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Analysis of CSC's Third Quarter Fiscal 2007 Business Results

Where Less Seems More

CSC Stock Rises Despite Sharply Lower Earnings; New Contract Signings Plummet, Too

SCOTTSDALE, Feb 6 - Sometimes less is more on a street called Wall where logic has a way of inverting itself. The latest Computer Sciences Corp. (CSC) earnings release is a case in point. Its third quarter fiscal 2007 net profit plunged 44% to $114 million on an anemic rise in revenues (up 1.7% to $3.6 billion, but down 1% in constant currency).

Furthermore, CSC called the latest results "preliminary." The company said it would delay the filing of its final 10Q report pending an SEC investigation of its executive stock option awards in the past.

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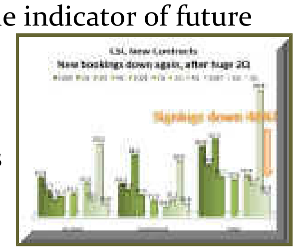
Yet Wall Street applauded the overall third quarter news, pushing the CSC shares up 5% in after-hours trading. (And the CSC shares kept most of that gain in early morning trading on Feb 7).

Why would investors cheer bad news? Here comes the inverted logic. Because it could have been worse. The CSC results were apparently better than expected. Profit excluding certain items was 85 cents per share. Analysts, on average, had forecast earnings before items of 83 cents per share and revenue of $3.64 billion, according to Reuters Estimates.

The investors also bought hook line and sinker CSC executives' rosy predictions of future earnings . The company forecast fourth quarter earnings per share before special items of $1.51 to $1.61 and revenue of $4.1 billion to $4.2 billion.

“Our third quarter results were as expected, and with our restructuring efforts, we are well positioned for the future,” said CSC chairman and CEO Van Honeycutt in a release.

Really? CSC's new contract signings, for example, a tell-tale indicator of future revenues and earnings, plummeted 48% to a $1.6 billion, the lowest quarterly total in recent history. But since the company did have a big second quarter (mostly due to the UK National Health Service megadeal), the CSC executives touted the overall year-to-date bookings in the release, which were up relative to last year (click on right thumbnail to view the chart). And Wall Street evidently bought that, too, without looking under the covers.



Business Segment Analysis

CSC’s U.S. federal government business was better than its commercial segment. The government sector revenues rose 6% to $1.30 billion. Within that total, CSC’s Pentagon business grew faster than that of the civil agencies.

By contrast, the worldwide

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(An update to "By Leaps and Bounds")

HP: New King of the Hill
(Analysis of HP's fourth quarter business results)

IBM: From Little Acorns Mighty Oaks Grow
(Analysis of IBM's "State of the Union")

Capgemini: By Leaps and Bounds *(Analysis of Capgemini's preliminary third quarter business results)*

Fujitsu: Good Performance Gets Better, More Global
(Analysis of Fujitsu's first half FY2007 business results)

IBM: A Slam Dunk Quarter
(Analysis of IBM third quarter business results)

Accenture's Emphatic Year-end Accents *(Analysis of Accenture's fourth quarter results) [Annex clients click here]*

IBM: Services in a Box
(Analysis of IBM Global Services' Ground-shifting Announcements)

Strong Comeback by IT Stocks in Third Quarter
(Analysis of top 20 IT companies' market and business trends)

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HP Firing on All Cylinders
(Stock sets new multi-year

commercial revenues were flat ($2.34 billion versus $2.35 billion the year before). The U.S. commercial revenue ($944 million) was down 5.5%, while European revenue was up slightly as reported ($1.03 billion), but down approximately 7% in constant currency.

CSC's non-European international revenue was $368.1 million, up 9.9% (approximately 5% in constant currency), compared with last year's $334.9 million.

The company said its commercial revenues for the third quarter continued to be (negatively) impacted by lower levels of outsourcing activity in Europe and the U.S. In the U.S. in particular, contract terminations and "rescoping" (reductions in business). Demand for consulting and systems integration services was also soft in the U.S. and Europe, CSC's largest markets that account for about 60% of its business.

In short, business sucked in the third quarter.

Outlook

For the full year ending March 31, CSC said it revenue would be up about 2%. This puts the growth at the low end of its November forecast of 2% to 3%. The company also left its annual earnings-per-share estimate unchanged at $3.71 to $3.81. Yet, Wall Street saw good news in the no news forecast anyway.

Click here for a detailed FY2007 CSC forecast (for Annex clients only)

Happy bargain hunting!

Bob Djurdjevic

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record following excellent third fiscal quarter results) [Annex clients click here]

Power of Manpower *(While others move to India, Russia... AMD invests in New York, hailing "phenomenal" quality of its labor force)*

Ebb Tide Lowers Most Boats *(Analysis of EDS' and CSC's latest quarterly results)*

IBM Stock Grossly Undervalued? *(Analysis of stock market valuations of IBM and its major competitors) [adds latest Fujitsu, Capgemini results]*

IBM vs. HP: A Tale of Two Blues *(Both companies are doing well in business, but only HP is favored by Wall Street; Big Blue trying to change that now with its new "India Opus") [Annex clients click here]*

Go East, Young Man! *(A speech delivered in St. Petersburg, Russia, May 25, 2006; click here for slides)*

IBM 5-Yr Forecast: Steady As She Goes *(Emphasis on quality continued) [Annex clients click here]*

Octathlon 2006: Accenture Again Wins "Gold!" *(HP gets "Silver," IBM "bronze") [Annex clients click here]*