Business Computers: AMD's Next Hurdle

Many Business Buyers Remain Loyal to Intel; AMD Must Crack This Segment

During 1998, AMD and Cyrix showed that the power of the Intel brand could be overcome in the consumer market. Given a choice between pricey Intel-based systems and less expensive alternatives, more than half of retail-PC buyers chose non-Intel models. Furthermore, as nine of the top ten PC makers began using AMD processors, the association of these chips with no-name PCs disappeared.

Impressive as this success was, however, it was not enough for AMD to achieve profitability. AMD has set its sights high, with a goal of 30% market share. The company is investing in fab capacity at a rate that requires it to achieve something close to that share if it is to have a reasonable business. Furthermore, to reach acceptable average selling prices, AMD needs to be a player in the performance-oriented segments; owning the low end isn't enough.

Let's assume for the moment that AMD succeeds in launching the K7 and meeting its performance goal, which is to outperform anything Intel has to offer. Let's make an even bigger leap of faith and assume that AMD can produce both K6- and K7-family chips in volume, and that it can match Intel's clock speeds. The barriers then become ones of market acceptance, and these may be equally formidable.

The first step for AMD is to reach further into the consumer PC market, in terms of both channels and price points. AMD has received great publicity for its success in the closely watched U.S. retail channel, but this channel represents only about 10% of the worldwide PC market.

AMD's next challenge is getting into more expensive PCs. Profit margins for high-end processors are vastly greater than those for low-end chips. AMD has reached high-end performance points with the K6 III, but most PC makers don't appear willing to pay any more for a K6 III than for a K6-2, despite its better performance, since most PC buyers focus simply on clock speed. Customers seem to see the K6 as a Celeron competitor, regardless of its suffix or performance.

If the K7 reaches its performance goals, AMD should be able to make a strong play for the high-end consumer market. Consumers have shown they are comfortable with AMD processors, and with the right marketing and support from key OEMs (notably Compaq), AMD should be able to establish the K7 brand with different positioning than for the K6. AMD's one weakness is that the K7 has 3DNow instead of SSE; although the instructions are functionally similar, Intel's marketing campaign for SSE is far broader, and in the long run, there is likely to be more software for SSE.

AMD's capture of Gateway as a customer is an important move beyond retail. Expansion into the direct channel and into high-end PCs is just the start, though. If AMD is going to attain its 30% share, it must penetrate the business market more deeply. So far, even though all the major PC makers except Dell use AMD processors, they use them mostly in their consumer lines. Business buyers are more conservative, and PC makers have been wary of taking the risk with a non-Intel processor in this segment.

Last November, I was on a panel at Comdex about alternative processors. In the audience were a hundred or so IT managers. When I asked how many would consider buying a non-Intel system for home use, a majority raised their hands. When I then asked how many would recommend a non-Intel system in their IT role, almost all the hands dropped. The very same people who saw an AMD or Cyrix system as a good choice for their home weren't willing to stick their necks out and recommend one at work. There used to be a common saying: "No one ever got fired for buying IBM." This apparently has become, "No one ever got fired for buying Intel."

AMD must overcome this barrier. AMD's share of U.S. desktop sales in the business-oriented dealer channel, according to Infobeads, was only 2% in April, compared with 43% in the consumer-oriented retail channel. AMD's bigger success is in small businesses, which often buy from consumer channels. AMD estimates it has a 24% share of the U.S. "white-box" market—systems from system integrators—of which it estimates 65% are sold to small businesses.

AMD has had considerable success moving into notebooks; its share in the U.S. retail market went from zero in 1997 to an impressive 43% in April 1999, matching its desktop share, according to Infobeads. Compaq even uses an AMD chip in one of its Prosignia business notebooks, and NEC sells an AMD-based business notebook in Japan. In the dealer channel, however, AMD portables remain invisible.

To move into the enterprise market, AMD must convince stodgy IT buyers—and the PC makers that sell to them—that there is no reason for AMD to be pigeonholed as a consumer supplier. AMD must show that the K7, and AMD itself, will prosper in the long run. It must establish its K7 bus architecture as a strong, well-supported alternative, and it may need to add Intel's SSE instructions. It will not be an easy or a quick fight, but there is no reason that AMD should not eventually achieve the same success in the business market that it has enjoyed with consumers. M

See www.MDRonline.com/slater/amdbizpc *for more on this subject. I welcome feedback at* mslater@mdr.cahners.com.