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MARKET CALLS

Earth to Techstocks: "Your 15 Minutes Are Up"

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Oracle beats, but the tech sector will still get beat up. The focus of economic recovery is elsewhere.

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Andy Warhol said that everyone gets 15 minutes of fame. After the market closed yesterday, technology investors got 15 minutes of hope from **Oracle**. And that's *all* they got. It's a perfect example of why we're still cautious on technology stocks, even as we're beginning to get bullish on US equities overall (see "Normal Valuation: Where Do We Go from Here?" June 11, 2002).

Right after the bell yesterday, Oracle -- whose off-cycle fiscal calendar always makes it the first big technology company to report in any earnings season -- put out a press release announcing that it earned $0.14 a share for the most recent quarter, $0.02 better than the consensus. Never mind that these results exclude the now-typical (yet nevertheless "non-recurring") investment impairment charge. And never mind that Oracle's guidance for this quarter had been widely acknowledged to be deeply sandbagged all along. All that mattered was that the bulls got their headline -- *"Oracle Beats!"* -- for 15 lovely minutes.

But then the 15 minutes were up, and the headlines from planet Earth started to get beamed in. **Advanced Micro Devices** announced its revenues for the current quarter could fall short by as much as $280 million, or 31% of previous guidance. A few minutes later, **Apple Computer** announced its revenues for the quarter could fall short by as much as $200 million, or 13% of previous guidance Then **Intel** announced a $100 million charge to discontinue its web-hosting business, filing that expensive little diversification brainstorm away forever in an increasingly well populated folder labeled "It Seemed Like a Good Idea at the Time."

By the time Oracle's conference call finally started an hour or so later, the 15 minutes of hope was pretty much forgotten. Yes, Oracle tried to keep things going with a second press release (a non-financial one, and thus operating outside the already low standards of what passes for truth nowadays) trumpeting customer wins in the last quarter, and stating "Oracle continues to see momentum for the latest releases of its products..." But in the conference call all that so-called momentum wasn't enough to keep Oracle from lowering guidance for the coming quarter (by the same $0.02 that they beat the last quarter), and muttering about how it's a "tough environment" and "visibility remains limited" and so on and so forth. If only real life could be like press releases...

The technology sector remains the most overvalued sector in the US equity market. Combined with telecom, it is showing no earnings recovery whatsoever. These most growth-sensitive sectors of the economy are still reeling from the wounds inflicted upon them during **Alan Greenspan's** misguided deflationary jihad against irrational exuberance. High valuations mean

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that investor hopes are still springing eternal, as though in some great unrequited love affair. As last night's shenanigans show so clearly, such things always end in tears.

But the overall market hasn't had to bear the weight of such hopes, and has now become fairly valued for the first time since those brief buying opportunities in September 2001 and October 1998. And at the same time, earnings outside of technology and telecom are recovering strongly -- and without any particular fanfare -- back now to within a mere 3% of their all-time peak. The less growth-sensitive sectors of the economy were less wounded to begin with, and will be the first to recover.

This isn't the way we'd like to see things developing. The best kind of economic recovery would be led by the economy's most innovative sectors. As it is, those sectors will have to bring up the rear, delivering investors disappointment after disappointment while companies that are straight from dullsville raise guidance, as **McDonalds** did on Monday. As long as that's the pattern, any recovery will deliver far less than the US economy is capable of.

But we don't deal the deck -- we just play the percentages. By the time the technology sector starts to recover, techstocks may finally have fallen to fair values, and we don't want to ride them down for that last leg. In the meantime we'd rather start positions in fairly valued or undervalued stocks in sectors where earnings are already recovering. It's practically a gift that recovering sectors are cheap, while stagnating ones are expensive. Is that gift going to be available for longer than 15 minutes? TM