HP Turnaround Progressing as Profit Forecast Tops Estimates (1)
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(Updates shares in seventh paragraph.)

By Aaron Ricadela
Feb. 22 (Bloomberg) -- Hewlett-Packard Co., the largest personal-computer maker, forecast fiscal second-quarter profit that exceeded analysts' estimates, helped by cost-cutting measures and a smaller-than-projected drop in service sales.
Profit, excluding some items, will be 80 cents to 82 cents a share for the current quarter, which ends in April, the Palo Alto, California-based company said a yesterday. That beat analysts' average 77-cent estimate, according to data compiled by Bloomberg. The shares rose the most in more than a year.
Hewlett-Packard is using job cuts to bolster profit as demand for printers and personal computers slumps and companies curtail purchases of higher-margin hardware and software. Chief Executive Officer Meg Whitman said she feels "pretty good" about fiscal 2013 and reaffirmed a prediction that the company will resume growth next year, evidence of progress on a five-year turnaround plan even as competitive pressures linger.
"They seem to be managing the restructuring better than we had expected -- it's still a work in progress," said Shannon Cross, an analyst at Cross Research, based in Livingston, New Jersey.
Fiscal first-quarter revenue fell 5.6 percent to $28.4 billion, compared with analysts' average estimate of $27.8 billion. Profit, excluding amortization, restructuring and other charges, was 82 cents a share, compared with the 71-cent prediction. Net income fell 16 percent to $1.23 billion, or 63 cents a share, from $1.47 billion, or 73 cents, a year earlier.
"I feel pretty good about the rest of the year," Whitman said in an interview. "I think we are beyond the announcements about the writedowns and restructuring."

Share Jump

The shares rose 8.1 percent to $18.49 at 9:34 a.m. in New York, and earlier touched $18.60 for the biggest intraday gain since September 2011. Hewlett-Packard had advanced almost 2 percent in the last hour to close at $17.10 yesterday. Almost 4.29 million shares traded in that timeframe, three times the average volume seen during the same period in the past five trading days.
"To me, it looks like someone had to have known something," Frank Ingarra, head trader at Greenwich,

Connecticut-based NorthCoast Asset Management LLC, said in a telephone interview. His firm oversees $1.4 billion. “There’s huge volume. I would be skeptical to think that someone didn’t have any idea.”

John Nester, a spokesman for the U.S. Securities and Exchange Commission, declined to comment on whether the agency was reviewing trading ahead of the announcement.

The stock has climbed 46 percent since Nov. 20, when the company disclosed an $8.8 billion writedown on the value of software company Autonomy Corp., which it agreed to buy for $10.3 billion in 2011.

Taking Root

Sales in Hewlett-Packard’s PC unit fell 7.7 percent to $8.2 billion during the first quarter, and the “deterioration” will only accelerate in the current quarter, Cathie Lesjak, Hewlett-Packard’s chief financial officer, said during a conference call with analysts yesterday.

Revenue from printers and related supplies declined 5.3 percent to $5.93 billion. Whitman told analysts she’s encouraged by efforts to price ink cartridges more cheaply for emerging markets, and by a new product called the Officejet Pro X that delivers laser-printer speed and quality using cheaper liquid ink technology.

In enterprise services, where sales were down 7.1 percent to $5.92 billion, two large customers Hewlett-Packard had expected to leave during the first half of the year delayed that decision.

Challenging Environment

“While the results were clearly better than expected, underlying fundamentals remain challenging for the company,” Abhey Lamba, an analyst at Mizuho Securities USA Inc., said in a note. Lamba has an underperform rating on the shares. “It posted declining year-over-year sales in every category except for desktops and networking.”

Sales of technology outsourcing and consulting services declined less rapidly than the company had forecast, and printers and ink are yielding higher profit margins than in the past, Lesjak said in an interview. A program to cut 29,000 jobs is also bolstering profits, she said.

At a meeting with investors in October, Whitman and Lesjak cut Hewlett-Packard’s earnings forecast for this year, blaming management upheaval and slow updates to key products. Seven weeks later, Hewlett-Packard said it would write down most of the value of the Autonomy acquisition after discovering the unit had misrepresented its sales, sending shares plunging 12 percent that day.

Gaining Traction

"I don't like the fact that we saw revenue declines in each of our major segments," Whitman said during a conference call. "Restoring growth is a priority, and we're on it."

Hewlett-Packard maintained its outlook for adjusted profit of $3.40 to $3.60 a share for the fiscal year.

Hewlett-Packard reported earnings two days after No. 3 PC maker Dell Inc. reported fiscal fourth-quarter sales and profit that topped analysts' estimates, reflecting businesses' demand for servers and software. Dell, which is transforming into a provider of a broad range of technology products, is planning to go private in a $24.4 billion deal.

Whitman said Hewlett-Packard plans to try to poach Dell's customers during the leveraged buyout process.

"We are going to go after those customers, because we understand perhaps better than most what opportunity instability represents," she said.

PC Weakness

Both companies are being dogged by a decline in PC demand. Shipments fell 4.9 percent in the fourth quarter, market researcher Gartner Inc. said. The rise of smartphones, tablets and software that runs via a browser are crimping sales.

There have been some bright spots for Hewlett-Packard in the computer market. Its share of fast-growing ultrathin notebooks was 14 percent in the fourth quarter, according to IDC, second only to Apple Inc. Whitman has also said the company will eventually re-enter the smartphone market, after discontinuing phones using software from its Palm Inc. acquisition in 2011.

The week before Valentine's Day, Hewlett-Packard convened its top 1,100 managers in Anaheim, California for a meeting to see the company's latest products. Starbucks Corp.'s CEO Howard Schultz and Jeffrey Katzenberg, CEO of DreamWorks Animation SKG, spoke at the event.

"The hope is that this is the floor and they've gotten a grip on the business," said Shaw Wu, an analyst at Sterne Agee & Leach Inc. Wu has a neutral rating on the shares. "They're giving guidance that actually makes sense."

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