

# HP cuts outlook on services revamp, slow PC sales

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In this March 15, 2011 file photo, Hewlett Packard Company CEO Leo Apotheker, speaks during an interview in San Francisco. After a leaked memo from the CEO Leo Apotheker warned of a rough path ahead, Hewlett-Packard Co. cut its full-year outlook Tuesday, citing a trifecta of woes that include the earthquake in Japan, soft PC sales and weakening performance in its crucial tech services business. A higher net income for the quarter was overshadowed by what lies ahead for the world's No. 1 PC maker, and company shares fell more than 5 percent before the market opened. (AP Photo/Paul Sakuma, file)

(AP) -- Hewlett-Packard Co. is bracing for weaker financial results this year as it overhauls its services business to undo what its CEO described as years of neglect under his predecessor.

For too long, the business focused on short-term results rather than expand into high-margin areas, such as helping businesses convert their

systems to new technologies, CEO Leo Apotheker said Tuesday.

Fixing that will cost the company in the short term, he said. HP cut its full-year earnings forecast Tuesday. Investors responded by sending its stock down more than 7 percent to a two-year low.

Apotheker, who became CEO in November, said HP never followed through on a strategy it laid out years ago to focus on the high-margin areas.

"We are now going to execute the strategy," Apotheker said.

That includes finding an executive vice president of services who will report directly to Apotheker, he said.

"We view these changes as logical, mostly proactive and positive for long-term operating profit expansion," said Jayson Noland, an analyst at Robert W. Baird & Co.

Although he didn't refer to his predecessor by name, Apotheker implied that he inherited the problems from Mark Hurd, who was forced out in August in the wake of an investigation into his relationship with a former contractor. Hurd, who now works for rival Oracle Corp. as co-president, declined comment through a representative.

To consumers, HP is known as a maker of printers and personal computers, but it has been expanding into providing computer networking and technical services to other businesses. Under Hurd, HP more than doubled its services portfolio with the acquisition of Electronic Data Systems for \$13.9 billion. HP became the second-largest company in the market behind IBM Corp.

Services now account for 28 percent of HP's revenue, nearly as much as

the PC business.

Apotheker's move to transform the services division is an indirect acknowledgement of a frequent criticism that EDS's work was too focused on low-margin tasks. In the services world, those can include basic services and outsourcing tasks, such as installing new PCs and servers and managing companies' data centers.

IBM often says that its advantage lies in its advanced software and deep industry expertise, which allow it to pursue more profitable work such as analytics and building "smart" power grids and transportation systems.

HP, the world's largest PC maker, is also struggling in the PC business. Apple Inc.'s iPad tablet is cutting into PC sales more deeply than PC makers had expected. Consumers are also holding back on PC upgrades because of the economy, Apotheker said, while sales to businesses are going well.

"There's no question that the impact of tablets has been slowing down the renewal rate of PCs. I think that is a trend that will ebb away. I think the PC will continue to be the main computing device in many homes," Apotheker said in an interview.

Tablets can't do everything PCs can, and the iPad needs to be connected to a PC periodically, for backups and software updates.

HP said it's still on track to launch its first non-Windows tablet, the TouchPad, this summer, based on software it got when it bought Palm Inc. last year.

The company reported its quarterly results a day early after a leaked memo from Apotheker warned that the company was bracing for "another tough quarter" in the May-July period. Apotheker said in the

memo that management needed to "watch every penny and minimize all hiring."

The company is now forecasting earnings, excluding one-time items, of \$1.08 per share and revenue of \$31.1 billion to \$31.3 billion for the current quarter, which ends in July. Wall Street analysts were on average looking for earnings of \$1.23 cents per share and \$31.84 billion in revenue, according to FactSet.

For the full fiscal year, which ends Oct. 31, HP now expects earnings of \$5 per share. That is short of its earlier predictions of \$5.20 to \$5.28 per share and below Wall Street expectations of \$5.24.

The company also lowered its fiscal-year revenue guidance range slightly, to \$129 billion to \$130 billion. In February it had forecast revenue of \$130 billion to \$131.5 billion. Analysts are predicting \$130.47 billion

HP's stock fell \$2.89, or 7.3 percent, to close Tuesday at \$36.91. Earlier, the stock hit a two-year low of \$36.04.

HP, which is based in Palo Alto, Calif., reported earnings of \$2.3 billion, or \$1.05 per share, for the three months that ended April 30. That's up from \$2.2 billion, or 91 cents per share, a year earlier.

Excluding special items, HP earned \$1.24 per share in the fiscal second quarter, above the \$1.21 per share that analysts polled by FactSet were expecting.

Revenue climbed 3 percent to \$31.63 billion, slightly above Wall Street expectations of \$31.55 billion.

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