



## Tech Valuations: Thoughts From Blackstone's Eric McAlpine

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Jeff Richards, partner with venture capital firm GGV Capital, recently had the opportunity to sit down for lunch with technology M&A and IPO guru Eric McAlpine of The Blackstone Group (BX). Together they discussed valuations of tech companies. Fortunately, Richards was kind enough to [transcribe the Q&A](#) exchange, which we have broken down for readers here.

To start, McAlpine has created the idea of "rare air," a concept that refers to a company's uniqueness and which makes it more desirable in the market compared to industry competitors.

For technology IPOs to gain "rare air" status, they should have significant scale and growth. Companies with over 10 years of proven success (in good economic times and bad) can also go a long way in proving to investors their company is a worthwhile investment.

"Beyond growth, important factors are things like sector leadership, long term margins at scale, and operating history." He makes an example of Facebook, Groupon and Zynga, all highly anticipated IPOs with a mix of these characteristics and potential to sell at a premium relative to industry averages.

Secondly, valuation multiples in the technology industry are predominately driven by a combination of earnings multiples and earnings growth. Because tech no longer has "the high earnings growth opportunity equity investors had come to expect," growth in the markets slowed "to around 10% overall, while the median Tech IPO since 2010 is growing at a median of 26% year over year, and an average of 38%."

Therefore investors are increasingly turning to tech IPOs with "rare air" to "gain exposure to growth and alpha" that they crave for their portfolios.

Given that high-growth tech stocks are a rarity, we were looking for ways to sniff out the ones that nevertheless appear to have bullish prospects.

For ideas, we started with a list of undervalued tech stocks, as defined by the price to earnings growth (PEG) ratio. All of the stocks mentioned below have PEG ratios below 1, which usually signals undervalued conditions.

To refine our list, we collected data on institutional buying and short covering, and identified the stocks showing bullish changes in investor sentiment.

All of the undervalued tech stocks mentioned below have seen increased institutional buying and increased short covering (both of them bullish trends). Do you agree that there's more upside to be priced into these names? Furthermore, do you think these names have the qualities to achieve "rare air" status?

List sorted by market cap. ([Click here](#) to access free, interactive tools to analyze these ideas.)

*List compiled by Eben Esterhuizen, CFA:*

**1. Teradyne** (NYSE: [TER](#) ) : Provides automatic test equipment products and services worldwide. PEG ratio at 0.54. Net institutional purchases in the current quarter at 5.9M shares, which represents about 3.18% of the company's float of 185.43M shares. Shares shorted have decreased from 19.35M to 16.82M over the last month, a decrease which represents about 1.36% of the company's float of 185.43M shares.

**2. Fairchild Semiconductor International** (NYSE: [FCS](#) ) : Designs, develops, manufactures, and sells power analog, power discrete, and non-power semiconductor solutions worldwide. PEG ratio at 0.81. Net institutional purchases in the current quarter at 4.5M shares, which represents about 3.57% of the company's float of 126.03M shares. Shares shorted have decreased from 5.24M to 3.92M over the last month, a decrease which represents about 1.05% of the company's float of 126.03M shares.

**3. AsiaInfo-Linkage** (Nasdaq: [ASIA](#) ) : Provides telecommunications software solutions and information technology (IT) products and services to telecommunications carriers and other enterprises in the People's Republic of China. PEG ratio at 0.77. Net institutional purchases in the current quarter at 6.2M shares, which represents about 14.21% of the company's float of 43.62M shares. Shares shorted have decreased from 12.92M to 11.90M over the last month, a decrease which represents about 2.34% of the company's float of 43.62M shares.

**4. Ebix** (Nasdaq: [EBIX](#) ) : Provides on-demand software and e-commerce solutions to the insurance industry. PEG ratio at 0.61. Net institutional purchases in the current quarter at 5.9M shares, which represents about 18.44% of the company's float of 31.99M shares. Shares shorted have decreased from 12.09M to 11.68M over the last month, a decrease which represents about 1.28% of the company's float of 31.99M shares.

**5. VanceInfo Technologies** (NYSE: [VIT](#) ) : Engages in the provision of information technology (IT) services. PEG ratio at 0.64. Net institutional purchases in the current quarter at 6.7M shares, which represents about 47.45% of the company's float of 14.12M shares. Shares shorted have decreased from 9.38M to 9.22M over the last month, a decrease which represents about 1.13% of the company's float of 14.12M shares.

*Interactive Chart: Press Play to compare changes in analyst ratings over the last two years for the stocks mentioned above. Analyst ratings sourced from Zacks Investment Research.*



See Full Screen

*Kapitall's Eben Esterhuizen and Rebecca Lipman do not own any of the shares mentioned above.*

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