

# ANNEX BULLETIN

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## **INDUSTRY TRENDS**

Updated 12/30/06, 12:30PM PDT

***Analysis of Top 20 Global IT Leaders' Business and Stock  
Performances***

# Happy Days Are Here Again

***Top 20 IT Stocks Gain \$207 Billion Since June; Microsoft by  
Far Biggest Member of \$1.1 Trillion-Market Cap Club***

**HAPPY DAYS ARE HERE AGAIN**

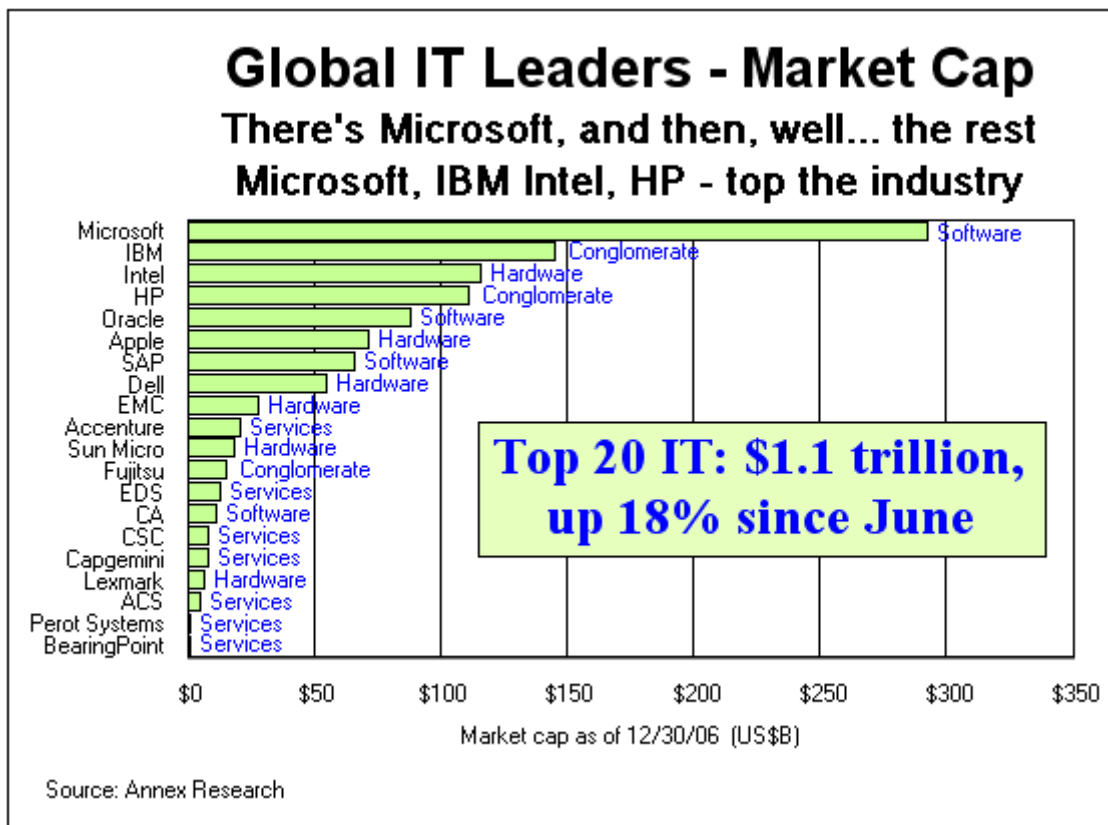
So long sad times  
Go long bad times  
We are rid of you at last

Howdy gay times  
Cloudy gray times  
You are now a thing of the past

Happy days are here again  
 The skies above are clear again  
 So let's sing a song of cheer again  
 Happy days are here again

(An excerpt from "[Happy Days Are Here Again](#)," song and lyrics by J. Yellen and M. Ager)

SCOTTSDALE, Dec 30 - "Happy days are here again," as the lyrics of an old Depression Era song suggest. Gone and forgotten are the 2006 summertime blues (see "[A\\$160 Billion Loss!](#)", June 2006). At least that's the impression one gets after analyzing the top 20 IT stocks' performances in the last six months. They tacked on almost another \$100 billion to their market cap in the fourth quarter, on top of the \$110 billion they had gained in the previous three months (see "[Strong Comeback](#)," Sep 2006).



Their market cap now adds up to \$1.1 trillion, up 18% since six months ago. Which means that, after declining about \$160 billion in the first half, they have gained about \$47 billion for all of 2006 (also see "[A \\$100 Billion Gain](#)," Dec 2005). No surprise there. Here's what we said about it back in September:

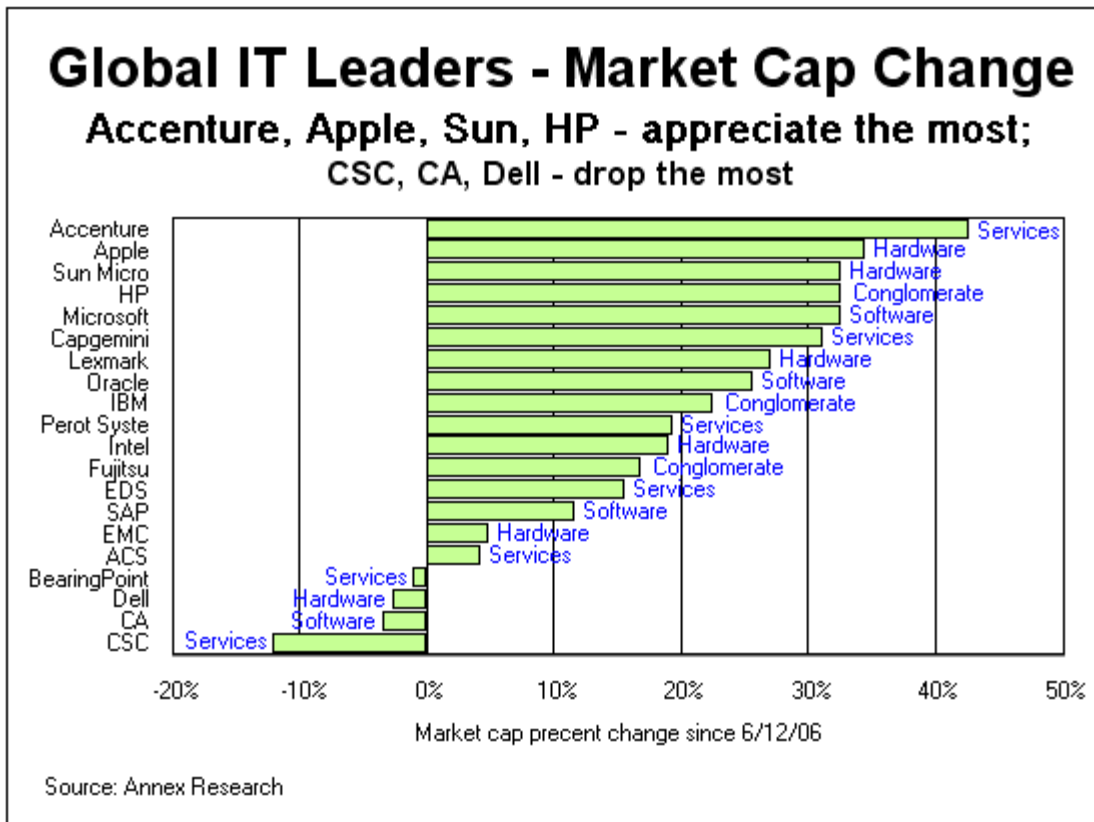
But the third quarter is usually the worst, and the fourth is the best. So

when the IT market bounces back with such vengeance in traditionally the worst quarter of the year, the outlook for a positive year-end finish is pretty good.

(An excerpt from "[Strong Comeback](#)," Sep 2006)

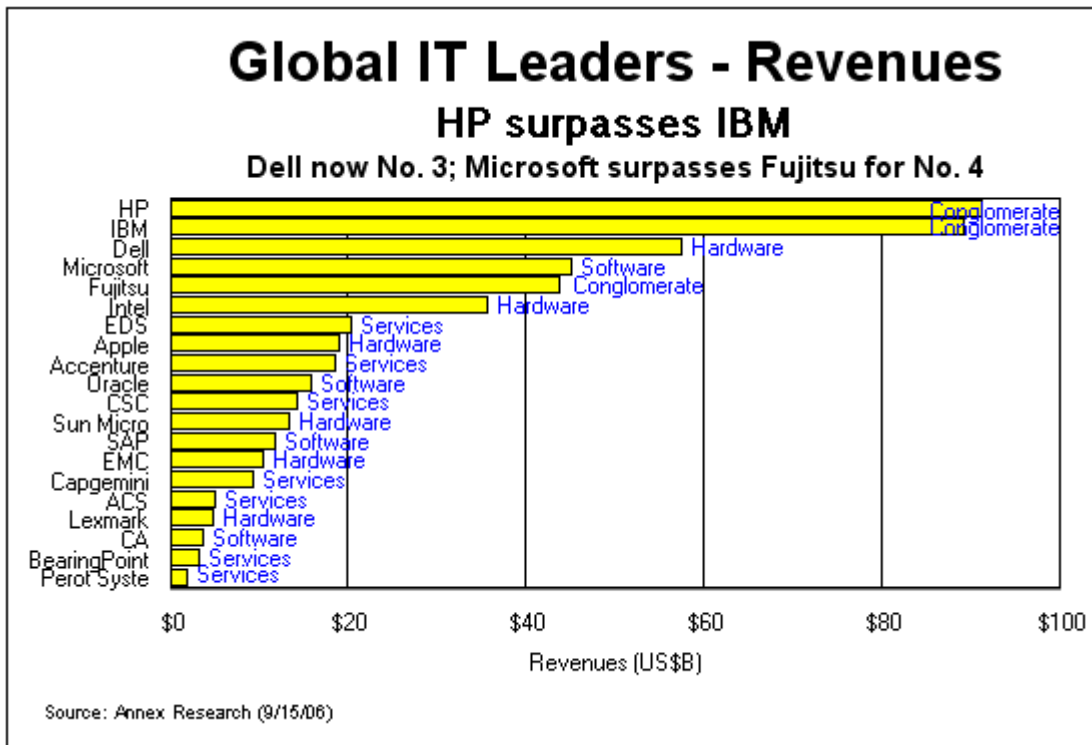
Nearly \$300 million of the Top 20's \$1.1 trillion market cap is attributable to just one company. There's Microsoft, and then..., well, the rest of the Top 20, when it comes to stock market valuations.

Not that IBM's \$146 billion-market cap is not an impressive number, up 23% since June. Or Intel's \$116 billion (up 19%); or HP's \$112 billion (up 33%) - the other three IT leaders above the \$100 billion-mark. But they are all at less than half of Microsoft's \$294 billion market cap (see the chart).

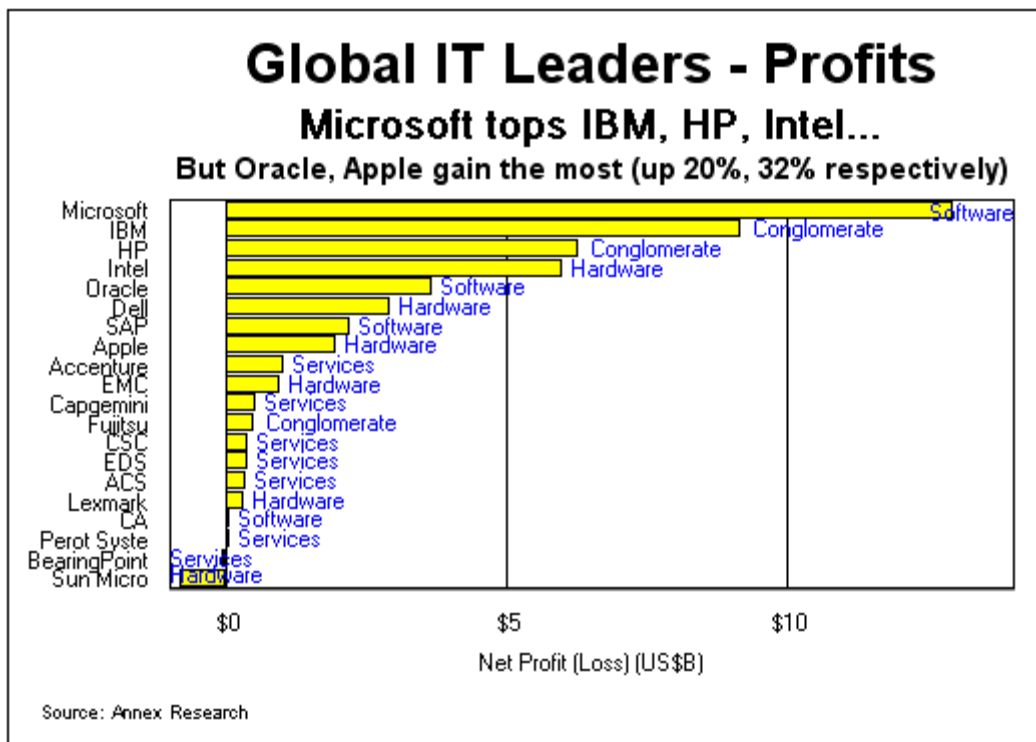


When it comes to market cap changes in the last six months, however, Accenture and Apple top the Top 20 list with 43% and 35% respective gains. CSC, CA and Dell hold up the rear.

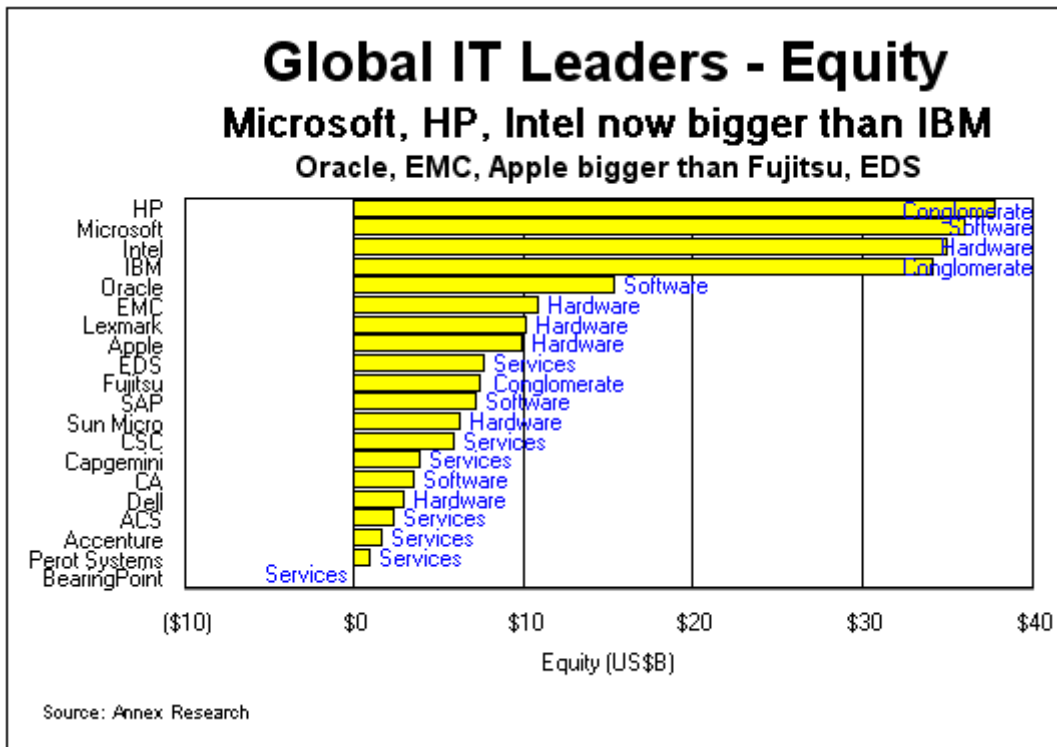
## Business Analysis



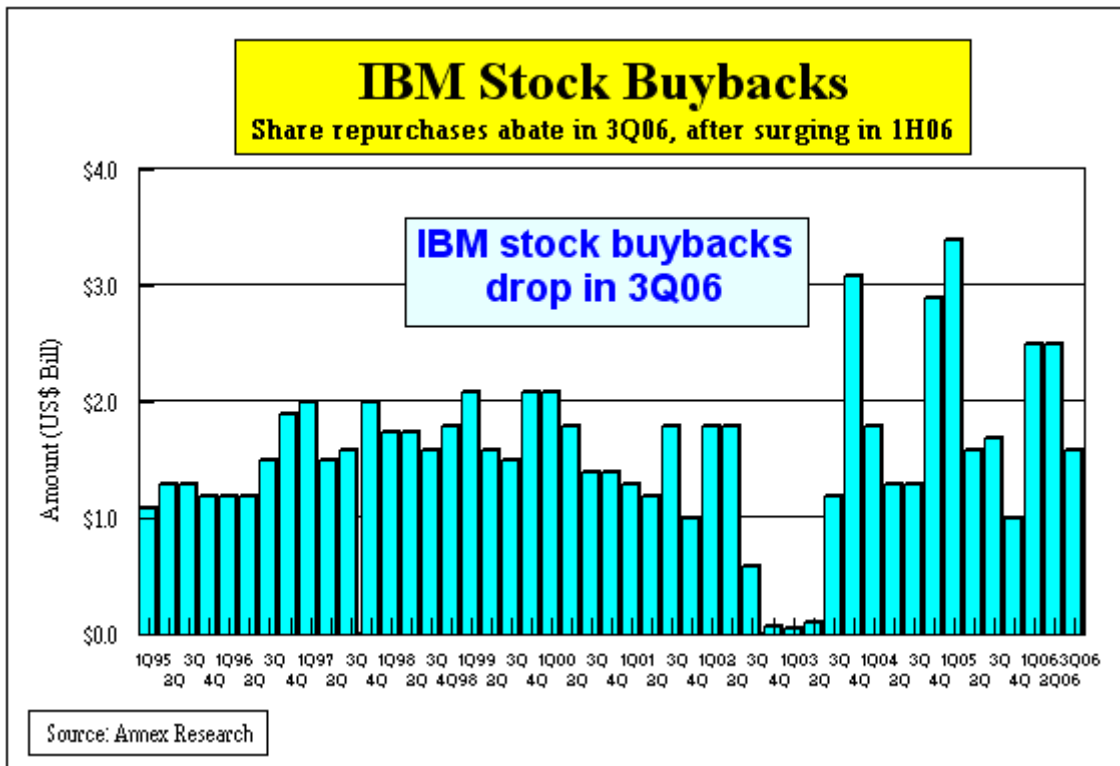
The top 20 IT companies we follow account for over half a trillion dollars (\$520 billion) of the industry's revenues, and for more than \$49 billion of its profits. HP is now the industry leader in terms of revenues...



...while Microsoft also towers over IBM, HP and Intel - in that order - when it comes to net profit.



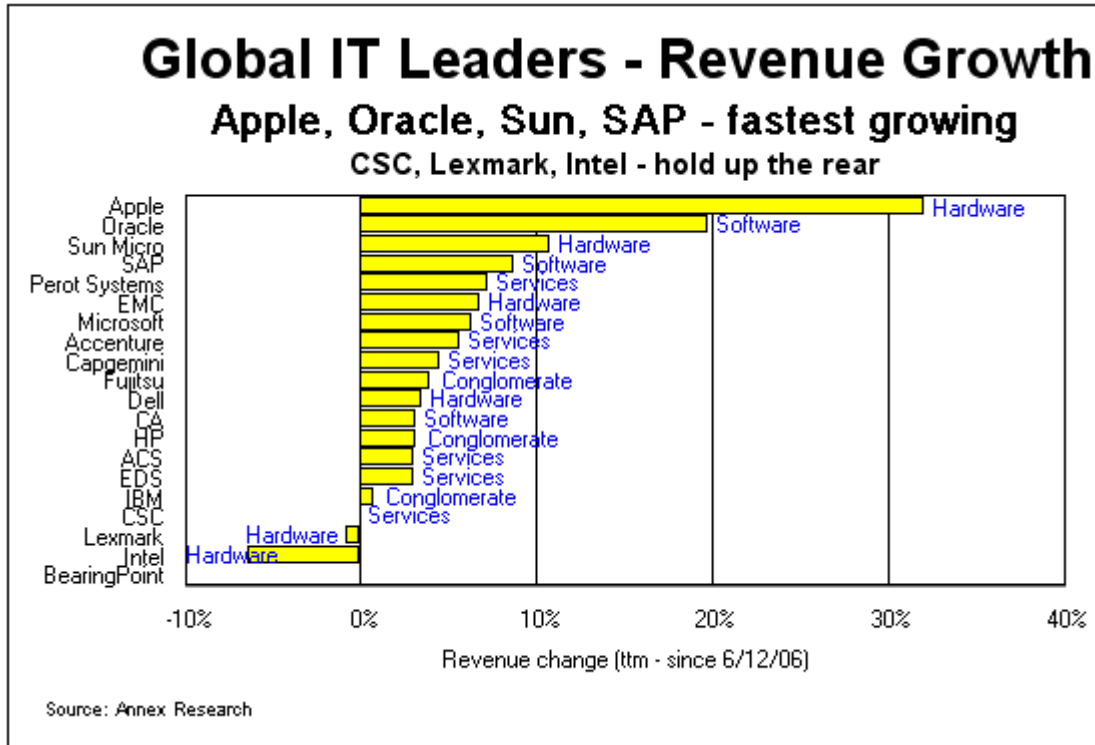
When it comes to equity, four companies are closely bunched up at the top. HP is at the top, closely followed by Microsoft, Intel and IBM.



Being the industry leader in terms of stock buybacks has its price (see "[A Fading Fad](#)," Sep 2006). The \$74 billion IBM has spent on share

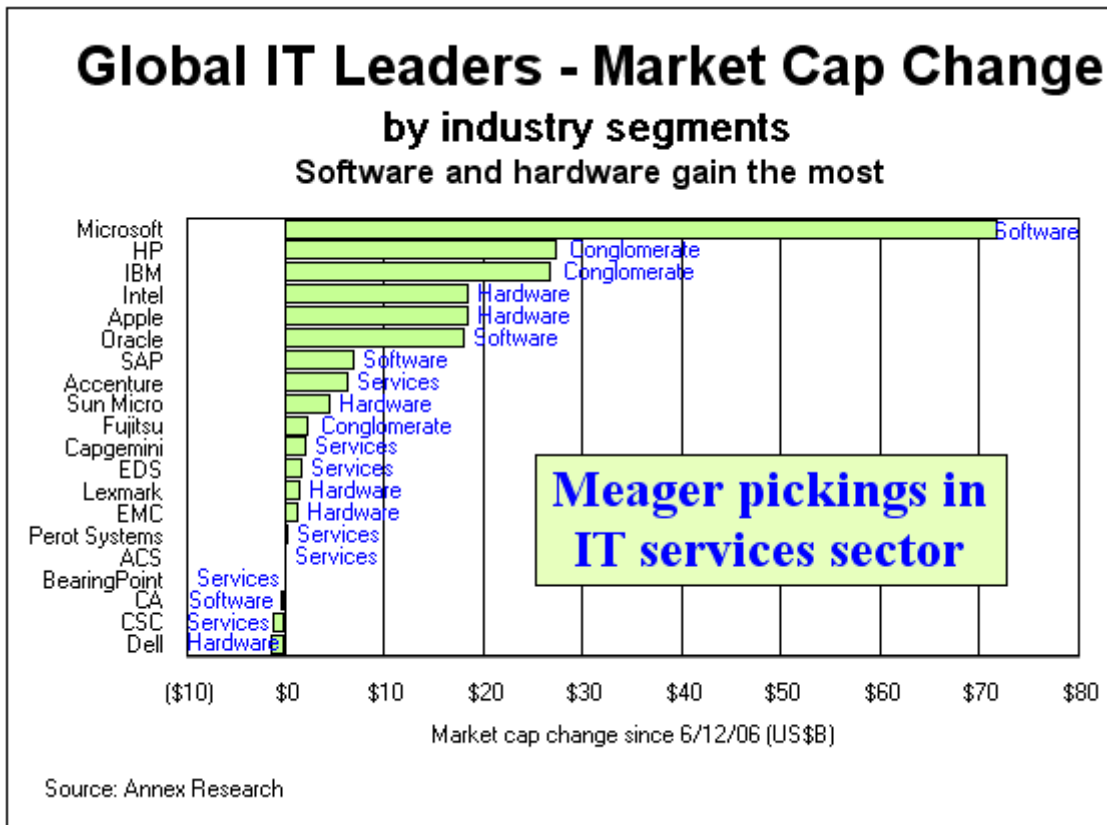
repurchases burned a pretty big equity hole. No wonder IBM is starting retrench a bit lately with its share repurchases.

Of course, all other top IT companies have been also spending billions of dollars the same way. But they've also kept proportionally more profits on their books than IBM.

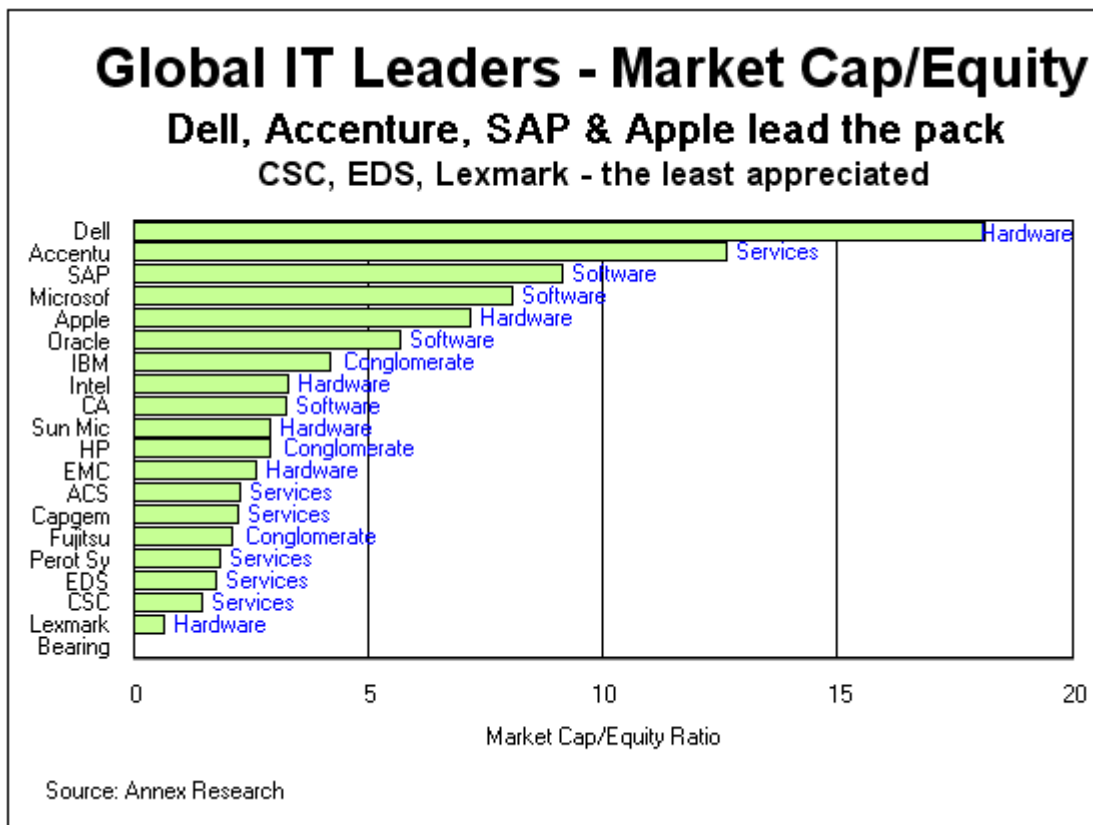


When it comes to revenue growth, Apple, Oracle, Sun and SAP top the list, with Lexmark and Intel hugging the bottom of the Top 20 list.

As a group, however, the Top 20 revenue and earnings growth has been less than impressive. The trailing 12 month revenues are up 4.1% since June, while their net earnings rose 3.4%. So the stock market's apparent enthusiasm about the IT stocks has a lot more to do with hopes for a rosier future than with reality of past achievements.

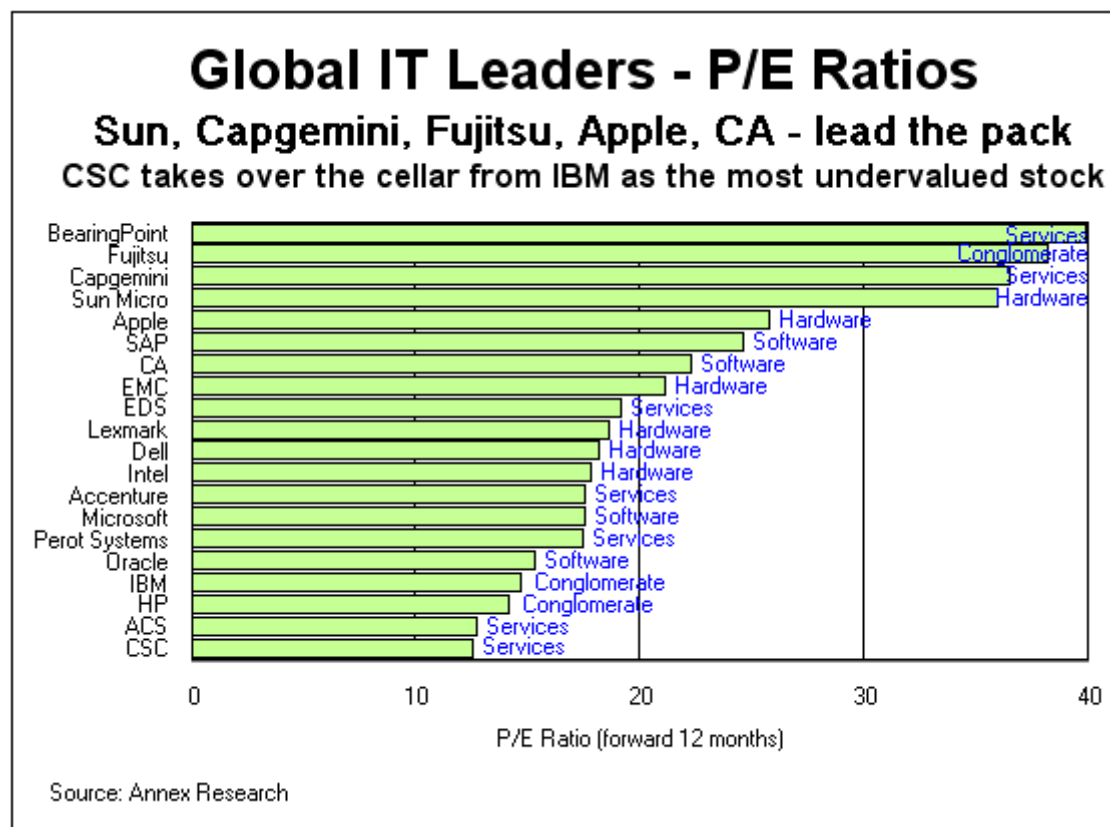


Market cap gains in the last six months were also fairly evenly distributed across the major IT industry segments. Hardware and software vendors have gained the most. With exception of Accenture, the services sector, on the other hand, has seen meager pickings when it comes to higher valuations. Although only CSC's market cap has declined, the increases of the most of the IT services vendors were nothing to write home about as compared to other industry leaders.



As you have seen in our recent Annex Bulletin, Dell is still the "King of Fluff," though it has abandoned the practice (stock buybacks) that installed it on the throne (see ["A Fading Fad,"](#) Sep 2006). So it should come as no surprise to our readers that Dell, however diminished, is still the leader of the pack in terms of market cap-over-equity ratio, the "fluff ratio" as we dubbed it in 1998. Nor that Accenture is second, proving one can win friends and investors' wallets on Wall Street *without* having to resort to major stock buyback-type "bribes."

No surprise in the cellar, though. CSC, EDS and Lexmark are holding up the rear.



Our final stock market profile cuts across the top 20 IT companies along their (forward) price/earnings (P/E) ratios. Once again, we have perhaps a surprising leader here - BearingPoint. With just recently published financials for 2005, and only orientation figures to guide investors for the first nine months of 2006, it is clear that Wall Street one of its own more on faith rather than fact (see ["Where You-Turn Means Upturn,"](#) May 2006).

Fujitsu, Capgemini, Sun and Apple have similarly imbued investors with confidence about their future earnings more than their Top 20 peers.

At the bottom of the ladder, CSC and ACS are the most underappreciated. Interestingly, HP, IBM and Oracle are just a notch above, despite their recent stock price rises. Which only goes to show us how much more appreciation potential there is still left in these three industry leaders, especially in the Big Blue stock.

## Summary

As we noted back in September, there have been several times over the last two decades when business fundamentals and market valuations were at a variance. During the last six months, however, the market has brought them more or less into balance.

There are exceptions, of course, the biggest discontinuity being Wall Street's continued under-appreciation of the IBM stock, though 23% less now than back in June. But that's an exception that only confirms the rule. Generally speaking, the IT stock market and business are fairly well aligned. The universe is unfolding as it should.

For detailed tables, [click here for Top 20 stock/business stats](#) 

*Happy bargain hunting!*


*Bob Djurdjevic*

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