

Microsoft's 2Q earnings dip despite Windows 8 lift

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Microsoft's latest quarterly earnings slipped, even as the world's largest software maker showed modest progress adjusting to a shift away from the personal computers that have been its financial foundation for decades.

The results announced Thursday are the first to include Windows 8. The program is a dramatic overhaul of the Microsoft Corp. operating system that powers most PCs. Windows 8 came out Oct. 26 with slightly more than two months left in Microsoft's fiscal second quarter.

Microsoft is counting on Windows 8 to help the company extend its franchise into tablet computers while still reaping revenue from a new breed of PCs. The redesigned software displays applications in a mosaic of interactive tiles instead of a staid menu. It can be controlled by touching on a display screen, as well as the traditional method of using a keyboard and a mouse.

Although sales of Windows 8 haven't been as impressive as investors hoped, revenue in Microsoft's Windows division climbed 24 percent from the previous year. That includes sales that had to be deferred from earlier quarters because the purchases were made before Windows 8's release.

When Windows 8 finally hit the market, Microsoft also unveiled its own tablet computer, Surface, as a showcase for the operating system. Microsoft didn't disclose Thursday how many Surface devices were sold in the October-December period.

"I don't think they want to provide that because it won't be impressive," technology analyst Patrick Moorhead said.

Analysts have estimated Microsoft sold 750,000 to 1 million of the Surface units during the quarter, far below the nearly 23 million iPads that Apple said it shipped during the same period.

Microsoft booked its Surface sales in the Window division, accounting for some of the gains from the previous year. The Redmond, Wash., company is trying to get the Surface into more hands by releasing the device in 14 more countries and coming out with a more sophisticated version that can handle all Microsoft programs. The new model, called Surface Pro, will debut Feb. 9. The one already out runs a streamlined version of Windows 8 called RT.

BGC Financial analyst Colin Gillis said he still has faith in Microsoft, saying the company "has multiple revenue streams that are still very nice businesses."

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"I kind of like the Windows segment," he said, adding that the 24 percent growth was "a little stronger than expected."

But another Microsoft division that includes another big moneymaker — the company's Office suite of software — didn't fare as well. Revenue in the Office division declined 10 percent, a shortfall that may have spooked some investors. Analyst Josh Olson of Edward Jones believes many of Microsoft's corporate customers may have held off on buying Office because a new version of that program is scheduled to come out early this year.

Microsoft earned \$6.4 billion, or 76 cents per share, during the final three months of the year. That was down 4 percent from \$6.6 billion, or 78 cents per share, a year earlier.

The company's total revenue rose 3 percent from last year to \$21.5 billion.

The earnings were a penny above the average estimate of analysts surveyed by FactSet, while the total revenue fell below analysts' projections by about \$100 million.

Microsoft's stock shed 43 cents, or 1.6 percent, to \$27.20 in Thursday's extended trading, after the release of results. The stock has remained stuck below its price before Windows 8 and Surface came out, signaling that investors aren't pleased with the products' performance so far.

"This is going to be a 'show-me' year for Microsoft, and there was nothing to really shout about in this quarter," Olson said. "So what we are seeing is sort of a shrug from investors."

Besides debuting Windows and Surface during the most recent quarter, Microsoft also released a new version of its operating phone for smartphones.

Moorhead called the Surface and the new software line-up the "keys to Microsoft's future."

If Microsoft's revamped software for tablets and smartphones catches on, it would help the company overcome a downturn in PC sales, which has reduced licensing revenue during the past year. Worldwide PC shipments fell 3.5 percent last year, marking the industry's first annual decline since 2001, according to the research firm Gartner Inc.

Despite Microsoft's high hopes and an elaborate marketing campaign, Windows 8 appears to have gotten off to a tepid start. Technology reviews have panned the software as too confusing and cumbersome to navigate, and none of the hundreds of devices running on Windows 8 emerged as a breakout hit during the holiday season.

A big chunk of Microsoft's Windows revenue in the holiday-season quarter came

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from sales that were made before the new operating system's release. Excluding revenue that had been deferred from previous quarter, Windows revenue increased 11 percent from the same period in 2011.

The Surface also hasn't been able to mount a significant challenge to Apple Inc.'s trend-setting iPad, Amazon.com Inc.'s Kindle Fire, Samsung Electronics Co.'s Galaxy or Google Inc.'s Nexus devices.

Reiterating information released earlier this month, Microsoft said it has licensed more than 60 million copies of Windows 8. That puts the redesigned system on the same early sales trajectory as its predecessor, Windows 7, after it came out in 2009. It's unclear how many of the devices that have licensed Windows 8 are still sitting on store shelves.

Gillis said Windows 8 is Microsoft's attempt to solve a disruption in the market that's taking place because of tablets.

"It's too early to declare it a success or a failure," he said.

"The sentiment on the PC market is just too negative," Gillis added, referring to the death knells that have been ringing through much of the technology industry during the past year. "Yes, there are disruptions going on but we still sell close to a million PCs a day."

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AP Technology Writer Barbara Ortutay in New York contributed to this story.

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