. presidential campaigning heated up.

"I read the ISSI deal as a substitute for OmniVision," said Scissors, who is at the American Enterprise Institute in Washington, D.C. "If they get pushback, they will try something else."

Because it is much smaller than OmniVision, the acquisition of ISSI is less likely to stir opposition, he said.

ISSI declined to comment, and the investment group did not respond to a request for comment.

China's sweeping plans have American semiconductor makers wondering how they'll fit in.

"The (Chinese) government has decided to spend literally billions of dollars trying to level the playing field a bit" between the U.S. and China, said Orville Schell, director of U.S.-China relations for the Asia Society, which commissioned a study of China's high-tech investments in the U.S. "I think the American semiconductor industry is torn between resisting Chinese intrusion into this field and buying into it."

Even at its most ambitious, the plan will not make China a dominant player internationally, and America will still have a leading role in the industry. Semiconductors are the third-largest U.S. export behind airplanes and automobiles, according to the Semiconductor Industry Association.

Association president John Neuffer said in a statement that his group hopes China's plan doesn't prevent foreign semiconductor companies from competing there on equal terms.

The scope of the program is new, but China has long invested in the U.S., particularly California. The study commissioned by the Asia Society found that the Golden State has been "by far the most important recipient" of Chinese high-tech investment, both in the number of deals - 148 since 2000 - and in value - $1.82 billion, with the Bay Area accounting for 40 percent of the investments. The goal often was "to gain a long-term foothold" in the U.S., or to develop markets in the U.S., rather than to pack a company up and ship it to China.

Last year Lenovo paid $2.1 billion for IBM's server business and paid $2.91 billion to Google for Motorola Mobility. Earlier, Lenovo also took a run at buying smartphone maker Blackberry, but the Canadian government reportedly stopped it on national security concerns.

Security concerns have also squelched a number of past Chinese attempts to buy U.S. tech companies. In 2011, the Committee on

Foreign Investment in the U.S. forced Chinese telecom giant Huawei to drop the acquisition of some assets from bankrupt Silicon Valley cloud computing startup 3Leaf.

"They're jump-starting what they already have with acquisitions of what they consider to be strategic technologies," said Craig Ellis, an analyst with B. Riley.

Despite the valley's concerns, some companies here are finding ways to work with the Chinese on their chip efforts. Beijing-based Tsinghua Unigroup, a subsidiary of a state-owned fund, recently bought Chinese chipmakers Spreadtrum Communications and RDA Electronics. Intel is investing $1.5 billion in Tsinghua and Spreadtrum will sell a family of Intel chips for smartphones, then design its own chips based on that architecture. Both companies will sell those chips.

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