

DST Systems (DST)

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Disclaimers

- I am not a registered investment advisor and I do not offer any investment advise
- No parts of this talk are suggestions to invest, not invest, buy or sell any kind of securities or other financial instruments

DST Systems - business

- Product areas:
 - Information processing, and computer software services and products.
 - Financial Services - proprietary software systems comprising mutual fund shareowner, subaccount, and unit trust recordkeeping systems for the U.S. and international mutual fund companies; a defined-contribution participant recordkeeping system for the U.S. retirement plan market; investment management systems to the U.S. and international investment managers, and fund accountants; a business process management and customer contact system for mutual funds, insurance companies, brokerage firms, banks, healthcare payers, healthcare providers, cable television operators, and mortgage servicing organizations; healthcare claims administration processing systems and services to healthcare payers, third party administrators, and medical practice groups; and pharmacy claims processing systems to healthcare plans, insurance companies, third party administrators, and pharmacy benefit managers
 - Output Solutions - single source, integrated print and electronic statement, and billing output solutions, as well as statement and bill production, marketing and personalization services, postal optimization, and electronic presentment, payment, and distribution solutions
 - Also owns and operates real estate properties, as well as has investments in equity securities, private equity funds, and other financial interests

DST Systems - Misc thoughts

- 89% US, 11% International
- 48% Investment management SW revenues, 17% healthcare, 15 telecom
- Financial services 2/3 revenues (really $\frac{1}{2}$ see below), output systems – $\frac{1}{2}$
- But not accounted above 1/3 revenues is “out of pocket reimbursements for postage”!
- Output systems business may decline with more Internet distribution and declining paper mail distribution
- BFDS, a 50% owned joint venture with State Street
- Healthcare reform probably non issue
- Investments: \$851.9 million -> 10.6 million shares of State Street Corporation, 22.3 million shares of Computershare Ltd. and 1.9 million shares of Euronet Worldwide, Inc., with a market value of \$460.7 million, \$228.8 million and \$41.4 million

Is it a good business?

- >10 year history of profits

- ROE:

• 9.40	13.80	15.50	14.70	46.90	29.90
85.70	47.70	75.50	102	2009:~38	

- Margins

- 2007: 37%, 2008:10, 2009: 10

- Balance sheet: tough to evaluate!

- Long term investments 1.4B, debt 1.2B, equity 630M.
- Only 400M net tangible assets!

- ROIC = Earnings / (Equity + Debt - Cash) = Earnings / (Assets - non-debt liabilities - Cash)

- $241.6 / (634 + 1200 - 100) = 14\%$ 2009 (not counting long term investments!)

Is business cheap?

- ROE 38%, ROIC 14% - assume 20%
- Earnings in 10 years = $ROE * Equity * (1 + ROE)^9 = \$654M$
- Equity in 10 years = $Equity * (1 + ROE)^9 = 326B$
- Market cap = $16M \times P/E (15) = \$3.3B$
- Rate of return = $\sim 15\%$ after tax (calculations omitted)
- If we assume 15% ROE: **8%**

- >3 P/Book - not a net net

Is business cheap?

- Discounted cash flow
 - Current earnings of ~241.5M
 - 10% growth for 5 years, leveling after that
 - 10% discount -> \$3.6B current valuation (if you buy company at <\$3.6B, you will get 10% return or higher)
 - 15% discount -> \$2.3B current valuation
 - 5% growth for 10 years, leveling after that
 - 10% discount -> \$3.4B current valuation
 - 15% discount -> \$2.1B current valuation
- Owner's yield = earnings / (market cap + debt - cash) = earnings/EV
 - $241.5B / (2B + 1.2B - .1B) = 7.6\%$