

Choice of CEO signals new direction for HP

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In this Jan. 27, 2010 file photo, Leo Apotheker, then CEO of German software company SAP, is seen during the annual financial statement in Frankfurt, Germany. Hewlett-Packard on Thursday, Sept. 30 2010 named Apotheker as its new CEO. (AP Photo/dapd, Daniel Roland, File)

(AP) -- The appointment of a German software executive as Hewlett-Packard Co.'s next CEO sends an unmistakable signal that the board of the world's largest technology company is prepared to gamble big on an aggressive push into the software business.

And analysts say it will need to do just that to avoid being left behind in its core personal computer and printer businesses that no longer offer much room for growth or big profits.

In a conference call that served as his formal introduction to Wall Street on Friday, former SAP AG CEO Leo Apotheker called software the "glue" that will hold together the different parts of the company. "Software is how we can make sure that the various parts of our technology actually fit well together," he said.

Even before his comments, it was telling enough that HP didn't choose the head of its PC or printer businesses - the company's traditional strengths - and instead tapped an executive who has spent more than two decades in the business software industry and far from Silicon Valley.

"HP is in the midst of a transformation," says R. "Ray" Wang, a partner at Altimeter Group LLC. "If they don't make the move into software in the next three to five years, they're going to find themselves in a really commoditized PC business with high volume and low profit margins."

The choice of Apotheker could cut both ways. He has no experience with consumer products, which make up a sizable portion of HP's business. He also faces the challenge of holding together a group of managers at HP that has turned the company's computers and printers into industry leaders. Some of those executives were passed over for the CEO job, which could turn them into potential defectors, analysts say.

"These are tricky waters to be navigating," IDC analyst Crawford del Prete said. "Job No. 1 has to be solidifying this team."

Wall Street isn't convinced that Apotheker, 57, is the right pick. HP's shares fell \$1.30, or 3.1 percent, to close Friday at \$40.77.

The debacle over former CEO Mark Hurd, who was forced out over allegations of sexual harassment and deceptive expense reports, sent HP's stock down more than 15 percent in the weeks after his departure on Aug. 6.

Apotheker has an international background. His parents escaped the Nazis, then settled in Aachen, Germany, after World War II. The family moved to Antwerp, Belgium, after he was born in 1953. After high school, Apotheker moved to Israel, earning a B.A. in economics and international relations at the Hebrew University in Jerusalem. He speaks five languages: English, Dutch, German, Hebrew and French.

In 1988, Apotheker began his career at SAP, which provides software that helps carry out a range of business functions, from tracking inventory to logging sales. He remained at the company for more than 20 years, founding and serving as head of SAP France and SAP Belgium.

He was promoted to co-CEO in April 2008, just as the recession started crimping business investment. To bolster revenue, the company announced an increase in maintenance fees. But customers protested, and SAP had to postpone the increase. He was also identified with the delay of a new software system. This led to his ouster in February of this year, but in other respects, he gets good marks from German commentators.

His abrupt departure from SAP aside, it is easy to see why HP feels it needs someone with a background in software.

Big companies and government agencies these days want to deal with technology vendors that provide the whole package of computers, software and services rather than dealing with the headache of putting it all together on their own. And the software piece of that equation is shaping up to be a much faster-growing, profitable business than hardware.

HP's own financial results bear that out. Its existing software business contributed just 2.8 percent of the company's \$30.7 billion in revenue for quarter that ended July 31. But it was the company's most profitable

segment, with a 21 percent operating margin. That compares to 4.7 percent in PCs.

With its own software business still small, HP will have to resort to acquisitions if it wants to build serious scale, the same way it bought Electronic Data Systems in 2008 to double its services business. Speculation is mounting that it might attempt to buy SAP.

HP will face stiff competition from other tech heavyweights looking to position themselves as the leading one-stop shop for information technology.

One is Oracle Corp., a former ally that jumped into the hardware business against HP this year with the acquisition of Sun Microsystems. The competition with Oracle is all the more bitter because the company's CEO, Larry Ellison, decided to snap up Hurd last month to serve as Oracle's president. HP sued to try keeping him out of the job, but has settled the case.

HP, based in Palo Alto, Calif., said Thursday that it will also be bringing in an Oracle alumnus to help lead the company. Venture capitalist Ray Lane, who was ejected from Oracle's No. 2 job by Ellison a decade ago, is joining HP as nonexecutive chairman.

The escalating rivalry could lead to bidding wars between HP and Oracle for smaller software players as both companies bulk up, said Caris & Co. analyst Curtis Shauger. "The gloves are off," he said.

IBM is another tech powerhouse making software acquisitions. Just last week, the company agreed to pay \$1.7 billion for Netezza Corp., a company that helps businesses sort through data on corporate servers. IBM says it has made more than \$12 billion worth of acquisitions in just that particular niche of the software industry over the past few years.

Apotheker is the third HP CEO in a row to be recruited from outside the company. Carly Fiorina came from Lucent, an AT&T spinoff. Hurd came from NCR Corp. The lack of promotions for top internal managers could encourage them to look for opportunities elsewhere.

Todd Bradley, whom analysts pegged as one of the leading internal prospects, would be a heavy loss, said Gleacher & Co. analyst Brian Marshall.

Bradley took over the company's PC business when it was in tatters and has managed to boost its margins. He upgraded HP's image with the celebrity-studded "The Computer is Personal Again" ad campaign soon after he was hired and cut costs. Within three years, HP outgunned Dell Inc. to snag the title of the world's No. 1 PC maker.

"He's done a great job. He definitely was on the short list," Marshall said.

Apotheker struck a conciliatory tone toward his new colleagues on Friday.

"The first thing I did when I joined this company was to reach out to each member of the senior executive team," he said. "We have talked. These are great professionals. They have HP in their blood and I am sure that as a team we will be working together for many years and do a great job."

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