ANNEX BULLETIN

Annex Bulletin 2010-04 **February 18, 2010**

A partially OPEN edition

INDUSTRY TRENDS

Updated 2/18/10, 2:30PM HST

Analysis of HP's and Capgemini's Latest Quarterly Results

HP, Capgemini Send Mixed Signals...

...Get Mixed Reactions; Investors Move in Contrarian Ways; HP Rebounds, Capgemini Tries to Stem Tide

HAIKU, Maui, Feb 18 – Within hours of each other, two leading global IT companies sent diametrically opposite messages to investors, who returned the favor with diametrically opposite reactions. After the markets closed last night, HP reported better-than-expected results in its first quarter of fiscal year 2010. Revenues were up 8% while net earnings rose 28%.

Before the markets opened in Europe, still the same day here in Hawaii (Feb 17), Capgemini published its fourth quarter figures. Revenues and profits were both down since a year ago, with earnings declining in double digits (the net was down 39%, while revenues dropped 4%).

So you'd think the investors would cheer HP and punish Capgemini? Think again. Wall Street and Paris Bourse returned the favor by reacting to the two IT news releases in contrarian ways. By mid-morning, the HP stock barely nudged upward (it was up 0.6%) while Capgemini shares soared 6%, after the Paris investors overcame their early jitters and saw blue skies ahead for the French company (see above charts).

HP Rebounds

Recent...

HEADLINES

Big Blue Poised for Growth Again - "State of the Union"-type analysis of IBM performance

Rally of Hope over Fact Continues - Analysis of Top IT Cos 2009 performances

Broken Windows, Broken Promises - "State of the Union"-type analysis of current PC/Windows quality

A Shrinking Giant - Analysis of HP's fourth fiscal quarter business results

IBM Stock Takes a Beating *(Analysis of IBM's third quarter business results)*

Obama's "Don Quixote" Swings and Misses *(Analysis of DoJ's latest antitrust investigation of IBM)*

Triple Trouble Hits Armonk *(Analysis of insider trading charges against a senior IBM executive)*

A Rally of Hope over Fact - Analysis of Top 18 IT companies' performances

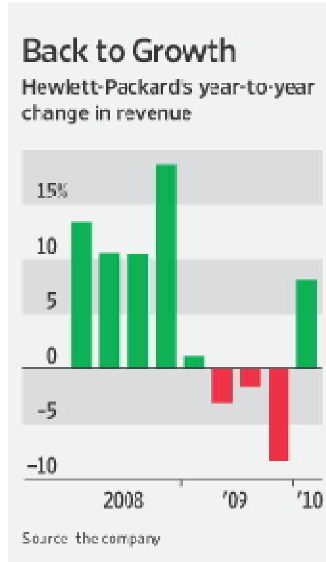
Tempest in a Tea Pot *(Analysis of latest IT services industry M&A's)*

Less Than Meets the Eye - Analysis of HP's 3QFY09 results

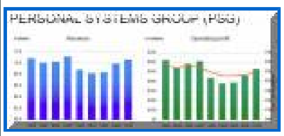
Big Blue Blows Lid Off Forecasts - Analysis of IBM's 2Q09 results

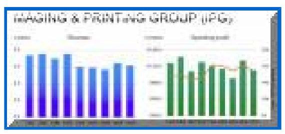
Apple, Google Lead

The latest HP results signaled a rebound in most of its product lines. This was the first quarter of growth after three consecutive declines (see the right chart).



What made the biggest difference in its first fiscal quarter of 2010, which ended Jan 31, was a 20% revenue upsurge in its PC business. And that, it turn, was driven mostly by the strong demand for Microsoft's new Windows 7 and the seasonal Christmas shopping season (for relative merits of the former, see Broken Windows, Broken Promises a "State of the Union"-type analysis of PC/Windows quality, with this writer's personal experiences with Windows 7 and HP PCs).





The Windows 7 quality and the longevity of this demand notwithstanding, HP's PC division did shine in the quarter. Its worldwide PC unit shipments jumped 26% in its quarter. The "standard servers" (Intel/Windows-based) business grew even faster, soaring by 27% since a year ago. Revenues of IPG (Imaging & Printing Group), HP's most profitable unit, the , also bounced back, rising 4% in the quarter. Commercial printer unit sales were up 11% and consumer shipments rose 18%.

All this prompted Mark Hurd, HP CEO, to claim on the conference call with analysts that the company gained share in the PC, server and printer markets during the quarter. In a sign of confidence, HP also boosted its fiscal-year revenue goal to a range of $121.5 billion to $122.5 billion, up from an earlier prediction of $118 billion to $119 billion.

Thanks to stabilizing prices, the company also managed to keep the PC profit margins steady at 5% of revenues, Cathe Lesjak, the CFO, told the analysts. The server margins jumped 2.3 points to 12.6% of revenue, while the profitability of the printer division declined from 18.5% a year ago, to 17% in the latest quarter.

Services Revenues Down, But Profits Improve

Predictably, the results of HP's services unit, which the company executives hailed as their brightest star in 2009, declined 1% to $8.7 billion in the latest quarter. It was the first full three-month period since HP acquired EDS in late August of 2008 that the company reported quarterly results on an apples-to-apples basis. We say "predictably," because that's what we

Comeback - Analysis of Top IT Cos' stock & business performances

Revenues, Earnings Drop - Analysis of Accenture's 3QFY09 business results

IBM Wins the "Gold" - Analysis of IT Services Octathlon 2009 results

Suddenly, All Lines Point South - Analysis of HP's 2Q09 business results

Back on Growth Track - Analysis of IBM Global Services 2008 results

Sometimes Less Is More and Down Is Up - Analysis of IBM's 1Q business results

IBM's Holistic Approach - Treating businesses like living organisms - secret of success

IBM Tries to Pull Dow, HP Up - Big Blue stock up sharply after CFO remarks at investor conf

Hurd's First Stumble - HP's 1Q09 revenues, earnings disappoint Wall Street

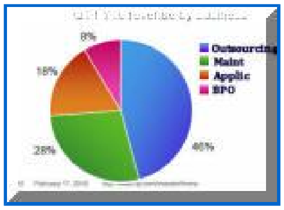
Two Thumbs Up for Big Blue - Analysis of IBM 4Q08 business results

Big Blue: All Heart - IBM creating new jobs in American Heartland

When You Catch a Tiger by the Tail... - An editorial about greed & success

Squeezing the Consumer Dry *(Greed fueled both bankers & oilmen's try to squeeze blood out of stone - consumer)* forecast six and nine months ago:

"The HP stock price drop might have been much steeper had Wall Street and the investing public really dug a little deeper into that alleged 93% surge in its services revenues, and an equally as "impressive" spurt in the related profit margins," we said in Aug 2009 (see Less Than Meets the Eye, Suddenly, All Lines Point South, and Hurd's First Stumble for our last three HP quarterly reports).



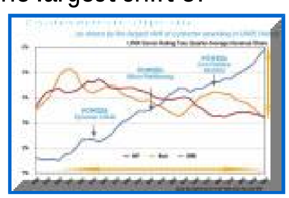
But HP's operating profit improved to 15.8% of revenue, up from 12.9% of revenue in the prior-year period. Clearly, the steep cost cuts that followed the EDS acquisition are paying off.

Meanwhile, outsourcing revenue increased 2% to $3.9 billion. Technology Services revenue decreased 2% to $2.4 billion. Application Services posted revenue of $1.5 billion and BPO business was $734 million, down 8% and 3%, respectively.

Unix Servers Decline

Meanwhile, what HP did not dwell on was the fact that its "Business Critical" (Unix) servers' revenue declined 22% in the quarter. There is but one main reason for it - IBM. "One man's loss is another man's gain," goes an old saw. That became evident earlier this month when Big Blue released its new Power 7 (Unix) processors.

The company released the charts that showed what IBM called "the largest shift of customer spending in UNIX history." The data showed massive migrations from HP and Sun to IBM Unix solutions. In the fourth quarter alone, there were nearly 200 competitive flights into the Big Blue fold; over 500 during 2009. There have been over 2,100 such migrations in the last five years, with 90% of from the Sun and HP customer bases (see the chart).



As a result, even before the Power 7 announcement, IBM has been gaining share in this market. After the latest technological boost, its System p products are likely to experience another spurt this year. Which means that competitive pressures on HP are only going to increase for the balance of 2010.

Outlook

For the second quarter of fiscal 2010, HP expects revenue of approximately $29.4 billion to $29.7 billion, GAAP diluted EPS in the range of $0.89 to $0.91, and non-GAAP diluted EPS in the range of $1.03 to $1.05.

HP expects full year fiscal 2010 GAAP diluted EPS to be in the range of $3.79 to $3.86, up

The Year of Living Dangerously - Analysis of global investment trends from its previous estimate of $3.65 to $3.75.

These estimates for both the second quarter and full year fiscal 2010 do not reflect the potential impact of the proposed acquisition of 3Com Corporation that HP announced on Nov 11, 2009.

Capgemini Tries to Stem Tide

By contrast to HP's rebound and the accompanying optimistic executive statements, Capgemini has been struggling to stem the demand tide which put pressure on its revenue and profits. For the full year, revenues were €8.4 billion (about $11.4 billion), down 4% from €8.7 billion in 2008. The drop in demand was particularly discernible in the second half of 2009.

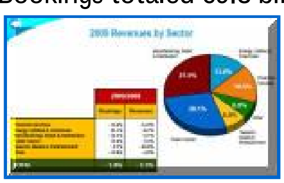
In a video interview with EuroBusiness Media, Paul Hermelin, Capgemini's CEO, said that "2009 was a challenging year because we started the year with still a pretty solid demand and we saw it crumbling in the second half." But he added, "I still I think the Group has shown a quite respectable resilience."

In other words, it could have been worse. Based on the reaction of most Paris investors, who pushed Capgemini's share up 6% today, they seemed to agree. They must have expected worse results, and were relieved to see only a small drop in revenue.

Yet, Capgemini's operating margins also suffered, declining from 8.5% in 2008 to 7.1% last year. But it was its bottom line that slumped the most - down 39% to €178 million (about $240 million).

On the plus side, Capgemini's new contract sales in the face of an economic slump can be indeed categorized as "resilient," to borrow Hermelin's adjective.

Bookings totaled €9.3 billion ($12.6 billion) in 2009, down only 2% on comparable figures



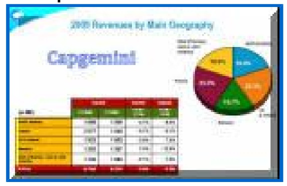
for last year. They were especially strong in Utilities and Public sectors (up 33% adn 14% respectively - see the chart). Also, Outsourcing Services – and particularly BPO (Business Process Outsourcing) – actually had a 14% surge in bookings.

Since new contract sales are a good indicator of future revenues and earnings, perhaps the Paris Bourse traders were also buoyed by a relatively good performance in this business category.

Capgemini's cash flow performance gave investors another reason to cheer. Net cash and cash equivalents at Dec 31, 2009 were €1,269 million, up €495 million since the end of 2008.

Business Segment Analysis

Geographies: France, Capgemini's largest region, reported a 6.1% drop in revenues. The operating margin was 6.2%, a decrease of less than one point.



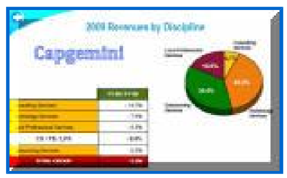
United Kingdom and Ireland was the only major region to report an increase in revenues (+7.5% adjusted for currency). This area improved its profitability to become the most profitable of the major regions (8.9%).

North America reported a revenue drop of 8.5%, adjusted for currency, but only 4.7% in U.S. dollars. The operating margins were relatively stable at 4.9%, down only 0.6 points since a year ago.

Back to Europe, it was the Benelux countries where revenues plummeted 12.9%. Yet this region maintained an operating margin rate of 8.7% for the year and even a double-digit rate in the second half.

Other world regions reported a fall in revenues of 7.6% on average, adjusted for currency, although Italy and Asia-Pacific "enjoyed remarkable growth," Capgemini said in a release. These areas reported an average operating margin rate of 10.4%, spurred by the profitability of the Asia-Pacific region, the Group’s leading resource center.

Horizontal Businesses:



• **Outsourcing Services**, which accounted for 36.4% of Capgemini's 2009 revenues, reported growth of 0.3%, adjusted for currency, despite the expected decrease in revenues generated by a major North-American contract. The operating margin rate improved to 7.2%.

• **Technology Services** reported a 7.4% drop in revenues and an operating margin rate down on 2008 at 6.9%;

• **Sogeti**, Capgemini's euphemism for SMB (small and medium size business deals), reported an 8.3% drop in revenues, but maintained the highest operating margin (9.7%).

• **Consulting Services,** reported the sharpest decrease of 14.7%. But its operating margin was down only 1.4 points to 11.4%.

Outlook

Looking ahead, Capgemini said in a statement that the demand "appears to be stabilizing in the first half of 2010." The company has noted "a significant increase in the appetite of clients for larger projects" and, "in several geographical areas, a turnaround in the attrition rate, which generally reflects an upturn in activity."

For 2010 as a whole, Capgemini forecasts a revenue contraction of between 2% and 4% in constant currency, with an operating margin between 6% and 6.5%.

So there you have it... two back-to-back news releases, as different as night and day, causing investor reactions that were also as different as day and night. HP's solid performance left investors cold, while Capgemini's declining results buoyed them.

What are we to deduce from this? Leave logic and reason at home when you come to play on Wall Street or Paris Bourse.

Happy bargain hunting!

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Volume XXVI, Annex Bulletin 2010-04
February 18, 2010

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