Are Yahoo and Microsoft Crazy?

| By MICHAEL MARKOWSKI |

Yhoo (NASDAQ: YHOO) is crazy to not take the $31 cash and share offer that Microsoft (NASDAQ: MSFT) has given it. Microsoft is even crazier to have made the "rich" offer in the first place. Yahoo's annualized free cash flow (FCF) has not grown since 2005, and its annualized revenue is now growing at approximately 10%. For its last five CJuarters, its annualized FCF has been in decline. The last time that Yahoo's FCF growth declined for five consecutive quarters was from March 31, 2001, to June 30, 2002, when its shares declined and remained under $10.00 for that entire IS-month period. Had Microsoft been monitoring Yahoo's FCF, they would have been a little more patient. I believe that without Microsoft's offer, Yahoo shares would have again eventually drifted down to $10.00.

In my June 2007 Winners and Sinners column, I suggested that readers avoid the shares of Yahoo, eBay (Ni\SDAQ: EBAY) and Amazon (NASDAQ: AMZN) because according to their respective decelerating cash-flow growth rates, the party was over for all three companies. Annualized cash flow from operations (CFFO) growth had fallen off a cliff for all three of them, in the form of low single-digit growth rates for eBay and Amazon, and a decline for Yahoo. The shares of all three have since declined.

I recommended that Priceline.com (NASDAQ: PCLN) shares should be purchased because its party was just beginning. Its annualized CFFO and its FCF at the time were accelerating by 83% and 89%, respectively. Priceline.com shares responded by going from $61.57 on June 1, 2007, to a most recent price of $114.02, an increase of 85%.

What is the status of these four now? If the deal with Microsoft doesn't happen, Yahoo looks pricey because it has very little cash-flow growth momentum. After hitting an all-time low annualized FCF growth rate of 3% in the 12 months ended March 31, 2007, eBay's most recent annualized FCF was back above 25%. Its shares are very attractive, since they are now trading for the first time at under 20 times FCF. Amazon's most recent annualized FCF has rocketed to an annualized 118%, and I expect that its shares wiJl outperfor'm the market over the next 12 months. Finally, Priceline.com's shares have reached full potential, based on its current price (to FCF multiple of 48), and its FCF growth has slowed to an annualized 32%. E