



Issue 346: Wednesday, November 26, 2008

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### Telecom Overview: A Welcome Surprise

In this week's edition of *The Telecom Connection*, I've started off with a review of **Dell's** (DELL) quarter. As expected, the revenue was below consensus estimates, but the big surprise came from the company's newly discovered ability to control costs. Dell still has some work to do, but there were certainly positives in the numbers.

There have been some additional developments in the memory markets in recent days as well. I'm hearing about a push for consolidation among some of the smaller companies in Taiwan. Prices remain weak, but **Micron** (MU) and **Intel** (INTC) announced their new NAND flash platform, created through a joint venture, that should significantly lower costs for both companies.

In the Tech Bits 'n' Bytes section, I've touched on a number of topics. These include the new entry into the smartphone arena, T.J. Rodgers of **Cypress Semiconductor** (CY) putting his hand in his own pocket, some interesting doings at the new **Clearwire** (CLWR), and an upbeat outlook for the first Android phone.

I've decided to skip the inventory commentary this week, and will only note that it is back within the "normal" range for now.

These are difficult times for all of us, but regardless of our circumstances, I'm sure we all have something to be thankful for. Here's hoping that everyone has a wonderful Thanksgiving holiday!

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## Dell Delivers Earnings

Revenue may have been a little on the light side, but it looks as if Dell's management got the memo about operating expenses. That, coupled with a better product mix, enabled the company to deliver a solid earnings surprise in the quarter.

The two critical areas on the company's P&L were gross margin and operating margin. Gross margin was 18.82%, an improvement of 30 basis points from last year and 160 basis points sequentially due to what was an improved mix and cost initiative. Obviously, we didn't see any "strategic pricing action" like we did last quarter, which had been a huge drag. Operating margin improvement was great, up more than 100 basis points on both a year-over-year and sequential basis. The company shed 2,200 employees during the quarter, and operating expenses declined \$170 million vs. the second quarter.

Within the company's commercial accounts (82% of revenue), revenue declined 6% vs. last year but operating income was up by nearly 1%. Notebook units were essentially flat, with desktops down 8% year over year and servers down 4% year over year. Enhanced Services actually grew 3% year over year as the company strives to penetrate a market that is actually twice the size of the hardware sales volumes. Geographically, all commercial operations struggled vs. prior-year revenue levels. Europe, the Middle East and Africa (EMEA) declined 5% year over year, the Americas declined 8%, and only Asia/Pacific experienced a modest (2%) gain. Despite the weak revenue performance, the Americas and Asia/Pacific both saw improved operating margins.

On the consumer side, revenue increased 10% from last year and operating income swung from a loss to a 4% profit as the company reduced operating expenses by 24% from the year-ago period. Overall unit growth was 32% -- 20% greater than the industry average -- with notebooks up 67% year over year but desktops down 20% from last year.

This past weekend's *Barron's* article on Dell was little more than a rehash of facts that have been in evidence for some time. No one is suggesting that Dell has solved its problems, but reducing its cost basis is an important part of the solution. Growth in the current environment is a luxury that few will see and Dell is no different. While business deteriorated throughout the quarter, particularly in the U.S. and Western Europe, the company did see good demand in Asia and the BRIC (Brazil, Russia, India and China) countries. Although Dell does not provide specific guidance, the company did indicate that it expects to see a challenging environment going forward.

Despite the challenges, Dell's direct model enables it to see and react to changes faster than most of its competitors. That same model also allows it to benefit from lower component prices faster than its competition.

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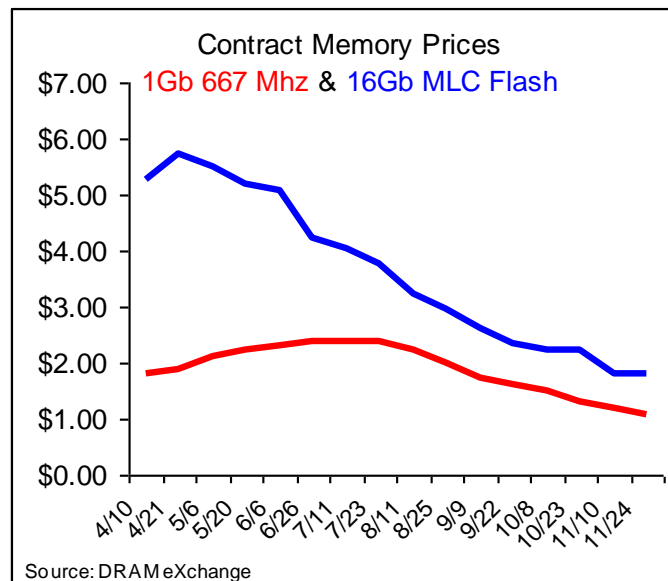
## More Memory Musings

In last week's newsletter, I noted several of the capacity-related developments taking place within the memory industry. Now with pricing remaining weak (see graph below), there are calls in Taiwan for consolidation of the small players in that country. David Sun, co-founder of memory module company Kingston Technology, is calling for no more than two memory companies total, while others are suggesting the government should facilitate mergers.

Inotera, Nanya, Powerchip and ProMOS are all struggling, and combined they have a negative free cash flow for the nine months ending Sept. 30 of about \$2.1 billion. These are the small players that struggle on the margin during downturns. Lacking size and generally not as well capitalized, they will frequently price very aggressively in attempts to gain incremental market share. But the one way to counter their efforts is to push costs down as quickly as possible, and we had some good news on that front this week from Micron.

Micron and Intel announced that their joint venture, IM Flash Technology, has commenced production of 32-gigabit multilevel cell (MLC) NAND flash memory devices at 34 nanometers (nm). Micron is the first flash company to reach production at 34nm, but others have come out with press releases claiming they expect to do the same. Micron anticipates that at least 50% of its wafer starts will be at the 34nm level by the end of the calendar year and will be at full production by early 2009.

Why is this important? A 34nm part is only 46% of the area compared to a 50nm part (current generation), and because silicon area equates to cost, there will be a substantial reduction in cost. Micron should be able to announce 15% or more sequential reduction in NAND flash costs for a number of quarters to come.



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## Tech Bits 'n' Bytes

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### • Smartphones Galore!

I don't know if many readers have had a chance to see one yet, but **Research In Motion** (RIMM) finally launched the Blackberry Storm on the Verizon Wireless network over the weekend. The device really looks sharp, but it is certainly borrowing many features introduced by **Apple's** (AAPL) iPhone. Despite the competition, what I think this will do is invigorate the development community with another great platform for new and ingenious applications. That's what will drive the smartphone market to grow at rates sufficiently higher than the overall handset market.

Also on the iPhone bandwagon, China Mobile acknowledged recently that it is still interested in having the iPhone on its network. The discussions between these two companies have been long and arduous, but let's hope they're able to come to an agreement by the end of the year.

### • Voting With Dollars

T.J. Rodgers is Cypress Semiconductor's founder, Chairman and CEO and is one of the industry's characters. Sometime over the last few days he voiced his opinion of his stock's price by purchasing 1.1 million shares in the open market. That raises T.J.'s ownership position to about 11% of the outstanding stock. Obviously, he can afford it and is taking the long view. But I do like it when executives are willing to open their own wallets and buy their stock.

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- **The “New” Clearwire**

Last week, “old” Clearwire shareholders approved the merger with **Sprint’s** (S) Xohm operations. With that hurdle behind them, the companies anticipate closing the deal in early December. As part of an interview with WiMAX Trends following the vote, Clearwire commented that one area it is interested in exploring is India. Clearwire is setting up a management company in the country, which is expected to auction its spectrum for WiMAX in early 2009.

- **Da Google Phone**

Taiwan’s High Tech Computer (HTC) was the first company out the door with a phone based on **Google’s** (GOOG) new Android platform on the T-Mobile network. It’s still early, but cellular-news is reporting that HTC has bumped up its estimate of sales for the remainder of the year to 3 million units from the original expectation of 500,000 units. Not a bad way to start.



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# The Telecom Connection Portfolio

Company Name	Date Initiated	Cost Basis per Share	No. of Shares	Amount Invested	Current Price	% Gain/Loss	IXTC at Buy Date	IXTC Return
Apple AAPL	2/15/06	\$100.56	300	\$30,168.00	95.00	-5.53%	235.36	-38.76%
Alvarion ALVR	2/22/07	\$8.98	2,510	\$22,538.00	3.09	-65.59%	244.90	-41.15%
Clearwire CLWR	11/12/07	\$13.50	500	\$6,750.00	6.02	-55.41%	257.91	-44.12%
Cisco Systems CSCO	3/30/05	\$22.51	800	\$18,009.00	16.39	-27.19%	223.36	-35.47%
Cypress Semiconductor CY	7/10/08	\$5.36	2,000	\$10,720.00	3.53	-34.14%	230.96	-37.60%
Dell (call options) DLYAD – 20 contracts	12/6/07	\$6.80	2,000	\$13,600.00	0.02	-99.71%	259.97	-44.56%
First Solar FSLR	8/28/08	\$263.55	150	\$39,533.00	127.77	-51.52%	239.62	-39.85%
Google GOOG	2/9/06	\$494.76	75	\$37,106.70	292.09	-40.96%	243.87	-40.90%
Level 3 LFLT	6/19/08	\$3.76	3,000	\$11,280.00	0.90	-76.06%	263.91	-45.39%
Netlist NLST	2/14/08	\$1.46	3,500	\$5,095.00	0.36	-75.27%	232.75	-38.08%
Qualcomm QCOM	8/14/08	\$55.02	500	\$27,510.00	33.45	-39.20%	256.15	-43.73%
Research In Motion RIMM	11/19/07	\$113.82	200	\$22,763.75	44.70	-60.73%	247.44	-41.75%
Riverbed Technology RVBD	7/26/07	\$32.56	450	\$14,654.25	9.37	-71.23%	244.32	-41.01%
SunPower SPWRA	2/14/08	\$89.70	300	\$26,910.00	34.01	-62.08%	239.54	-39.83%
SunPower SPWRB	9/29/08	\$70.95	548	\$38,880.60	25.85	-63.57%	190.17	-24.21%

(The model portfolio continues on the next page)



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<b>Microtune TUNE</b>	2/8/07	\$5.23	2,500	\$13,075.00	2.35	-55.07%	244.96	-41.16%
<b>Micron (call options) WGYAZ – 125 contracts</b>	8/28/08	\$2.26	12,500	\$28,250.00	1.25	-44.69%	251.83	-42.77%

### The Telecom Connection Portfolio – Performance

<b>Total Average Return</b>	- 52.70%	Performance results listed here reflect values of stocks as of the close of the most recently completed trading day, and do NOT take into account dividends paid, interest earned or commissions. Results are updated overnight and posted prior to the market open the following business day. Sales are taken from the most recent purchase of that stock unless otherwise stated. The 2008 YTD Return figures reflect changes since the beginning of 2008. The Total Average Return figures reflect changes since inception on 8/14/2001.
<b>2008 YTD Return</b>	- 60.19%	

### Nasdaq Telecom Index Performance

	Portfolio Inception	Open Level	Current Level	% Gain/Loss Since Portfolio Inception	2008 YTD Return
Nasdaq Telecom Index (IXTC)	8/14/2001	262.84	144.13	- 45.16%	- 46.79%

*At the time of publication, Mr. Faulkner was long CLWR, CY, MU, NLST, TUNE, TUNE calls.*

To see the full Telecom Connection model portfolio, including closed positions, visit <http://www.thestreet.com/k/tc/portfolio.html>



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For securities that Mr. Faulkner holds at the time of publication of an issue of *The Telecom Connection*, Mr. Faulkner will not be permitted to sell the position until one month from the date the security was first recommended for purchase in *The Telecom Connection*.

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If you enter orders to buy or sell securities after 10:30 a.m. ET, it is possible that Mr. Faulkner may have purchased or sold such securities at a price more advantageous than the price you will obtain.