

Dell's 2Q10 Results Show Continued Weakness in Hardware Market

Adrian O'Connell

Dell's fiscal 2Q10 results confirm that weakened demand continues to affect the hardware market. Although the market hasn't improved significantly since the previous quarter, demand appears to have stabilized.

Event

On 27 August 2009, Dell announced the results of its second fiscal quarter 2010, which ended 1 August 2009. The company reported earnings per share of \$0.24, according to generally accepted accounting principles (GAAP), with net revenue of \$12.8 billion. Dell's revenue declined year to year by 22%. Broken out by product segments, desktop PC revenue declined by 33%, mobile by 21%, servers by 19%, storage by 20%, services by 11%, and software and peripherals (S&P) by 15%.

Analysis

Dell's fiscal 2Q10 results are in line with reports from other hardware vendors and offer further evidence of a continued weakness in demand in the hardware market. Dell's units increased by 10% over its previous fiscal quarter and its revenue by 3%, which is a sign of the stabilizing levels of demand that Gartner has observed in the hardware market. Despite tough market conditions, Dell achieved an operating income of \$671 million and ended the quarter with \$12.7 billion in cash and investments. Again, as during fiscal 1Q10, Dell did not say that it sees signs of imminent improvement in demand; however, the company stated that it expects increased demand from a hardware replacement cycle at the end of the calendar year and during 2010.

Dell's forecast is consistent with Gartner's view of the rest of the hardware market and broader patterns of demand. Gartner's most recent IT market forecast sees revenue declining 16.3% in the computer hardware market in 2009 before improving in 2010 (see "Dataquest Insight: IT Spending Growth for 2009 Revised Down Further to Minus 6.0 Percent"). Gartner expects the PC replacement cycle to start at the end of 2010 at the earliest, which will coincide with Windows 7 deployments by midsize and large companies. Gartner believes Dell is coping with shifts in purchasing patterns in the hardware market, but could bolster its overall strength by expanding into complementary market areas.

Dell faces two challenges:

- Managing its business during the current environment of economic weakness
- Wrestling back share from its competitors in the key market segments that it addresses

Dell has made significant advances as a result of its tight focus on costs. Operating expenditures were down 14% year to year during its second fiscal quarter, representing further improvement in cost control. Dell also stated that 40% of its overall volume now passes through contract manufacturers, which will help the company regain its previous efficiencies and align itself with the current market, as the PC market is increasingly based on preconfigured processes.

Dell also stated that Brazil, Russia, India and China (BRIC) made up 10% of its revenue in the quarter, declining 17% year to year, but increasing 16% sequentially. The BRIC countries and other regions represent a substantial opportunity for Dell; its business still skews toward the U.S., which accounted for 45% of Dell's PC revenue in calendar 2Q09 (compared with 30% for HP and 24% for Acer). In 2010, however, Dell may benefit from its U.S. presence, as Gartner expects the U.S. market to recover earlier than EMEA markets.

During fiscal 2Q09, revenue from Dell's Large Enterprise unit declined year over year by 32%, Public declined by 16%, SMB declined by 29% and Consumer declined by 9%. The weakness of the Large Enterprise unit is in line with trends in the hardware market overall, and can be traced to organizations' deferral of projects and extension of their system life cycles. Dell's EqualLogic

business and its reinvigorated blade server line offer some bright spots, but Gartner believes that if Dell seeks to regain share from the competition, it must continue to improve its positioning in enterprise systems. Gartner's preliminary server findings indicate some improvement, as Dell's share of 2Q09 server volumes increased to 23.8% from 22.2% in 1Q09.

RECOMMENDATIONS

Dell customers and prospective customers:

- Use the current downturn to drive aggressively for improvements in contract terms. If you are willing to make purchases now, you still have a good opportunity to negotiate, even though vendors are seeking to maximize their current levels of revenue and profitability during the economic downturn.
- Continue to consider Dell as a viable supplier of IT hardware.

RECOMMENDED READING

- "Dataquest Insight: IT Spending Growth for 2009 Revised Down Further to Minus 6.0 Percent" —The rise in the value of the U.S. dollar, low consumer confidence levels and continuing IT budget cuts continue to affect Gartner's forecast for IT spending growth in 2009. **By Richard Gordon and others**
- "Vendor Rating: Dell" — Dell is continuing to retune its organization and investments in response to global economic challenges and to the general move away from highly standardized hardware purchasing. **By John Enck and others**

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REGIONAL HEADQUARTERS

Corporate Headquarters

56 Top Gallant Road
Stamford, CT 06902-7700
U.S.A.
+1 203 964 0096

European Headquarters

Tamesis
The Glanty
Egham
Surrey, TW20 9AW
UNITED KINGDOM
+44 1784 431611

Asia/Pacific Headquarters

Gartner Australasia Pty. Ltd.
Level 9, 141 Walker Street
North Sydney
New South Wales 2060
AUSTRALIA
+61 2 9459 4600

Japan Headquarters

Gartner Japan Ltd.
Aobadai Hills, 6F
7-7, Aobadai, 4-chome
Meguro-ku, Tokyo 153-0042
JAPAN
+81 3 3481 3670

Latin America Headquarters

Gartner do Brazil
Av. das Nações Unidas, 12551
9º andar—World Trade Center
04578-903—São Paulo SP
BRAZIL
+55 11 3443 1509