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CORPORATE PARTICIPANTS

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Hewlett-Packard Company - Chairman, President, CEO

Jim Burns
Hewlett-Packard Company - Head of IR

CONFERENCE CALL PARTICIPANTS

Katy Huberty
Morgan Stanley - Analyst

PRESENTATION

Katy Huberty - *Morgan Stanley - Analyst*

Good morning and welcome to the HP presentation. Technology saves the day once again. We actually have Mark who is stuck in traffic. He's blaming it on the weather, but I'll say that business is (technical difficulty) and so he's running late. But we do have him on the line. And up with me on stage is Jim Burns, Head of Investor Relations; just in case we lose him we can carry on with the presentation. And then, just as a heads up, Mark may be coming in during the discussion live.

Before we get started, HP wanted me to tell you that this presentation may contain forward-looking statements that are subject to risks and uncertainties. Please refer to HP's SEC report for a discussion of those risks. Also, my personal holdings and Morgan Stanley disclosures are available at www.MorganStanley.com/researchdisclosure.

So just by way of introduction, since Mark joined HP in 2005 the Company's revenues have increased 50% to a $120 billion run rate and non-GAAP earnings have nearly tripled. And I think I can speak for Mark in saying that there's plenty of additional work to do and we'll walk through some of those opportunities in this presentation. So, Mark, can you hear us?

Unidentified Participant

We're having trouble hearing Mark.

Katy Huberty - *Morgan Stanley - Analyst*

Okay.

Jim Burns - *Hewlett-Packard Company - Head of IR*

Ask your question again. Mark, are you there? Keep talking, maybe they -- we're having trouble with the volume guy (inaudible).

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I don't know how much larger I can talk, Jim. Can you hear me?

Jim Burns - *Hewlett-Packard Company - Head of IR*

I don't think it's your issue with talking, Mark. We're trying to see if we can get the audio up a little bit.

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Katy Huberty - *Morgan Stanley - Analyst*

Mark?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Can you hear me, Katy?

Katy Huberty - *Morgan Stanley - Analyst*

Maybe what we'll do while they work on the sound is I'll jump into some of the business segment questions with Jim. And then as Mark either gets on the line or arrives in person, we'll discuss some of the higher-level strategic thinking.

So, starting with IPG. The economic downturn really gave HP cover to address some of the cost efficiencies within IPG. How much of the -- well, first of all, what was done in 2009 to help address the efficiency issues? How much of that do you think has already paid off in results? And then what does that flexibility or what does that give you in terms of flexibility going forward?

Jim Burns - *Hewlett-Packard Company - Head of IR*

Yes, we did -- in many ways 2009 was a year of tremendous change for the printing business. We took a significant level of cost out; we simplified our product family and our SKU offerings. And what we see now is as the printing market has returned to growth, and we do expect to grow printer units double-digit this year, we were able to get 16% unit growth this quarter while having 17% operating margins. So margins at sort of the top part of our period here.

So the costs that we've taken out over the last year -- and it's been in a number of different areas, supply-chain probably being the biggest one -- has allowed us now to get aggressive in the market, aggressive with the growth. We could have done even more growth had we had the product all lined up the way that we would have liked it. It's not just placing units, we're placing the right kinds of units.

Wireless printers which grow -- which you print typically 10% to 15% more than non-wireless, we had basically 100% growth in that this quarter. Office ink that competes against low end laser, again prints multiple times consumer ink printer, tripled volume for us this quarter. So the growth that we're getting is the right kind of growth.

And so I do think that we have a strong ability to, given the work that we did last year, to continue to throttle [forward] with the growth. And the idea being that if the economy improves and the workforce improves and our installed base gets back growing -- our install base has been pretty flat and consumption on a sell-out basis has been pretty flat, we can start feeling supplies growth again this year.

At the same time, we're making a lot of investments in areas like retail photo kiosks -- won the largest retailer in the world with that -- managed print services, oh, gosh --.

Katy Huberty - *Morgan Stanley - Analyst*

Nice timing.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I'm sure you're doing a better job than (multiple speakers).

Jim Burns - *Hewlett-Packard Company - Head of IR*

I'll let you sit here. I'll let you take it from here, Mark.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Okay, I need a microphone.

Katy Huberty - *Morgan Stanley - Analyst*

Can we get a microphone up here?

Jim Burns - *Hewlett-Packard Company - Head of IR*

Take mine.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I'll just speak loudly. I'm so sorry, Katy. Just this rain (multiple speakers).

Katy Huberty - *Morgan Stanley - Analyst*

I was telling them that you blamed it on the rain, but business is just so good that you're running late.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I was going to say, lots of customer calls. Thank you. It's not a funny crowd, is it?

Katy Huberty - *Morgan Stanley - Analyst*

So maybe what we'll do is just take a step back and set the stage and what Jim and I were doing was going through some of the business segments. But I want to start high level. I don't know if you heard my introduction, but I walked through --.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I could hear you perfectly.

Katy Huberty - *Morgan Stanley - Analyst*

Good. So the numbers over the last five years suggest that you have presided over one of the most successful restructuring stories in technology. But --.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Could we stop now.

Katy Huberty - *Morgan Stanley - Analyst*

Work is done.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Yes, thank you.

Katy Huberty - *Morgan Stanley - Analyst*

But you often say that the work is never going to be done. But as we think about the next five years of your tenure, what are the top priorities for you beyond just continuing the cost efficiencies?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

We've got to go grow. I mean, at the end of the day the industry is about $1.9 trillion. Because of what we've done with our portfolio we've opened ourselves into a position where we can now compete for about $1.3 trillion to $1.4 trillion of it. For us, we've got about, as I think Katy said in her opening, about a $120 billion run rate depending whose numbers you listen to and the effects of currency.

But frankly, our portfolio has put ourselves in a position where the portfolio is better than the results. And so while I like the point on the results, those are comparative results as opposed to absolute results. And I still say our absolute results are -- they're mediocre. I mean, in the context of our close rates are too high. And I -- before somebody says, gee, that sounds like a good problem, it's actually a bad problem because we don't compete for enough of the market.

So when we get in front of customers we tend to win. When you see win rates get too high you simply start looking at the fact that I need to compete for a bigger percentage of the business. So we are competing today for about 50% to 60% of the market and obviously we'd like to compete intellectually you'd think for 100% of the market.

And so for us that requires us getting partners and getting salespeople in front of more customers more often. And we've got a lot of work to do to get that right. I mean, if you went back through the history of the Company, the Company is an engineering and services company by trade. And I don't -- a very good one, one of the best in the history I think of the industry. But when we think about going to market -- and you'd think in five years that I/we would have done a better job on this. But we've increased the sales force over the last five years by about 50% and we're still loaded with opportunity.

So don't get me wrong, we have things to integrate still, we still have to get all of our services business integrated. We still have to improve pieces of our portfolio. But if I looked at the first five years we've spent $40 billion on R&D and M&A over the past five years. And that's put our portfolio in a completely different competitive position. And we've got to get our go-to-market model in the same position as our portfolio.

I'd also add, trending to our good is the fact the market is moving our way. I mean, when you look at it from digital content is now doubling every 18 months, data is doubling every four years. The cost of housing and processing and storing and moving and servicing this is going up. And so that pressure on IT communities is going to increase, it certainly plays to our strength. So I think that's the stuff we've got to work on. Secret message (multiple speakers).

Katy Huberty - *Morgan Stanley - Analyst*

Yes, apparently. You mentioned the sales figures and the growth in the sales force, you obviously have to continue to execute on that. But we just heard from Microsoft and you recently expanded (multiple speakers).

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

How are they doing?

Katy Huberty - *Morgan Stanley - Analyst*

I think they're doing well.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Good. Good news.

Katy Huberty - *Morgan Stanley - Analyst*

You recently expanded the partnership with Microsoft. What does that give you in terms of broadening the technology portfolio and the go-to-market advantage?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

You know, maybe I'll stroll so I can make connections to see out here too. But I'd say, listen -- with Microsoft, Katy, the relationship has never been deeper with them. We are their biggest customer. The depth of the engineering relationship is probably the biggest change I'd say over the past several years. Where now this new deal we just announced is us jointly putting about $250 million incremental together into different programs. And that's for us trying to better -- was Steve up here? Was Steve up here when he was here -- when Microsoft was up?

Katy Huberty - *Morgan Stanley - Analyst*

No.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Okay. I think Steve and I have worked -- we meet every couple months and really spend time not just trying to get our go to market right, but trying to intertwine our engineering programs. Management is a big area for us to get lined up, which we did. We're trying to optimize the performance, a very different piece of the software including the database exchange, etc.

So probably I'd say in the five years I've been at HP the two have never been closer. So I think very positive for us, we think a big opportunity to drive growth. We're making tremendous progress on the cloud activity. I will say I'm a little cautious on this term, cloud, because it means so many things to many different people and I've been quoted as saying I don't like the cloud. That's just not true.

I just think it needs get broken down into very discrete services and discrete offers that customers can touch. And a lot of what we did with Microsoft was all around sort of the new evolution of the technology of the cloud and discrete services we together can offer into the market.

Katy Huberty - *Morgan Stanley - Analyst*

So if you think about the positioning of your various product segments, where do you feel best about being able to go and take share in the near term versus where do you think there's the most work to do?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I don't want to compare each of our businesses (multiple speakers).

Katy Huberty - *Morgan Stanley - Analyst*

I'd like (inaudible).

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I'll have tons of fun with that internally. But listen, I think each of our businesses is in some ways very well-positioned. I mean, IPG, I heard you talking a little bit with Jim when I came in. IPG is about as well-positioned as we've ever had. And I'll talk about IPG just for a second.

We've spent a lot of time trying to get the supply chain right. When you ship three printers a second it creates a massive scale of things moving around. And when you're growing 8% or 9% a lot of warts in the supply chain tend to get hidden. When all of a sudden you have an economy like we had in 2009, those warts start to show up and we saw them in 2007, 2008. We've done a lot of work.

That's really important to us because not only does it make us more competitive to be able to go get more units, it opens up new markets to us. All of a sudden a $50 printer that cost us too much money to make now looks like an attractive thing to put in the market because the supplies connect to it, makes the whole system look positive. So actually it creates more total available market to us at the same time as it lowers our cost.

The fact of the matter is now in combination with innovation, we've done a lot of innovation in IPG that's started to yield more technology. For example, a wireless printer for us gives us 25% more productivity than a traditional inkjet printer. You put an inkjet printer at home, we get -- and then you consolidate to two or three printers -- from two or three printers to a wireless, we get 25% to 30% more pages out of that wireless printer.

So the innovation -- and wireless printers are now -- I won't give you a number, but think of them as more than a million units a year. It's becoming a material part of our portfolio. Now we have to ship less units to get more pages. Same thing with now what we call -- we talked about this Officejet, this is now going into the think what you would have thought of as low-end laser and we're now shipping Officejets into the kind of productivity that you would have had to laser to get before and we now get inkjet sort of ecosystem results as a result of it.

So the combination of the supply chain coming down and the innovation coming up, the fact that we can now take managed print services -- we had back to five years ago, we had no business in managed print services. Let me tell you what this is. This is like us going to a big bank and saying give us all your printing and we'll take 25% cost out of your printing ecosystem. We

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then get all the printing revenue of that company. All the supplies, it is 100% supplies connect. And we get all the services and we get that deal for five years.

So in IPG we've moved into new segments like MPS, we've built our graphics business which is very high-end, high productivity, 100% connect supplies business, we've opened up a retail photo kiosk business and we've just closed not only -- not only a very big retailer in the US, really big, but we -- I don't remember their name -- but we closed another really big one in the United Kingdom. Big one. And the two of them together, now this is huge because, again, those retail photo kiosks stay installed nine, 10 years and we get 100% supplies connect.

So getting that retail photo kiosk and the MPS and the graphics big, now with the innovation, now with the supply chain, puts us in a position now we can go gain share. And we can go gain meaningful share. And as you saw, one of the most encouraging numbers I thought we had in the quarter was we had a very, very sustained sellout of supplies with still a high unemployment rate.

And that's a very big deal to us because we've seen it come down. Now obviously the good news on the reported numbers if you've seen a convergence of reported and sell out. The actuality is we have some reverse hedging in our numbers because of last year that actually the supplies sellout is higher than the reported number. That will sustain for a couple more quarters, but underneath it you have a very strong sellout now coming.

So I think a lot of that, Katy, is just us putting the business in a position to compete. We feel very good about our networking folks, the ProCurve folks have put themselves in a very strong position. They've not only gained revenue share, they've gained significant port share. So you measure it two ways, number of ports sold and revenue, and they've gained in both.

Obviously we're very encouraged that 3Com since the acquisition announcement has gained as well. We don't have it closed yet; we've got US/Europe approval, we've got a couple of other countries we want to get. But we feel very good about that segment. Feel great about the server segment, obviously grown 27%. They've had sustained growth.

The best thing I can tell you about PSG and servers -- and PSG, I do want to say one thing about them. They declined last year in Q1 20%, Q1 2009. Q1 of 2010 and they grew 20%. So just to give you context, they're right back where they were in 2008 going through this entire economy, did it again on 5% operating profit. And more importantly, are giving the rest of our businesses, our server business, our storage business and our networking business, tremendous scale to leverage off of.

I would tell you PSG and server business though, if I looked across the Company over the next several years, one of the biggest improvements we'll make is in the supply chain. So with all the cost advantages that we think we have, we're a long way on an absolute basis from where we need to be. We still run our supply chain with over 400 locations to store capital -- materially above where it needs to be.

We still have over 300 applications running our supply chain, still have a lot of people running our supply chain, we still have various processes across each of our businesses, every region and every business unit has a different process for supply, for demand. So we have material opportunities for us to improve in the supply chain.

So I think our businesses, Katy, product side are all pretty well positioned. We've worked hard on it. Storage is a place we'd like to do better. We think the trends in storage are moving our way, internal storage now because of converged infrastructure, that's networking storage and servers integrating together. It's coming our way. And we can leverage the cost of our supply chain and industry standards, both trends we think play in our way.

What we've been able to do with left-hand networks, which is nothing more than software sitting on top of industry-standard components, has just grown through the roof. What's not growing is really the high end storage stuff. So our view is long-run to continue to push on this industry-standard storage piece.

The last piece I'll say is services. For us, we've done a lot of work to get ES in shape, that's enterprise services. We feel good about it. We've done what you would think you would do in the first four or five quarters of really blunt instruments to get the capacity right, to get the utilization right, to get the business stabilized.

I would say you should think of us in 2010 trying to make the business as opposed to good to try to make it great. Getting the processes nailed, getting consistent processes, consistent view of how we run a data center, consistent yield how we deliver a service. What our technology backbones are as we deliver Help Desk and Service Desk and try to put those in a sustainable position to compete and grow (inaudible).

We are not, let me compare that to running around the market trying to take every deal running around. We have a very, very strong pipeline right now in ES. But it is very important for us, and I can tell you we can show even better numbers growth wise if we wanted to just go get deals. We want to get good deals that are good deals in our portfolio for the next five years.

And so I will tell you that the only sort of wart I will tell you on this is you can imagine a bunch of services people that historically have looked at a business that looks like this and now look at a business that's positioned like this. And sometimes you get people who say, this is great, because you know these deals that didn't look so good before now look a lot better. And the point we continue to say is we actually want it to get better.

And so for us, we've got about -- we've still got some time to make sure we get those processes right. And so we'll be a little bit like we were in HP services. For any of you that followed the Company in 2005, we were very, very careful about what deals we took. We want to take good deals that drive profit at the same time as we get the business right.

That said, our pipeline is about as strong as we've -- well, it's as strong as we've ever had. But I want to make sure you understand our priorities. It's to get the business right. So that's how I go through our businesses real quick. Probably longer than you wanted.

Katy Huberty - *Morgan Stanley - Analyst*

No, perfect.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

That's how I position it.

Katy Huberty - *Morgan Stanley - Analyst*

Let me follow up on storage given that's an area you said you want to work on. You brought in a new executive to run storage and networking. You've made some acquisitions in both areas.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Right.

Katy Huberty - *Morgan Stanley - Analyst*

How much time are you going to give him to get the product set right, get the good market right?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Well, tough lady. We brought in -- I think it's Dave Donatelli you're talking about. He runs the whole server business, the storage business, the networking business. So he's got all of those pieces. He actually got -- he was in the penalty box for a couple months as he came in because of some -- a couple legal issues. He's only been on the storage thing really since January 1. So he's got another week or two before we expect to see a big turnaround.

So, I think Dave is doing an excellent job. I think he is driving on the converged infrastructure piece very hard. I think you've seen. continue to see Dave's got a very deep history in quality processes, supply-chain, go-to-market models. So, listen, I tell you, I think the business is in very good hands. I'd tell you we have our top people on it. But again, any business is not just one person, right? It's any more than it's the CEO or the CFO, it's a team of people.

I think it's a very strong team in that group. I think you'll see the server numbers continue to be strong. And let's not lose the fact that when you look at blades and servers, that hasn't been just one quarter, that's four years of continued gains in share position and I think gains and improvements in the business. And we think there's more to come.

In addition, in networking, I think you're going to see a very strong position. And in storage it isn't just about getting the raw storage numbers right, it's getting the value props right, aligning the storage with the server, aligning the storage with the networking capability, aligning into this converged capability so that we're offering one integrated set.

I think if Dave were here he would tell you that we are the only company on the planet that can offer the depth of competency in the networking stack, in the storage stack and in the server stack. And you might say, why is that important? Because those stacks are converging. And you have to have depth of IP in each of the three stacks. So when you start playing in the "cloud", nobody cares what's behind the curtain.

No one -- if I showed you some of the big cloud infrastructures, i.e. what -- Katy referenced Microsoft, you wouldn't see a -- if I showed you that infrastructure you'd say is that a server? Is that a storage device? Is that a networking device? And my answer would be yes, it's converged infrastructure. And that's why having IP in all three stacks is important. So we'll try to compete in each individual stack, but also across the stack. So, listen, we have high expectations and I'm sure, I'm sure he and the team are up to them.

Katy Huberty - *Morgan Stanley - Analyst*

In networking you obviously just made an acquisition yet to close.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Yet to close.

Katy Huberty - *Morgan Stanley - Analyst*

With 3Com. The skeptics questioned the lack of a brand, the lack of a big installed base in mature markets. What are those skeptics missing? And as a follow on, Brocade made an acquisition in this space. It's proving harder to get the revenue synergies. Why is 3Com different than that situation?

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Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Yes, so I don't know anything about the skeptics and all that stuff. I can tell you what we saw. We sold just pure great technology. So we took it in -- we took it into three places -- our engineering organization and networking; we took it into ES which is one of the biggest -- EDS which is one of the biggest networking consumers in the world, and we took it into our IT organization.

And imagine our IT group is zealots, zealots for another brand. When you tell them, listen, go test this stuff, our IT guys were like really as close to "no" as you could get. I had to tell them, listen, I'm not asking for your opinion, right, just go test it. When they came back, we want to swap everything. Costs down over 25%, performance up 30%.

By the way, just as importantly, when you look at L2 through L6 sort of networking spaces, a common management layer across all pieces, not these various different unique pieces of management software. Very innovative stuff with a very strong roadmap. So we, Katy, starts with just the raw technology. The raw technology was something we hadn't seen, it was different from anything we either had or saw in the market. So that's sort of point one.

Point two, as much opportunity as we have in increasing our go to market, we're not going to have any problem getting people to test it. So our issue coming out of the chutes will be we're going to have to be selective about where we do proof of concepts. So, we're not going to have any -- 3Com is not set up and this is one of the negatives we have to be careful of in an acquisition.

It's a little bit like what I described with the ES thing, and this is going to sound strange to you. When you come to a place like HP and you come from a place like 3Com it just looks fantastic. And if you're not careful you can get consumed very quickly with all the opportunity if you don't laser focus on the best one.

So all of a sudden having -- you're at 3Com and 100 companies say, come do proof of concepts. The discipline to say no, I'm going to go do 20 right is not the easiest discipline when you put it into an organization. It's a bit like our services funnel right now. Hey, did you know our services funnel is EX% bigger than it was before? I don't care. We want good deals. We want to focus on ensuring we scoped them right and nailed them, it's the same thing with 3Com.

So, Katy, I don't think we're going to have an issue with interest, that's by far our biggest -- our issue is going to be these proof of concepts will take a couple quarters to go through. You've got to go in and you have tests, you've got to get certified, you've got to get mail out, everything laid out to do transitions. I feel as good about that as we do about our ProCurve position.

And I hope our ProCurve position, I don't know about the other company you mentioned, but when you look at the steady improvement in ProCurve, it's been a doubling effect over basically two or three years, it's a steady stream of improvement.

So I would tell you there's a market out there that wants this kind of value proposition. There's a technology stack that we think is disruptive, we'll get plenty of it back. We have to make sure we keep the discipline to make sure we do this in a thoughtful way and don't get consumed with too many tests and just make sure that we nail this thing step by step. I think we're very optimistic about it.

Katy Huberty - *Morgan Stanley - Analyst*

One of the businesses that you didn't mention as you walked through the gives and takes and the positioning of each was software. You've made a number of acquisitions since you came to HP. Perhaps there is some integration left to build a platform and go to market? What are the priorities in software to accelerate growth?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Yes, I think they just need to sell more stuff. At the end of the day I think they've got a pretty good R&D pipeline, I think they've got a pretty strong value prop. They've sort of had sporadic share gains over the past three or four quarters. If you go look at one quarter they gained share, another quarter they're a little behind and they gain.

And I think, to be very blunt, we haven't done as good a job not just integrating the software, I think that part is doing pretty well, Katy, I think it's getting the sales force integrated because the history of us is -- remember, it's $40 billion in four years of R&D and acquisitions to put this portfolio in place. And not every account team has the same level of capability across each of our account teams, on top of the fact we've put 50% more salespeople out there at the same time.

So I think we still have the growing pain, if you will, of the absorption of the portfolio and that alignment into the existing sales force plus the new sales force that we brought in and get them as software and services centric as we possibly can. The pull effect on a services deal and a software deal is material when you get it right. So listen, in many ways I'm very pleased with the software folks, but they have to sell more stuff.

So if you looked under the covers, Katy, a lot of positives there. Remembering too for us, software is more important than just the software results you see on a P&L by quarter, software is a key automation tool for our services business. Remember, if you don't -- what we sell in software, we sell server automation, we sell storage automation, we sell networking automation, we sell data center automation, we sell the run time software on top of all that, we sell application testing, we sell application Q&A.

To give you an example what EDS is putting up right now is a SaaS, software as a service, testing capability. That now you as a small and medium business can test your applications through the infamous cloud through a data center. The alignment of that software business to our services business -- I just gave you that one example as the kind of huge opportunity that we've got.

When I talk to about automating the services backbone, that's all done with our software. So it's not just a separate business for us, it's an ecosystem. We've built this massive industry-standard supply chain leveraged by IPG, PSG, ESN across our company. Our software business is stacks of software that sit on top of that infrastructure and simultaneously automates our services business.

Now we want to sell each of the separately into the market and try to improve our business and gain share, but they also work together as one integrated ecosystem. So I think in many ways, Katy, our software business, because they've got multiple responsibilities, have done a very good job. I'd still like them to sell more stuff.

Katy Huberty - *Morgan Stanley - Analyst*

We have about five minutes left. So let me see if there's a question in the audience or two. Right here. Just wait for the mic.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

I can hear you.

Unidentified Audience Member

You mentioned converged infrastructure a couple times. Is that going into customer pilots, into production, is it really happening it or is it a nice thing to talk about?

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Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Well, it's clearly a nice thing to talk about, I think. We have pilots in probably 100 -- I won't even get into numbers, but it's in the hundreds of companies and there are real deals going down right now. I'd argue to you a product we call Blade Matrix is a manifestation of that converged infrastructure. You're going to find inside of Blade Matrix a storage array and a networking device.

Now at the same time, just to make sure I make it more complicated for you, we're selling a piece -- we have a software business inside our Blade's business called Virtual Connect. So Virtual Connect, what it does, it's software that sits on a blade that actually virtualizes the number of ports you need from a network perspective. So we're actually reducing the ports by selling you software out of the blade and, if you will, shrinking the networking total available to market.

We then want to come in with a better TCO and a better performance on the networking ports that therefore we haven't virtualized. And the reason I bring that up to you is there's going to be a bunch of these technology disruptive things that bring together the networking storage and server piece with software wrapped around it. And I'll tell you that if you look out four to five years, I don't think -- if you don't have depth of IP in each of these stacks you're going to be at a huge competitive disadvantage.

And so that's what I think when we talk about Dave and one of the reasons I think Dave wanted to come to HP was the realization of, hey, I can leverage each of these stacks with depth of IP and create an almost impossible to copy value prop.

So for us it's the blade space, it's the server space, it's the software in that space, it's the leverage of the storage back towards networking and into servers and the alignment of the networking to it. And we're frankly agnostic to whether you virtualize those ports and do it through the blade or whether you deploy more networking ports but want a better TCO on it.

And we'll show you the ways to do it either way that makes sense for you depending on your architecture and your position. So it is real. First of all, I'd tell you every company is talking about it. We have lots of tests out there now and we have literal orders that have shown up. So, it's real.

Katy Huberty - *Morgan Stanley - Analyst*

Any other questions? In the back here.

Unidentified Audience Member

Thank you. You mentioned virtualization. In your view how much of an opportunity or risk is desktop virtualization in particular to your PC business?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

We love it. The more virtualization for us on the desktop we think the better. One, obviously we've got the leading position in the thin client market so we obviously like it from that perspective. And thin clients have a significant amount of software in them, so it's obviously a great mix position for us in terms of the change in the mix. It also gives a tremendous amount of -- we have 21, 22, depending on your number of shares, position in the PC market into -- it virtualizes into a server market that obviously we even have a higher share position.

So we like the switch that if it in fact occurs. But I will tell you virtualization as a category, and I don't mean this to be negative, but it's another one of those topics technology companies come up with that when you go to the customer virtualization has created about as much sprawl in some as cases as it has efficiency in the process.

So I think like you would any of these terms like virtualization, like cloud, we need to keep a reality around it. I think you will see virtualization on the desktop. I think more importantly in big companies, while I think you're seeing a lot of corporate refresh beginning to kick up in the latter part of the year, I think you're seeing companies try to be a little bit more thoughtful about how they do it.

What kind of job requires a thin client? What kind of job requires a mobile unit, what kind of job requires a thick client as opposed to these big where I'm just going to replace everything with one type of solution?

So I think you'll see a mix of that. But desktop virtualization is in a -- it isn't a -- everything gets fixed with that. But we embrace it, we like it. We like to see disruption. One thing you can think about HP is we very much are against trying to protect legacy. We're all about standardization -- open, moving, changing because we believe if we don't do it somebody else will. So think of us as trying to be at the forefront of that.

Unidentified Audience Member

Great, thanks.

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

Thank you.

Katy Huberty - *Morgan Stanley - Analyst*

Let me just wrap up with one last question. We talked about several instances where you use HP's balance sheet to fill out the technology portfolio. You spend, aggressive at times, on share repurchases. How do you balance those two uses of cash in the next couple of years?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

So I hope you all think we do. We have a disciplined process about how we think of M&A. It's got to make strategic sense, it's got to make financial sense and we've got to be able to run it. At the same time we look at our shares, as I'm sure you can imagine, as extremely attractive. We're committed to zero dilution as a principle and zero dilution plus where it makes sense and we'll continue that path.

So I think it's like anything else, it just requires the management to be disciplined as we think we are. Make sure you're clear on M&A. We not only look at the disciplined process before we buy, we have a measurement system after we acquire as to the success per acquisition, per unit. And we hold our management accountable for those acquisitions. And we can tell you three years later whether an acquisition was a better use of capital than buying back stock.

And so we can actually tell you by unit, by group what deals have been literally accretive and the best use of capital and we can stack rank those relative to the quarter of our stock buyback, relative to an acquisition. And so it holds us all accountable for making the grade -- and every acquisition we make we compare to buying back stock. And we compare to of another type of use of the capital.

So, I think we have a disciplined process. We're not about to get any more lax on it. We feel very good about our opportunity to produce cash over the next several years. And it requires us to maintain that discipline which we'll do, Katy.

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Katy Huberty - *Morgan Stanley - Analyst*

Okay. We've run out of time. So we have to wrap up. Any closing remarks that we didn't touch on?

Mark Hurd - *Hewlett-Packard Company - Chairman, President, CEO*

No. I think we've hit on a lot of them. I mean, we feel very good about the work we've done to put ourselves in a position to perform. We've got growth opportunities, we need to go to nail those. To Katy's opening point, we still have cost opportunities, we have to go help fuel those, which we'll do. We will stay very focused on making sure we execute the strategy we've described and make sure we get it done. Thanks.

Katy Huberty - *Morgan Stanley - Analyst*

Thank you so much for your time.