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GG and the Gorilla Game

Long term buy and hold seems to be totally discredited. Trading, Elliot Waves and all manner of TA is now in vogue. Reminds me of women's hems going up and down -- one old timer says to another, where were the hot pants when we could do something about them?

It has been discovered that long term buy and hold is not buy and forget, you do have to tend your garden, do some weeding, do some pruning and add a few new varieties at appropriate times. Times might be accelerating but the clock is not yet turning so fast that LTBH must be abandoned. But we do need to be more exacting in our selection standards. When the bulls are on a rampage, almost anything goes but in more "normal" times (whatever that means) we do need to be more selective. How to reconcile GG and the market?

There are certain principles that markets obey that can be set in stone, the most important being that earnings and earnings growth drive prices higher. The best valuation tool is and will be the discounted present value of future cash flows. While markets exist, this valuation method will be valid. The problem is to find the right numbers to stick into the formula.

There has been a lot of debate on the forum about supply side economics, about "build it and they will come," and about better mouse traps. GG says that the best technology wins. Nay sayers retort that VHS beat out Beta and I say that Windoze beat out the Mac. On the other hand, CDMA is putting up a valiant fight against all opposition. Who can settle this argument? Mr. Market (not Wall Street but Main Street).

It is quite clear that Mr. Market has given Gillette and Coca Cola a thumbs up. This is one of the reasons why Warren Buffett likes them, because they have acquired a "franchise" that constitutes a barrier that the competition will find difficult if not impossible to climb. How do you acquire a similar franchise in the high tech world? By becoming a Gorilla or a King. A Gorilla, according to Geoffrey Moore, who coined the term, is a company that has an "Open Proprietary Architecture with High Switching Costs." These are few and far between but you only need two or three of them to have a very stable portfolio.

The problem in the Telecom is that carriers and service providers have to have mutually compatible protocols if the Internet and telephony are to be global, world wide services. This reduces the opportunities for proprietary architectures. In the fibersphere, where DWDM is the norm, there is no such proprietary architecture. In cellular, there is CDMA which did win the battle against Ericsson in 1G but now we are witnessing the fight for 2 and 3G. There is no guarantee that CDMA will be the winner until Mr. Market declares it to be so. In mobile there is a real Gorilla, the company that owns the most popular 16-32 bit RISC architecture.

But there is more to the Telecom than the infrastructure which is mostly what GG talks about. Once you have the hardware in place, it is used and operated by software and this is an area where Gorillas and Chimps should abound. You need security and virtual private networks (Checkpoint Software). You need to make sure that your network operates efficiently (Micromuse). You need to track usage and bill customers (Portal Software). I am certain that Portal Software is emerging as the undisputed winner of its tornado. Although not quite as sure of Checkpoint and Micromuse, they seem to be the best candidates.

Up to now we have identified five known or strong gorilla candidates. How about Kings? A King is a company that excels in execution like Dell or Walmart. In cellular, the RF chip maker preferred by the potential Gorilla is RF Microdevices. In the fibersphere, the most promising provider of abundant lambdas is Avanex. With the demise of Lucent (not a vast exaggeration even if it still breathes), Corning should be the King of fiber. With financing drying up and potential competitors facing imminent bankruptcy, Global Crossing with its "zero cost" approach to building the infrastructure, should become the Neptune carrier. Of course, Kings have to be watched a lot more closely than Gorillas because it is a lot easier to disrupt them.

With four or five Gorillas and four or five Kings to populate a portfolio, I really don't see the need to say that LTBH is dead. On the contrary, I think it's alive and well and much more productive than the churn produced by most traders. In this post I am naming five Gorilla candidates (QCOM, ARMHY, MUSE, PRSF and CHPT) as well as four King candidates (AVNX, GLW, GX and RFMD). Of these, six are mentioned by name and one is implied in the [Worry free portfolio](#) posted on

October 24 last year. There is no need to churn and to chase the latest and greatest. Between George Gilder (GG) and Geoffrey Moore's [Gorilla Game](#) (GG) there are plenty of Telecosmic stocks to chose from and the bears on Wall Street are giving us a great opportunity to pick most of them up at bargain basement prices.

Just today someone said on the forum that a bear of this quality takes eight or ten years to scare away. That may be so. But if you buy companies with earnings that are growing and if you buy them at reasonable P/E ratios, then you are doing the best you can. Flipping in and out may work for seasoned traders but it does not work for novices who let their emotions take charge. On the other hand, a well researched Gorilla is a long time hold that will, sooner or later, respond to the most basic valuation used on Wall Street, the discounted present value of future cash flows. If revenues are there and if earnings are there and if management is not idiotic, in the long run the value will show up in the form of stock price appreciation.

Denny

"Demand creates queues. Supply gets rid of them."

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