

# ANNEX BULLETIN

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## IT SERVICES

Updated 11/25/07, 8:30PM MST, adds [Institutional Owners...](#)

*Analysis of EDS' Third Quarter Business Results*

### An Enchanted Quarter

#### *EDS Stock Bounces Back with Vengeance after Being Pummeled in Last Three Months*

SCOTTSDALE, Nov 2 - Talk about bouncing back with vengeance. After being pummeled by investors in the last three months, losing nearly 30% of its value since late July, the EDS stock shrugged off the broader market woes this morning, surging by more than four points, while the Dow industrials declined in triple digits for a second day in a row (see the chart).



And what drove such divergent behavior? Excellent EDS's third quarter results, released this morning. Net earnings were up 80%, while new contract signings soared to \$5.7 billion, up 61% from a year ago - the best sales performance in five years. Third quarter revenues were up 6% to \$5.6 billion (up 4% on an organic basis, excluding acquisitions, divestitures and one-time events).

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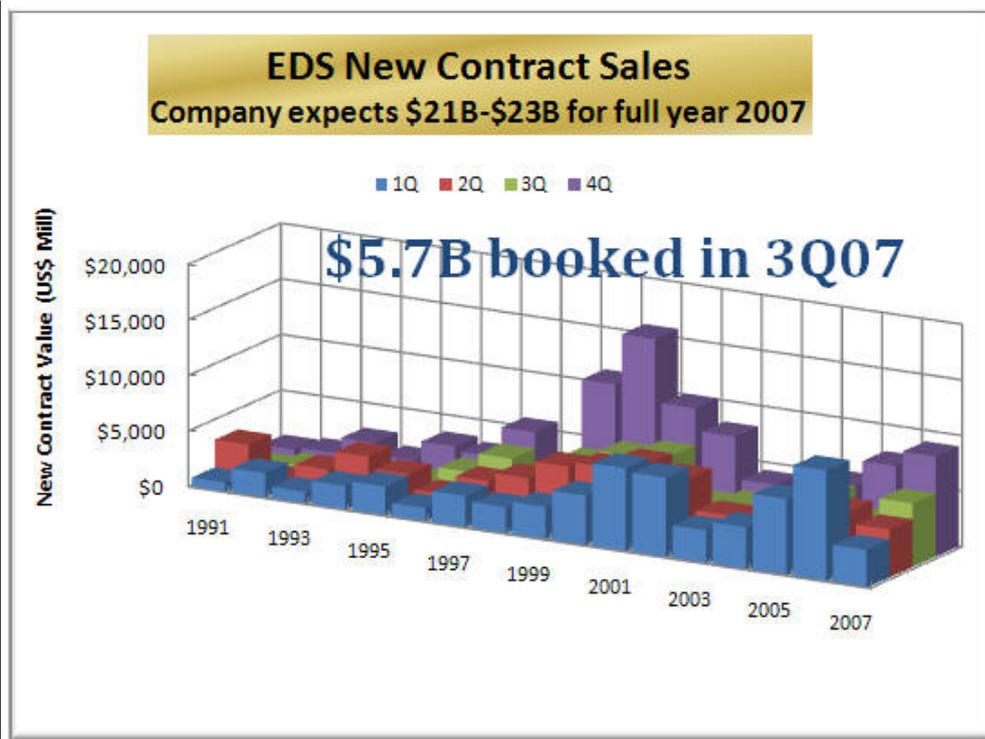
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For the full year, the company expects new contract sales of \$21 billion to \$23 billion. Which means EDS is counting on at least \$8 billion in the current quarter to reach that goal.

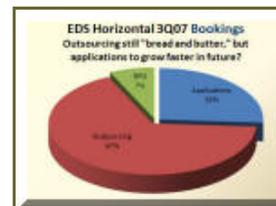
Despite such excellent performance in the latest quarter and in today's trading, the EDS stock has lots of lost ground to make up relative to competition, as you can see from the chart on the left. The company is expecting to that by continuing its growth momentum in the fourth quarter.



The new CEO Ron Rittenmeyer said that the company's 2008 sales pipeline increased by more than 20% since a year ago, noting particular strength in financial services and government.

Ouch! The main reason for the recent blood bath on Wall Street were the results of financial services companies. And as we saw a couple of weeks ago, the IBM shares also got clobbered because of even a hint of weakness in this sector (see "[On the Button Again](#)," Oct 2007). So we hope for the sake of the EDS shareholders that the company has figured out some sort of a special niche in which to prosper in the financial sector amid all the writeoffs and layoffs.

At the same time, EDS continued to expand its presence in the higher-margin applications market. They accounted for a little more than a quarter of all new signings in the quarter. Outsourcing, at two-thirds of the total, still continues to be the dominant segment.



As a result of the company's deliberate strategy to "move up the stack" this year (as we reported back in February - see "[On Sunny Side of Street: Climbing Up the Stack](#)," Feb 2007), a significant improvement in profitability is already discernible. Gross margins in the current quarter were about 15%, a big jump from the sub-10% margins that pervaded its results for several years under the Michael Jordan



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administration (see "[All Pain, No Gain](#)," Oct 2003).

For the full year, we expect the EDS 2007 gross margins to be about 14%, up from 12.6% last year, and 11.4% in 2005. We also expect its net earnings in the \$810 million range, up 62% from 2006.

For detailed EDS forecast tables and charts, Annex clients can click on the link below.

For our detailed EDS P&L table and forecast, [Annex clients click here](#).

*Happy bargain hunting!*

*Bob Djurdjevic*

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## Institutions Ignore Good Results, Defect in Drove

SCOTTSDALE, Nov 25 - The EDS stock has been in the cellar relative to competition ever since Michael Jordan announced in July he was turning the reigns over to a new CEO (Ron Rittenmeyer). Share prices are down about 30% since then. As with Accenture, even a very good third quarter report card didn't help (see "[Enchanted Quarter](#)," Nov 2007).



The EDS stock continued its slide afterward, as you can see from the above chart. By contrast to Accenture, the largest EDS shareholders have been fairly loyal. Only five of the Top 15 reduced their positions in the third quarter, and only moderately at that (by less than 6% at the most).

But many other smaller institutional holders evidently headed to the sidelines as the sold-out positions in the third quarter outnumbered the new ones by about three-to-one.

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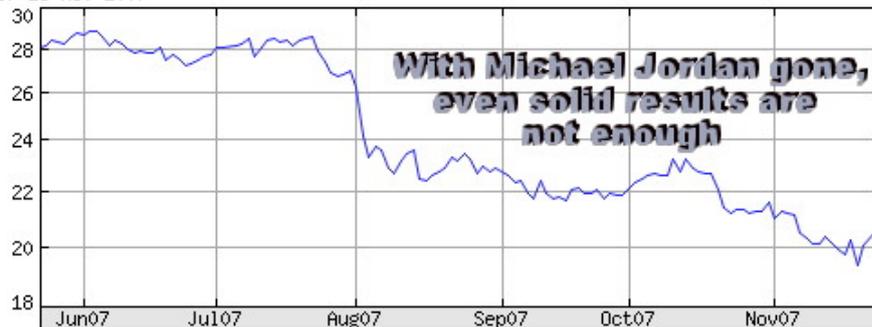
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ELECTRONIC DATA SYSTEMS CORP  
as of 23-Nov-2007



**EDS shares down ~30% since July, institutions continue to bail out**

Overall, EDS continues to have the highest institutional shareholding percentage of all Top 20 IT stocks we follow (96% as of Sep 30). Which means the company is more vulnerable to the institutional gossip when it comes to price swings.

For nearly four years, that meant good news for EDS. Its disappointing and at times dismal results didn't seem to affect the stock very much. Wall Street loved Michael Jordan. He could do no wrong. As long as Jordan was at the helm, it almost didn't matter what happened in the EDS business (see "[Teflon Mike](#)," Nov 2004). Well, now that he is gone, it similarly doesn't seem to matter much that the results are so much better. The stock is being pummeled anyway.

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Bob Djurdjevic, Editor  
(c) Copyright 2007 by Annex Research, Inc. All rights reserved.  
e-mail: [annex@djurdjevic.com](mailto:annex@djurdjevic.com)

8183 E Mountain Spring Rd, Scottsdale, Arizona 85255  
Tel/Fax: +1-602-532-7789

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