

ANNEX BULLETIN

Annex Bulletin 2006-20

May 2, 2006

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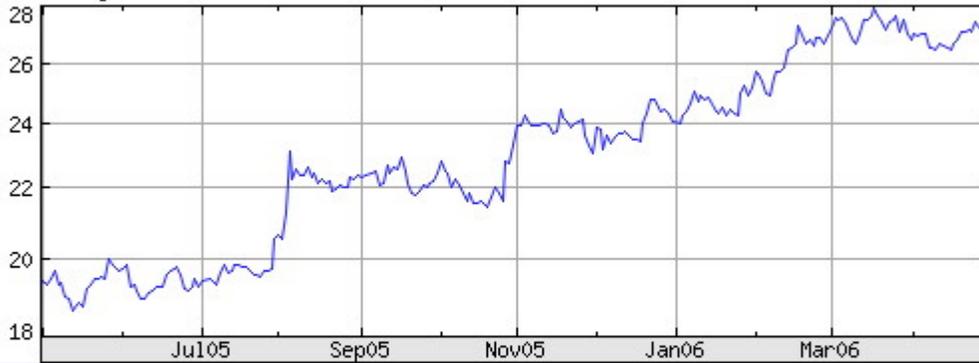
Analysis of EDS' First Quarter Business Results

Up and Down Quarter

EDS Improvements Come from Low Margin Megadeals

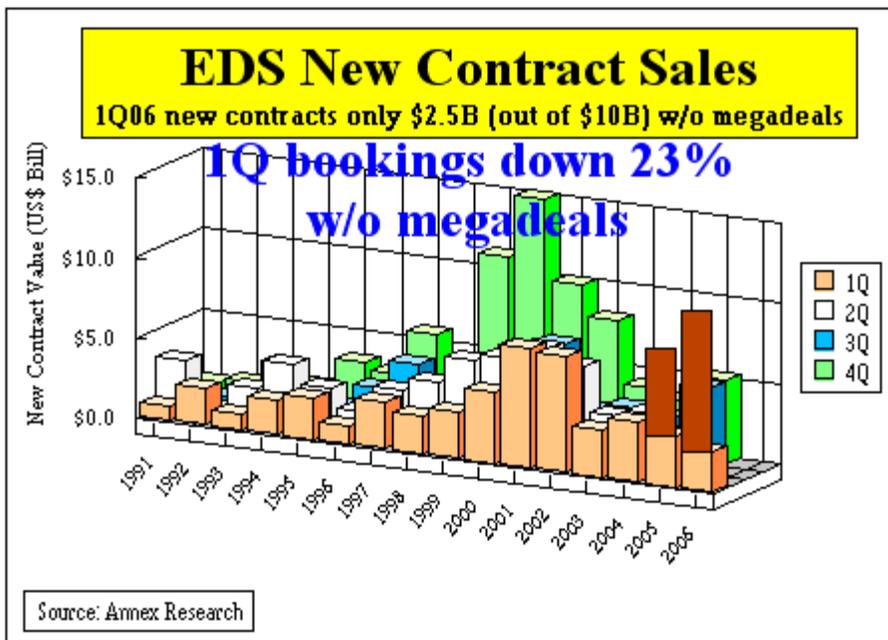
SCOTTSDALE, May 2 - EDS shares were flirting with their 52-week high of \$28.08, set on March 6, after the company released its first quarter 2006 business results. The EDS stock was trading at \$27.60 in after-hours trading, on top of a gain in the last two days of about 50 cents, in anticipation of solid earnings report. And solid it was.

ELECTRONIC DATA SYSTEMS CORP
as of 1-May-2006



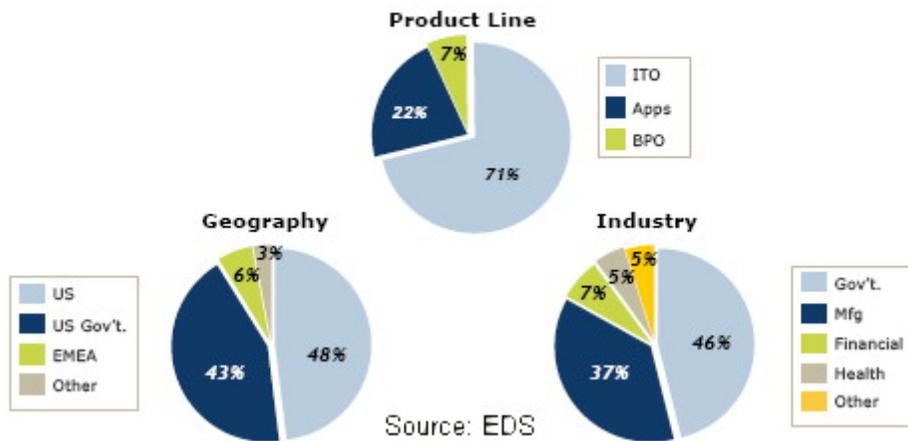
EDS shares approach 52-wk high after solid 1Q06 results

Net earnings jumped six-fold to \$24 million on revenues of \$5.1 billion, up 7% over the corresponding period a year ago. Alas, even this vastly improved profitability means a mere 0.5% net margin at the bottom line. Such is the fate of a megadeal-chaser.



EDS's new contract sales make the same point in spades. The company hailed an apparent 45% boost in new contract signings, from \$6.9 billion in 1Q05 (restated from \$7.1 billion) to \$10 billion in the latest period. But take away the renewals of the 2006 megadeals (GM, U.S. Navy), and the big U.K. MoD \$3.85 billion megadeal win in 1Q05, and what is left is a 23% decline in net new bookings (down 18% from the restated 1Q05 total).

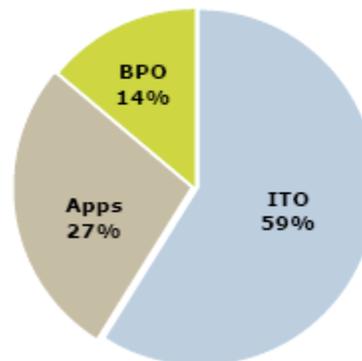
1st Quarter 2006 Signings Performance
Contract Signings — \$10.0B



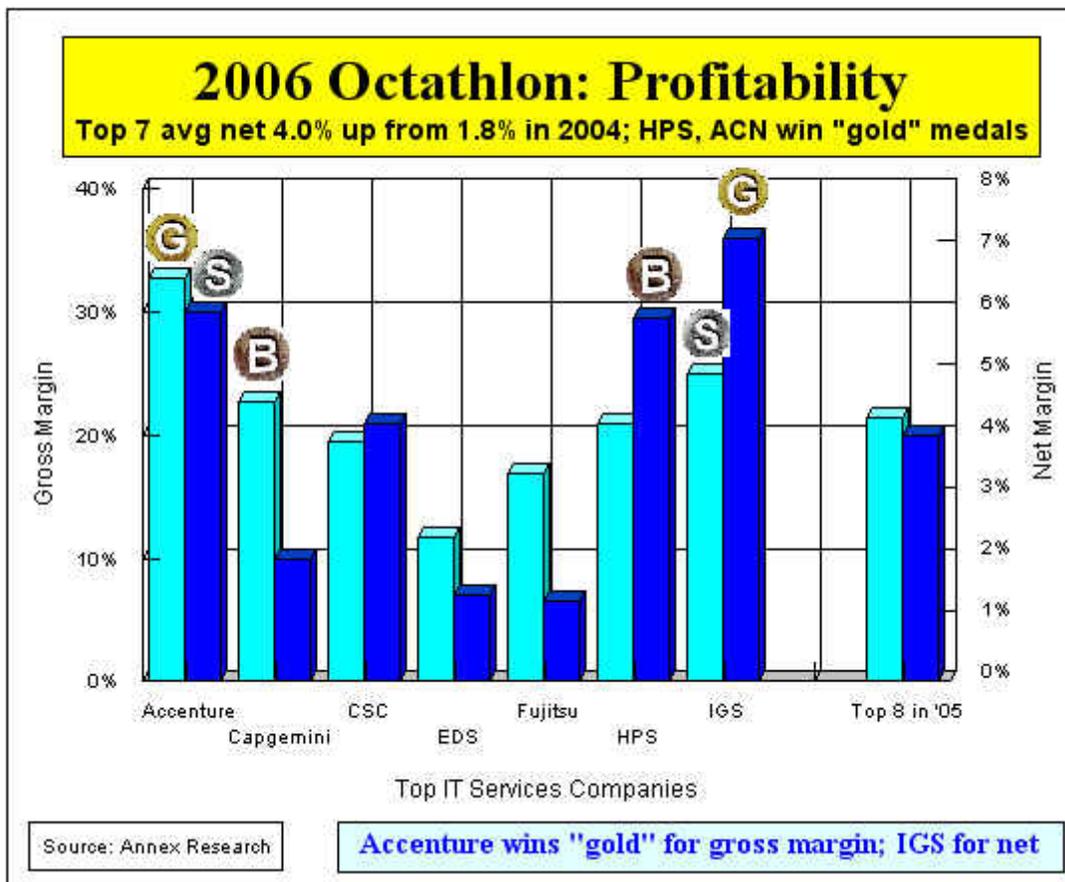
Worse, compared to the 1Q04 and 1Q02, the last year of the Dick Brown administration, the latest new bookings are down 34% and 65% respectively. The company's new CFO, Ron Vargo, admitted in a teleconference that followed the earnings release that only 22% of the first quarter new contract signings were truly new accounts (meaning, 78% were renewals).

So the EDS improvements seem to be *solely* based on its megadeal wins. Given how competitive, and thus relatively unprofitable they are, not just for EDS for most megadeal winners, no wonder the company's bottom line is barely above break-even.

1Q 2006 Revenue

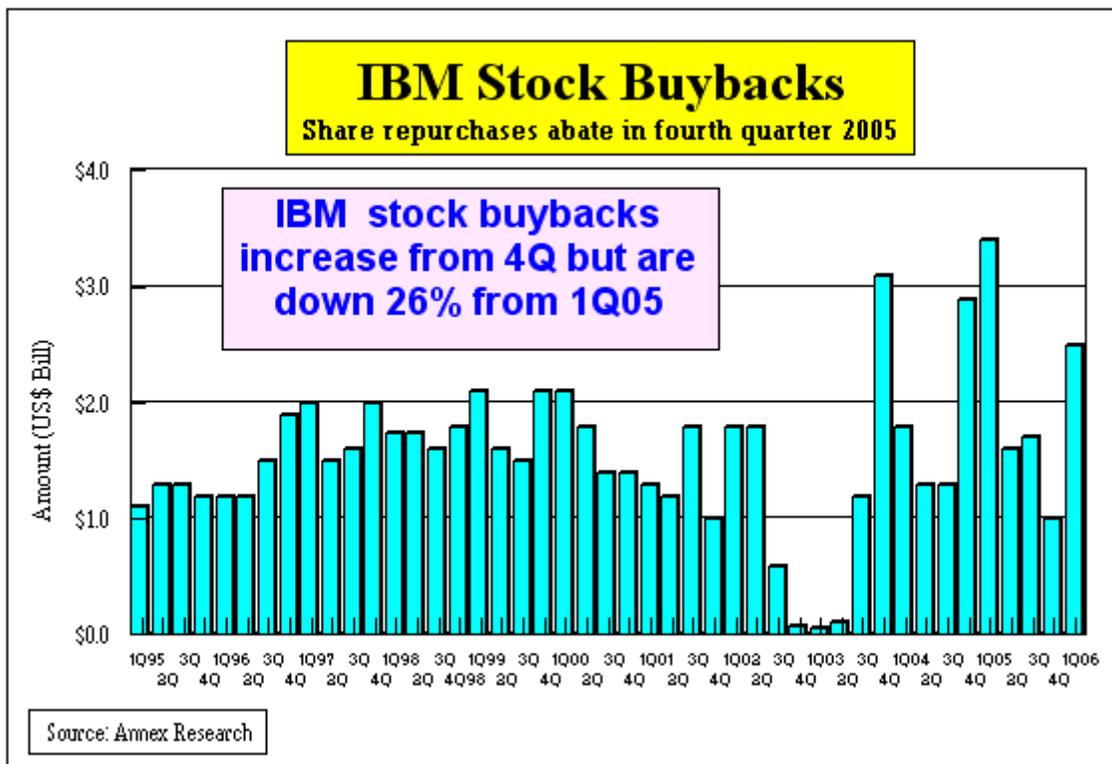


Just how "big" the EDS "win" at GM was, can also be surmised from the fact that, for the first time ever, the company chose NOT to disclose its GM revenues in the first quarter. We estimate that the GM revenues would be down 30% for the year to \$1.26 billion (see [EDS 2006 P&L](#)).



The fact that Wall Street is cheering on such a company close to 52-week highs, can only mean one thing: Wall Street is protecting its investment in EDS. Also, the company's profit margins, the *lowest* among the top IT services industry players (see above chart), are still better than the huge losses EDS racked up in the 2003-2004 time frame. So investors' sense of relief could be analogized to a person who feels great after he stops hitting his head against the wall.

The \$400 million-placebo EDS offered Wall Street in the first quarter may also be a factor in easing the investors' headaches. The \$400 million-placebo? Yes. EDS has joined the companies that think they can bribe Wall Street into giving it favorable recommendations by buying back their shares. In the first quarter, EDS spent \$401 million on stock buybacks versus zero a year ago. And its Boards has approved up to \$1 billion in share repurchases.



To see just how frail and perilous such an investment strategy can be, EDS only needs to look at IBM. The Big Blue stock is stuck in the low 80s despite tens of billions of dollars of stock buybacks the company has expended (see above chart). It is, therefore, not just a little ironic that EDS has chosen to start its share repurchases at a time when its major bigger competitor is scaling down such wasteful activities.

For a detailed password-protected profit and loss forecast, Annex clients can click on [EDS 2006 P&L](#)

Happy bargain hunting

Bob Djurdjevic

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