

Motorola: don't call it a comeback—yet

Roger O. Crockett and Olga Kharif

Prospects brightened for the handset maker last quarter, but much improvement came from cost-cutting. New smartphones will face strong competition from Apple, Palm, and others.



Holy qwerty keyboards, Wall Street. Struggling Motorola (MOT) posted a profit—albeit a small one—for the first time in a year. The Schaumburg (Ill.) handset manufacturer reported earnings of \$26 million, or 1¢ a share, up from \$4 million a year earlier.

Even more promising, Motorola said that in the current quarter it may turn a profit of as much as a cent, excluding charges related to expense reduction moves or other one-time events. The period that ended in June "was a solid quarter for us," co-CEO Greg Brown says in an interview. "It was a return to solid fundamentals. It's good to get some sense of momentum back."

Analysts were heartened by signs that the company has stopped burning cash and were hopeful that Motorola's fortunes will improve as the effects of the recession wear off. "We are on the other side of a financial Armageddon," says Broadpoint AmTech analyst Mark McKechnie. Analysts at Charter Equity Research upgraded their rating of the stock to a buy, from underperform, citing increased profitability. "Improvement in consolidated gross margins and slightly higher phone sales suggests the business has at least stabilized," Charter analyst Ed Snyder wrote in a July 30 research note. Weary investors boosted Motorola shares 9.4%, to 7.19.

Excited about Android

But beware: The momentum comes largely on the back of aggressive cost-cutting. Motorola said it cut 8,000 jobs in the first half of the year. Much of the fat has been squeezed from the mobile-devices business led by co-CEO Sanjay Jha. He is concentrating on weeding out unprofitable devices and betting the unit's recovery on advanced smartphones, due on shelves by late September or early October, based on the Android software created by a Google (GOOG)-led coalition of developers. "The real excitement is about their Android platform," says McKechnie. "We've seen Motorola pull itself out of tough situations before [with phones like the Razr]. I am wondering if Android will give Motorola another little run."

Android might help. But Motorola has a poor track record when it comes to delivering compelling products on time. And when its phones do arrive, there will be fierce competition. Rivals are already well ahead. Taiwan's HTC is introducing its second Android phone, the promising MyTouch 3G, while Samsung and LG are expected to unveil Android phones in the third quarter. Motorola's phones will also lag the introduction of Apple's (AAPL) latest hit, the

iPhone 3GS, and Palm's (PALM) Pre. "It's going to be a crowded space," says analyst John Jackson at researcher CCS Insight.

Jha understands the stakes and is taking Motorola's comeback step by step. "Last year we had no 3G devices, no [new] smartphones," he says in an interview with BusinessWeek.com. "We are in a substantially different position now. The important part is we are launching meaningful devices and that is the basis of how we will build 2010. The skepticism is valid, but this is very different from not having a portfolio at all."

Progress is also dependent on Motorola's other divisions, which specialize in home entertainment and wireless networks for businesses and government agencies. While those businesses have faced strong "economic headwinds," Brown says, the forecast for the remainder of the year looks brighter. "Last year in the fourth quarter there was a structural economic collapse that hurt Motorola and others," Brown says. "This year from an economic standpoint we are on the mend. We don't have treacherous potholes to be wary about." Intrepid rivals, lackluster handsets, and missed delivery dates, on the other hand, could still trip Motorola up.

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