

Ro Le
rvl@rice.edu

Concord EFS, Inc. (NYSE: CEFT)

Sell

December 5, 2001

Industrial Sector

Business Services

MARKET DATA

Price	\$30.90
52 Week Range	\$33.72-\$17.81
Price Target	\$36.00
Book Value	\$17.58
Raw Beta	1.4
Shares Outstanding	503.7 million
Market Capitalization	\$15.6 billion
Revenue Last 12 mo	\$1.6 billion
Net Income Last 12m	\$185.7 million
EPS 5 Yr. CAGR	32.9%

COMPANY OVERVIEW

Concord EFS is the leading provider of infrastructure for cashless commerce. Concord provides electronic transaction authorization, processing, settlement, data capture, and fund transfer services across the United States. Concord's services include electronic payment, credit and debit card transaction processing for supermarkets, grocery stores, convenience stores, and financial institutions. The firm's network services provide ATMs in truck-stops nationwide. Concord also provides trucking companies and truck drivers with ATM bank cards, fuel purchase cards, and banking services, including payroll processing. Concord is currently holds 70% of supermarket industry. Concord also targets the oil and gas market where the convenience "pay-at-the-pump" continues to gain acceptance. Going forward, the company targets any business that has high volume of cash and checks. Its goal is to replace cash and checks with electronic payments. In addition to retailers, fast food restaurant industry is in the company's hit list. Concord's largest subsidiary is EFS National Bank, an electronic processing hub that offers mostly electronic banking. Concord has been expanding through acquisitions.

INDUSTRY OUTLOOK

Concord EFS, Inc. belongs to the Business Services. The Business Services sector includes the cashless commerce infrastructure providers. Financial transactions are increasingly gravitating toward electronic exchange which makes for a promising outlook for companies targeting this market. The electronic commerce transaction is relatively immune to economic downturn due to non-discretionary nature of its business focus: grocery stores, and gas stations. Given the clear benefits of the convenience of always having the right amount of payment for any purchase plus the security of not carrying cash, the debit card services are catching on. Services to the cashless transactions at the grocery stores and gas station is experiencing a phenomenal growth rate of 30% a year. It is also estimated that by 2007 60% of all supermarket payment would be electronic.

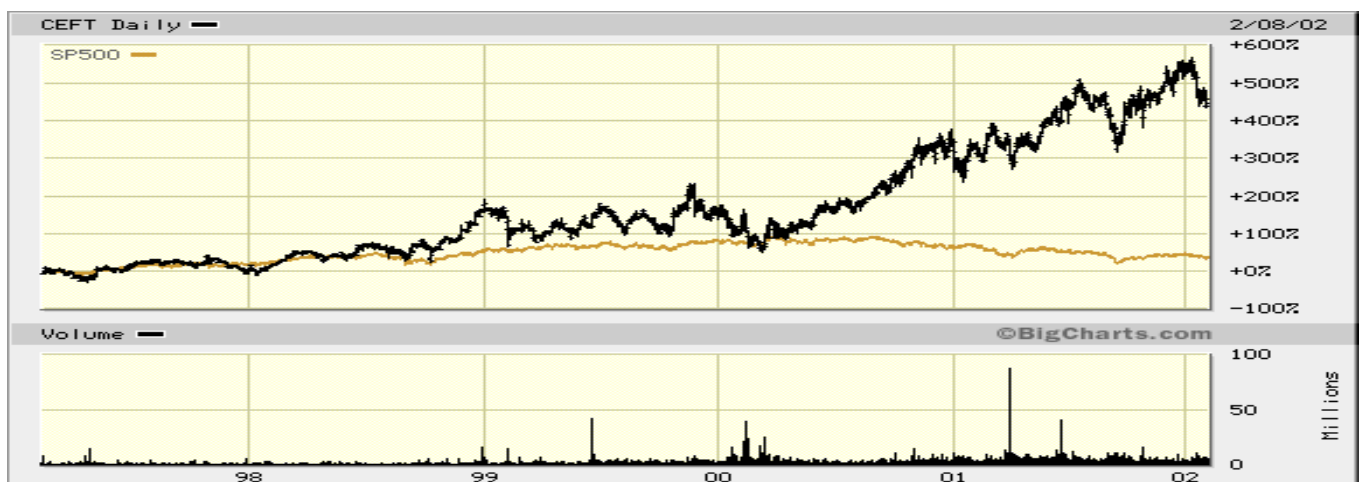
- Transaction convenience and financial privacy are continuing to be the key drivers in the business services sector. Unlike internet services which experienced setback in recent couple years, the electronic commerce is experienced continual growth.

COMPANY OUTLOOK

- As a leading processor of online debit and Automated Teller Machines transactions in the industry, Concord is relatively immune from an economic slowdown. The company benefits from long-term processing contracts with 85% of its transaction volume is fee based, not dollar volume. Also with roughly 70% of CEFT's transactions coming from non-discretionary markets, such as gas stations and supermarkets, the company believes its 2001 and 2002 performance estimates are in solid position.

- ❑ In the third quarter this year, more than 1,700 Wal-Mart stores were connected to Concord for PIN-secured debit card payments. Certification has begun for Citizens Financial Group, Concord's largest Network Services processing client. Citizens, which signed a long-term contract for debit card, ATM, and gateway processing services, is expected to add over 100 million transaction annually once the current certification is complete.
- ❑ Concord's third quarter earnings was \$0.16 per share, exceeding the consensus estimate by a penny. Revenues rose 20% year-over-year to \$437.1 million which was shy of the consensus expectation of \$451.1 million in sales. Third quarter results missed on the top line is likely to make investors cautious in the near-term. However; with an intermediate-term growth rate greater than 20% and a large, yet-to-be-penetrated market, the downside from the current level should be limited.
- ❑ Concord strategy is growth through acquisition. Over the years, well place purchases of innovative companies have fueled Concord's phenomenal five years average sales growth at a dizzying rate of 60%. Earlier last year, the purchase of Star System provided Concord a leg up in PIN-secured payment network and a leader in secured, real-time electronic transactions. STAR was a pionmeer in check electrification and secured internet transactions. In December of last year, Concord announced an agreement to acquire The Logix Companies, LLC, an innovative electronic transaction processor and service provider. Logix technology will supply new features to Concord's ATM processing, check conversion, and risk management services. Logix's product lines fits well with Concord's infrastructure and present many opportunities to reduce operating costs.

PERFORMANCE



Concord's share price has outperformed S&P 500 both in one year and five year performance win-

dow. This fact has not been lost with the investment community as CEFT's shares are sold for P/E in excess of 70.

PROFIT MARGINS

Concord's Net Profit Margin of 11.7% was lower than the 5 year average of 14.9%. However; it is still twice the current S&P's value of 5.1%. The fact that CEFT is able to obtain a higher Net Profit Margin despite lower Gross Margin (33.5% vs. 47.1%) comparing to S&P in-

	CEFT	S&P500
Gross Margin	33.5	47.1
Pre_Tax Margin	18.7	8.8
Net Profit Margin	11.7	5.1

icated that Concord has lower SG&A and D&A costs than S&P 500.

HISTORICAL GROWTH RATE

Concord manages a strong sales growth rate of 40.8 % vs. almost no growth for S&P 500. Also Concord declines in income and EPS are significantly below S&P 500 rate of decline.

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Growth Rate, %	CEFT	S&P500
Sales (Qtr vs. Year ago Qtr)	40.8	0.7
Income (Qtr vs. Year ago Qtr)	-1.4	-26.5
EPS (Qtr vs. Year ago Qtr)	-13.8	-28.6

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FINANCIAL CONDITION

Concord was able to fuel its phenomenal growth with very little debt. No wonder it is a favorite of in-

	CEFT	S&P500
Debt/Equity Ratio	0.07	1.09
Current Ratio	2.9	1.3
Quick Ratio	2.8	0.9
Interest Coverage	24.3	2.2

EARNING GROWTH RATE PROJECTION

Consensus analyst estimate published by FirstCall placed Concord FY 2002 as well as five year earning growth rate of close to 30%, at three time S&P growth rate. To discount for analysts' typical optimistic view, I have chosen a growth rate of 20% for Concord's earning.

	CEFT	S&P500
Last 5 Yrs.	51.4	8.4
FY 2001	-5.2	-21.7
FY 2002	28.6	11.7
Next 5 Yrs	29.4	10.3

P/E VALUATION

Currently Concord shares have a P/E ratio of 72.5. Even when the growth rate of 28.6% is factored in, CEFT PEG is 2.5 indicating its shares are over-valued.

	CEFT	S&P500
2001 P/E	46.8	24.9
Current P/E	72.5	31.9
2002 EPS Growth	28.6	11.7
2002 PEG	2.5	2.7

DCF VALUATION

ValuePro 2002 General Pro Forma Screen CEFT

Period	Revenues	NOP	Adj. Taxes	NOPAT	Invest.	Deprec.	Change in Invest.	Change in Working	FCFF	Discount Factor	Discounted FCFF
0	1586.7										
1	1983.38	489.3	176.05	313.25	122.97	125.75	-2.78	6.86	309.17	0.91	281.34
2	2479.22	611.62	220.06	391.56	153.71	157.18	-3.47	8.58	386.45	0.83	320.75
3	3099.02	764.53	275.08	489.45	192.14	196.48	-4.34	10.72	483.07	0.76	367.13
4	3873.78	955.66	343.85	611.81	240.17	245.6	-5.43	13.4	603.84	0.69	416.65
5	4842.22	1194.58	429.81	764.77	300.22	307	-6.78	16.75	754.8	0.63	475.52
6	6052.78	1493.22	537.26	955.96	375.27	383.75	-8.48	20.94	943.5	0.58	547.23
7	7565.98	1866.53	671.58	1194.95	469.09	479.68	-10.59	26.18	1179.36	0.53	625.06
8	9457.47	2333.16	839.47	1493.69	586.36	599.6	-13.24	32.72	1474.21	0.48	707.62
9	11821.84	2916.45	1049.34	1867.11	732.95	749.5	-16.55	40.9	1842.76	0.44	810.81
10	14777.3	3645.56	1311.67	2333.89	916.19	936.88	-20.69	51.13	2303.45	0.4	921.38
Residual									24508.27		9803.31

Discounted Excess Return Period FCFF	5473.49	Total Corporate Value	17236.3
Discounted Corporate Residual Value	9803.31	Less Debt	(119.5)
Short-Term Assets	<u>1959.5</u>	Less Preferred Stock	(0)
Total Corporate Value	17236.3	Less Short-Term Liabilities	<u>(671.9)</u>
		Total Value to Common Equity	16444.9
		Intrinsic Stock Value	32.65

Discounted Cash Flow Model

ValuePro Model Key Parameter

Excess Return Period, yrs	10
Growth Rate, %	25
10-Yr Treasury Yield, %	5
Equity Risk Premium, %	3
Company WACC, %	9.5
Revenue, \$MM	1,587
Debt, \$MM	119.5

SUMMARY

- ❑ Overall, Concord has been performing very well. P/E versus growth analysis indicated that the stock is over-valued. DCF model analysis indicated an intrinsic valuation of \$32.82 per share based on 25% earning growth. If the conservative earning growth rate of 20% is used, the intrinsic stock value of \$28.0 At the time of this analysis, Concord share price was approximately \$31.0
- ❑ Concord is the “Porsche” of the Business Services industry, and the “Porsche” doesn't come cheap. It is selling at a hefty P/E multiple of greater than 70. While there are no overbearing risks on the downside at the current level, the current price is likely reflects solid and unchanged fundamental. Therefore, up-side potential is minimized. While the pending acquisition of Logix will support long-term growth, Concord is facing short-term issues of efficiently integrate Logix business into Concord system. Concord has been a good horse. It carried the Wright Fund far since its purchase at \$13.46 per share. This horse is slowing down. It is time for us to protect our profit.
- ❑ We recommend a SELL of 500 share of Concord EFS at market price for profit taking.