

FINAL TRANSCRIPT

Thomson StreetEventsSM

HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Event Date/Time: May. 28. 2009 / 9:00AM ET

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

CORPORATE PARTICIPANTS

Mark Hurd

Hewlett-Packard - Chairman, President & CEO

CONFERENCE CALL PARTICIPANTS

Toni Sacconaghi

Sanford Bernstein - Analyst

Rod Bourgeois

Sanford Bernstein - Analyst

PRESENTATION

Toni Sacconaghi - *Sanford Bernstein - Analyst*

Toni Sacconaghi, I am the IT hardware analyst here at Bernstein. You may notice that I am up on stage and that is because we are now all victims of New York City traffic. Mark landed in New York this morning at 7.30 and has been en route and in the car ever since. So unfortunately he is within striking distance but literally not yet here.

So we are going to take a 10-minute break if folks want to get coffee and anything to eat. We will definitely not start for at least 10 minutes, but Mark is en route and as you all know his competitive spirit and his athletic prowess he may have to hoof it the last half mile. So if he comes in here huffing and puffing and in a sweat we will chalk it up to what we all like about in Mark.

So that being said let's take a 10 minute break I will get back to you and give you an update at that point. Hopefully, Mark will be here then.

Good morning again. We are in this highly uncomfortable situation where Mark is still stuck in traffic. He is expected to be here in about 15 minutes. So what we thought we would do in the interim given that we have a number of Hewlett-Packard -- people who are interested in the Hewlett-Packard company is I am going to start with Rod Bourgeois, our services analyst, and take any questions and try and provide an analyst's perspective on Hewlett-Packard.

I will set the table in terms of the kinds of things that I am hearing from investors and then, ultimately, Mark will come in and perhaps you will get the same or different answers from him in terms of what is happening at the Company. So, I apologize, it's obviously an unforeseen situation and I think Rod and I are going to be uncomfortable about who is going to sit in front of the sign that says Mark Hurd. But I am going to make Rod sit there.

I would welcome any questions that you have about Hewlett-Packard specifically. I will provide my perspective and what I hear from investors, and then hopefully Mark will come in and you will get that perspective as well. Sorry, it's kind of a poor substitute but at this point we are all victims of New York City traffic.

Rod Bourgeois - *Sanford Bernstein - Analyst*

This is working out great for me, by the way. To get to interrogate Toni is my life's dream I think at this point. So Toni, let me start with the insightful question of why is HP stock currently where it's sitting right now?

Toni Sacconaghi - *Sanford Bernstein - Analyst*

Boy, we had better get question cards coming up here fast if I have got Rod asking me questions like this.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Let me tell you what I hear from investors about HP's stock. HP's value proposition for investors over the last several years has been that it is an exceptionally well-run company with very strong and seemingly effortless EPS growth. And much of that has been attributable to Mark Hurd and his management style and his success to date. I think as a result of that earnings have gone up consistently and the Company was afforded about a market multiple associated with that.

I think what has happened over the last two quarters or so is that investor value proposition has been questioned. Investors have said, look, the notion that HP can facilely grow earnings is more in question now. The first-quarter revenue -- they missed revenue for the first time. That was uncharacteristic of HP. They lowered revenue guidance for the year and lower EPS guidance. That was uncharacteristic of HP.

And in the second-quarter they made their numbers but there was no -- they didn't raise numbers and revenue guidance for the full year was fractionally lower than it had been before.

And so I think investors said, boy, HP's ability to facilely make numbers and transparency and our conviction level in HP being able to continue to make numbers and grow EPS very helpfully has been called into question. As a result of that I think there has ultimately been multiple compression associated with it.

So if you think about the stock today -- and guidance is pointing to about \$3.80 in earnings, the stock is trading at \$34, so on that non-GAAP posted number the stock is trading at nine times earnings. The market today is at 15 times earnings. So you have gone from a stock that investors had been awarding close to a market multiple to a stock that is trading at a 35% discount to the market.

I think there may be some modest worry about where ultimately my earnings go but I don't think many investors think earnings are going to be below \$3.50. I think investors say maybe \$3.80 might be a struggle. It might be \$3.65 or \$3.70. So it isn't the notion that people don't believe the E, it's that investors are not affording HP the multiple that they were before.

Now my perspective on that is ultimately valuation matters. The more portfolio managers that screen stocks and look at well-run companies and say, wow, I can buy HP at nine times earnings and I can buy HP at eight or nine times cash flow, ultimately, I think you will get some reevaluation in that multiple. But in the short term the sentiment and the premium associated or the market multiple that it received before I think has been mitigated.

Rod Bourgeois - Sanford Bernstein - Analyst

All right, Toni, let's talk about the imaging business. How does the Imaging business fit in to that thesis and what is your outlook for Imaging?

Toni Sacconaghi - Sanford Bernstein - Analyst

Clearly, one of the big controversies around the stock has been the printing business. Some investors have told me look, Toni, I bought Hewlett-Packard because printing historically was 50%-plus of the profits and I viewed that as a highly predictable business. It was like a consumer goods company. I was buying P&G and if the economy turns south, people would still print and supplies wouldn't change and that is what generates all the profit.

Well, what has happened at HP is we have seen supplies growth go from plus 9% in the third quarter of '08 to about minus 14% in the just reported quarter. So we have had this dramatic deceleration and investors have said I don't understand. This isn't the printing business that I thought I wanted to own. This has characteristics that I would have not have anticipated.

So as a result of that I think there has been unease about what the printing business is. It's intrinsically more cyclical than many investors would have thought and I think there is a worry associated that the weakness that we have seen in printing may be

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

more than just cyclical. Maybe there are some secular of factors; that people are printing less in offices, that green initiatives are starting to take hold. The remanufactured cartridges are becoming more prevalent.

And so, again, in investors' psyches I think the notion of HP was something that I thought and imaging was key to HP or the printing business is not exactly what I thought has contributed to some of that unease. Now that said, my belief is the printing business is still a good business. That it is going to be a growth business going forward, albeit a single-digit and probably low single-digit growth business going forward. But it will be a growth business going forward.

The phenomenon that we are seeing in the Imaging business today is entirely cyclical. I really don't think that secular trends occur in two quarters and the precipitous decline that we have seen in supplies growth has happened in two quarters. People don't change 25 years of printing behavior in two quarters. That by definition can't be a secular factor.

At the margin is there a little more remand today? Yes, just like there is more private-label food being sold today. But at its core I think the printing business is a low single-digit grower. I think, ultimately, it will recover to levels that we have seen from a profitability and sustainable growth perspective and that it is not secularly impaired.

Rod Bourgeois - Sanford Bernstein - Analyst

All right. So your clients are giving me some good interrogation material here.

Toni Sacconaghi - Sanford Bernstein - Analyst

Okay. I just keep praying that Mark is going to walk in the room. No one will be happier to see him than me.

Rod Bourgeois - Sanford Bernstein - Analyst

Well, we compare him to Gershner. We will let him walk in the room. Compare HP Services vision relative to IBM's Services strength.

Toni Sacconaghi - Sanford Bernstein - Analyst

Well, I think my belief is that -- I am a hardware analyst. That is my title by trade, but hardware is a crappy business to be perfectly frank. I am lucky I am still employed. But hardware over time ultimately commoditizes and margins decline. What I think many of the companies that I follow have done to recognized that and said value migrates from hardware to software and services. And, ultimately, we have seen that in the portfolio changes of many of the companies that I follow.

IBM has transformed itself over the last 10 years to a services and software company where 90% of their profits are coming from services and software. EMC went from a company that was essentially 80% hardware to a company that is essentially 45% hardware today in seven or eight years. That same kind of evolution is happening at Hewlett-Packard.

They bought Mercury, which was a significant software acquisition, for \$4.5 billion. They bought EDS, which was a \$13 billion services acquisition, in the spirit of migrating away from hardware and building a set of solutions. The solutions tend to have more recurring elements to them and are more backlog driven.

In general, they don't face the same kind of commoditization and pricing pressure as hardware businesses. And so I think the vision of migrating a portfolio to a composition of value-added services that have better margin characteristics and better recurring revenue is something that HP is following.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Now if you look at the portfolio compositions of the two, IBM has a large consulting business. It's about \$20 billion. HP has a small consulting business, about \$3 billion. On the outsourcing side they are roughly equally sized so they are both about \$20 billion so from a managed services outsourcing perspective the companies are very similar. From a consulting perspective, which typically is shorter term contracts under one year in duration, IBM has a significantly broader capability that extends back to the fact that they bought Price Waterhouse Coopers in 2002.

Rod Bourgeois - Sanford Bernstein - Analyst

So HP has got a good ways to go on the services front?

Toni Sacconaghi - Sanford Bernstein - Analyst

On the outsourcing side I would say pound for pound, size wise, capability wise they are pretty similar. On the consulting side, yes, the breadth and size of IBM is significantly larger.

Rod Bourgeois - Sanford Bernstein - Analyst

Great, all right. So what should we make of HP and Cisco's falling out and potentially becoming major competitors?

Toni Sacconaghi - Sanford Bernstein - Analyst

Well, I think this is a good question for Mark and I had planned to ask it.

Rod Bourgeois - Sanford Bernstein - Analyst

I am asking you the question.

Toni Sacconaghi - Sanford Bernstein - Analyst

Here is my take. HP and Cisco used to have a fairly cozy relationship. Carly Fiorina had been on the board of Cisco and HP sold networking gear. But I actually went and backtested this, and HP never mentioned their networking business on 20 straight conference calls between I think it was 2000 and 2004. Ne'er a mention and it was a \$500 million business and it was hidden in other businesses.

The business was ostensibly for sale for a period of time and not viewed as strategically important. Basically, what happened is when HP sold servers Cisco ultimately came in and did the networking. Now what happened, I think, about the time that Mark became CEO at HP was he said look this is a very valuable asset. We have a networking business called ProCurve. It's a valuable asset. We should be leveraging it more.

And so what HP has done over the last several years is what I think intelligent businesspeople would do which is try and expand their addressable market. I think to a certain degree Cisco has lost that privileged reference position that they had and perhaps in response to that had said we need to ensure that we continue to get networking businesses out of corporate data centers. And so if you look at Cisco's business about a third of it is enterprise, about 70% of it is service providers.

But if 30-year business from Cisco is ultimately selling in to enterprises and that enterprise business used to be referenced by HP, but HP is now going to hold and capture some of that business, that scares them. If a CIO is building a data center, the first

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

person they call is the server vendor. And that server vendor is HP and HP is going to capture the networking, you are feeling left out if you are Cisco. So I think Cisco moved into the server market as a result of that.

So what we have now is Cisco saying I want to be one of the first calls when someone is opening a data center. I want to get the call for the server and I am going to provide the networking. HP is saying the same thing. Hey, I can give you the server and I can give you the network. And so what we are having is we are having a confluence, a migration in offerings between vendors and I expect that to continue.

People are getting into each other's business and when that happens people feel like their toes get stepped on. Competitive juices start flowing and clearly I think that probably characterizes the situation that exists between HP and Cisco. They were cozy partners before and now they are competing much more aggressively on both sides of the business.

Rod Bourgeois - Sanford Bernstein - Analyst

Nice. A couple of questions about whether there is an IT spending recovery occurring and let me just give some context. We hosted an IT services conference just a couple of weeks ago. Eight out of the 10 companies basically said the worst is behind us in terms of cuts to discretionary spending, and in terms of ramp up on maintenance-related deals basically cost savings-related contracts there is very good trends happening in that part at least in my sector.

What are you seeing in the hardware side in terms of an IT spending recovery or is there a recovery?

Toni Sacconaghi - Sanford Bernstein - Analyst

If I had to characterize IT spending I think US is farming and may actually be getting fractionally better. I think the evidence from China is that government stimuli are working and China had a very strong quarter across the hardware space. I think Europe is the big question mark. I think it's flat to actually getting weaker.

And so when we think about that US and China are about 50%, 55% of IT spend. You have half the world or a little more getting fractionally better and you have half the world or a little less getting flattening or maybe getting a little bit worse. So I think IT spending is not going to get worse. The question is it going to get any better.

I am not sure it's going to get materially better before the end of the year. In Q4 you have an easier comp so IT spending is going to get better on an OpEx basis, but from a spending perspective I think we are going to have a relatively slow and modest recovery. But I don't think we are going to get worse.

What is interesting is the stock market feels like we are going straight up from here. I certainly don't disagree that we are going to go straight down from here but I think we are going to trickle along the bottom for a little while.

Rod Bourgeois - Sanford Bernstein - Analyst

Great. What are you watching to get a read on how the tech spending environment is playing out? Are there some leading indicators that you are focused on right now?

Toni Sacconaghi - Sanford Bernstein - Analyst

I look at corporate earnings. I think if you look at corporate earnings that are really good; [bleeding are coincident indicator] for technology spending. And so we have observed before that corporate earnings went negative in the third quarter of '07, tech spending started to slow down about one to two quarters later.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Corporate earnings are supposed to pick up in the third quarter of this year. We think that tech spending will start to pick up zero to two quarters later than that, so we are looking between Q3 '09 and Q1 2010 for tech spending to pick up. So that is kind of how -- that is one of the very simple leading indicators. If you look at S&P 500 earnings and the rate of change of earnings growth, we think that is a simple leading indicator for technology companies.

Rod Bourgeois - Sanford Bernstein - Analyst

Great. Will HP be a net beneficiary from low-cost PCs gaining share of the PC market?

Toni Sacconaghi - Sanford Bernstein - Analyst

This is a really contentious topic and I am fascinated by it because I think low-cost PCs will become more and more prevalent going forward. So you can do almost anything you need to do with a \$400 computer today. There is a proliferation of different kind of offerings that ultimately -- I am getting the two-minute signal so that is an encouraging sign. Mark is probably on the premises.

So I do think that you can get very good, high functioning PCs for \$400 and I think there are myriad offerings on the processor side that will enable that going forward. So ASPs for PCs are going to go down and probably go down at a more accelerated rate going forward. That is not good for the revenues of PC vendors.

Now that said I actually think there may be an opportunity for PC vendors to boost margins going forward, because I think PC vendors are consolidating around the two or three big vendors. And they are going to have a lot more power and they are going to have a lot more choice in terms of picking an Intel processor or an NVIDIA ION platform or a Qualcomm Snapdragon platform. I think you are going to see alternative operating systems largely in the Linux forms going forward.

So if you are a very dominant PC vendor, like HP or Dell will be going forward, I actually think you have the opportunity to be much more of a shaper and extract higher margin from your suppliers. Historically, Intel and Microsoft got all the margins in this industry. I think with new competition in both software and hardware and the processor side you are actually going to see the PC vendors extract more money going forward.

So I expect ASPs for PCs to go down, perhaps more steeply than they have in the past. Conversely, I think there is an opportunity for PC vendors to flex their muscle and actually improve margins.

Rod Bourgeois - Sanford Bernstein - Analyst

Great. Why shouldn't all Street analysts use GAAP EPS for HP given that that would allow for better apples-to-apples comparisons across the different stocks?

Toni Sacconaghi - Sanford Bernstein - Analyst

This is a little bit of a religious war. HP is non-GAAP so the \$3.80 consensus number is non-GAAP. That includes about \$0.15 of restructuring; it also includes about \$0.55 of amortization of intangibles. So that \$3.80 number on a GAAP number is somewhere around \$3.10.

So if you were going apples-to-apples HP's GAAP number is \$3.10. That is what you should compare against IBM's \$9.20 number. I think if you are trying to model cash flow though non-GAAP number may be more appropriate.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Is \$0.50 of amortization intangible something that you should penalize HP for? It's capital that has already been spent on acquisitions. Should you take that out of future earnings? Arguably that is not representative of normalized cash flow. So to make your life simple all GAAP earnings is the easiest way to look at it and HP's first call number should be discounted.

I think the prudent thing to do is actually to look at all numbers on a cash flow basis. It just involves a lot more work. Cash flow is very hard to normalize and to figure out, so most people go by earnings. But I think penalizing for amortization of intangibles, particularly in the HP's case, is overly punitive.

Rod Bourgeois - Sanford Bernstein - Analyst

For the longer-term investors out there, what are big longer-term trends that you think are going to be most impactful on your coverage universe? Do we think about cloud computing or is that too cloudy of a question?

Toni Sacconaghi - Sanford Bernstein - Analyst

I think there are one or two really big secular themes. The first one is convergence and convergence into handset devices. The amount of stuff that is going to go into your cell phone over the next five or eight years is going to be industry redefining. Navigation is going in, gaming is going in, camera is going in, video is going in, music is going in. The convergence and devices and the value migration from separate devices to this device is going to be significant.

So I am getting a lot of nods and Mark is here. Thank you for helping out.

Rod Bourgeois - Sanford Bernstein - Analyst

All right. Excellent. I guess I have given Mark an easy comparison behind his name tag.

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Hi, Rod. How are you doing?

Rod Bourgeois - Sanford Bernstein - Analyst

Good to see you Mark.

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Yes, I love this city but I don't miss some of the things.

Toni Sacconaghi - Sanford Bernstein - Analyst

You have to humor us with a 30-second summary of how painful your commute in was.

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

You know, I got in here so early with about a little over two hours to get here. And I am what 2.5 so -- sorry.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Toni Sacconaghi - Sanford Bernstein - Analyst

I am going to plunge right in. Mark agreed to do a fireside chat. So Mark maybe you can start by giving us your perspective on IT spending for this year. How do you see demand playing out? And if you had to pick a letter of the alphabet to describe the shape of the recovery what might that letter be?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Maybe an E. No, Toni, I think in Q2 we saw -- the fact that our revenue was basically right on what we predicted 90 days out I think was a positive sign in the sense of stability. The fact that we could predict \$27.350-some billion 90 days out and hit that is a positive thing compared to what we saw in Q1 which was, frankly, a roller coaster from the beginning.

We saw good signs in China, which was material enough to comment on. We saw some better things in US consumer. So I think we saw a more stable market, yet a stable market at a lower level than any of us would like. At the same time the build up now of four-year-old desktops, four-year-old notebooks, four-year-old servers; I mean, this is creating quite a bubble. And so we sort of feel like there is going to be a time where there is going to be some real opportunity here.

I am not going to predict for you when, Toni, because I think people are trying to squeeze their budgets for as much as they can get out of them. But as you have seen from the share numbers, we feel pretty well-positioned to take advantage of it when it does occur.

I will feel better about it when I see signs more consistently across Europe. We have seen some good signs that we have talked about, but I would like to see it across more markets to really feel as good as I think people are hoping for.

Toni Sacconaghi - Sanford Bernstein - Analyst

I am going to try rapid -- use this as a rapid fire session given the limited time.

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Okay. You need me to answer quicker?

Toni Sacconaghi - Sanford Bernstein - Analyst

No, actually that was pretty good so keep answering like that.

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Thank you, Toni. Thank you.

Toni Sacconaghi - Sanford Bernstein - Analyst

What is your conviction in your revenue outlook? And I ask this in the context of your revenue forecast for the full year initially was obviously -- was off and the market decelerated much more rapidly than anyone expected. Even this quarter you hit your revenue numbers right on. At the margin you were a little -- at lower end of your previously guided to range for the year. Not a big deal, but again enough that investors made note of that.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

So how should investors, given there is a small asterisk beside revenue performance in the last two quarters on an otherwise pretty unblemished record, how do you feel about revenue, your conviction around revenue outlook going forward given the uncertainty of the environment?

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

I think we are very confident in EPS. We have generated a cost structure that we feel really good about. And I might add because I have also heard comments about that, that it's a very sustainable cost structure that I think will bode well for us as the market is rebounding.

I am not as revenue-centric, Toni, in the way I think of this current environment. My view of these recessions maybe is better said this way. You prepare your cost structure before you get into one of these to be when you are going through one of these. So you do the cost structure during good times to take advantage of it in a bad time.

During these times you prepare to go broke and it's really the growth is what comes out of this is more interesting to me. Short term we are not going to do crazy things just to drive a revenue number, Toni. So I would be more focused and confident in EPS as we have said all along. Now at the same time we have been gaining share and I would tell you -- you see the share numbers. Service share numbers are out today and those are good numbers for us.

I take those as a mixed bag, Toni, because we have not been pricing to gain share. So the good news is we are gaining share, the bad news is we are gaining share which tells me the market still is perhaps not as strong as we predicted in some of our modeling. So it's good news and bad news, but we are very confident in EPS. And the revenue we will see how it goes. I do think you are seeing a little bit more stability in the market as I mentioned earlier, so that is the way I would take our forecast, Toni.

Toni Sacconaghi - *Sanford Bernstein - Analyst*

How do we think about more normalized environment? You mentioned that certainly in this kind of an environment your focus is on delivering EPS. You have articulated previously a longer-term model, a more normalized model of 4% to 6% revenue growth for the Company and earnings growth that is significantly better than that. Has this downturn or your tenure at HP changed your outlook or the potential for this company on a normalized longer-term basis?

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

No. Rapid fire, right?

Toni Sacconaghi - *Sanford Bernstein - Analyst*

Okay.

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

Rapid fire.

Toni Sacconaghi - *Sanford Bernstein - Analyst*

Five years from now how different is HP's portfolio composition from today?

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Well, maybe a better question -- I don't mean to reword your question, it was a great question, Toni -- would be how the market might adjust. Because I think that we see the world of infrastructure -- let's just take that for a second -- of server, storage, and networking -- and you do a lot of analytics, Toni. The market sizes and raw revenue sizes are roughly equivalent. They are within \$10 billion of each, but the gross margin profiles are very, very different in terms of industry gross margins.

We increasingly see those three sectors having two common things -- using more and more industry standards starting at standard high-volume components and being sourced similarly. Today's storage, average storage industry components is probably less than 40%. We think we can take that north to 90%. Networking, very low; we think we can take that north of 90%.

So if you want to compete in the infrastructure business five years from now you better have massive scale leveraging industry-standard components, which we think will be x86-oriented; standard power supply, standard cable, standard hard disk drives, etc. Wrapped in software, management software tools and delivered potentially through Services via the Cloud or via on-site services. And that is the strategy we have built, Toni.

So when you look at how our portfolio will change -- I also believe those products won't necessarily be delivered as a server, a storage device or networking device. They will be delivered sometimes as hybrids like what we have released with Matrix, which is the first Cloud infrastructure in a box. A server, a storage device, and a network device all integrated together.

So we feel great about our portfolio. We feel great about our software position. We feel great about our Services position. The EDS position, we think, is for all of the Oracle, Sun, Cisco, stuff you hear out there. The most transformational acquisition I would say out there has been HP buying EDS. The opportunity for us to now deliver our services with the scale and the capability we now have has dramatically changed our position.

I am not telling you our portfolio won't adapt some but our organic capabilities now are unlike anything we have ever had.

Toni Sacconaghi - Sanford Bernstein - Analyst

Let me push on the question about industry-standard components, storage, and networking. Is the implication of that that margins are going to come down? Those are historically high-margin businesses predicated in part on proprietary ASICs or whatnot. Is the implication that you are an attacker to lower margins ultimately over time as industry standard becomes more prevalent, just like what happened in the server space?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

So I think, Toni, you have got -- rapid fire. So I think what we did to the server business and the server market, which is now over 60% industry standard, you should think of us doing to the storage business and to the networking business.

Toni Sacconaghi - Sanford Bernstein - Analyst

With all the margin repercussions associated with that as well?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

Yes, sir. I believe that is what customers want. Customers are asking for value to be unlocked. You have got to have the scale to be able to deliver those capabilities across all of those segments. And customers increasingly want leverage and they increasingly want the flexibility to integrate those capabilities across those various pillars.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

I don't think -- unless you have got a play in all of those segments -- if you are in the storage business and you are not in the server business and you are not in the networking business, it's tough. If you are in the networking business, you are not in the storage business, you are not in the server, it's tough.

And you have also got to have scale. Then it's not going to be good enough just to have the components, you have got to have the software differentiation that sits on top of the platform. And then you have got to have the choice point to deliver it on-site to the customer so the customer can execute or deliver it and provision it through a service. Toni, that is the strategy we have been building for four years. We feel uniquely capable to deliver it.

And I think this recession is a timeout, so to speak, and during this we have been trying to get our cost structure right, sustainable, and invest in growth because we are trying to prepare for that growth. Now is the time you prepare for it. You don't deinvest in growth now, because when it comes you are not prepared to take it. So that is why this second the revenue number is -- it's relevant, but it's not the most important thing on my mind.

The most important thing on my mind is having our cost structure right, delivering the investor-appropriate returns from an EPS perspective, doing the best we can from a share position, but getting ourselves positioned for what we think will be a pretty material opportunity for us.

Toni Sacconaghi - Sanford Bernstein - Analyst

Regarding acquisitions, do you have a relatively hard-and-fast rule that HP needs to fully digest an acquisition before making another? When you bought Mercury you said we have to digest it. We think it will take a year. Is that a pretty well hard-and-fast rule?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

It's hard and fast in the context that we have a very rigorous filter for acquisitions. It has to make strategic sense, it has to make financial sense, and we have got to be able to do. So if there is an acquisition that we are executing that we can't digest then, yes, that would be a thing that would stop us from acquiring. Because you don't acquire something and mess it up, you acquire something to unlock more value. So that is what we are doing.

Toni Sacconaghi - Sanford Bernstein - Analyst

And when is EDS largely complete in terms of being a significant capacity absorption --?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

We are making good progress on it. I think we have got another couple of quarters, but I would not want to -- first of all, I think the acquisition has been a home run for us really. I felt good about it when we announced it. I know not everybody did. I felt better about it when we closed it in September. I feel great about it now.

Second, I would not take the completion of the EDS integration as a smoke signal from HP that we are now looking for another acquisition. We feel good about our organic capabilities. Now we will continue to always look at what is in the market, but the daily rumor of who it is we are buying today I can tell you seems a bit overblown.

We feel very comfortable with our organic capabilities. If in the end it showed up that we bought nothing else, we feel good about our organic position. And don't take that statement as we are not or we are, it's just I want to make sure it's clear we have

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

a very rigorous filter on how we execute M&A. We think we are very disciplined about it and I think our track record of performance in M&A shows that. At the same time if there isn't something that fits that filter we won't be doing an acquisition.

Toni Sacconaghi - *Sanford Bernstein - Analyst*

Given your aspiration in the enterprise market, servers and storage and networking, the one area from a market share perspective where you have the lowest share is networking. You obviously have a great foundation in ProCurve. Do you feel that with the industry standard scale that you have and with the ProCurve business that you have a sufficient footprint and sufficient capability to execute your vision in that market? Or do you need to partner and acquire going forward?

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

Well, I think we will always evaluate our position, Toni. I think ProCurve is a very strong franchise. We have added a wireless capability to it in the last eight to nine months. We are leveraging a lot of our capability from our general industry standard platforms and integrating our networking capability with our server capability with our storage capability so we have a very, very strong base to operate from.

We will always continue using the same filter I described earlier to evaluate opportunities that are out there, but we feel good about the position we have got.

Toni Sacconaghi - *Sanford Bernstein - Analyst*

I am going to ask you two more questions.

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

Sure.

Toni Sacconaghi - *Sanford Bernstein - Analyst*

You talked a little bit about the longer-term model not changing; revenue 4% to 6%. Is there a mental model in your head? HP is a \$110 billion company, given that kind of growth rate what HP should be able to on a sustaining basis do in terms of either EPS or cash flow growth?

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

Well, EPS growth will be higher than revenue growth. And I know that wasn't where you wanted me to land.

Toni Sacconaghi - *Sanford Bernstein - Analyst*

Not at all. Major let down on that one.

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

But, listen, at the end of the day we spend more than \$100 billion a year so it's a massive spend pool. We are better at it than we were and not as good as we need to be. We have big opportunities and we are in the early -- the EDS acquisition has brought

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

a whole new set of inefficient costs, maybe that is the way I will describe it. We tried to be transparent about the real estate opportunity in the last quarter.

The opportunities that exist today in Technology Services, which is one of our big Services businesses, in EDS itself and our overhead structure now combined with the EDS overhead structure in IPG, we have now moved what was a mid-inning sort of process around HP to in some cases -- some of those cases, early innings again for us in terms of getting our cost structure right. So we have opportunities to do that.

In addition, the mix, the way I just described to you the evolution of the market, those margin pools, while you talk about them in terms of the market getting interrupted the way we did with the server pool, that is upside for us. That is more margin than we get today. So when we look at the opportunity for us to do what we think we can do in those other segments we think we get an opportunity to affect productivity with the cost structure, but also our mix from a margin perspective at the same time.

So if you can get that kind of revenue growth, drive up productivity, and adjust mix, we think our opportunity to improve EPS is material.

Toni Sacconaghi - Sanford Bernstein - Analyst

In light of what you just said, we can get margin expansion; we have got a lot of costs to work on. You obviously buy back a lot of stock. I mean, to me if you are growing revenue at that kind of level doing double-digit EPS growth should fault out of the qualitative description that you just described. Is that not an appropriate inference?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

I think we have got a good chance to improve EPS, Toni. I really do.

Toni Sacconaghi - Sanford Bernstein - Analyst

Last question, you have 200 investors in the room. Investors always want to know about stocks. In a minute and a half what is the value proposition to investors about HP given where the stock price is right now and given where we are in the economy?

Mark Hurd - Hewlett-Packard - Chairman, President & CEO

The stock price is low. I have got to tell you I am not happy about it. I don't truly understand it. We deliver. We do what we say. We have got a big market in front of us. We have got a tremendous technology portfolio. We believe we have invested properly to line up for what should be a boon; I can't tell you what time that is going to come. The aging of the infrastructure is there, we can see it. We know there is an opportunity when you recover.

You are buying into a company with a very, very focused strategy that has a cost structure that is yet improving, that is sustainable, that we believe we have margin pools we can attack in the industry and take advantage of. We have now got a Services business that now we can add to our portfolio as another crown jewel. So I think when you look at stocks you look at strategy and management, and I will tell you this we won't try to embellish the opportunity. We will try to tell you what it is and we will deliver on what we say. And I do think that is a solid value proposition, Toni.

Toni Sacconaghi - Sanford Bernstein - Analyst

Terrific. Well, thanks very much for being here, Mark. Appreciate your efforts for being here.

May. 28. 2009 / 9:00AM, HPQ - Hewlett-Packard at Sanford C. Bernstein & Co. Strategic Decisions Conference

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

Sorry for being late. Thank you.

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