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INDUSTRY TRENDS

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Analysis of Hewlett-Packard's First Quarter FY06 Results

Recovery Continues

HP Reports Another Solid Quarter on Its Road to Recovery

SCOTTSDALE, Feb 15 - Hewlett-Packard (HP) reported another solid quarter after the markets closed today, sending the stock up nearly four points in after-hours trading to new six-year highs. Earlier today, HP shares declined 2.5 points in regular trading ahead of its first quarter fiscal year 2006 earnings release. But the actual results showed that the recovery under the leadership of Mark Hurd, who took over as HP CEO last April, is clearly continuing unabated.

HEWLETT-PACKARD CO
as of 14-Feb-2006

New 6-yr record



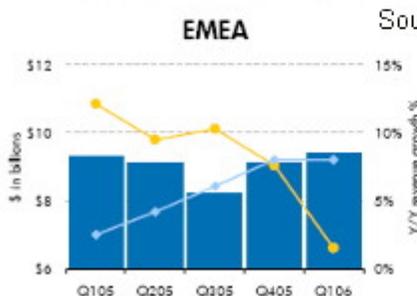
HP stock surges 4% in after-hours trading on better-than-expected 1Q06

The main reason for the upsurge in the HP stock price was a better-than-expected EPS number (48 cents per share vs. 44 cents per share Wall Street analysts had forecast). That is a 30% jump from the corresponding quarter a year ago, Carly Fiorina's last.

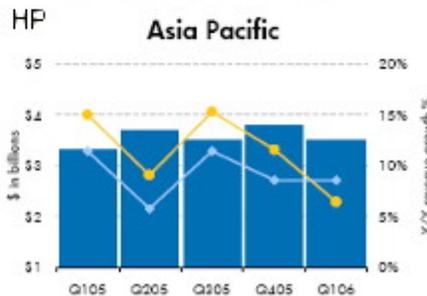
"Which means we are on track, and the results are showing up both in our top line and in our margins," said Mark Hurd, HP's CEO, in a post-release teleconference with analysts. "However, we know we have more work to do, and we know we can do better," he added.

Business Segment Analysis

Regional revenue trends



Source: HP



Geographies. Worldwide revenues were up 6% (up 8% in constant currency), with North America leading the world with a 10% increase to \$9.7 billion. Asia/Pacific also showed respectable growth (up 6% to \$3.5 billion), while Europe grew only 1% to \$9.4 billion. Sequentially, however, Europe was the only region to grow in the last two quarters, with Eastern Europe leading the way, while Western Europe continued to be sluggish.

But it was the "emerging markets" that showed the best growth. "China and India were exceptionally strong," said Hurd. "China is no longer an 'emerging market'; it has emerged," he added with a great deal of emphasis on the last verb.

Foreign currency translations wiped out between two and three points of the growth. It is a trend that the company's CFO, Bob Wayman, expects to continue in the near future, such as in the current quarter.

In summary, however, Hurd characterized the overall global demand as "pretty steady."

Product Lines. Among the HP product lines, the Imaging and Printing Group, which accounts for the biggest share of the company's overall earnings, reported an 8% increase in revenues (to \$6.5 billion). Operating profit rose from \$932 million to \$973 million, a 14.9% margin. By contrast, rival Lexmark last month posted a 47% drop in profit, hurt by tough price competition.

Revenue in HP's PC group also rose 8% from the year-earlier quarter to \$7.4 billion, as unit shipments of PCs and notebooks climbed 16%. Just as important for HP shareholders, the PC operating margins jumped from 2.1% a year ago to 3.9%.

In the Enterprise Storage and Servers Group, revenue increased 5% to \$4.2 billion. Operating profit was \$326 million, a 7.7% margin, up from 1.7% a year ago.

The only HP product line to show a decline in revenue was HP Services. Revenues dropped 2% to \$3.8 billion, although they rose 3% in constant currency. Hurd explained the decline the unit was focusing on improving its profitability. Indeed, operating margins rose from 7.4% to 7.8%. Hurd said his goal was to see the HPS operating margins closer to 10% in the future on a 4% to 6% revenue growth.

Outlook

So things are evidently improving across the HP product lines and in most geographies. Looking ahead, the company expects full fiscal year 2006 revenues to be in the \$90 billion to \$91 billion range, with net earnings of \$1.90 to \$1.95 per share. Which is higher than the \$1.83 per share average that Wall Street expected prior to today's release.

The turnaround is evidently continuing, and with it, the HP stock keeps moving up.

Happy bargain hunting!

Bob Djurdjevic

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