

ANNEX BULLETIN

Annex Bulletin 2007-14

April 17, 2007

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IBM FINANCIAL

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Updated 4/16/07, 4:30PM PDT

A Preview of IBM First Quarter Business Results

IBM Stock Still Grossly Undervalued

Priced at Peer P/E Ratios, IBM Should Be Worth \$124?

SCOTTSDALE, Apr 16 - IBM stock is inching up toward its closing price of 2006 (\$97), but it is still down for the year and is grossly undervalued relative to its peers.

INTL BUSINESS MACHINES
as of 13-Apr-2007



**IBM stock still grossly undervalued!
A fair price at \$124?**

Our latest analysis, done on the eve of Big Blue's first quarter results, basically confirmed what we said nearly five months ago. IBM stock should be worth \$124 if priced at peer P/E ratios. We said as much in late November when we also took the market temperatures of IBM and its five peer competitors (see "[A \\$125 Stock](#)," Nov 2006).

And how did we arrive at such conclusion? By analyzing the business fundamentals and

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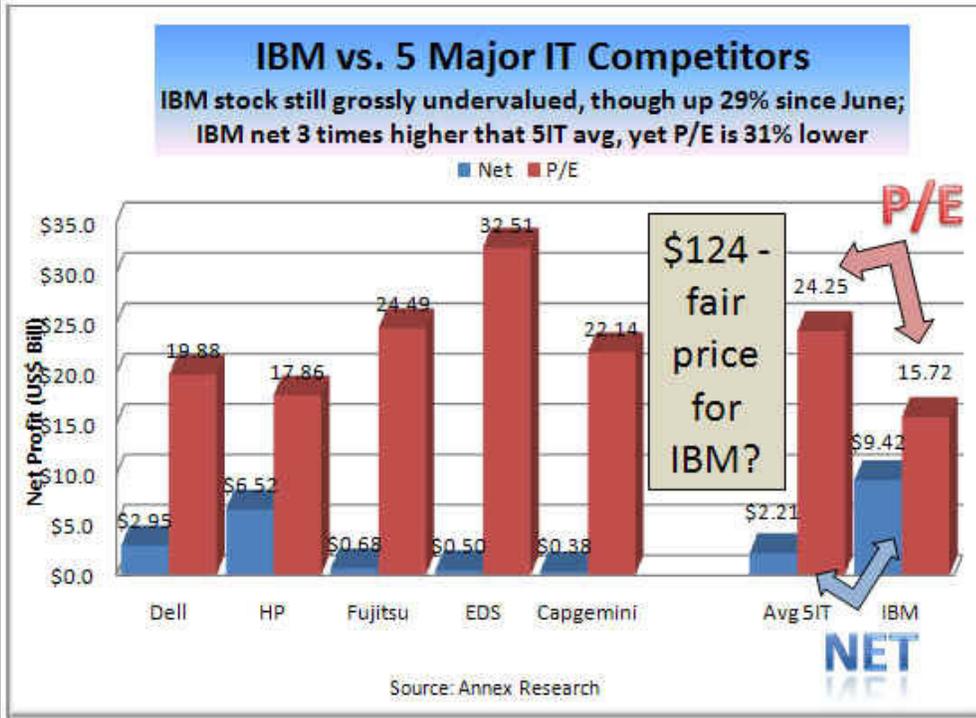
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[Caggemini Caps Great Year, Saves Best for Last](#) (Analysis of Caggemini's fourth quarter business results)

[EDS: On Sunny Side of Street](#) (Analysis of EDS' fourth quarter business results)

market data of IBM, HP, Fujitsu, EDS and Capgemini - three conglomerates and two global services competitors.



As you can see from the above chart, the IBM net profit is about *three times higher* than the average of these five competitors, yet its price/earnings (P/E) ratio is *31% lower*. Putting it another way, if the IBM peers' average P/E ratio were applied to Big Blue's business fundamentals, its stock price should be \$124 per share. Instead, IBM closed today at \$96.18, up 1.3% on the day (Apr 16).

[CSC: Where Less Seems More](#) (Analysis of CSC's third quarter fiscal 2007 business results)

[Fujitsu: Sales Up, Profit Down](#) (Analysis of Fujitsu's third quarter fiscal 2007 business results)

[IBM Shatters Records](#) (Analysis of IBM's fourth quarter business results)

[IBM Stock Passes Century Mark](#) (Analysis of Big Blue's Stock Performance)

[Happy Days Are Here Again](#) (Analysis of Top 20 IT leaders' latest stock market and business performances)

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[Hedging the Bets](#) (Analysis of latest institutional shareholdings of leading IT companies: IBM, HP, Accenture, EDS, CSC, BearingPoint, ACS, Perot) [[Annex clients click here](#)]

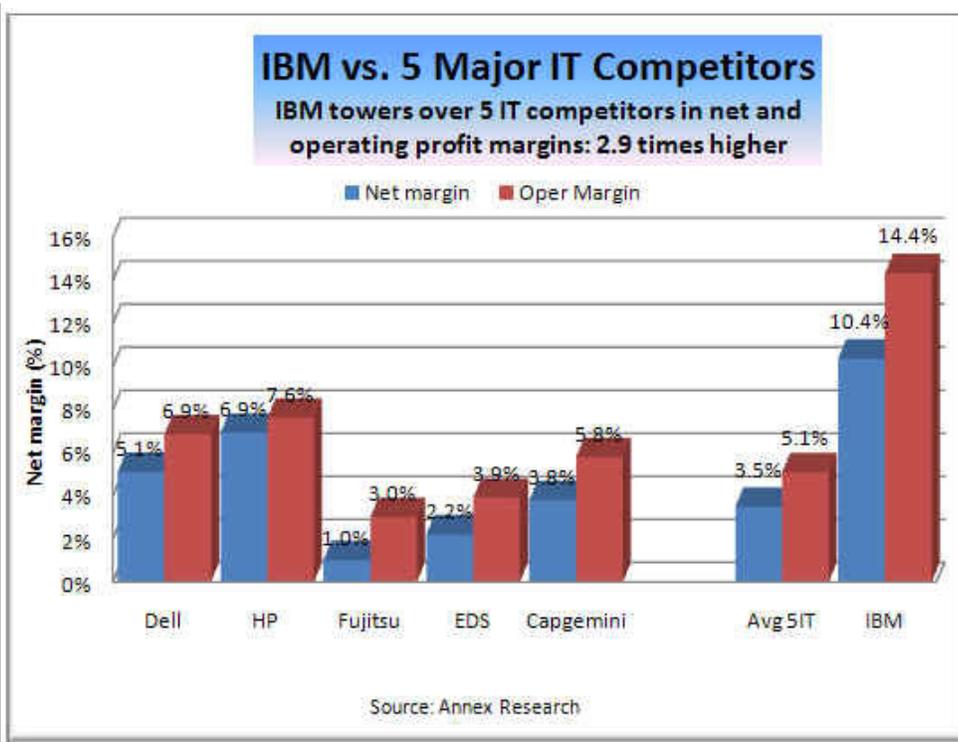
[Globalization Accelerates](#) (Analysis of United Nation's annual survey of global investments)

[IBM: A \\$125-Stock?](#) (An update to "From Small Acorns Mighty Oaks Grow")

[Capgemini: Longest Sustained Stock Price Rise](#) (An update to "By Leaps and Bounds")

[HP: New King of the Hill](#) (Analysis of HP's fourth quarter business results)

[IBM: From Little Acorns Mighty Oaks Grow](#)

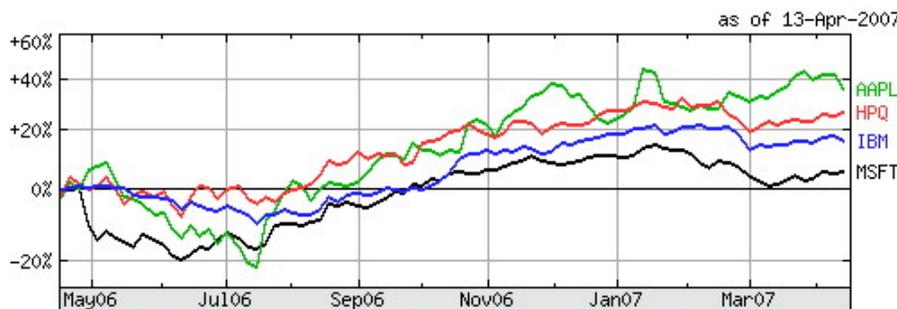


The same pattern is discernible from a comparison of IBM vs. five major competitors' profit margins. IBM net and operating profit margins are about three times those of its peers (see above chart).

Outlook

Based on everything we have seen and heard in the marketplace during the first quarter, this pattern will continue after tomorrow's results are release, if not widen in IBM's favor. IBM is likely to hit or exceed analyst expectations (revenues of \$21.86 billion, EPS of \$1.21, according to Thomson Financial).

It remains to be see if the company gets the credit for it on Wall Street this time around that has eluded it in the past. During the last year or so, investors seem to be more preoccupied chasing the values elsewhere in the IT industry, such as Apple or HP, for example.



While looking up wistfully at HP, Apple, IBM can for once look down at Microsoft

(Analysis of IBM's "State of the Union")

[Cpgemini: By Leaps and Bounds](#) *(Analysis of Cpgemini's preliminary third quarter business results)*

[Fujitsu: Good Performance Gets Better, More Global](#) *(Analysis of Fujitsu's first half FY2007 business results)*

[IBM: A Slam Dunk Quarter](#) *(Analysis of IBM third quarter business results)*

[Accenture's Emphatic Year-end Accents](#) *(Analysis of Accenture's fourth quarter results)* [[Annex clients click here](#)]

[IBM: Services in a Box](#) *(Analysis of IBM Global Services' Ground-shifting Announcements)*

[Strong Comeback by IT Stocks in Third Quarter](#) *(Analysis of top 20 IT companies' market and business trends)*

[Stock Buybacks: A Fading Fad](#) *(Dell, erstwhile "King of Fluff," suspends its stock buybacks)*

[Cpgemini: Growth Continues](#) *(Revenues, net profit up in double digits, margins also improve)*

[HP Firing on All Cylinders](#) *(Stock sets new multi-year record following excellent third fiscal quarter results)* [[Annex clients click here](#)]

[Power of Manpower](#) *(While others move to India, Russia... AMD invests in New York, hailing "phenomenal" quality of its labor force)*

Meanwhile, while looking up wistfully *up* at the HP and Apple stock gains in the last 12 months, IBM shareholders can console themselves by looking *down* at Microsoft. For once! Wall Street has treated the erstwhile IT industry highflier in the last year with even more disdain than the Big Blue stock. That was the first time something like that has happened since Microsoft's rise to prominence in the IT industry (see the thumbnail chart).



[Ebb Tide Lowers Most Boats \(Analysis of EDS' and CSC's latest quarterly results\)](#)

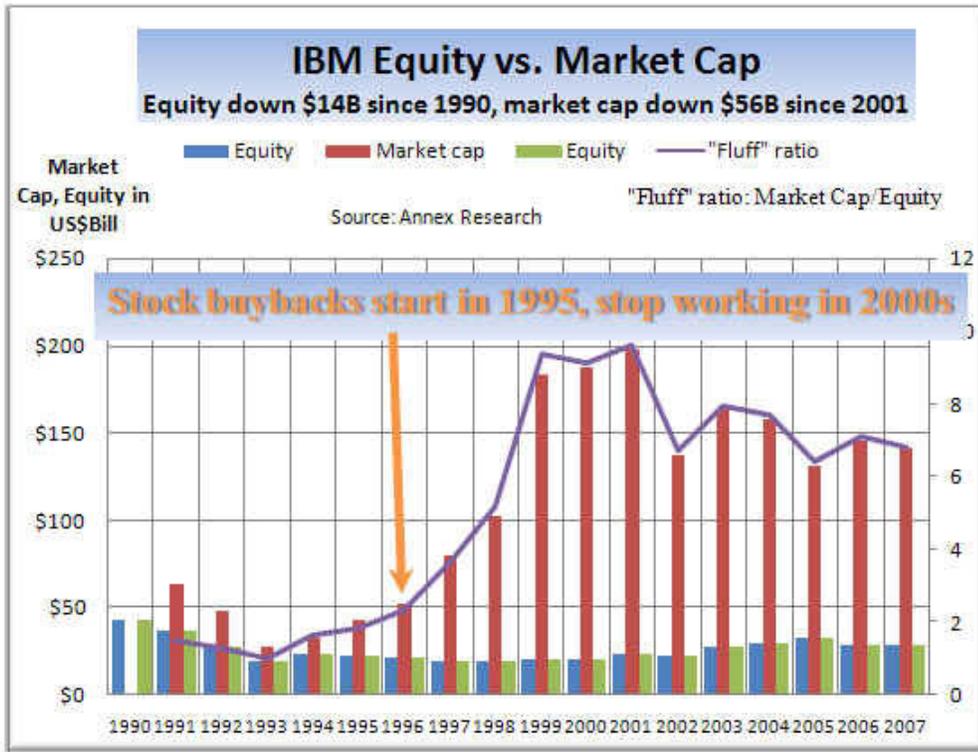
[IBM Stock Grossly Undervalued? \(Analysis of stock market valuations of IBM and its major competitors\) \[adds latest Fujitsu, Capgemini results\]](#)

[IBM vs. HP: A Tale of Two Blues \(Both companies are doing well in business, but only HP is favored by Wall Street; Big Blue trying to change that now with its new "India Opus"\) \[Annex clients click here\]](#)

[Go East, Young Man! \(A speech delivered in St. Petersburg, Russia, May 25, 2006; click here for slides\)](#)

[IBM 5-Yr Forecast: Steady As She Goes \(Emphasis on quality continued\) \[Annex clients click here\]](#)

[Octathlon 2006: Accenture Again Wins "Gold!" \(HP gets "Silver," IBM "bronze"\) \[Annex clients click here\]](#)



Meanwhile, IBM's one-string instrument for propping up the stock price isn't working anymore. Even though the company has spent \$76 billion since 1995 trying to entice Wall Street into favorable valuations, most of it in the last 7 years (see the thumbnail chart), Big Blue's market cap keeps sliding even faster than the drop in shareholders equity.



Maybe if the company stopped minding Wall Street opinions, and started minding its business (by investing all these billions into acquisitions instead of lining investment bankers' pockets), favorable valuations would also soon follow?

[Click here](#) for detailed IBM tables and charts (Annex clients only)

Happy bargain hunting!

Bob Djurdjevic

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