Issue # 92

December 28, 2000

1. Strong Buys

VerticalNet Gains by Selling an Online Exchange

By Paul DeMartino

The Internet Analyst[SM] *combed through research submitted to the Multex.com database this week, looking for Strong Buys. In order to be included in this column, a stock must receive a firm's highest rating, and the valuation methodology must be included in the report.*

FIRST DATA (FDC): On Dec. 19, First Union Securities initiated coverage of payment-processing company FIRST DATA. The firm's investment thesis for the company is familiar enough: a large share of a niche market plus high growth in that market equals big bucks in the future. In this case, First Union points particularly to FIRST DATA's electronic payments processing businesses. One is FIRST DATA's Western Union division. First Union says that it accounts for 45% of profits, and is expected to grow 15% to 17% over the next two years, based largely on the strength of its international operations and profitability on a per-agent basis. The other is electronic transactions – including online functionality – which First Union figures accounts for 35% of profits and with a growth rate of 14% to 16% over the next two years. This business benefits from the underlying growth of card transactions. In all, First Union estimates that FIRST DATA will earn $2.14 a share in 2000 and projects earnings of $2.45 a share in 2001. Its target price is $69, calculated with a price-to-EBITDA (earnings before interest, taxes, depreciation and amortization) ratio. FIRST DATA shares closed at $49.38 on Dec. 22. Research on FIRST DATA was accessed 466 times and 121 new reports were added to the Multex.com databases from Dec. 11 to 17.

LIBERATE TECHNOLOGIES (LBRT): U.S. Bancorp Piper Jaffray reiterated its STRONG BUY on LIBERATE TECHNOLOGIES on Dec. 21 after the leading provider of software for set-top boxes reported what the firm called its "best quarter as a public company." For its fiscal second quarter, which ended Nov. 30, LIBERATE generated $11.7 million in revenue; Piper Jaffray had expected $9.5 million. LIBERATE lost $0.07 a share compared to the firm's estimated loss of $0.18 a share. Piper Jaffray says LIBERATE is benefiting from the rapid deployment of its software by cable operators. Around 370,000 LIBERATE-enabled boxes were shipped in the quarter, compared to the firm's expectation that the company's software would be deployed on about 100,000 set-top boxes in the quarter. In addition, Piper Jaffray expects LIBERATE's software to be deployed by AT&T (T), the largest cable operator in the United States, in the first part of 2001, and expects deployments by UNITED PAN-EUROPE COMMUNICATIONS (UPCOY), the largest European cable company, to begin in the first quarter of 2001. The firm raised its revenue estimate for fiscal 2000, which ends in May 2001, to $49 million from $41.5 million. The firm cut its estimated fiscal 2000 loss to $0.41 a share from $0.61 a share. U.S. Bancorp's 12-month price target is $30, based on a price-to-sales metric. LIBERATE TECHNOLOGIES closed at $14.50 on Dec. 22. Research on LIBERATE was accessed 318 times and 33 new reports were contributed to the Multex.com database, from Dec. 11 to 17.

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VERTICALNET (VERT): On Dec. 20, Dain Rauscher Wessels upgraded the shares of VERTICALNET to a STRONG BUY-SPECULATIVE from a BUY-AGGRESSIVE. The report was prompted by an agreement the company reached with Converge, an online marketplace formed by a consortium of technology companies, including AMD (AMD), SOLECTRON (SLR), COMPAQ COMPUTER (CPQ) and GATEWAY (GTW). VERTICALNET will sell its online exchange business to Converge for a 20% equity stake in Converge, a $107.5-million, three-year contract for services and $60 million in cash. The astute investor might notice that this business is roughly 16% of VERTICALNET's profits. Nevertheless, Dain Rauscher believes this deal is a good idea for VERTICALNET. First, it sheds the uncertainty concerning volatile semiconductor prices just as that industry appears to be slowing. The deal should also improve the accuracy of analysts' forecasts going forward. In addition, about $22 million in inventory related to electronic components is eliminated. Finally, the transaction should solidify VERTICALNET's business model as a B2B enabler. Dain Rauscher estimates pro-forma earnings of $0.78 a share in 2000 and earnings of $0.11 a share in 2001. Its six-month target price is $50 based on a price-to-sales ratio. Shares of VERTICALNET closed at $4.63 on Dec. 22. Research on VERTICALNET was accessed 1,131 times and 155 reports on the company were added to the Multex.com database from Dec. 11 to 17.

Recent Strong Buys:

December 21 You Say Sorrento, I say Osicom

December 14 i2 Technologies Shares a Strong-Buy Report With Ariba

2. The Sell Report

Agency.com

Better, But Not Good Enough

By Aram Fuchs

When I turned my focus on RAZORFISH (RAZF), I was surprised that the e-business consulting company was not planning any layoffs despite the fact that fourth-quarter revenue would fall about $27 million from the third-quarter's $77.1 million (The Sell Report, The Internet Analyst, Dec. 21, 2000).

Well, here in New York's new media community there has always been a rivalry between AGENCY.COM (ACOM) and RAZORFISH, mainly because both got started at about the same time and both immediately generated the buzz needed to be considered "cool" here.

The two companies followed essentially the same pattern for several years. They each got their share of marquee clients. AGENCY.COM has, among others, BRITISH AIRWAYS (BAB), BANK OF AMERICA (BAC) and COLGATE PALMOLIVE (CL). RAZORFISH's clients include TIME WARNER (TWX), COCA-COLA (KO) and FORD MOTOR (F). Both companies went public in 1999 and saw their stock immediately soar to obscene heights. As their stocks rose, both companies acquired small, boutique Web shops that enabled them to show dramatic revenue growth and even a modicum of profits.

Their stocks benefited because the companies were seen as being able to profit from the Internet boom, without the risk of having to compete for the attention of consumers. The strategy is affectionately known to investors as "selling jeans to miners," because while many people invested in various aspects of the Gold Rush of 1847, one of the only companies to survive was Levi Strauss &Co.

Now, the Gold Rush is over and these companies are facing difficult times. But while RAZORFISH believes that the contraction in the Web-developer space is a brief respite before another boom, it seems at first glance that AGENCY.COM understands that it must make very difficult decisions in order to minimize shareholder losses.

AGENCY.COM is laying-off 190 people, of which 130 are billable consultants. This is a key distinction, because the company earns its keep by charging their clients for the time that these consultants spend on a client's project. Firing the consultants is the equivalent of an industrial company closing down a factory.

So it is hard to understand why, with fewer billable consultants, AGENCY.COM's guidance to analysts for 2001 remains so optimistic. The company did lower its forecast of 2001 revenue to $253 million from around $313 million, but that number still represents growth of 23% to 27% based on an estimate by Goldman Sachs. (Goldman was the lead manager of AGENCY.COM's December 1999 initial public offering.) Obviously, AGENCY.COM thinks demand will pick up again and they will have to hire back employees.

We don't think that projection is prudent. When an industry starts contracting by more than 20% quarter-to-quarter, it doesn't just magically start growing at a 20% rate a couple of quarters later. As we all should know by now, these revenue numbers are educated guesses on management's part. Why should we believe the company's 2001 numbers when the their fourth quarter estimate – made in the third quarter – was off by so much?

So while it looks like the management team of AGENCY.COM is being more sober than its cross-town competitor RAZORFISH, they still are not being as sober as Fertilemind.net thinks they should be.

Aram Fuchs is the CEO of Fertilemind.net, an independent Internet equity research and consulting firm. At the time of publication, he did not have any interest in the securities mentioned in this article. Mr. Fuchs frequently buys and sells securities that are the subject of his articles, both before and after publication.

Recent Sell Reports:

December 21: Razorfish: When Vision Only Comes in the Rose-Hued Variety
December 14:.Tough Choices for an Online Loan Marketplace

3. The Independent View

Online Winners and Losers in November

By Greg A. Kyle
President and CEO of Pegasus Research

The Big Get Bigger …

There is a Darwinian process going on in the online media world, where the large portals keep pulling ahead in viewership, distancing themselves from the rest of the pack. As the chart below shows, the gulf between the top-tier portals – AMERICA ONLINE (AOL), YAHOO! (YHOO) and MICROSOFT's (MSFT) MSN – and the mid-tier portals – TERRA LYCOS (TRLY), EXCITE@HOME (ATHM) and WALT DISNEY INTERNET GROUP (formerly Go.com) (DIG) – is growing larger and larger.

United States traffic growth for the mid-tier Web properties has remained relatively stagnant all year, while the Big Three have seen their traffic grow 17% to 32% since last December. Of the top-tier Web properties, MSN has the slowest growth. In the few months since the merger with Spain's Terra Networks formed TERRA LYCOS, that portal has actually seen its U.S. traffic decline. However, we suspect that international growth – particularly in Europe and Latin America – has been accelerating for the combined company.

What does 2001 hold? Pegasus Research expects the big to get bigger, in effect duplicating what has happened in broadcast TV, where three major networks capture the bulk of viewer eyeballs. This, we believe, will ultimately translate to solid advertising revenue growth over the coming years for the major horizontal portals. We still see the online ad industry on track to grow at a 32.7% compound annual rate through 2004. This includes our outlook that growth rates are moderating from 99% in 2000 to 15% by 2004. As for the winners, we expect to see AOL and YAHOO! in particular, grow above the industry average as they continue to capture market share.

Pegasus Research International
Independent Research for the Internet Investor

Going Vertical Is Not Paying Off

In the ongoing debate between the horizontals and the verticals, the verticals are quickly losing the battle. Traffic growth has been going to those sites that can demonstrate the broadest availability of content. This does not favor the niche sites. As an example, Scott Kurnit of ABOUT (BOUT) said at the New York Society of Security Analysts' recent Internet Economy conference that its women-oriented channels receive more traffic than IVILLAGE (IVIL), WOMEN.COM (WOMN) and Oxygen.com combined.

Unfortunately for the verticals, revenue growth has also been tied to those sites that have the broadest reach. This is not surprising considering the revenue concentration present in the online media sector. The Top 10 Web properties typically receive 72% to 75% of all industry revenue, and this concentration is growing. As traditional advertisers move to the Web, they are committing their online ad dollars to those sites with the most eyeballs. Verticals, for the most part, suffer from a dot-com advertising base, and this advertising source has quickly dried up as cash-starved Internet companies slashed their marketing budgets.

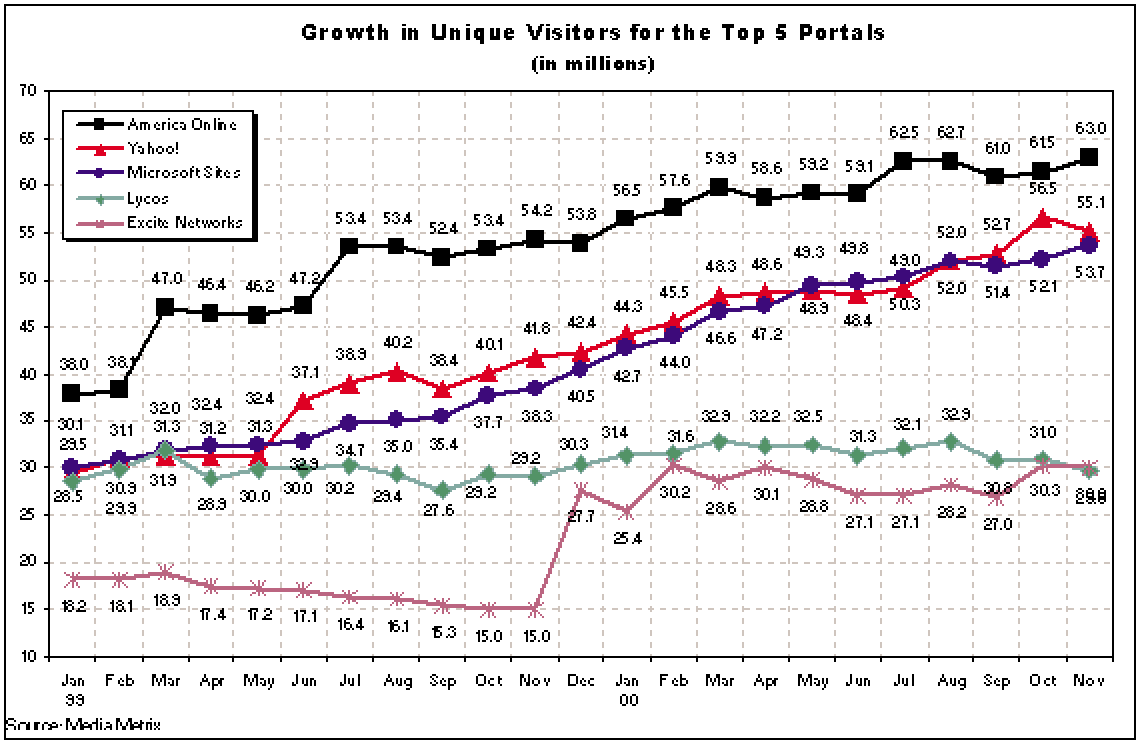
The outlook for 2001 is not particularly rosy for many of the vertical media properties. Unless they can quickly capture a strong, traditional bricks-and-mortar client base, revenue could be hard to come by. This translates into what we see as an intense consolidation period over the next six months.

E-Tailers Wishing for More Visitors

Leading up to the end of the holiday season, only a few online retailers have been successful in posting solid visitor gains. AMAZON.COM (AMZN) continued its double-digit traffic growth, as its unique visitor base expanded 10.2% in November to 19.1 million, which follows October's 13.4% gain. At Pegasus Research, we view this as a solid indication that despite weakness in the sector, AMAZON.COM is on track to meet its revenue target for the quarter. Recent data also tend to suggest this. In the second week of December, AMAZON saw traffic to its Web site grow faster than the industry average. Surprisingly, EBAY (EBAY) has also been enjoying a holiday lift in its traffic. During November, monthly unique visitors grew 10.2% to 17.7 million according to Media Metrix.

Other e-tailers have been less fortunate. BARNESANDNOBLE.COM (BNBN) has not been as successful at pulling in visitors into its online stores. Traffic grew only 7.6% during November to 6.7 million unique visitors. ETOYS (ETYS) did not even rank in the Top 50 in November, despite the fact that it was the middle of the holiday shopping season. In contrast, its rival TOYS 'R' US (TOY), which teamed with AMAZON to run its Web site, managed to break into the Top 50 for the first time at number 49 with 6.4 million unique visitors. The poor showing for ETOYS no doubt played a large role in the company announcing that sales for this holiday quarter would be far below expectations.

Who will be the e-tailing winners this season? Although final traffic numbers will not be in until well after Christmas, AMAZON.COM is likely to be one of the few major e-tailers that will be successful in translating visitor traffic into solid revenue growth for the quarter. For the rest of the pure-play online retailers, it will be a hard-fought battle against the bricks-and-clicks.



Pegasus Research is an independent research firm that provides unbiased, objective analysis on the emerging Internet economy.
For more information, contact Pegasus at (212) 687-1522.

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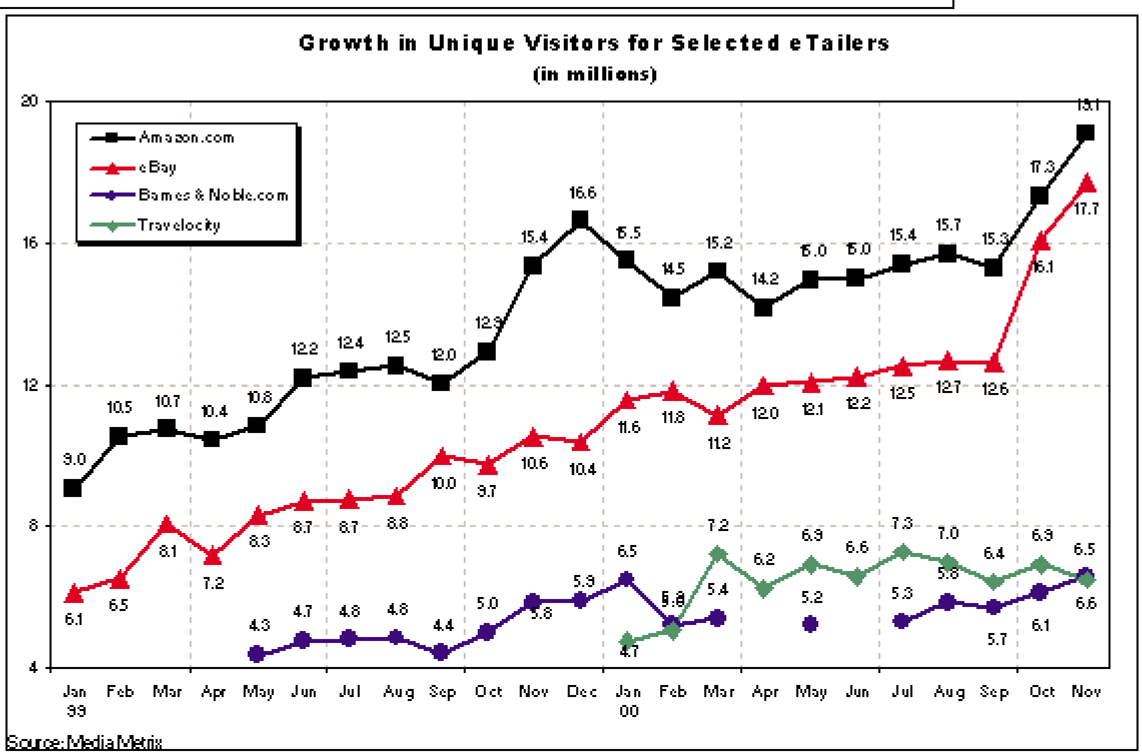
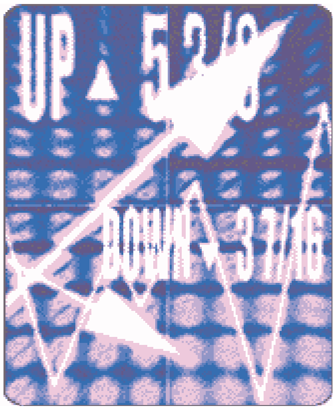


4. Upgrades & Downgrades



Quick Delivery Wins Praise for SmartForce

By James C. Condon

SMARTFORCE (SMTF): Morgan Stanley Dean Witter upgraded this leading e-learning company to OUTPERFORM from NEUTRAL on Dec. 22 largely on the strength of its pipeline and its ability to provide a rapid solution to business training needs. The brokerage says that SMARTFORCE is becoming a one-stop shop for Web-based training solutions through its library of 1,300 courses. The courses are primarily information-technology (IT) related and had been chosen by 2,500 corporate clients by the end of 1999. Morgan Stanley says that talks over the past several months with existing and potential customers, as well as sales people and executives in the industry, suggest that adoption of the SMARTFORCE product is extremely strong and that the outlook for future contracts is very positive. Furthermore, the firm believes that SMARTFORCE's ability to deliver a rapid solution to time-sensitive business problems is differentiating the company from its competitors. In an industry with lengthening sales cycles and time-consuming software installations, SMARTFORCE uses existing content, customization tools and its integrated platform to provide an answer. "The solution can be deployed in as little as a couple of weeks," says the firm, "and by addressing immediate business needs it can generate rapid return on investment."

The brokerage says its checks in the industry lead it to believe that the slowing economy is not affecting demand for SMARTFORCE's products. In addition, Morgan Stanley says that over the past quarter, SMARTFORCE has added redundancy to the hosting function for its platform, and believes dependence on one Web-hosting provider is no longer a concern. While it says there is potential upside to its forecast 2001 and 2002 earnings, the firm left all estimates unchanged. Morgan Stanley sees a loss of $0.41 a share in 2000, and earnings of $0.14 a share in 2001. For 2002, the firm is forecasting earnings of $0.69 a share. Its 12-month price target is $40 a share based on a 1.4 PEG (P/E-to-growth) ratio, SMARTFORCE's 1997-99 average. SMARTFORCE closed at $33.44 on Dec. 22.

COGNOS (COGN): On Dec. 22, Merrill Lynch downgraded its near-term rating on this provider of e-business intelligence software to NEUTRAL from ACCUMULATE after the company announced fiscal third-quarter results on Dec. 21. COGNOS provides software that is part of the growing field of e-business analytics. The driver for the growth of this type of software is the rapid adoption of e-commerce, which creates a need within companies to quickly mine and analyze mountains of data generated by online transactions and make business decisions based on that analysis. Merrill says that COGNOS reported disappointing sales in its fiscal 2000 third quarter, which ended Nov. 30. License revenue was $64.8 million, up 26% from the previous year, but about 7% below Merrill's estimate. Total revenue of $124.6 million was up 28% year to year, but 2% below expectations. In addition, the balance sheet weakened, with days of sales outstanding, a gauge of how efficiently a company is turning sales made on credit into cash, rising to 93 days from 81 days in the fiscal second quarter.

The brokerage was confused by management's remarks on the conference call discussing the results. Despite maintaining that its pipeline was as large as it has been, management lowered its revenue estimates for the 2000 fiscal fourth quarter and fiscal 2001, which ends in February of 2002. Merrill says its checks lead it to conclude that the market for e-business analytics remains strong and that COGNOS's problem is company specific and related to sales force execution. "Until we see evidence that the company's sales force execution problems are behind it," says Merrill, "we elect to move to the sidelines." The firm lowered its fiscal fourth-quarter revenue estimate to $144.5 million from $149 million and cut its earnings estimate for the quarter to $0.25 a share from $0.29 a share. For fiscal 2001 it now sees revenue of $617.6 million, down from $641.7 million and earnings of $0.81 a share, down from $1.03 a share. COGNOS closed at $19.25 on Dec. 22, down 29% following the earnings report.

BEA SYSTEMS (BEAS): This leading provider of software infrastructure that supports and integrates enterprise and e-commerce applications was upgraded to BUY from ACCUMULATE on Dec. 22 by Jefferies & Co. BEA SYSTEMS' middleware product handles the coordination of data, messages and transactions between applications, databases and legacy systems. Its WebLogic application servers allow companies to rapidly design and deploy e-commerce platforms. According to Jefferies, checks in the industry indicate that BEA continues to see "robust" business in the application server space. Further, the brokerage is encouraged that BEA has been able to offset weakness in the telecommunications market – 30% of second quarter sales – with other customers. "We hear from our sources," says Jefferies, "that leading up to a recession, BEA SYSTEMS and Web channel players will be the last expense to be cut." The firm expects earnings of $0.11 a share in 2000, rising to $0.24 a share in 2001 and $0.37 a share in 2002. Revenue in 2000 is estimated at $464.4 million. For 2001, Jefferies sees revenue of $815.1 million, rising to $1.21 billion in 2002. The firm's $89 a share price target is based on a multiple of 31-times 2002 revenue. BEA SYSTEMS closed at $72.25 on Dec. 22.

For more on BEA SYSTEMS, please see Top Company Picks, The Telecomm Analyst, Dec. 19, 2000.

CEO of Online Brokerage Is a Buyer

By Craig Columbus
President, insiderSCORES.com

Last month, TD WATERHOUSE (TWE) saw its largest insider purchase since March 2000, the month the stock price hit its 52-week high of $27. Stephen McDonald, the online brokerage's chief executive officer, bought 10,000 shares from Nov. 22 to 29, at $13.88 a share.

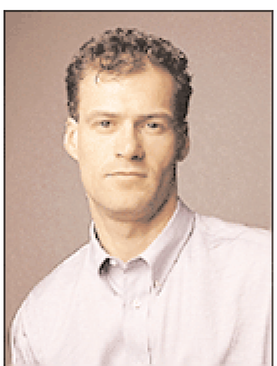
The purchase marked the first insider activity of any kind since May, and TD WATERHOUSE shares were trading near their 52-week low when Mr. McDonald's purchase occurred. Mr. McDonald has acquired TD WATERHOUSE shares on twice before, and on those occasions, the stock has risen following his purchase. In the six months following those two previous prior purchases, TD WATERHOUSE shares rose an average of 31%. Since the November purchase, TD WATERHOUSE shares have declined slightly and closed on Dec. 22 at $13.06. *– Eric Lopkin*

Recent Upgrades & Downgrades:

December 21: E-Business Consulting, No. Wireless Internet Banking, Yes.

December 14:An Online Teacher of 'Soft' Skills Rates a Buy

5. Hot Lunch


E-marketer
Geoff Ramsey

Part I: Measuring the Yardstick

Geoff Ramsey, Co-Founder and Managing Partner, E-marketer

Interviewed by Eric Lopkin

I sat in the offices of The Internet Analyst℠ *as I interviewed Geoff Ramsey who was at home. Snow fell outside, as New York City got its first taste of the winter season's fluffy companion.*

[ERIC LOPKIN] Geoff, in a nutshell, can you tell our readers what E-marketer does?

[GEOFF RAMSEY] E-marketer is a New York based firm that aggregates, filters, organizes, and analyzes information and statistics about the Internet. We look at over 300 research firms that are out there, assess their data analyses on various aspects of the Internet and aggregate that information. Then we try to distill it down to the essential points and explain how to look at the numbers. We deliver this information in our reports and presentations, and soon we'll have available a database of Internet statistics.

[EL] What are your most recent reports?

[GR] We recently launched the e-global report, as well as an e-mail marketing report. We produce approximately 40 reports a year which come out every other week or so. We cover about 13 different topics, including all four regions of the world: Asia, Europe, Latin America and North America. Other topics include e-commerce B2B and B2C, e-business, online advertising, e-mail marketing, financial services, wireless and broadband.

[EL] Give us a little information on your methodology. How do you take the disparate reports and combine them?

[GR] It's a multi-step process and it goes back to what I was saying before about aggregating, filtering, organizing and analyzing. The first step is to aggregate the data. With our database of research companies we monitor and scour the Internet, as well as offline publications and reports, to pull all of the information in on a given topic. Once we've aggregated all that information, we then filter it. That involves a number of things, including weeding out the information that is redundant or irrelevant and distilling it down to the essential points. It also includes doing our source comparison charts. Let's say we're looking at how big holiday shopping is. We will take all of the various estimates from the research companies that are measuring it – I think there are 12 or 13 of them now – and line them all up and present an unadjusted view of what the various research firms are saying.

That's really the tip of the iceberg because then we do the analysis portion of this. Why are these numbers so disparate? You find there are three reasons for that. One is that research firms use different definitions. In this case that could mean that they're measuring different time periods. FORRESTER RESEARCH (FORR), in measuring the holiday season, only looks at the last five weeks of the year. JUPITER MEDIA METRIX (JMXI) looks at November and December. Most of the other research companies, including us, look at October, November, and December, saying that covers the holiday season in total because October does count for something too. It's an apples-to-oranges comparison if you just look at the numbers superficially, so it's very important to understand what they're measuring. Once we do that, we normalize the data based on the different definitions. If we hold the time period constant, and we have statistical ways of doing that, we can then isolate that variable and focus on what these research companies were projecting. We do that in a number of different ways.

Part of the filtering process is also looking at the different methodologies employed by the research firms. Not all methodologies are created equal. Some research firms will use a relatively small sample size, say asking 40 executives what they think they're going to do in e-commerce next year. Others will use a large sample of 1,000 or so customers and ask them what they expect to spend. Obviously, a larger sample size will create, in most cases, a better, or more accurate, prediction. On the other hand, there are serious flaws in asking consumers what they expect to spend, because people tend to exaggerate or have no idea of what they're going to end up spending. So there are inherent flaws in any research. We try to weigh the various research methodologies and the reputations of the research companies to be able to compare one research number to another.

Once we've done that – and the process involves a lot of probing and talking to analysts and looking at the actual research reports – we normalize the data and come up with our own number based on all the information and getting underneath the numbers. We then come up with a number that we find is the best, true fit with all of the data we're looking at. Our number for holiday shopping is $12.5 billion for October, November, and December.

[EL] How accurate have your estimates been?

[GR] The challenge there is that no research firm out there can agree on what the ultimate measurement stick is. GARTNER GROUP (IT) is obviously going to say it's GARTNER GROUP. FORRESTER RESEARCH is going to say it's FORRESTER. When we were looking at holiday shopping, our number was $7.3 billion and the numbers ranged from $4.4 billion to $15 billion. At the end of the day, no one really had a clear sense of what the true number was. When the United States government surveyed 2,000 e-tailers, it came up with a number of $5.3 billion, but their survey didn't include travel, which most other researchers were including. If you add $2.2 billion, which was our estimate for travel, you get to $7.5 billion, which was close to our $7.3 billion estimate. Even the U.S. government admits that its methodology was somewhat flawed in that it didn't have as significant a sample size as they would have if they were looking at offline retailing. In other words, we really have no measuring stick in place for these things, and that's why people are still left confused after the fact as to what the real number was. What we are seeing, though, is that over time the numbers start converging. And because of our predictive model, and the fact that it's based on all of the other, normalized research data, we find our model has worked extremely well in predicting what's going to happen and measuring what's happening today.

[EL] Who are your competitors?

[GR] I'd be lying if I said we didn't have competitors. What I will say is that I don't think we have any direct competitors. Very often, people ask if we're competing with FORRESTER and JUPITER, and in a sense my answer is "Not really." One reason is that we really use them as suppliers; we use their information to create our own estimates, and we're not shy about showing all of the different numbers. That's part of what makes us E-marketer: We want to present a transparent view of the world. FORRESTER is never going to tell you what JUPITER is saying; we will. We want everybody to know what everyone is saying. We lay all the cards out on the table.

We also don't view them as competitors because people come to E-marketer because they want a bird's eye view of all the different research going on. They want a consensus. They want to know what everybody is saying and what we do to make sense out of it. If you really want to drill down on supply-chain management, or go in depth on e-travel, then you're going to go to FORRESTER or whoever is the expert in that area. And you'll know who the expert is by reading our reports. The data is going to be weighted towards FORRESTER or JUPITER or whoever has the skinny on that aspect of the market. In that sense, we're a different place on the food chain. We serve as a lead generator for FORRESTER and JUPITER. The other competitors are really the barrage of media out there that present information about the Internet – magazines like Industry Standard, Business 2.0 and, to a lesser extent, Fortune and Forbes. But these are reporters writing on topics. They really don't go beneath the numbers to see how the Internet relates to itself. You can look at e-commerce in isolation or you can look at it in the context of the infrastructure in a given market and number of Internet users and see how the whole model comes together. That's what we do.

Recent Hot Lunches:

December 21 Part II: Leveraging a Bricks-and-Mortar Presence to Promote Wellness on the Web-Bruce Shear, Chairman and CEO, Pioneer Behavioral Health

December 14 Part One: Casinos, Railroads, and Addictions – Bruce Shear, Chairman and CEO, Pioneer Behavioral Health

6. Executives Zero In

NBC Internet

William Lansing, Chief Executive Officer

Interviewed by George S. Mack


NBCI's William Lansing

A brand can be worth billions of dollars. But building brands on the Internet hasn't exactly been easy. Why not leverage a respected old media name like, NBC? That's exactly what the folks at NBC INTERNET (NBCI) were thinking. The San Francisco-based portal is the result of a rather elaborate rollup of Internet properties that included XOOM.com, Snap.com and NBCi. The company also includes the television network's flagship Web site NBC.com, which is operated as a separate but related site. Today NBC INTERNET is 39% owned by the National Broadcasting Company, which is 100% owned by GENERAL ELECTRIC (GE). And to show what the top brass thinks about Internet initiatives, you can find John F. Welch Jr., GE's chairman and chief executive, as well as Robert C. Wright, NBC's president and CEO, on the board of this microcap media portal.

But being an Internet media giant takes more than a brand name. Somehow you've got to grow revenue quickly, but that's gotten harder since the dot-coms began losing altitude and airspeed. And with NBC INTERNET stock down 97% over the past 12 months, investors have found that even the prestigious NBC brand name can't protect an Internet investment in a bear market of Web stocks. At the end of November 1999, NBC INTERNET received, in return for 39% equity, $405 million of television advertising credits from NBC, of which $298 million remained as of Sept. 30, 2000. Moreover, there was $314 million in cash and equivalents on the balance sheet with $382 million in long term debt. The ads and the cash together are worth roughly $9.50 a share – for a stock that closed at $3.13 on Dec. 22. Will Lansing, the company's new CEO, is a no-nonsense former GE executive who reported direct to the chairman while he was at the giant conglomerate. Can he make the television advertising model work in the Web space?

[THE INTERNET ANALYST – GEORGE S. MACK] Tell me about your revenue model.

[WILLIAM LANSING] Our revenue model, like that of most portals, is a combination of media sales and e-commerce transaction revenue. Ours is about 80% media sales and about 20% e-commerce. I define e-commerce broadly to include our direct marketing efforts as well as other e-commerce.

[GSM] You merged all your separate properties – XOOM.com, Snap.com and NBCi into one NBC INTERNET portal. You did this back on Sept. 25 during the Olympics – a great time to start advertising. Why did you fold in all the properties?

[WL] Our decision to merge the features and functionality into a single offering and all the brands into a single brand, had to do with two things. First, it was designed to improve the consumer's experience and make it easy to get around the site. Users can have one ID and one password, which is good all around the site. They don't have to re-register or be referred to different sites to take advantage of all the functionality. Secondly, from a brand standpoint, our vision was to spend the money to acquire the consumers only once. Once inside, we could re-circulate users within the offering and expose them to all the features and functionality, rather than spend the customer acquisition money many times to acquire the same user or member. So it was a practical, economic consideration that brought us to putting them all together.

[GSM] You must have had that idea the very day you became the primary decision-maker in the company.

[WL] You know, we did. And in hindsight, it was obviously a very good idea, because it worked. At the time, however, there was concern that the NBC brand name is so closely tied to the television network. Some consumers might think we are merely the Internet billboard for television content – that we might be the place to get the television schedules, the fan clubs for the stars on ER and Friends and not much more. And so, part of the challenge was that if we were going to go with the Peacock brand, we would also have to spend some promotional resources – some money – to educate the consumers that we are more than just an entertainment offering – that we're a actually a broad-based portal.

[GSM] It sounds like it should be a no-brainer.

[WL] It was a no-brainer to go with the multi-billion dollar brand. We did some homework, and we came to the conclusion that it would take somewhere between $500 million and $1 billion to build a really strong broad-based consumer brand in the United States today. Even though we had some brand equity in Snap.com and in XOOM.com, we didn't have the kind of promotional muscle to put those on the map next to other big name brands. But NBC does. It's already a multi-billion dollar brand. We agree it was a no-brainer, although for a no-brainer, we spent some time debating.

[GSM] Media Metrix estimated that you were the 11th most visited Web site in September with 14.8 million unique visitors. After a full month with your merged properties, how did you do in the October ranking?

[WL] We actually moved down to 13th, but that was the result of some consolidation that went on in the Top 15. But our actual number of unique users in October was well over 16.5 million, up from 14.8 million in September. We saw a significant 14% bump in unique users in October from September. In November we moved up in ranking to 14th with 16 million users.

[GSM] Your stock is down over 95% in the past 12 months and is now trading at its 52-week low. The question is what do you have to do to get investors' interested in this stock again?

[WL] My view is that the stock price lags reality. Right now the stock is depressed by two things. One is general market conditions, which are obviously awful. But we can't do anything about that. There's also a general investor antipathy to Internet media sales, which is our primary revenue model. I also think that before we merged all our properties and cleaned up the branding, there was some noise and confusion about what our strategy was. I think the company is running very smoothly right now, and now that our strategy is clear and focused, I think investors will start to recognize that. We still have to wait for market conditions to improve – to be lifted. When YAHOO! (YHOO) is as depressed as it is, it's no surprise that we're depressed also.

[GSM] Your new television ad campaign with the actress as spokesperson is stunning. There's a tremendous amount of energy in the ads, but they aren't obnoxious. Is it working?

[WL] We've put a lot of energy into trying to find just the right balance. First, to answer your question, yes, it's working well. We're very pleased in the uptick in traffic that's coming with this promotion. The message goals of the ad were to do a few things. One was to establish us as being in the broad portal space. We're really starting to stress the different types of functionality you can get with us – clearly more than just entertainment. In terms of Ingrid Torrance, the actress as a spokesperson, we were looking for someone who would be attractive to men and to women – not so attractive that she'd put off women but attractive enough to interest men. She could be a soccer mom, she could be single – she's very versatile. I think we succeeded

[GSM] Tell me a bit about your strategy for growing the business.

[WL] We're very focused on acquisition of visitors and trying to turn visitors into users – meaning visitors who come back multiple times. And we also want to convert users into members – people who register and give us some information about themselves. They might personalize their My NBCi page, for instance. We're driving traffic to our site with just under $100 million a year in television promotion, which makes us a Top 5 NBC advertiser. That means we're right up there in the top tier of consumer promotion. We're also getting traffic from in-program promotion. For example, we have a promotion with the NBC Saturday Night Movie. Every Saturday night we give away $100,000. You have to go online, register, answer a couple of questions, and you're eligible for the sweepstakes. That's been enormously successful for us.

[GSM] As a portal, when you accumulate a person's name, it's an asset for you. But I'm wondering if the privacy advocates are any threat to the portals – you, YAHOO!, TERRA LYCOS (TRLY) and others. Could they cause you a problem in the future?

[WL] I think that's a very good question. We have a very high respect for our members' privacy. Although we collect data from them with their permission, what we try to do is make sure we use it well. We use it to personalize their My NBCi page so they get back the sports scores they're interested in, the weather they care about, the stock quotes they care about, and we use it to send them appropriate product offers with e-mail. I don't think consumers perceive that as a privacy violation. I think they perceive it as a good trade. We don't sell or pass on any of that information to third-party partners without the member's permission.

[GSM] YAHOO! is the classic portal, but they don't have the backing of GE, and they don't have the NBC brand name. They don't have the ad campaign you have, but they're profitable, and growing a bit faster than you – even on top of their already big numbers. Do you have to start putting up faster growth numbers?

[WL] I think you're right that we have to focus on our growth rate, but we're not focused on growth at any cost. We're focused on profitable growth. Part of the reason our Media Metrix ranking is where it is, is because we won't chase empty calories. We're very focused on running a profitable business.

[GSM] Will, with the new management, your new ad campaign, your consolidation of all your properties, can you surprise analysts in 2001?

[WL] It's a possibility. We're feeling very good about our business. We feel good about our people, our functionality, our product and our ability to sell advertising. The question is, when does the media sales market firm up? Right now we're in a rocky time.

[GSM] In five years, could you be as big as YAHOO! is today?

[WL] Yes, that's not out of the question.

[GSM] When will you become profitable?

[WL] Our plan is to reach cash breakeven profitability at the end of 2001.

Vital Statistics
NBC Internet (NBCI)

Market Cap	$196.3 million
Shares Outstanding	62.8 million
Recent Stock Price	$3.13 (12/22/00)
52-Week Range	$106.13 – $2.94
Price to Est. 2000 Revenue	1.6-times
Price to Est. 2001 Revenue	1.3-times

Years end in December	**EPS**	**Revenue millions**
1999A	($5.85)	$74.0
2000E	($3.14)	$123.9
2001E	($2.15)	$152.6
2002E	($1.17)	$190.7

Source: Wedbush Morgan Securities

Recent Executive Zero Ins:

December 21

December 14 Alloy Online-Matthew C. Diamond, Chairman, CEO and Treasurer

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MALE	79.16%,
FEMALE	19.67%,

Top 10 countries where our readers are located*:

1. United States	6. France
2. Canada	7. Italy
3. United Kingdom	8. Australia
4. Germany	9. Belgium
5. Switzerland	10. Japan

Top 10 occupations of TIA readers*:

1. Director/Manager	6. President/CEO
2. Individ. Investor	7. Consultant
3. Professional Office	8. Vice President
4. Financial Advisor	9. Doctor/other health care
5. Engineer	10. Sales/Marketing

Top 5 most popular pages for last week:*

1. Upgrades & Downgrades
http://www.theinternetanalyst.com/individual/001221sections/updowngrade.asp

2. Strong Buys
http://www.theinternetanalyst.com/individual/001221sections/strongbuys.asp

3. Top U.S. Picks
http://www.theinternetanalyst.com/individual/001221sections/toppicks_us.asp

4. The Sell Report
http://www.theinternetanalyst.com/individual/001221sections/sellreport.asp

5. Independent View
http://www.theinternetanalyst.com/individual/001221sections/indview.asp

*demographics are based on a weekly TIA e-mail survey for 12/18 through 12/24/2000

7. The Real Deal

Investors Still Want to Buy

By Charles V. Payne
Founder, CEO and Principal Strategist of Wall Street Strategies

The good news from the Dec. 26 trading day is that investors are still waiting to be overall net buyers of stocks. The bad news is that there is still not enough money flowing into the market to simultaneously sustain both a speculative and defensive rally.

Be that as it may, the breadth – 1,754 advancers against 1,161 decliners – was also a positive sign. In fact, the Dow Jones industrial average is in a very nice uptrend since its Dec. 21 intra-day low and forms a mini-double top at 10,785. The Nasdaq, on the other hand, is still being punished by the continuing artillery barrage from the bears. These guys would have packed the Enola Gay with half a dozen atomic bombs. It stands to reason that investors have come to expect inconsistent behavior from the techs and thus not expect sustained rallies from Nasdaq.

That said, look for traders to pick their spots in the technology sector, while value investors will get a little more aggressive on the blue-chip side of the equation.

Outside Influence

Last night, the Japanese market took it on the chin on the news that industrial production fell a surprising 0.8% in the month of November. The "R" word is applicable globally and it will be interesting to see if it has any effect on the United States stock market. Certainly, with the Japanese unemployment rate on the rise – it hit 4.8% in November – and the yen falling to a 16-month low against the dollar, there will be some calls for lower interest rates. Does that sound familiar?

On these shores, investors are sifting through the news that the index of leading economic indicators fell 0.2% in November, matching the consensus analyst forecast. The November dip follows a revised decline of 0.3% in October. Furthermore, the November drop means that the index has now fallen in eight of the past 10 months and signals that economic growth will continue to slow in the coming months.

Pockets of Strength

The online retailers saw some strength on the day after Christmas as YAHOO! (YHOO) announced that holiday sales at its U.S. Web sites nearly doubled from last year's level.

YAHOO! gained more than 5% to close at $31.19, although it is surrendering some of that gain in trading on Dec. 27. YAHOO!'s good fortune also helped AMAZON.COM (AMZN) and AMERICA ONLINE (AOL) to show smaller gains.

After the fifth biggest percentage gain in Nasdaq history on Dec. 22, the decline on the day after the holiday was to be expected. So let's not force the issue. Keep your power dry – the holiday-shortened week will give us better opportunities to buy.

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8. Trends & Innovations

Micron Technology Could Magnetic Memory Cloud a Recovery?

By Dave Sterman

The operating history of chip maker MICRON TECHNOLOGY (MU) appears almost biblical. A string of lean years are invariably followed by a stretch when the company mints profits.

For example, the company hemorrhaged cash in fiscal 1998 and 1999, when the memory chip makers had too many plants cranking out too many chips, causing prices to fall and profits to evaporate. Then, in fiscal 2000, which ended in August, MICRON earned $1.5 billion, or $2.56 a share, as demand caught up with supply.

But it now looks as if MICRON could be entering yet another period where sales and profits lay fallow. The company recently reported quarterly profits that were slightly below expectations. On the company's conference call, management admitted that pricing for its memory chips continues to fall, implying further weakness in coming quarters.

Upturns and downturns are the norm in the cyclical semiconductor industry. But in the case of MICRON, a prolonged downturn could bring major headaches for the company. That's because a new technology is being developed that could supplant DRAM (dynamic random access memory). MICRON controls 22% of the massive DRAM market. Dynamic chips are unable to retain information over a period of time and must be re-charged every 15 nanoseconds (one-billionth of a second).

Scientists have long believed that by radically altering the architecture of the memory chips they can eliminate the need to constantly refreshing them with electricity. Increasingly, they are touting the strengths of MRAM, which stands for magnetic random access memory. MRAM works by measuring tiny changes to the resistance of the magnetic layers in a memory cell. Unlike DRAM chips, which are powered by "leaky" capacitors, MRAM chips require little energy. As a result, power consumption is comparatively small. That should be a real boon to developers of laptop computers and handheld computing devices.

IBM (IBM), a major force in the semiconductor industry thanks to a slew of key R&D breakthroughs, expects to be the first to market MRAM chips. In conjunction with Germany's INFINEON TECHNOLOGIES (IFX), IBM hopes to produce sample chips by 2003 and reach volume production in 2004. MOTOROLA (MOT), HONEYWELL (HON) as well as traditional DRAM vendors such as MICRON, SAMSUNG ELECTRONICS (SMSEF), and NEC (NIPNY) are all said to be looking into the MRAM technology. But for now, IBM seems to be the nascent industry's front-runner.

Wall Street analysts haven't started to calculate the potential size of the MRAM market. And no one is predicting that demand for DRAM chips will instantly dry up once MRAM chips hit the market.

Trouble is, MICRON TECHNOLOGY, along with other DRAM makers, now appears to be caught up in a looming industry downturn that, if history is any guide, could last a couple of years. An eventual rebound in demand for memory chips could emerge just as MRAM chips start to garner quite a bit of industry buzz. In other words, just as the skies clear for DRAM makers, a new front could roll in.

Recent Trends & Innovations:

December 21 Get Ready for Some Hot Air on Streaming Media

December 14 Higher Energy Prices Are Rekindling Interest in Technology Companies

9. Venture Capital

The Best and Worst of Times

By Stephen DeNichilo

Hindsight is always 20-20, isn't it? Remember this time last year? Remember all the hysteria about the Y2K bug? I clearly recall watching the cheesiest made-for-TV movie ever on NBC about the possibility of the Y2K bug wreaking havoc all over the world. Traffic lights breaking, elevators plummeting, jet planes crashing – it was nuts. Then the day came and went. OK, so I did take a quick deep breath right before the ball dropped in Times Square, but I knew things would work out. It's funny when you recall how we acted.

Since that crazy night (the New Jersey shore is nuts around New Year's by the way) we have etched another year on the wall. A little wiser, with lower portfolio returns, we lick our collective wounds and look to the future. Ah the future! While it's futile to chase the horizon, Alan Kay, the pioneer of the laptop computer, once said, "The only way to predict the future, is to invent it." So invent I shall. Allow me to step onto my soapbox, take a deep breath, speak from the diaphragm and bestow on you some trends we are likely to see in the coming year. The best part of the future is that it is unwritten, allowing anyone with Microsoft Word to predict where we'll end up. One shouldn't even care if their predictions might be way off base – even a broken clock is right two times a day.

Top 10 Trends for 2001

10. Regulation FD will crush the infallibility of research analysts

Once upon a time, in a galaxy far, far away, Zeus reached down from the heavens and bestowed on Ivy League M.B.A./C.F.A./Ph.D.s infinite wisdom and power, allowing these mere mortals to move our portfolios 20% in either direction, with the power of a single research report.

Things have changed. With the implementation of the Security and Exchange Commission's Regulation FD ("Fair Disclosure"), chairman Arthur Levitt spearheaded an attempt to level the playing field – allowing us "non-analysts" to be privy to the same information at the same time as everyone else. Since taking effect in the fall, we have heard less and less about "earth-shattering" reports from top analysts.

Granted, the market has been in the dumps, but I don't think that it's coincidental that all of a sudden large, established companies with track records of nailing estimates, are slowly missing forecasts and leaving analysts to massively downgrade.

In the past, this was how it worked. When a company would sense that sales were coming in a little light, during analyst-only meetings or cozy quarterly lunches, top brass would "guide" analysts to lower their estimates. Analysts would in turn call their favorite mutual funds and hedge funds to let them know about the impending estimate change. The mutual funds would sell and the hedge funds would short. The next day, estimates would be lowered with a positive BUY-reiteration spin and the stock would drop. Hedge funds would quickly cover their short sales, softening the blow and we would all accept the lower current estimates knowing that in the long-term all will be well.

What do MICROSOFT (MSFT), COMPAQ COMPUTER (CPQ), GATEWAY (GTW), BROADCOM (BRCM), APPLE COMPUTER (AAPL), INTEL (INTC), MOTOROLA (MOT) and ETOYS (ETYS) all have in common? In recent weeks, out of nowhere, they have all announced significant shortfalls in fourth-quarter estimates and have caught most investors by surprise. APPLE, in fact, announced that for the first time in over three years, it would be in the red because of a $600 million shortfall in revenue. APPLE's shares have lost nearly 70% of their value since the beginning of the year. Nobody saw this coming? Now, 12 of the 17 analysts covering APPLE rate the stock a HOLD, after two years of BUY recommendations.

Now that Regulation FD has taken away analysts' edge, I foresee a shake-up in the industry. Analysts will have to prove their million-dollar salaries by taking risks, and downgrading or upgrading a company based on analysis/metrics/experience, rather than revenue numbers that have been spoon-fed from a company's management.

9. We understand what optical networking is all about.

When it rains it pours. All it takes is a couple of feature articles in The Wall Street Journal, a mention in Barron's, a clear leader and BAAM! – the next trend emerges. Wall Street embraced optical networking in 2000 as an altering-technology. Optical networking will make the transfer of information faster, better, and more efficient. But along with new technologies comes the slow ability to value them and the inevitable copycats. In 2001 the world will be begin to understand what optical networking is all about.

The metamorphosis from copper wires to strands of glass is profound. The constant increase in Internet users and the use of larger applications programs have created an insatiable need for bandwidth. A leading telecommunications market researcher, RHK, has predicted the optical networking sector will grow to $23 billion by 2003. So what will the world learn about this sector that they don't already know? Two things: which companies will be around 10 years from now and how to value them.

Big mutual funds and VCs have shoved their billions of dollars into the optical space after the dot-com fallout. If the sector's margins begin to fall or if sales slow, most professionals will be left with the lights out and billions of dollars to move elsewhere. Much like the PC, semiconductor and dot-com industries have shown before – first there is a rush to get into the space followed by an inevitable shakeout.

Right now, many complex optical components are still built by hand, which keeps prices very high. Competition and advancements will bring more automation to the process, thus lowering prices and margins. Optical prices have to fall, or the technology will never become mainstream – that's the way it has to be. At first, VCRs cost more than $300, and now you can buy one for $65. It's not JDS UNIPHASE's (JDSU) fault that prices are falling, but these companies are still richly valued.

In 2001, leaders in the sector will emerge and we'll learn how to value these leaders – for good or bad.

8. Financials will falter

This is a simple one. A slow IPO market, lower trading volumes, and market volatility create a moment of truth for financial stocks. Companies like MORGAN STANLEY DEAN WITTER (MDW), CITIGROUP (C), CHASE MANHATTAN (CMB) and J.P MORGAN (JPM) must prove that their profits are not tied just to underwriting fees and proprietary trading. In the past, Wall Street giants made a killing by underwriting highly valued technology companies and, for the time being, that window is closed. Coupled with individual investors losing confidence and proprietary trading hardships, we will see broker/dealers move towards percentage-fee generating accounts, and offer clients other banking services to increase margins. While Wall Street will certainly not close shop, most will rethink their strategies in light of the market. Eventually they will have to adapt but, in 2001 most will experience growing pains.

7. Amazon.com will turn a profit

AMAZON.COM (AMZN) will announce fourth quarter 2001 earnings of $0.26 a share. OK, I am kidding, but the coming year will be the moment of truth for the venerable dot-com. The world will know once and for all if e-commerce can generate a profit. AMAZON is the brand leader, has the most cash, and the most products – and if it doesn't work out, that's all she wrote, folks. This time next year there will be no more debate about the company. There will be no more case studies, needless jabs or questions about the business model. The company that sparked the B2C explosion will either make it or not, and that will be the end of that.

6. Broadband will still be a year away

Last Christmas, I called my local cable company CABLEVISION SYSTEMS (CVC) to ask about getting a cable modem, and I immediately sensed a light chuckle through the phone. I called again this year, and much to my dismay, high-speed Internet service was still unavailable. This is hysterical. In this country, we act as if we are the gods of all technology, doubling speeds every six months. Still, here I am, dialing up at 56k (in theory, because in reality the connection rarely makes it above 40k). What am I doing wrong? For the average individual, who has network connections at work, this makes home Internet use nothing more than a chore, as we wait patiently for Yahoo! to download.

A recent FORRESTER RESEARCH (FORR) study reports that by 2001, broadband connections in the United States will double. That would be nice. E-marketer, an online research firm, estimates that by 2003, 32 million users in America will subscribe to broadband. Currently AMERICA ONLINE (AOL), the leading dial-up provider, has about 28 million subscribers. AOL, founded in 1985 and the clear brand leader in Internet service, has taken 15 years to reach 28 million subscribers. Without a clear brand leader or even the technological capability to reach everyone (unlike AOL, everyone has a phone line), these broadband penetration estimates seem high. Bottom line: If you build it affordably, they will come. Some companies charge over $75 a month. That's just a little too high right now. Broadband will come – but not just yet. Someone needs to become the clear leader.

Don't change that channel, the conclusion of the Top 10 Trends of 2001 will be featured next week.

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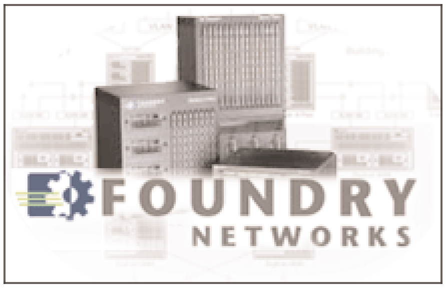
10. The Analyst's Spotlight



Foundry Networks

Erik Suppiger, Networking Analyst, Chase H&Q

Interviewed by Taylor Smith

The Internet Analyst℠ *recently spoke with Erik Suppiger, who covers the networking industry for Chase H&Q, about FOUNDRY NETWORKS (FDRY). The company lost half of its market value on Dec. 19 after it told analysts and investors that fourth-quarter earnings would be roughly half of the consensus estimate of $0.24 per share. (Chase H&Q has not done any investment banking work for FOUNDRY NETWORKS and Mr. Suppiger does not own stock in the company.)*

[THE INTERNET ANALYST – TAYLOR SMITH] What does FOUNDRY NETWORKS do?

[ERIK SUPPIGER] FOUNDRY sells Layer 3 switching equipment. [Layer 3 is the network layer in the International Standards Organization's hierarchy of communications protocol. Internet protocol (IP) is a Layer 3 standard.] Between 60% and 65% of the company's revenue comes from sales to companies in the service provider market, with a concentration in North America. FOUNDRY also offers customers smaller product lines that include Layer 4 through Layer 7 switching equipment and Internet routing.

[TS] What else, besides the company's revised earnings forecast, has contributed to FOUNDRY's recent stock market woes?

[ES] The North American service provider market is starting to show some cracks in terms of a slowdown in sales growth and a drying up of available capital, especially with the smaller companies. DSL-oriented competitive local-exchange carriers (CLECs), Web-based ISPs and regional ISPs have all been affected by these sales slowdowns.

However, FOUNDRY also sells equipment to top-tier service providers – which include companies like QWEST COMMUNICATIONS (Q) and AMERICA ONLINE (AOL), whose markets seem to be more stable.

[TS] What do you see for the service provider market going forward?

[ES] I believe that the service provider market is going to experience continued volatility for the next several months. I don't see any signs of a quick recovery, though I do see the potential for some consolidation in the industry.

[TS] What is your rating for FOUNDRY's stock?

[ES] I currently have a BUY rating on the stock. For calendar year 2000, I expect revenues of $377 million and earnings per share of $0.71. Revenue should rise to $523 million in 2001 with earnings per share of $0.72.

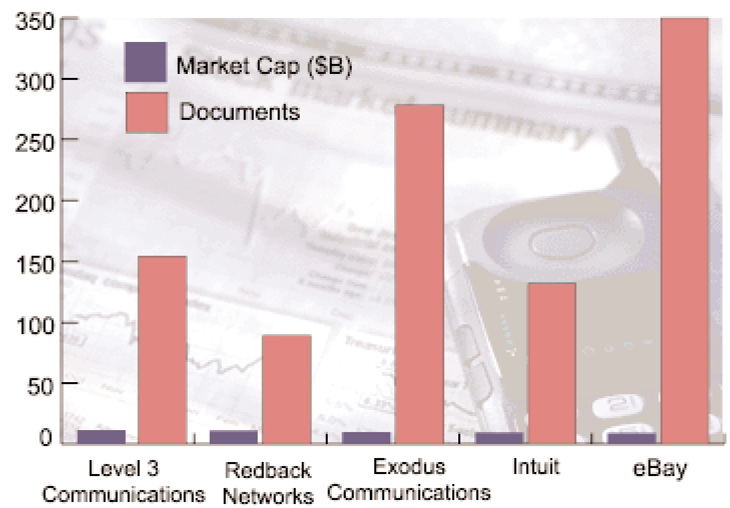
Vital Statistics Erik Suppiger Network analyst, Chase H&Q	
Education	Boston University
Industry	Networking industry
Companies	3COM (COMS), CABLETRON SYSTEMS (CS), EXTREME NETWORKS (EXTR), FOUNDRY NETWORKS (FDRY), F5 NETWORKS (FFIV), SUNRISE TELECOM (SRTI), CHECK POINT SOFTWARE TECHNOLOGIES (CHKP) and SONICWALL (SNWL)

Recent Analyst's Spotlights:
December 21 Razorfish: Vincent Colicchio, Southwest Securities
Decenber 14 Network Appliance-James D. Poyner, C.E. Unterberg Towbin

11. Top U.S. Picks

Ciena's Purchase of Cyras Systems Is No Threat to Redback Networks

By Eric Lopkin



21	Level 3 Communications	LVLT	
	Documents 154	MarketCap $11.29	
22	Redback Networks	RBAK	
	Documents 89	MarketCap $10.86	
23	Exodus Communications	EXDS	
	Documents 278	MarketCap $9.77	
24	Intuit	INTU	
		Documents 132	MarketCap $9.05
26	eBay	EBAY	
		Documents 350	MarketCap $8.81

N.A. Not available

LEVEL 3 COMMUNICATIONS (LVLT): This global communications and information services company offers IP-based services including broadband transport, co-location services, submarine transmission services and Softswitch-based services. LEVEL 3 recently expanded its offerings into the Indianapolis, Ind., and Sacramento, Calif., markets, bringing the number of its advanced data centers, called Gateways, to 54. In a recent report Credit Lyonnais Securities said that it expects the number of Gateways to grow to 73 by the end of 2001. It also expects management to guide revenue estimates higher, based on sales of dark fiber. Research on LEVEL 3 was accessed 1,243 times and 154 new reports were added to the Multex.com database from Dec. 11 to Dec. 17.

REDBACK NETWORKS (RBAK): On the news of CIENA's (CIEN) purchase of Cyras Systems, shares in REDBACK, an advanced networking solutions provider, dropped approximately 22%. The concern of investors was how REDBACK would compete against CIENA. Robertson Stephens says that it believes the sell-off was overdone and the company now represents an excellent buying opportunity. Its reasoning is that CIENA and REDBACK don't compete in exactly the same space, so the new acquisition won't affect REDBACK. Robertson Stephens reiterated its BUY recommendation as well as its 2000 earnings estimate of $0.04 a share. Research on REDBACK was accessed 1,542 times and 89 new reports were added to the Multex.com database from Dec. 11 to Dec. 17.

EXODUS COMMUNICATIONS (EXDS): Lehman Brothers initiated coverage of the co-location, Web-hosting company on Dec. 13 with a rating of OUTPERFORM and a $45 price target. Lehman believes that the company's recent move into managed hosting services will not only open up a new market, but allow it to sell more advanced services to its existing customer base. The firm recommends the stock "because of the company's market leadership, new strategic focus on managed hosting and the relative liquidity of its shares. As one of the dominant hosting players, EXODUS is likely to lead a rebound in Internet infrastructure stocks." Research on EXODUS was accessed 2,440 times and 278 new reports were added to the Multex.com database from Dec. 11 to Dec. 17.

INTUIT (INTU): On Dec. 21 this provider of small business accounting and management solutions announced it had completed its acquisition of privately held EmployeeMatters for $41 million in INTUIT stock and assumed liabilities and $8 million in interim funding. The acquisition will expand the company's offerings to include human resource management, benefits and payroll services via the Internet. INTUIT currently plans to promote the new offerings under both the QuickBooks and EmployeeMatters brands. The company also plans to develop the capability for customers to integrate the data from their EmployeeMatters products and services into future versions of the company's small business products. The acquisition will help further diversify the company as its tax-preparation products come up against increased competition from H&R BLOCK (HRB) and MICROSOFT (MSFT). Goldman Sachs believes that INTUIT will be able to withstand the increased competition easily and reiterated its MARKET OUTPERFORM rating on Dec. 22. Research on INTUIT was accessed 706 times and 132 new reports were added to the Multex.com database from Dec. 11 to Dec. 17.

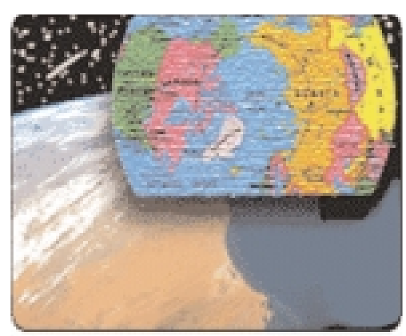
EBAY (EBAY): The world's largest online trading community has launched a new trading Web site for users in Austria. The site, which is an extension of EBAY Germany, brings together in one area EBAY listings that originate in Austria. Dain Rauscher Wessels says that this expansion demonstrates the scalability of EBAY's platform and operations. The firm reiterated its BUY rating for aggressive portfolios on Dec. 19. EBAY recently reached an agreement with GENERAL MOTORS (GM) that involves joint promotions and community events on eBay Motors, where consumers can bid on cars, trucks, parts, and accessories. In addition, GM will become the exclusive automotive sponsor of EBAY subsidiary Kruse International, an auctioneer of collector cars. Research on EBAY was accessed 1,264 times and 350 new reports were added to the Multex.com database from Dec. 11 to Dec. 17.

12. Global Prospects

BCE Emergis

A Canadian Player Emerges as B2B Power

By Mike Robbins



Canada's BCE EMERGIS (IFM) doesn't get all that much attention in the United States, but it might just be one of the most attractive B2B plays on the continent. That's the opinion of many of the Canadian investment banks that cover the stock. Ian Prittie of National Bank Financial and Jason Zandberg of Goepel

McDermid both rate the stock a BUY, while David Shore of CIBC World Markets and Farhan Syed of Yorkton Securities rate it a STRONG BUY. The four have set 12-month target prices ranging from $90 Canadian to $125 Canadian. The stock closed at $43.45 Canadian on Dec. 22, far off its high of $189.50 Canadian. To date, most U.S. investment banks have not initiated coverage.

BCE EMERGIS specializes in e-procurement, e-transaction security, and e-billing and payment, with a focus on the health care (48% of third-quarter revenues), telecommunications (26%), financial services (24%) and transportation (2%) sectors. By most accounts, this leaves BCE EMERGIS very well positioned. The e-procurement market is expected to grow perhaps 50% annually through 2003. The financial services and health care verticals in particular are considered strong growth areas. Mr. Prittie anticipates 100% annual growth. Mr. Zandberg adds that electronic bill presentment and payment (EBPP) should grow at a 100% rate annually through 2005. At last count, BCE EMERGIS was involved in 80% of Canada's Internet bill payment transactions, primarily through its 10-year contract to act as technology provider and operator for e-Route, a Canadian consortium of financial institutions. "[BCE EMERGIS] has a stranglehold on the EBPP market in Canada through the major banks," Mr. Zandberg explains.

Canadians have proven much more willing to adopt electronic bill payment than Americans, adds Mr. Shore. However, BCE EMERGIS is also making a concerted effort to expand south of Canada's borders, with some success. In this year's third quarter, 38% of revenue came from the U.S., up from only 3% a year earlier. In some fields the company already has a very secure foothold in the States. In health care transaction processing, for example, EMERGIS not only provides claims processing for nine of the 10 largest Canadian insurance companies, but also for eight of the nine largest U.S. insurers.

Considerable concern has rightly been voiced in 2000 regarding a coming e-marketplace shakeout – the sector has grown from zero e-marketplaces in 1995 to more than 1,400 recently. But BCE EMERGIS bulls point out that the company has the size and financial backing – BCE (BCE), Canada's largest telecommunications group and one of the nation's largest companies, owns slightly more than two-thirds of EMERGIS – to survive in such an atmosphere. "Should there be a shakeout and consolidation phase in the industry, we believe EMERGIS is more than able to play consolidator, owing to its size and prominence," wrote Mr. Prittie of National Bank Financial.

BCE EMERGIS offers a wide range of services to customers in a variety of sectors, and thus finds itself in competition with a range of other companies. But it is, arguably, more comparable to COMMERCE ONE (CMRC) than any other American company. Some analysts make use of this comparison in labeling BCE EMERGIS a bargain. As they note, COMMERCE ONE recently traded at nearly triple the multiple of BCE EMERGIS, based on estimated 2000 revenue – this despite the fact that, unlike BCE EMERGIS, COMMERCE ONE is not expected to be profitable in 2000 or 2001. "We believe that this discrepancy in the valuation will be narrowed" says Mr. Prittie, "as BCE moves more into the U.S. marketplace and also achieves a U.S. stock listing and more exposure to American investors."

13. IPO Update

All Quiet on the New Issue Front as the Year Closes

By John Filar Atwood

It turns out that 2000 was the year the Internet valuation bubble finally burst. And along with it went Internet initial offerings, which now face a long road to recovery in 2001.

For years, analysts have expressed surprise at the reception given to unproven companies by IPO investors. Until this year, Internet companies were able to defy conventional, fundamentals-based valuations.

"In 2000, however, there has been a complete re-evaluation of the longevity of the fundamental business models of Internet companies," according to Jesse Soto, senior securities analyst at Highmark Capital Management. The companies had no profit goal in sight and were mired in a spend-to-build operating mode, he noted. As a result, they didn't break even as quickly as people had hoped, and investors finally gave up on them.

"We've moved from complete over-optimism to sobering reality," says Mr. Soto. Mr. Soto says that in retrospect, the slowing of the economy was the major factor that caused people to rethink technology investing this year. He believes that at the other end of investors' re-evaluation of Internet companies will be a very different IPO market.

"There will not be the same kind of blind faith in early stage, venture-type companies as we saw in 1999 and early 2000. Only more established companies will succeed in the IPO market."

Mr. Soto adds that strength in the broader market and a change in investor sentiment will be necessary to start to bring back IPOs. He noted, however, that a market that has been down for this long would likely make its comeback very slowly.

14. Rants & Raves

Opinion

Tax-Loss Selling Continues as We Bottom

By K. C. Grainger
Grainger Beaulac Inc.

It takes a long time to establish a bottom in the market, and as we saw in the last year, a market top can take a long time to be established, as well. Just because a market bottom appears to be in process of being formed, the market doesn't seem to want to rush to confirm that prognosis. Bob Morrow and I started warning investors in September 1999 of an impending market top. It took a while, but stock by stock, the Internet market topped out.

If you look at a chart for the overall market you will see that the blue chips haven't done much of anything for the last several months. Individual stocks and the Nasdaq are a different story. Many stocks can be found that probably have bottomed. Many Internet and high-tech issues may have excellent moves higher. But many will never come back. They will simply run out of cash.

We all know that the Federal Reserve is crucial in determining the direction of the stock market. Outside of a recession, nothing has a greater influence on market direction. The Fed knows what has to be done. A rate cut has to be forthcoming or else both the stock market and the economy will suffer.

Long bear markets usually start with interest rates moving up and a contraction in the money supply. Neither is occurring right now. Actually, both numbers are quite positive for the markets. And if no recession is approaching, the market is set for another bull move. If the Fed does cut rates, the potential is there for a 30% rally in the S&P 500 and the Dow Jones industrial average, based on historical comparisons. If they move up to that degree, Nasdaq will put in a great performance as well. This seems to be the time to be long – not short.

While the S&P 500 and the Dow industrials did not have a bear market by historical standards, the Nasdaq did. The valuations that the Nasdaq carried early in the year were excessive, and consequently had to undergo a more severe decline than the more moderate correction as we saw in the blue chips.

Investors looking for this year's highs to return ought to think twice. Even if you own a solid high tech or Internet, it will be extremely difficult for that stock to return to its old highs. On average it takes four years to do so. For example, LUCENT TECHNOLOGIES (LU) should be capable of a move to near $30 within the next 10 months – hey, that's double the current price. But a move back to its old high of $78.13 is out of the question – for years. NORTEL NETWORKS (NT) is potentially capable of getting back to $55 to $60 in the next 10 months. But if Bob and I are correct in those targets, we will probably see a painful bear market soon after LUCENT and NORTEL hit those prices.

The bottom line is that we still believe that we will have a good 10 months or so ahead. But prudent investors will be taking money off the table during that time. It's a shame, but too few investors have the discipline to take that step. – *With Robert S. Morrow, Robert S. Morrow Institutional Advisory Services*

Letters to the Editor

2001: The Economy and the Stock Market

Katherine M. Harmeyer writes: The fundamental backdrop that supports your technical analysis for the equities market over the next 12 to 18 months (Rants & Raves, The Internet Analyst, Dec. 21, 2000) is potentially as follows.

Assume that the inventory build-up that occurred in the third quarter of this year decelerates rapidly and substantially going into the first and second quarters of 2001, and the economic downturn currently expected by Wall Street is thereby avoided. Under those circumstances, the widely anticipated interest rate cut – perhaps 50 basis points – by the Federal Reserve's Open Market Committee at its Jan. 31 meeting (possibly followed by a further 25 basis point cut at the March 20 meeting) should spark a nice rally in the equities market in the first half of next year.

U.S. consumers will continue to spend freely if the stock market takes off again. That's why the Fed was reluctant to cut rates at its Dec. 19 meeting without first knowing whether real economic growth in the fourth quarter accelerated from the 2.2% growth rate in third quarter. (That's just what has happened each time in the last four years when it has appeared that the economy finally was slowing down.) Consumer spending fueled by home equity gains should protect the U.S. economy from recession in the near term. Note that mortgage refinancing applications have risen by 95% during the last four weeks. Economic data suggest that homeowners are spending the proceeds of their refinancings, rather than using the money to pay down debt, as was the case when mortgage refinancings increased in the early 1990s.

The potential problem for the economy – and for the Fed – is that the current shortage of energy is not a transitory problem. The strains that higher energy costs and wages have placed on corporate profits may re-emerge by the third quarter of 2001 because of OPEC production cuts, increased energy demands and the still-tight labor market. The Fed could be forced to raise interest rates again late next year to rein in inflation. At that point, consumers may be "tapped out," having used up much of their home equity gains and achieving small, if any, real income gains. If appreciation in the residential real estate market levels off, or if home prices begin to decline at a time when the stock market is flat to down, the economy could stagnate for a prolonged period. There will not be a significant catalyst to fuel consumer spending, which accounts for two-thirds of U.S. gross domestic product

Further, consumer indebtedness is at a 20-year high in this country, so unless real wage gains improve substantially in 2001-02, which, given the corporate profit picture, is not likely, consumer spending is likely to be depressed for some time.

A prolonged recession in the U.S. would, of course, have a negative impact on global economies, as American consumers have provided much of the demand for cheap imported goods since the Asian financial crisis surfaced. The Japanese economy is showing signs of lapsing back into recession. It appears doubtful that the European economies will be able to provide a significant source of consumer demand, particularly if energy prices, which disproportionately affect European consumers, spike up again next year.

Thus, the next recession is likely to be severe and of global proportions, and will not be susceptible to a quick fix.

Convergence Industry Index (in alphabetical order)

Company / URL, Ticker, Stock price*, EPS*
Market cap*, Location
Description

Public:

ACTV / www.actv.com (IATV) $4.34 -$0.54
221.24M New York Software to synchronize TV programming with Net content delivery

AT&T / www.att.com (T) $17.06 $1.78 64.04B
New York Telecom, Internet, computers, cable TV

BellSouth / www.bellsouthcorp.com (BLS) $40.13 $2.19 74.96B Atlanta Telecom, Internet, cable and digital TV, wireless access

Chequemate International / www.3d.com (DDD) $0.44 -$3.04 5.53M Marina Del Rey, CA 3-D TV network; Net-transmitted video; special effects software

ClearWorks.net / www.clearworks.net (CLW) $1.63 -$0.21 28.78M Houston Bundled Net/phone/video services; networking

Comverse Technology / www.comverse.com (CMVT) $91.38 $1.58 15.04B Woodbury, NY Phone/computer access to voice/fax/e-mail; multimedia systems

Convergent Communications / www.converg.com (CONV) $0.69 -$7.38 20.42M Englewood, CO Telecom & Net services, networking, Web/e-business development

Datalink.net / www.datalink.net (XLNK) $2.88 -$0.65 42.84M San Jose, CA Web-to-wireless platform for delivery of content; software

Deutsche Telekom / www.dtag.de (DT) $30.19 $1.48 91.46B Bonn, Germany Telecom, cable TV, radio, Internet, programming

General Electric / www.ge.com (GE) $47.88 $1.23 474.38B Fairfield, CT Telecom, broadcast and cable TV, Internet, computers

Gemstar-TV Guide International / www.tvguideinc.com (GMST) $43.25 $0.17 17.70B Pasadena, CA Technology for delivering cable & Net content to various platforms

Global Crossing / www.globalcrossing.com (GBLX) $12.81 -$2.00 11.35B Hamilton, Bermuda Fiber optic telecom and Net service, Web hosting, software

Handspring / www.handspring.com (HAND) $33.94 -$0.98 4.31B Mountain View, CA Handheld computers offering wireless Net and modem connection

InfoSpace / www.infospace.com (INSP) $6.00 -$0.71

1.89B Redmond, WA Content for Web sites and wireless; software

ITXC / www.itxc.com (ITXC) $6.72 -$1.51 295.14M Princeton, NJ Net-based voice & fax service, voice-enabled applications

Liberate Technologies / www.liberate.com (LBRT) $12.69 -$2.19 1.31B San Carlos, CA Software platform for content to delivery via Net and telecom

Lucent Technologies / www.lucent.com (LU) $14.19 $0.68 47.38B Murray Hill, NJ Telecom equipment, Internet, content, computer networking

Microsoft / www.microsoft.com (MSFT) $43.44 $1.71 231.62B Redmond, WA Internet, telecom, computer hardware, cable TV

Nextlink / www.nextlink.net (NXLK) $15.56 -$2.90 5.69B McLean, VA DSL service, Net access, Web design & hosting, VPNs

Nokia / www.nokia.com (NOK) $39.94 $0.64 186.47B Espoo, Finland Mobile phones, Internet, computer hardware, interactive TV

Oracle / www.oracle.com (ORCL) $29.50 $1.13 165.12B Redwood City, CA Database software enabling Net access from PCs and appliances

Palm / www.palm.com (PALM) $25.63 $0.10 14.50B Santa Clara, CA Handheld computers offering wireless Internet connection

Primus Telecommunications / www.primustel.com (PRTL) $1.94 -$4.74 78.32M McLean, VA Telecom and Net services, networking, Web hosting and design

Pumatech / www.pumatech.com (PUMA) $3.81 -$0.72 167.20M San Jose, CA Software for exchanging data via Internet and telecom

Real Networks / www.realnetworks.com (RNWK) $5.56 -$0.46 876.93M Seattle Software for playing audio and video over the Internet & broadband

Research in Motion / www.rim.net (RIMM) $65.94 $0.07 4.72B Waterloo, Canada Handheld computers offering wireless Net and modem connection

SBC Communications / www.sbc.com (SBC) $44.88 $2.45 151.90B San Antonio, TX Telecom, Internet, cable TV, networking

Scientific-Atlanta / www.sciatl.com(SFA) $37.81 $1.45 6.09B Norcross, GA Set-top boxes for cable and Net transmission; networking services

Sony / www.world.sony.com (SNE) $69.56 $0.95 63.36B Tokyo Media, Internet, computer monitors, telecom

Source Media / www.sourcemedia.com (SRCM) $0.73 $2.86 12.60M Dallas Streaming media content via Net, cable; networking services

TiVo / www.tivo.com (TIVO) $5.50 -$2.21 238.75M San Jose, CA Set-top boxes for cable and Net transmission

United Pan-Europe Communications / www.upccorp.com (UPCOY) $9.88 N/A 4.36B Beverly Hills, CA Set-top boxes for cable & Net transmission, telephony

USA Video Interactive / www.usvo.com (USVO) $0.49 N/A 56.98M Mystic, CT Video on demand systems and software via Web and telecom

Virage / www.virage.com (VRGE) $5.25 -$1.67 105.90M San Mateo, CA Software for distributing media via Internet and telecom

Wave Systems / www.wavesys.com(WAVX) $5.06 -$0.96 241.21M Lee, MA Secure delivery of content over Net by cable, satellite; software

Winstar Communications / www.winstar.com (WCII) $11.31 -$9.41 1.04B New York Telecom and Net services, Web site creation, custom applications

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