Qualcomm shares slide on forecast

Profit helped by tax boost; heavy legal spending weighs on outlook

By Dan Gallagher, MarketWatch
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SAN FRANCISCO (MarketWatch) -- Qualcomm Inc. shares took a hit Friday after the wireless technology company reported a big jump in quarterly earnings but issued a forecast that was below Wall Street's estimates.

Late Thursday, Qualcomm reported an 84% surge in profits for its fourth fiscal quarter, thanks to strong demand for the company's chipsets that power wireless phones as well as a one-time tax benefit.

But the company's earnings forecast for the current fiscal year was below analysts' estimates, in part due to heavy spending on its numerous legal battles.

"We believe that little growth in a period of intense litigation makes the risk-reward trade-off excessive and will result in earnings and multiple compression in the near-term," analyst Ed Snyder of Charter Equity Research wrote in a note to clients.
Snyder maintained a market perform, or neutral, rating on the stock, noting that the company is seeing increasing competition in the marketplace.

Ittai Kidron of CIBC World Markets remained bullish on the shares, saying that Qualcomm still has strong business fundamentals with growing demand for the wireless CDMA technology that the company pioneered. But he admitted that the "disappointing guidance could leave a bad taste in investors' mouths" after expectations got built up with a positive pre-announcement on Sept. 25.

"Bottom line, the soft outlook will take some time for investors to adjust to, but strong market fundamentals will help the adjustment," Kidron wrote in a report.

At last check, Qualcomm shares were down 3.8% at $38.28. The stock is off about 20% since peaking above $47 nearly six months ago.

Strong earnings gain

For its fourth fiscal quarter ended Sept. 30, the wireless technology company reported earnings of $1.13 billion, or 67 cents a share, up from $614 million, or 36 cents a share, in the same period last year.

Excluding charges related to stock-options as well as a benefit from an audit of prior years' tax returns, the company said earnings would have been $911 million, or 54 cents a share.

Revenue grew 15% to $2.31 billion for the period from $2 billion last year.

Analysts were expecting earnings of 53 cents a share on revenue of $2.26 billion, according to consensus estimates from Thomson Financial.

The bulk of growth for the quarter came from the company's chipset business, where revenue grew 24% to $1.4 billion. Revenue at the licensing business slipped 2% from the prior year to $647 million.

At the wireless and Internet segment, revenue jumped 25% to $245 million. This unit includes the company's BREW service, which provides wireless data services.
The company spent heavily during the fiscal year on legal expenses, stemming from its wide-ranging battle over patent licensing with rivals such as Broadcom. Legal costs totaled more than $200 million for the year ended Sept. 30, the company said.

Little progress on legal front

Qualcomm holds numerous patents covering CDMA, a popular wireless technology standard that forms the backbone of many next-generation networks coming online in the U.S., Europe and Asia. Wireless device makers such as Nokia and Ericsson have challenged the company's patents, seeking to lower the royalty rate they must pay for use of the technology, which they claim is too high.

Qualcomm is also in several patent infringement disputes with Broadcom, which has accused the company of infringing on its own technology. Broadcom scored a victory earlier this year, when the International Trade Commission issued an injunction against cell phones using Qualcomm's chipsets. The matter is under appeal.

In a conference call, Qualcomm president Steve Altman said no progress has been made in settlement talks with either Broadcom or Nokia.

"To meet our needs, any settlement must reflect the industry -recognized value of our intellectual property and permit all of our businesses to continue to thrive and contribute to the technological advancement and growth of the industry," Altman said.

Forecast below Street targets

For the current quarter ending Dec. 31, the company said it expects earnings to come in between 50-52 cents a share on a pro-forma basis. Wall Street expected earnings of 52 cents a share for the period.

For the 2008 fiscal year, Qualcomm expects earnings to come in between $2.03 and $2.09 a share falling under the current Street forecast for $2.18 a share in earnings.

A factor in the lower-than-expected earnings is that the company is not including royalty payments that would be owed by Nokia under the current licensing agreement between the two companies. That agreement is currently the subject of multiple lawsuits between the two companies.

Qualcomm said the amount of royalties it believes Nokia would owe under the existing deal for 2008 would total 25-30 cents a share.

Another factor for the year will be even higher spending on legal costs. The company said it expects legal costs to increase by about 4 cents a share for the 2008 fiscal year. ■

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