



April 18, 2006

FactSet Research Systems (NYSE: FDS)

Sell It While It's Hot

Initiating Coverage

Rating: Underweight

Market Price (Common):	\$43.20
Price Target:	\$39.95
Mispricing:	7.51%

Key Ratios & Statistics

52-Week High	\$44.61
52-Week Low	\$27.06
Avg Daily Vol (Mil)	4.798
Mkt. Cap. (Mil)	\$2,102
Shares Out (Mil)	48.679
Dividend Yield	0.46%
Payout Ratio (TTM)	12.8%

Financial Strength

Quick Ratio (MRQ)	2.37
Current Ratio (MRQ)	2.37
Price/Earnings (TTM)	28.35
Price/Sales (TTM)	6.09
Price/Book (MRQ)	6.78

Management Effectiveness

Return on Equity (TTM)	26.51%
Return on Assets (TTM)	22.09%
Return on Investment (TTM)	26.51%
Gross Margin (TTM)	69.40%
Operating Margin (TTM)	32.77%
Profit Margin (TTM)	22.19%

Please see the important disclaimer at the end of this report.

• **Investment Summary**

Favorable market conditions on two fronts - financial services and application software - have bolstered earnings and equity prices for FactSet Research Systems, a provider of portfolio analytics and other financial news and analysis software to asset managers and investment bankers. But with dwindling domestic demand growth for its core product offerings, downward pressure on margins, and highly competitive market environments threatening secondary revenue streams, FactSet faces a slippery slope ahead. Furthermore, its plan of expansion into thoroughly penetrated submarkets - such as fixed-income analytics, structured product analytics, financial data management, and financial news - remains problematic.

• **International Growth Offers Hope**

Strong international growth - especially that relating to equity analysis software, FactSet's core and highly profitable competency - represents a ray of hope for FactSet equity holders, as the revamping of FDS software to cater to international investors has effectively doubled the size of the firm's target market. But while European and Asian-Pacific adoption rates continue to rise, pressure from financial analysis, news, and data providers such as Reuters, Bloomberg, Thomson, and Moody's will similarly intensify, and FactSet simply lacks the breadth of services and incumbency advantages to compete effectively against such behemoths.

• **Bad News from the Behavioral Finance Perspective**

High acquisition spending, stock-for-stock considerations, and recent insider selling activity suggest a similarly disappointing end to the FactSet stock-price run-up.

• **Betting the Farm on Inorganic Growth**

Smoke-screen acquisition spending has created inorganic and unsustainable top-line growth that fails to refine and broaden FactSet's offerings, at least to an extent justifying the market's valuation. The true impetus behind the recent shopping spree is more likely a combination of stockpiles of cash due to a dearth of investment opportunities in the firm's core competencies, managerial overconfidence, and an overpriced stock. High acquisition spending of this ilk leads inevitably down the path of low future returns, and FDS should be no exception.

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Investment Overview

We are initiating coverage of FactSet Research Systems (NYSE: FDS) with an Underweight recommendation. Without a doubt, core revenue-, profit-, and growth-generation remains impressive, but not to the extent that can justify a Price/Earnings (TTM) of 28.35, a Price/Sales (TTM) of 6.09, and a Price/Book of (MRQ) 6.78. High growth in the near-term growth remains plausible, but increasing margin pressure, namely with regard to FactSet's secondary revenue streams, and a slew of competitors in the mature financial services industry will likely prevent the realization of the market's ambitious dreams for the 28-year-old firm. While FDS enjoys a virtually monopolistic status in the area of equity portfolio analytics, their operations - and more importantly, their margins and profitability levels - are not transportable into other submarkets of the financial analysis, data management, and financial news spheres.

Solid Foundation: Company and Product Overview

FactSet was founded in 1978 to serve the investment community through exceptional client service and the state-of-the-art financial software systems. The 28 year-old firm possess the lion's share of the market for equity analytics in the United States, and its robust product offerings and incumbency advantages in that submarket have sustained profitability and growth for decades.

The firm aggregates over 200 financial databases, replete with fundamental and technical data on firms and securities from across the globe. FDS offers this data and the tools to analyze it effectively to asset managers, risk management officers, research and performance analysts, financial marketing professionals, sell-side researchers, and investment bankers. Applications offer functions such as company and cross-company analyses, industry analyses, security screenings, equity and fixed-income portfolio analytics, risk measurement, alpha testing, portfolio optimization, and real-time financial news and security quotes. The products FDS offers are fully integrated with Microsoft Office applications for ease of use and implementation.

The revenues of FDS originate in monthly subscription services, about 75% of which are sold to investment management clientele. Investment banking clients constitute most of the remaining subscribers. The firm had 1,266 employees as of February 28, 2006, of which about a third cover sales and consulting, a third engage in research and development, and the final third supply administrative support.

Of the main product suite offered by FDS, which includes applications for portfolio attribution, risk analysis, and quantitative analysis, the Portfolio Analytics workstation represents the largest revenue generator. As of February 28, 2006, 446 clients representing about 3,600 users subscribed to this service. FDS uploads over 500,000 portfolios of its clients nightly for financial analysis.

Organic innovation remains promising for the firm, as several recent product releases have enhanced the marketability of FDS equity analytics software, the firm's core competency. New releases include SPAR 2.0, a retooling of the firm's return-based analysis software for asset managers, Alpha Testing 3.0, a program that back-tests portfolio strategies, and Portfolio Spring Board, an entirely new software product that undertakes an integrated assessment of a portfolio, which then serves as a starting point for in depth analysis.



The firm also extracts revenues from investment banking professionals. IBCentral, a software product released in Fiscal 2005, serves the informational needs of investment bankers and even includes a wireless application within the package, affording clients round-the-clock access to models and information. FDS intends to refine this offering and shift all of its investment banking clients over to this product. As deal activity worldwide remained strong in 2005, FDS expanded this aspect of its operations through subscription growth of 9.9%. Recession, low growth, competition

FactSet Marquee, the firm's real-time news and quotes software product, represents a possible source of sustainable growth for FDS. Client usage of the application more than doubled during Fiscal 2005, largely in part due to the adoption of global exchange quotes in the application, which took place in the second half of the fiscal year. Marquee coupled with DIRECTIONS allow clients to view quotes and news in real time while accessing in-depth historical analysis on the same platform. Fiscal 2005 saw a new push to develop FDS's own financial information content to complement the content it aggregates from providers such as "MSCI, Thomson, Reuters, FTSE, Compustat, IDC, Dow Jones, Northfield, BARRA, ASP, DRI, EconWin, Merrill Lynch, and Lehman Brothers," according to management guidance. Examples of in-house content now provided by FDS include a stock ownership database for companies of the United Kingdom and the FactSet People database, which documents biographical information of business executives.

Primary Operations Remain Strong and Growing

After 25 consecutive years of revenue growth, FDS and its management find abounding reasons for optimism. Since the 1996, IPO, net revenues have grown at a CAGR of almost 24%, and the first half of Fiscal 2006 saw a 21.8% increase in revenues, year-on-year. Also for the first half of Fiscal 2006, net income rose 14.5% to \$38.4 million year-on-year. Free Cash Flow has exceeded net income, a further sign of financial strength. Cash reserves remain healthy, with \$90 million (mrq) according to the Q2 conference call, and management remains in a nimble position to exploit new investment opportunities, should they arise.

Total clients rose to 1,576 in Fiscal 2005, up from 1,059 in Fiscal 2004, though much of this growth was inorganic. Forward looking subscriptions, defined as the expected revenues for the following 12 months from current subscribers, totaled \$352.9 million in September, 2005. This implies an average of about \$200,000 of subscription income per client per year. The number of financial professionals within the FDS client base rose 27% to about 26,800, the largest increase in the last five years. FDS Portfolio Analytics Workstations reached 425 clients, or about 3,300 individual users, as of August, 31, 2005. At the end of the second quarter of Fiscal 2006, clients rose to 1,666, including 20 new firms from the February acquisition of europsychus.com Limited. This represents an increase of 229 clients or 16% over the previous 12 months.

FDS revenues increased 24.1% in Fiscal 2005 to \$312.6 million, and international growth played a key role, as European revenues increased 74.1% to \$68.3 million and Asian-Pacific revenues grew 30.4% to \$15.2 million. However, organic growth in the international arena was a less impressive 22%. International revenue for the second quarter of Fiscal 2006 grew 28.6% to \$26.5 million, which represents organic, currency-constant growth of 22%. European revenues grew 27.8% to \$21.6 million and Asian-Pacific revenues climbed 32.1% to \$4.9 million over the period. Subscriptions from non-US based clients have reached 29% of total subscriptions, a metric likely to continue to rise.

Buyer power remained low as no single client accounted for more than 3% of total subscription revenue as of February, 2006, and the ten largest subscribers provide less than 15% of total subscriptions. Client



retention rates again exceeded 95%, representing the strong product offerings of FDS but also the high costs of switching that may prevent further domestic market share gains.

Management also noted the continuing trend of greater interest from mutual funds than from hedge funds, with regard to FDS investment analysis products. International growth in their equities products, and to some extent their real-time quotes and news products, remains promising and may allow the firm to sustain double-digit sales growth rates. The following table from the Fiscal 2005 SEC 10-k, displays the relatively strong revenue growth realized in Europe and in Asia Pacific.

THOUSANDS

	U.S.	EUROPE	ASIA PACIFIC	TOTAL
YEAR ENDED AUGUST 31, 2005				
Revenues from clients	\$229,010	\$68,346	\$15,288	\$312,644
Other income	1,075	66	1	1,142
Depreciation and amortization	15,191	3,025	102	18,318
Segment operating profit*	76,453	23,536	9,032	109,021
Provision for income taxes	36,938	1,460	—	38,398
Total assets	217,131	125,091	5,307	347,529
Capital expenditures	19,317	2,592	26	21,935
YEAR ENDED AUGUST 31, 2004				
Revenues from clients	\$200,944	\$39,247	\$11,719	\$251,910
Other income	1,772	—	—	1,772
Depreciation and amortization	13,622	940	96	14,658
Segment operating profit*	66,120	16,015	5,468	87,603
Provision for income taxes	31,358	—	—	31,358
Total assets	166,343	60,806	2,778	229,927
Capital expenditures	37,178	490	170	37,838
YEAR ENDED AUGUST 31, 2003				
Revenues from clients	\$178,139	\$34,088	\$10,068	\$222,295
Other income	2,282	7	—	2,289
Depreciation and amortization	16,179	1,265	97	17,541
Segment operating profit*	57,732	15,281	3,714	76,727
Provision for income taxes	27,578	—	—	27,578
Total assets	241,732	10,582	3,845	256,159
Capital expenditures	8,205	148	104	8,457

Finally, while some sell-side analysts have expressed concern about the rise in accounts receivables, up \$1.9 million to \$58.9 million according to the Q2 conference call, we see no reason to doubt management's assertion that this is merely the result of new invoices from higher subscription growth. In fact, the provision for doubtful accounts has fallen over the past three fiscal years.

FDS Equity Prices Remain Unjustifiably High

The FDS primary market space is essentially capped by the number of equity analysts and firms in the market. In the domestic market for equity analytics, FDS has achieved the penetration typical of a virtual monopolist in a mature industry, and the growth stories paraded by Wall Street seem frankly unrealizable. While the first half of Fiscal 2006 saw a 21.8% year-on-year increase in revenues, only 16% of this growth was organic, with the remaining 5.8% resulting from business operations owned less than one year. The average subscription per client remained largely stable, growing 1.8% to \$228,000 since



November, 2005. Excluding acquisition-related growth, even management expects (organic) revenue growth between 14% and 15%. In order to sustain the revenue growth rates high enough to justify current equity prices, FDS requires both massive international adoption of its equity analytics platform and a series of highly positive-NPV acquisitions. As discussed later, these eventualities are unlikely.

Management indicates that profit growth will result not from expanding margins, but rather from broad revenue growth. Margins remained very stable in 2004 and 2005, as operating margin increased 0.1% to 34.9% and net margin stayed at 23.0%. In the 2nd quarter conference call, management expressed the expectation that margins would continue at this “straight line” path. The likely reality is that increasing pricing pressure and other sources of margin pressure will erode margins in the future. Our rationale follows:

- In Fiscal 2005, Data costs increased by \$9.0 million, due to FDS acquisition targets and the high ratio of subscriptions to content usage, on which some data fees are based. In the first half of Fiscal 2006, data costs continued to rise, increasing by \$4.7 million year-on-year. We forecast this trend continuing.
- In accordance with SFAS 123R, FDS expected to expense \$2.5 to \$3 million of stock based compensation in the first quarter of Fiscal 2006. These expenses will further erode net margins.
- Much of the expected growth of FDS revenues comes in its secondary revenue streams, where competition is more fierce and margins are inherently lower. Expanding into these submarkets will place downward pressure on FDS margins going forward.
- While much of their Fiscal 2005 SG&A, 55%, was due to real estate spending, some of which on the one-time relocation of their headquarters. But continued office expenses and further relocations in the future, such as the consolidation of the London offices in Fiscal 2006, will result in continued high real estate spending in future years.
- On the other hand, software optimization lowered hardware requirements, and falling computer hardware prices in general have further benefited the net margins realized by FDS. Telecommunications costs also fell \$0.8 million during Fiscal 2005, which is especially significant due to the implication for the COGS relating to Marquee, FDS’s real-time news and quotes software.
- For these reasons, we allow margins to remain constant until 2007, after which they erode in our forecasts, as discussed below.

Recent insider trading activity, high acquisition spending, and stock-for-stock considerations further suggest low returns for FDS equity. According to Yahoo! Finance, FDS insiders have sold 34.9% of FDS shares in the last 6 months, the most active period of insider trading ever, though much of it is related to the liquidation of the estate of Howard Wille, an FDS co-founder. Nonetheless, the volume and decided direction of insider trading serves to indicate that management and insiders may believe FDS equity to be overvalued. Stock repurchases, statistically indicative of equity price upside, came to a halt in August of 2005, after 1,500,000 shares were repurchased at an average cost of \$20.03, less than half of today’s FDS market price. Since then, management has engaged in a series of acquisitions, many of which using FDS common stock as a means of payment. According the Fiscal 2005 SEC 10-k, “On August 1, 2005, the Company issued 305,748 common shares as part of the consideration in the acquisition of DSI [Derivative Solutions, Incorporated]. On September 1, 2004, the Company issued 385,601 common shares as part of the acquisition price of the JCF Group of Companies. On January 4, 2005, the Company issued 44,613 common shares as part of the acquisition price of TrueCourse.”

According to management, the effective tax rate is expected to be between 35.9% and 36.5% going forward, but Fiscal years 2005, 2004, and 2003 included income tax benefits of \$1.9 million, \$1.5 million and \$1.3 million, respectively, which reduced the rate in each period to 34.9%, 35.1%, and 34.9%,

respectively. To continue our conservative approach to valuing the equity of FDS, we use 35% going forward, as discussed below in the valuation section.

Acquisitions: Past, Present, and Future

FDS undertook \$92 million of acquisitions in Fiscal 2005, even though their net income was only \$72 million, and they have already made another \$28 million of acquisitions in 2006. This imprudent acquisition spending underscores the reality that FactSet has exhausted the positive net present value investment opportunities related to its core competency - equity analytics. After 27 years of market dominance, this is hardly surprising. But while many of the companies acquired by FDS have compelling product offerings that enhance the breadth of service FDS can provide, the synergies FDS hopes to realize may prove non-existent. While FDS still enjoys virtual hegemony in the equity analytics sphere, the firm cannot leverage this market power into other financial analysis submarkets, due to the intense competition and formidable incumbents awaiting it there.

In August of 2005, FDS acquired Derivative Solutions, Incorporated, which was a Chicago-based vendor of fixed-income security analysis software. The consideration was \$42.5 million in cash and 305,748 of FDS common stock, equivalent to about \$9 million. The firm provided bond analytics, and portfolio and risk management solutions to banks, asset managers, and other financial entities, and its acquisition brought 73 new clients and 406 users into the FDS client base. The idea behind the acquisition was to augment the modeling capabilities of FDS software with respect to fixed income and structured products. Fiscal 2006 will see the integration of the Derivative Solutions analytic engine into the Portfolio Analytics Workstation, which again is the largest sales-driver of the product suite.

In September of the same year, FDS purchased London- and Hong Kong-based StreamVPN Limited for a consideration of £13 million, or about \$23.9 million. Further consideration will be delivered contingent upon the realizations of certain revenue targets over the following 14 months. The firm provided tools to aggregate and optimize the value of equity research to sell-side brokerage houses and asset managers. After the acquisition, StreamVPN was renamed after its flagship product, Alpha Network, which functions as a platform that aggregates, monitors, and evaluates investment ideas from sell-side researches and in-house analysts. FDS has begun integrating Alpha Network into its platforms, such as Marquee and DIRECTIONS, but will also continue to sell the product as a stand-alone.

Other less recent acquisitions include the September 2005 purchase of JCF Group, a French-based firm that aggregated analyst forecasts, and that of TrueCourse, Inc., which offered software for the investment banking community. Both have been fully integrated into the FactSet product offerings. TrueCourse also included SharkRepellent.net, a web application that analyzes defensive prospects for firms in danger of hostile takeover.

The firm also acquired the outstanding equity of europrospectus.com Limited for \$7.5 million in cash on February 17, 2006. The former 25-employee business entity compiled and provided access to stock and bond prospectuses, offering full text searching capabilities.

According to the Fiscal 2005 annual report, management hopes to “invest in rounding out... risk analysis offerings” in Fiscal 2006, which may suggest further acquisitions in that arena or in house development and expansion of existing platforms. However, the timing and magnitude of future acquisitions remains opaque, and our forecasts of acquisition spending are discussed in detail below.



Competitive Positioning

While FDS enjoys sustainable competitive advantage and incumbency in the market for equity analytics, the firm cannot hope to replicate such market power in the submarkets it has recently sought to penetrate via acquisition spending. While its equity analysis segment, offering products seemingly integrated into Microsoft operating systems, represents a reigning monopolist in the financial services sphere, countless competitors, many of which are financial services providing colossuses in their own right, pose a continuing threat to profitability and growth in other submarkets, such as fixed-income analytics, structured product analytics, financial data management, and financial news.

On the financial news front, incumbents such as Capital IQ, Thomson, Reuters, Bloomberg will likely prevent future substantive market share gains by FDS Marquee technology. Russell Mellon offers product offerings far superior to the recent attribution engines in the FactSet PA suite, and YieldBook and other fixed-income analytics providers pose a formidable threat to the broad adoption of FDS's Derivative Solutions software. And the benchmark data of FactSet, while rather comprehensive with regard to domestic financial markets, still lags the major players of FTSE, iBoxx, SWX, and Pictet in the international arena. Even data management, where FDS hopes much of its revenue growth will materialize, poses problems for the firm, as Rimes Technologies and a trend for asset managers to insource data management solutions may also prevent widespread adoption. Given the range of large, well-established, and highly competitive corporations eager to defend their market shares within the FDS target submarkets (such as Bloomberg, FT Interactive Data, Reuters, S&P, COMPUSTAT, ITG, CSFB HOLT, RIMES Technologies), in the medium term, it seems as though FDS has bitten off more than it can chew. Our revenue and margin forecasts take these realities into consideration, as discussed below.

Valuation

Based on a thorough analysis of three different discounted cash flow models and relative valuation multiples based upon public comparables, we calculated the target stock price for FactSet Research Systems to be \$39.95. This estimate comes directly from our discounted cash flow model. Although we performed a relative valuation analysis, we feel that the lack of true comparables for FactSet renders the resulting multiples too inconsistent for us to utilize as anything other than a guide. However, based on the calculations detailed in Exhibit 3, the value of FactSet as calculated using relative multiples confirms the range of the valuation we calculated using our discounted cash flow model. Note that we report all monetary increments in U.S. dollars unless otherwise indicated.

DCF Inputs

Resembling the overall software industry's capital structure of 99.95% equity and 0.05% debt, FactSet's capital structure has been 100% equity since the company went public in 1996. The company has never issued long-term debt, and FactSet's balance sheet debt has been zero on every annual reporting date since 1996. The company did issue \$1.710MM in notes as part of the acquisition of StreamVPN Limited in September 2005 (representing 0.492% of FactSet's capital structure); however, the company can repay the note at any time, and we expect the firm to extinguish the note prior to the next annual reporting date in August 2006. In addition, the firm currently has a \$25MM revolving line of credit of which it has drawn \$3.1 million in aggregate



since 1998. FactSet is required to pay annual interest of 0.125% of the unused portion of the line of credit to the lender (JP Morgan Chase). This amounts to annual interest payments of \$27,375, or 0.0078% of FactSet's FY2005 capital base of \$347.53MM. Given the immaterial nature of FactSet's future debt commitments (0.0078% of the equity balance), we assume a debt and interest balance of zero going forward. Because we expect the debt-to-equity ratio to remain constant, we employ the Weighted Average Cost of Capital approach to value the equity of FactSet Research Systems.

The cost of capital for the firm was calculated using the Capital Asset Pricing Model. The risk-free rate was derived using the current yield on a 10-year US Treasury Bond, 5.036%, minus an assumed 1% premium demanded by purchasers of long-dated bonds. This results in a risk-free rate of 4.036%. We assume a market risk premium of 4% based on our future expectations of long-term stock market returns. We estimate the equity Beta for FactSet by regressing 10 years of monthly data using the following formula: $r_p - r_f = \alpha + \beta(r_m - r_f) + \varepsilon$.

We used a number of inputs for $(r_p - r_f)$, and $(r_m - r_f)$ in our calculations. For $(r_m - r_f)$, we used the CRSP value-weighted returns of the AMEX, NYSE, and NASDAQ indices minus a self-constructed risk-free rate derived from the monthly yield on the risk-free 10-year U.S. Constant Maturity Treasury index. We calculated $(r_p - r_f)$ using the monthly returns of FactSet's U.S.-listed common stock minus our self-constructed risk-free rate.

We also compiled raw Betas reported by Bloomberg (versus the S&P 500 Price Index) in addition to raw and adjusted Betas calculated by Bloomberg using the S&P 500 Total Return Index. To contextualize our results, we present the Betas estimated by these methods for FactSet's competitors. Finally, we produced 5-year rolling Beta estimates of FactSet's equity using the CRSP returns described above. After averaging the Betas we calculated from CRSP with the representative Betas from Bloomberg for FactSet and its competitors, we arrive at a Beta of 1.18 for FactSet.

We encountered difficulty finding publicly traded companies to serve as a reasonable proxy to FactSet for the purpose of comparison. FactSet's most significant competitor – Bloomberg – is a private company, and the vast majority of its competitors are organizational divisions within large, multinational conglomerates such as Thomas, Reuters, and Pearson for which insufficient segment reporting data is available. In the end, we chose Reuters, Thomson, and ITG (a provider of agency trade execution and portfolio analytics software) as our representative industry sample.

FDS 5-yr Rolling Beta Estimates, w/ 10-yr Constant Maturity as Rf	
Period*	60-Observation Beta Estimate, using CRSP
1996-2000	1.267071534
1997-2001	1.439833892
1998-2002	1.472839571
1999-2003	1.369774066
2000-2004	1.162630264
2001-2005	1.403641995
Mean	1.352631887
GeoMean	1.34824654

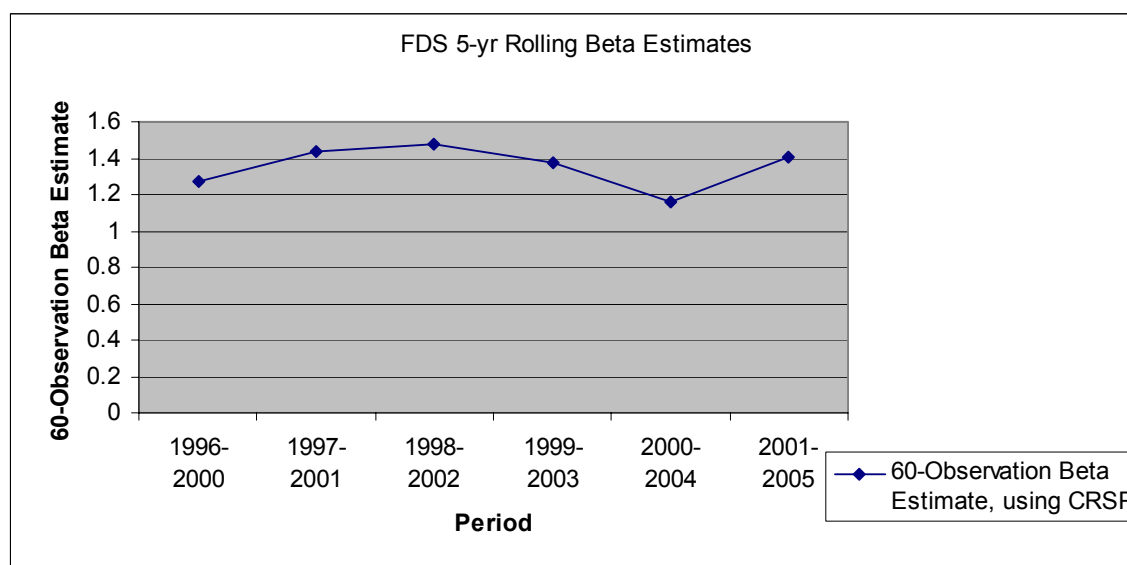
* Data for each estimate begins in January and ends in December, inclusively



	CRSP Value-Weighted, w/ 10-yr Constant Maturity as Rf	Bloomberg Reported	Bloomberg S&P Total Return, Raw	Bloomberg S&P Total Return, Adjusted
FDS	1.35	1.31	1.31	1.21
Reuters	N/A	1.98*	1.8**	1.53**
ITG	0.98	0.89	0.88	0.92
TOC	0.87	0.78	0.78	0.85

* Index is FTSE 100

** Index is FTSE 100 Total Return



Given that FactSet's Beta over the period from 1996 to 2005 has been essentially range-bound between 1.20 and 1.40, we are being extremely conservative in our Beta estimate of 1.18, since lower Betas result in a lower cost of capital and, as such, a higher valuation. While our estimate is indeed quite conservative in nature, we also feel that FactSet's Beta will drift downward towards the Beta of competitors such as Thomson and ITG over the next ten years as the company grows in size and scope. With inputs of $r_f = 4.04\%$, $\beta = 1.18$, and $(r_m - r_f) = 4\%$, we obtained a cost of equity of 8.770% for FactSet Research Systems.

We calculate the WACC using the following formula: $WACC = D/(D+E) \cdot (1-T) \cdot r_D + E/(D+E) \cdot r_E$. We use the YE2005 value of debt of \$0, current market value of equity of \$2.103B, an effective tax rate of 35% based on historical tax rates and management guidance, and a return on debt equal to 6.5%, which represents a cost of debt typical of established enterprise software providers. However, since FactSet is a debt-free company, the WACC calculation is equal to the cost of equity, yielding a WACC of 8.770%. Based on the current market price of \$43.20, we can conclude that, *ceteris paribus*, the market is interpolating a WACC for FactSet of roughly 8.25%, which seems like an extraordinarily low cost of capital for a high-growth, all-equity software firm such as FactSet. Please see the sensitivity analysis provided at the end of the report for further information.



Financial Statements and Forecast Assumptions

In this section, we discuss the assumptions on which the forecasted income statement, balance sheet, and statement of cash flows are based.

Sales

To model sales growth, we first dissect FactSet's revenue stream into two major categories: geographic segment growth and client growth. We then develop separate sales forecasts for FactSet going forward for each category.

U.S. generally accepted accounting principles – specifically SFAS 131 – require firms to report pro-forma operating income and sales revenue for each major operating segment as defined by the management of the company. Like most firms, FactSet breaks down revenue into three distinct geographic segments – North America, Europe (EMEA), and Asia Pacific (APAC). Within each geographic revenue segment, we forecast sales growth carefully based on historical relationships, management guidance, and industry trends, considering the evidence for and against the extrapolation of historic relationships into the future.

Industry trends have benefited FactSet significantly over the last three years, and we expect the favorable macroeconomic tailwind to continue through 2008. As a software provider to the financial services industry, the firm's fortunes are tied very closely to the application software industry, the level of spending in the financial services sector, and, in an indirect sense, by the ebb and flow of global capital markets. The application software industry has rebounded from the dog days of 2002 and 2003 to post incredibly strong growth in 2004 and 2005, and 2006 is expected to be a banner year for software providers. In addition, strong equity markets, low inflation, and a long-overdue economic rebound in Japan have led to explosive growth in the asset management industry (where FactSet draws 75% of revenues) and in investment banking (where FactSet draws the remaining 25% of its revenues) since 2003. According to a report by The Hennessee Group, the number of hedge funds more than doubled from 2000 to 2005 (from 4,000 funds in January 2000 to 8,035 funds in January 2005). Growth in assets under management since 2003 has also provided mutual funds and institutional managers with higher fee-based income, allowing these firms to enhance their investment systems, add headcount, and increase spending on discretionary purchases such as FactSet. Finally, the investment management industry is undergoing a revolutionary change in the way that data is managed across the global enterprise. In the last two years alone, a combination of mega-sized asset managers such as UBS Global Asset Management, Fidelity, JP Morgan Fleming, State Street Global Advisors, and Schroeders have spent billions of dollars to enhance, streamline, and centralize their data management infrastructure.

In summary, FactSet has experienced the best of both worlds since 2004 – strong markets, significant discretionary spending and headcount increases at financial services firms, and a software industry on the rebound. However, we need to be very careful about projecting our future growth estimates for FactSet based on the successes the company has enjoyed over the last three years. A small negative twitch in global equity markets or the long-awaited consolidation in the hedge fund industry may materially affect FactSet's sales growth in future periods. We generally forecast favorable industry conditions for FactSet going forward, and use these



projections to show that FactSet is moderately overvalued even under the assumption of relatively smooth sailing in the global economy over the next ten years.

Since 1996, FactSet has experienced rapid growth in its core North American market. The firm expects sales to increase more than 20% in North America during 2006, representing one of FactSet's most impressive growth years in recent history. We are projecting North American revenue growth to remain strong through 2008, at which point we expect a decline in revenue growth corresponding to the normal ebb and flow of the business cycle. We then expect revenues to increase 10% in 2010 and 2011 as the economy rebounds, after which we anticipate that revenue growth will trend slowly towards its terminal growth rate of 3% per annum. We expect FactSet's international growth to outpace domestic growth in the future for two key reasons: (1) FactSet has operated in North America for more than 25 years, and the North American market is essentially nearing the point of saturation; and (2) according to Bloomberg, the number of asset managers is now growing faster in Europe and Asia than it is in North America.

FactSet is very keen on expanding its operations outside of North America, and as a result, we forecast higher revenue growth in APAC and EMEA than in North America until 2015, when we assume that FactSet reaches its terminal growth phase. International revenue comprised 29% of FactSet's revenue in 2005, representing a material increase of 9% over the comparable figure from 2004. Our model projects international revenue to grow to 36% of FactSet's sales by 2016, reflecting the firm's continuing efforts to expand their non-U.S. revenue streams. Since 2003, FactSet has significantly expanded its presence in Europe, and year-over-year growth in Europe has reflected this increased level of investment. We project sales growth in EMEA to outpace growth in the saturated North American market until 2009, when EMEA will begin to trend towards the terminal revenue growth rate of 3%. The company is also actively seeking to expand its presence in APAC, and we expect headcount increases and significant capital infusions in the Tokyo, Hong Kong and Sydney offices over the next two years. As a result, year-over-year sales growth in APAC should solidly outpace revenue growth in Europe and North America through 2010, when APAC sales growth will begin to trend towards the company's terminal sales growth rate of 3%.

A summary of our sales growth expectations based on the three geographic segments is provided in the following table.

Sales Growth	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Overall	13.3	24.1	25.0	19.0	12.8	8.1	12.6	11.0	8.8	6.5	3.2	3.0	3.0
North America	%	%	%	%	%	%	%	%	%	%	%	%	%
Europe	12.4	13.5	23.1	15.0	10.0	5.0	10.0	10.0	8.0	6.0	3.0	3.0	3.0
Asia Pacific	%	%	%	%	%	%	%	%	%	%	%	%	%
	15.1	74.3	27.8	25.0	15.0	10.0	15.0	10.0	8.0	6.0	3.0	3.0	3.0
	%	%	%	%	%	%	%	%	%	%	%	%	%
	16.4	30.5	32.1	50.0	35.0	30.0	25.0	20.0	15.0	10.0	5.0	3.0	3.0
	%	%	%	%	%	%	%	%	%	%	%	%	%

Our second revenue model is based upon FactSet's expected client growth rates. The firm publishes its basic subscription prices and average revenue per client (APRC), which we are projecting to be \$225,500 in 2006 based upon management's Q2 guidance coupled with FactSet's somewhat lower historical growth rates. Going forward, we project the average revenue per client to grow with inflation, which we assume to be 2% per annum. We then pair our APRC estimates with expected net client growth rates in order to project future sales revenue. Our expected net client growth rates are based upon management guidance for 2006, the average



historical net client growth rate of 10.23%, increased expansion in Asia Pacific during 2007, the maturing of the industry in future years, and the ebb and flow of the normal business cycle. Our terminal client growth rate is 1%, which matches the terminal growth rates for our geography-based model after factoring in the 2% inflation premium built into our ARPC projections. As of February 28, 2006, no single FactSet client represented more than 3% of revenues, and the average client renewal rate was 95%, which matches the firm's renewal rate from prior periods. As such, we assume the renewal rate stays constant at 95% over the life of our model. A decline in renewal rates would reduce future expected sales growth, strengthening our investment recommendation.

FactSet's Portfolio Analytics product suite represents the firm's flagship equity research platform, and, as such, constitutes the firm's most important product line. Due to its importance to the growth of the firm, FactSet publishes client data and average users per client (AUPC) for the Portfolio Analytics suite (although the firm does not disclose *revenue* from this important product line). The pricing of Portfolio Analytics is extremely complicated, and is based primarily on four characteristics: (1) the size of the client (greater than or less than \$1 billion under management), (2) the number of users at the firm, (3) the types of add-on functionality chosen by each client and each user, and (4) whether each client purchases the suite as a whole or purchases individual modules. All marginal users after the third user at a given client pay the same license rate of \$9,000 for basic Portfolio Analytics functionality. As such, we project revenue of \$9,000 for each user license during 2006, after which we expect license seat revenue to increase by 2% annually with inflation. In addition, we use FactSet's published list prices to model the most popular combination of Portfolio Analytics product modules in order to arrive at an estimate of the annual "first user" charges per client, which we calculate as being \$126,000 for each client during 2006. We then increase our 2006 estimate linearly into future periods at the rate of inflation (2%). Our analysis of the Portfolio Analytics suite is provided for purely informational purposes, but the analysis sheds quite a bit of light into the importance of this product line to the firm's overall growth strategy.

A summary of our client growth expectations for FactSet is presented below:

Sales Growth	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Overall	13.3%	24.1%	25.0%	17.3%	12.2%	9.7%	12.2%	12.2%	9.7%	7.1%	5.1%	3.0%	3.0%
Number of Clients	1437	1576	1734	1994	2193	2357	2593	2853	3066	3220	3316	3350	3383
%YOY Growth	46.5%	9.7%	10.0%	15.0%	10.0%	7.5%	10.0%	10.0%	7.5%	5.0%	3.0%	1.0%	1.0%
Avg. rev. per client (\$MM)	0.175	0.198	0.226	0.23	0.235	0.239	0.244	0.249	0.254	0.259	0.26	0.27	0.27

Our final step is to take the arithmetic average of our annual sales growth estimates from the geographic segment growth model and the client growth model in order to arrive at FactSet's projected net sales from 2006 to 2016. Taken together, these sales assumptions result in FactSet's revenue increasing from \$313MM in 2005 to \$930MM in 2016.

FactSet's management team has a reputation for providing analysts with fairly accurate short-term earnings and margin forecasts. We therefore feeling slightly more comfortable using management's short-term guidance than we normally would. However, we take management's guidance as an upper bound on all projections extending beyond 2006. The table shown on the following page paints a clear picture of the relationship between management's guidance and actual results during the period from Q1 FY2002 to Q2 FY2006 (courtesy of Morgan Stanley):



Measure	Q1	Q2	Q3	Q4
F2002(A)				
Revenue - guidance	48.0-49.5	49.0-50.5	51.0-52.5	52.5-54.5
Revenue – actual	49	50.4	52.4	54.1
Operating Margin – guidance	28.80%	29.20%	29.5-29.6%	30.00%
Operating Margin - actual	29.20%	29.90%	30.80%	32.10%
	OK/OK			
F2003(A)				
Revenue - guidance	54.0-56.0	54.5-56.0	57.0-59.0	58.5-60.0
Revenue – actual	54.8	56.7	59.1	59.7
Operating Margin – guidance	31-32%	31.5-32.5%	32.5-33.5%	33.00%
Operating Margin - actual	32.60%	33.30%	33.00%	34.30%
F2004(A)				
Revenue - guidance	58.0-60.0	59.5-61.0	62.5-64.0	65.5-70.0
Revenue – actual	59.3	61.4	63.6	67.7
Operating Margin - guidance	34.5-36.0%	35.0-36.0%	34.5-35.5%	34.0-35.0%
Operating Margin - actual	35.50%	35.00%	34.30%	34.30%
F2005(A)				
Revenue - guidance	73.0-75.0	75.0-77.0	77.0-80.0	80.0-82.0
Revenue - actual	74.1	76.5	79.3	82.8
Operating Margin - guidance	32.0-34.0%	34.0-35.0%	34.0-35.0%	34.0-35.0%
Operating Margin - actual	34.90%	35.30%	34.50%	34.80%
F2006(E)				
Revenue - guidance	88.0-90.0	91.0-93.0	95.0-97.0	
Revenue - actual	89.7	93.7	96.3 E	
Operating Margin - guidance	29.5-31.5%	30.0-32.0%	31.0-33.0%	
Operating Margin - actual	30.60%	31.60%	31.90%	

Cost of Goods Sold

Our cost of goods sold assumptions are based on historical gross margins provided by Bloomberg, FactSet's SEC filings, and data contained in the firm's annual reports. Due to poor disclosure policies, FactSet does not provide data on gross margins for each product line, presumably for competitive purposes. Although SFAS 131 requires FactSet to report its net profit margins for each operating segment, the firm is not required to disclose gross margins for each geographic segment or each product line. As a direct result of FactSet's disclosure policies, we are not able to project cost of goods sold for each geographic segment or product group. FactSet currently possesses a higher-than-average gross margin (75%) relative to the industry norm of 70%, likely due to explosive sales growth from its existing product set during 2004 and 2005. FactSet's management has indicated that the firm expects margins to be stable at around 75% for the foreseeable future. However, as the firm grows, and the industry becomes more competitive,



FactSet's gross margin should trend towards the industry average of 70%. As such, our model optimistically allows FactSet to retain its 75% gross margin through 2007, after which a gradual decrease in gross margins leads to gross margins of 70% through the terminal valuation date.

We should also note that our industry margin of 70% is based upon the average industry gross margin for the application software industry. As a data provider, FactSet also sells products which command a slightly lower margin – estimates from Yahoo! Finance indicate an average gross margin of 65.4% for major providers of financial services data. As such, we feel that our terminal margin of 70% is very generous to FactSet, further strengthening our investment recommendation.

Sales, General, & Administrative

FactSet's S,G&A expenditures represented roughly 47% of gross profits during 2005. Although higher S,G&A expenditures caused operating margins to decline by roughly one percentage point in each of the last three years, FactSet's management has indicated that the firm expects margins to be stable for the foreseeable future. As indicated elsewhere in this report, FactSet made a few large "one time" purchases during 2005 that are not expected to recur in future periods, strengthening management's argument. Although we optimistically assume that margins will be stable in 2006 and 2007, two factors cause us to project lower operating margins for FactSet in 2008 and beyond: (1) the firm is making large investments in its international operations, which may lead to higher staffing levels, increased real estate rental expense, and higher travel costs; and (2) FactSet currently enjoys an operating margin of around 33%, which is significantly higher than the industry average of 28%. We again take the optimistic view and hold margins constant for 2006 and 2007, after which we reduce FactSet's operating margins to the long-term industry average of 28%.

Other Income Statement Items

We forecast depreciation and capital expenditures using a plug that allows net PP&E to grow endogenously as a function of sales growth parameters. We discuss those forecasts later on in the report. Based on FactSet's historical effective tax rates (for example, 35.2% in 1H 2006, 34.9% in 2005, 35.1% in 2004, and 34.9% in 2003), we assume a 35% effective tax rate going forward. We note that FactSet's management is guiding for tax rate estimates of 35.9-36.5% for FY2006. However, we choose to stick with the optimistic assumption that tax rates will remain at 35% through the terminal date. In addition, the impact of the potential negative change in market valuation from a 1% increase in the tax rate is immaterial to our investment recommendation.

Balance Sheet and Statement of Cash Flows Assumptions

We forecast cash and cash equivalents as last year's cash plus last year's net income minus cash outlays to shareholders. We estimate cash outlays to share holders using a historical dividend payout ratio of 12.31% and a share buyback ratio of 18.82%, based on management's Q2 2006 guidance on share repurchases and an existing order directing the firm to repurchase up to \$50MM in shares over the next few years.

As per accounting regulations, Goodwill stays constant for existing investments; it is not amortized. FactSet's existing intangibles are amortized in line with management guidance for 2006 and in line with sales growth thereafter.



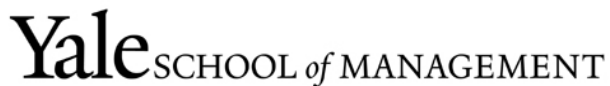
We exclude 95% of FactSet's cash balance in our working capital calculation because it simply accumulates on the balance sheet and, as such, is not 'working' to produce the operating profits accrued to the firm. We assume that a modest 5% of annual cash is used for operating purposes, and include this value in our working capital calculation. This is a conservative assumption; one could argue that 10% or more of the company's cash balance will be tied up in working capital, in which case FactSet's free cash flow will decline, leading to a lower valuation. As long as the firm is not using this excess cash for operating expenses and instead is investing this cash in zero net present value projects, this assumption will be valid.

Acquisitions

Over the last two years, FactSet has spent a significant percentage of its free cash flow (for example, 128% of free cash flow in 2005) to acquire technologies which will complement and expand the firm's existing product offerings. Continuing this trend, the firm has already spent \$27.87 million in FY2006 to make two strategic acquisitions geared towards broadening the firm's equity analytics and data delivery capabilities. When valuing a growing software company with high profits and low capital expenditure requirements, one can make a number of assumptions about how the firm will choose to reinvest free cash flow back into the business. In the case of FactSet, management has indicated that it does not expect to increase dividend and stock repurchase payout ratios, and the firm has been very stingy making capital expenditures. In the absence of unexpected shareholder dissent, there are only two key ways exist for the company to reinvest its earnings into the business. One is to simply invest excess cash in passive, zero-NPV investments such as U.S. bonds and allow cash & marketable securities to passively accumulate on the balance sheet. The other option is to continue making strategic acquisitions in the hopes of expanding product breadth, differentiation capabilities, and geographic reach.

In order to ensure that our assumptions about FactSet's future uses of free cash would not affect our investment recommendation, we modeled the firm using three distinct scenarios related to the firm's likelihood of making future cash acquisitions:

- Scenario 1: FactSet will make no future acquisitions beyond the acquisitions already completed during FY2006. All excess cash (save for the 5% assumed to be used for working capital) will be reinvested in zero-NPV projects. This is the most optimistic scenario since . Under the assumption of no future acquisitions, our model produces a stock price of \$46.65 for FactSet, which represents an 8% premium over the current market price of \$43.20.
- Scenario 2: FactSet will make acquisitions in all future periods. The amount spent on acquisitions each year is equal to the average of the firm's spending on acquisitions during the previous five years. This is a "middle-of-the-road" scenario, since the moving average stabilizes at around \$25 million per year as it approaches the terminal date. Under this scenario, acquisition spending does not increase in line with sales growth, reflecting the fact that FactSet should generate higher organic growth in later periods as a result of past acquisitions. As a result of this strategy, our model produces a stock price of \$39.95 for FactSet, representing an 8% discount to the current market price of \$43.20. *We use this scenario as our base case for the purposes of this report.*
- Scenario 3: FactSet will make acquisitions in all future periods. The amount spent on acquisitions each year is equal to the firm's actual 2006 acquisition expenditures scaled in future periods to increase in line with sales growth. This is the most pessimistic scenario; it assumes that FactSet will be required to spend around 39% of its annual after-tax earnings on



FactSet's two most recent transactions are used as a proxy to determine how assets acquired via acquisition should be allocated between the various accounts on the balance sheet. With one insignificant exception, the companies that FactSet has acquired to date have possessed zero debt; the vast majority of their capital structure has been in the form of private equity. As such, we do not project FactSet's future acquisitions to impact current liabilities or the firm's capital structure. Fully 85.8% and 86.5% of the purchase price for Europrospectus.com, Ltd. and StreamVPN, Ltd., respectively, were allocated to the Goodwill and Intangibles account, with the remaining percentages being allocated to tangible assets such as property, equipment, receivables, and cash. For simplicity, we assume that 85% of the acquired assets from FactSet's future transactions are added to the Goodwill & Intangibles account, with the remaining 15% of acquired assets being added to FactSet's cash balance. The underlying result is that the return FactSet earns on its acquired assets will be equal to the return it will earn on its existing assets.

Model Changes:	Parameters				Acquisitions?		
FDS Price: \$43.20	Cash % used in WC	Beta	10-yr CAGR	No	Yes, Level	Yes, Increasing with Sales	
Base Case	5%	1.18	10.26%	46.65	39.95	34.17	
10% Cash in WC	10%	1.18	10.26%	44.68	38.34	32.86	
Higher Beta	5%	1.35*	10.26%	42.59	36.47	31.27	
9% CAGR	5%	1.18	9.00%	41.66	35.13	30.29	

We scale net PP&E with sales, which assumes constant returns to scale for those production inputs. We scale receivables, inventories, prepaid expenses, other current assets, other assets, accounts payable, accrued expenses, and other current liabilities with sales growth.

Given the above assumptions, the Cash Flow Statement is easily constructed, and we generate all-equity cash flows that increase from \$62.71 million in 2006 to \$158.02 million in 2016 using our base acquisition case (Scenario 2) from above.

Our model results in the following margins, ratios, EVA, and price multiples going forward (again, using the base case described above):

[illegible]



Economic Profit (% above WACC)	24%	19%	17%	12%	10%	9%	8%	7%	6%	5%	4%	3%
Sales Growth	24%	25%	18%	13%	9%	12%	12%	9%	7%	4%	3%	3%
Gross Margin	75%	75%	75%	73%	70%	70%	70%	70%	70%	70%	70%	70%
Operating Margin, before Depreciation	40%	40%	40%	36%	35%	35%	35%	35%	35%	35%	35%	35%
Operating Margin, after Depreciation	35%	33%	33%	29%	28%	28%	28%	28%	28%	28%	28%	28%
Net Margin	23%	21%	21%	19%	18%	18%	18%	18%	18%	18%	18%	18%
Net Income Growth	24%	16%	18%	0%	4%	12%	12%	9%	7%	4%	3%	3%
Liquidity Ratios												
Current Ratio	2.18	2.68	3.24	3.73	4.22	4.60	4.96	5.35	5.79	6.31	6.89	7.47
Quick Ratio	2.04	2.53	3.08	3.57	4.05	4.43	4.79	5.17	5.61	6.12	6.70	7.27
Receivable Turns	6.25	6.34	6.03	5.76	5.53	5.48	5.33	5.14	4.96	4.79	4.64	4.53
A/R Collection Period	58	58	60	63	66	67	69	71	74	76	79	81
Payable Turns	4	4	4	4	5	5	5	5	5	5	5	5
Payment Period	98	86	88	82	76	75	75	76	77	78	78	78
Cash Conversion Cycle	-40	-28	-27	-18	-10	-8	-7	-5	-3	-2	0	2
Performance Ratios												
Asset Turnover	0.90	0.90	0.86	0.82	0.77	0.74	0.72	0.69	0.65	0.61	0.57	0.54
Return on Assets	38%	33%	31%	26%	23%	22%	22%	21%	19%	18%	17%	16%
Equity Turnover	1.45	1.29	1.21	1.12	1.02	0.98	0.94	0.89	0.83	0.76	0.70	0.65
Depreciation as % of Net Sales	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%
Annual CapEx as a % of Depr. Expense	1.49	1.13	1.13	1.13	1.13	1.13	1.13	1.13	1.13	1.13	1.13	1.13
DuPont Breakdown: (1) Operating Margin	0.35	0.33	0.33	0.29	0.28	0.28	0.28	0.28	0.28	0.28	0.28	0.28
(2) Asset Turnover	0.90	0.90	0.86	0.82	0.77	0.74	0.72	0.69	0.65	0.61	0.57	0.54
(3) Financial Leverage	1.30	1.28	1.27	1.25	1.23	1.22	1.22	1.21	1.19	1.18	1.16	1.15
Free Cash Flow Assumptions												
CapEx as % of After-Tax EBIT	31%	27%	27%	30%	31%	31%	31%	31%	31%	31%	31%	31%
Acquisitions as % of After-	129%	34%	21%	21%	20%	18%	19%	19%	19%	20%	15%	15%



Tax EBIT

Dividends as % of After- Tax EBIT	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%
Share Repurchases as % of After- Tax EBIT	19%	19%	19%	19%	19%	19%	19%	19%	19%	19%	19%	19%
Totals	190%	91%	79%	82%	83%	80%	81%	81%	82%	82%	78%	77%

Our model predicts that FactSet will produce economic profit of 3.06% at the terminal date, which signifies a terminal ROE higher than the firm's cost of capital. ROE does fall as the industry matures, but given that FactSet currently has a virtual monopoly on equity analytics data in the United States, and given the significant economies of scale that FactSet can leverage due to its large installed base of North American customers, producing economic profits in the terminal date is indeed possible. Arguments that ROE should converge to cost of capital only support our investment thesis.

As previously mentioned, FactSet currently enjoys gross margins and operating margins that are significantly higher than industry norms. As is the case with many growth companies in technology-intensive fields, FactSet has been able to successfully leverage a relatively small suite of products into ongoing commercial success stories, which has allowed the firm to increase sales at a faster rate than it has expanded its research and sales staff in recent years. As a result, FactSet's gross and operating margins from 2004 through Q2 2006 averaged 75% and 33%, respectively. However, as the firm expands its geographical footprint and product range, and with the possibility of a vertical price squeeze on the horizon for FactSet's data management products, we expect margins to decline towards the industry norms of 70% and 28%, respectively, by the terminal date. If FactSet's margins are allowed to remain at 75% and operating margins can be sustained indefinitely at 33%, our model projects a stock price of \$45.40, representing a 4.5% premium over the current market price. As such, the market does not appear to be factoring the potential for margin erosion into its current valuation of FactSet's common stock.

Model Results & Valuation Summary

Using the Weight Adjusted Cost of Capital Methodology discussed above, the formula $[PV = PV(\text{All Equity Cash Flows}) - \text{Debt Outstanding} + \text{Cash}]$ resulted in an equity value of \$1.873 billion, or \$39.95 per share of FactSet's common stock. This represents a 7.5% decrease from the market price of \$43.20, and supports our conclusion that FactSet's equity is moderately overpriced. Exhibit 1 contains our full discounted cash flow analysis.

The following sensitivity analysis reveals the extent to which FactSet is overvalued, even after relaxing key assumptions.



Sensitivity Analysis						
WACC	Terminal Growth Rate					
		3.75%	3.50%	3.25%	3.00%	2.75%
	7.000%	67.25	63.70	60.63	57.94	55.56
	7.250%	62.41	59.41	56.79	54.47	52.42
	7.500%	58.23	55.67	53.41	51.40	49.60
	7.750%	54.58	52.37	50.41	48.65	47.07
	8.000%	51.36	49.44	47.73	46.19	44.79
	8.250%	48.50	46.83	45.32	43.96	42.72
	8.500%	45.95	44.48	43.15	41.94	40.83
	8.770%	43.48	42.19	41.02	39.95	38.97
	9.000%	41.58	40.42	39.37	38.41	37.52
	9.250%	39.70	38.67	37.72	36.86	36.06
	9.500%	37.98	37.06	36.21	35.43	34.71

Exhibit 1 – DCF Model

Terminal Growth=	3.00%
Equity Premium=	4.00%
WACC=	8.7697023%
% Debt in capital structure =	0
Cost of Equity=	8.7697023%
Cost of Debt=	6.50%
Risk Free Rate=	4.036%
Beta=	1.183425576
% Cash used in WC calcs	5.00%
Effective Tax Rate=	35.00%

$$rE = rF + B(rM) = 0.087697023$$

$$WACC = D/(D+E) * (1-T) rD + E/(D+E) * rE$$

PV = PV(All Equity Cash Flows) - Debt Outstanding + Cash

Value of Equity= 1944.932785 \$million

		FCFt	Gross Discount Rate
PV(FCF2006)=	60.9771462	62.70994333	1.028417157
PV(FCF2007)=	78.46898077	87.77589467	1.11860628
PV(FCF2008)=	73.27756228	89.15715595	1.216704721
PV(FCF2009)=	70.98653085	93.94400814	1.323406103
PV(FCF2010)=	74.37765367	107.0640202	1.439464878
PV(FCF2011)=	75.60250112	118.3709617	1.565701663
PV(FCF2012)=	75.60334435	128.7531787	1.703009038
PV(FCF2013)=	74.11325538	137.2842712	1.85235786
PV(FCF2014)=	70.61268549	142.2707304	2.01480413
PV(FCF2015)=	69.74120835	152.8376108	2.191496455
Terminal Value=	1148.950066	158.0168036	2.38368417

PV(All Equity Cash Flows)= 1872.710935

Debt = 0

Market Value of Equity=	2102.924	\$million
Market Value of Debt=	0	\$million
Shares Outstanding=	48.679	\$million
TARGET PRICE:	39.95	per share
Current Price	43.20	per share
Overpriced by:	7.51	%



Cash not used for WC = 72.22185

Exhibit 2 – FDS Equity Pricing Chart

■ FACTSET RESH SYS INC
as of 4/17/2006

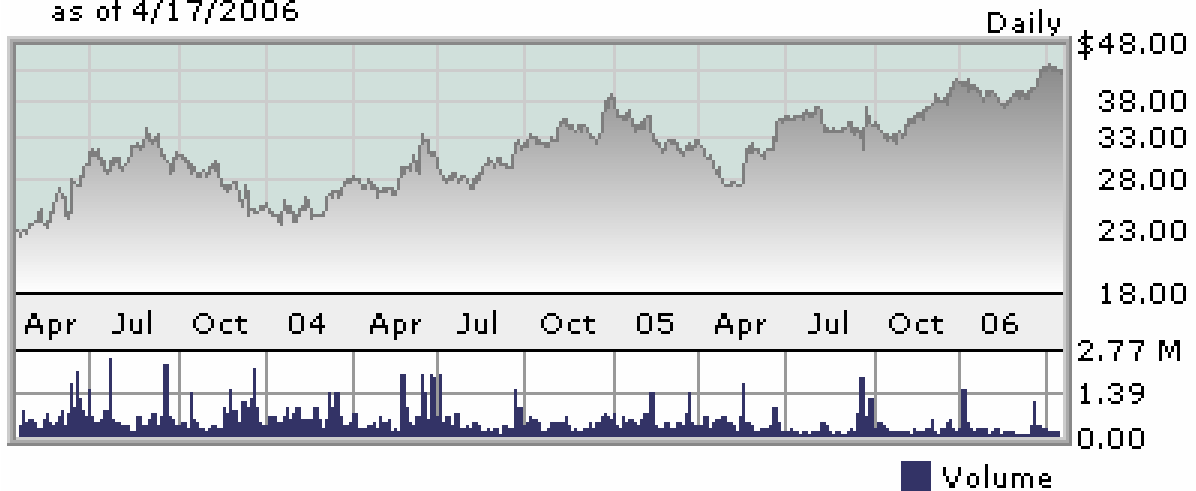




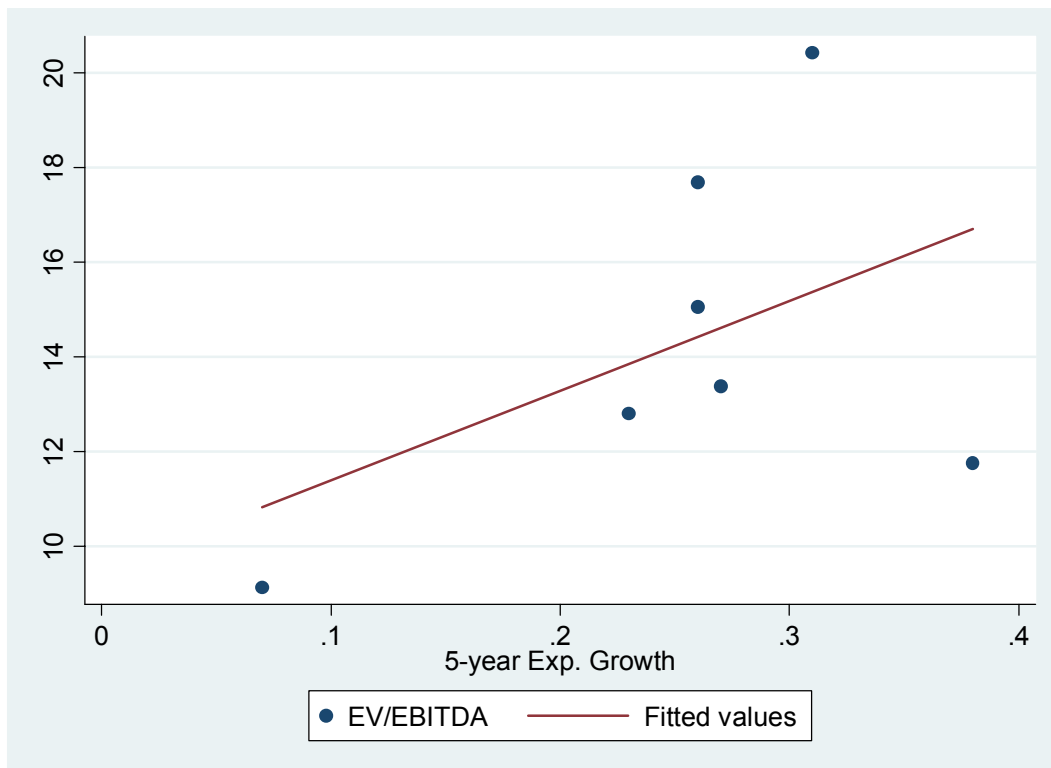
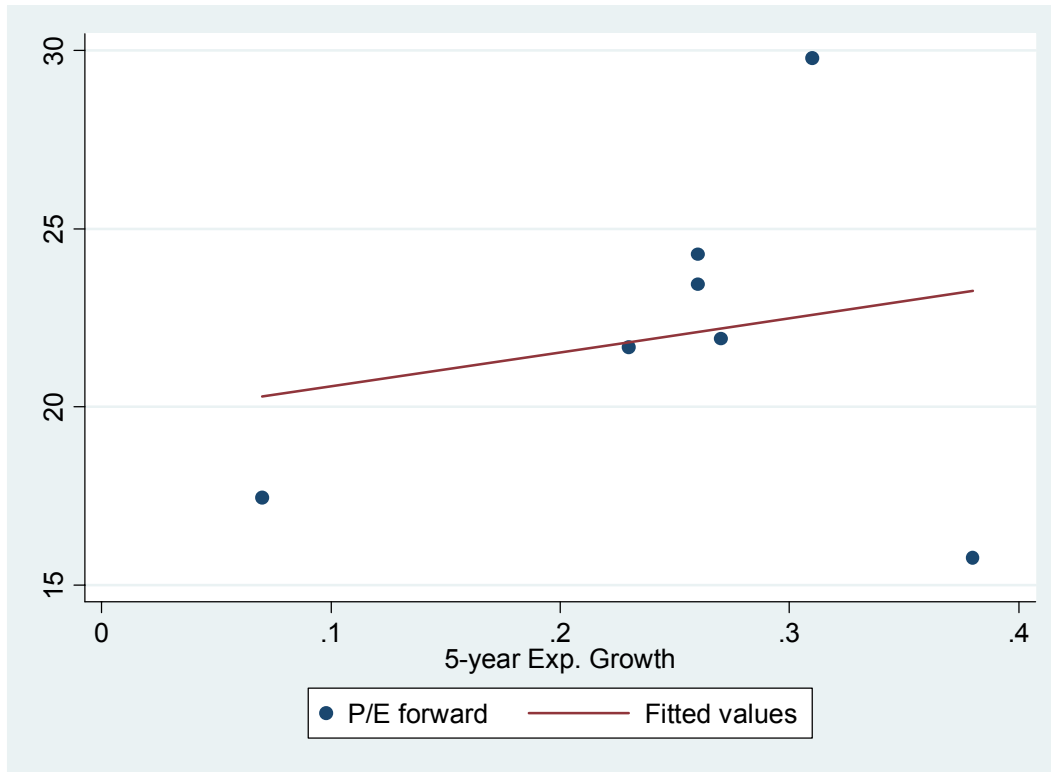
Exhibit 3 – Relative Valuation Model and Industry Graphs

Company	Price	P/E forward	5-year Exp. Growth	P/BV mrq	ROE ttm	P/S ttm	Net Margin	EV/EBITDA
FDS	43.2	24.27	25.87%	6.78	28.18%	6.09	22.19%	15.05
ITG	51.09	23.44	25.67%	4.73	16.26%	5.4	16.58%	17.69
Thomson	39.24	21.68	23.08%	2.58	9.43%	2.93	10.75%	12.79
Reuters	39.39	15.76	37.88%	9.2	30.39%	2.1	5.94%	11.75
McGraw-Hill	58.05	21.91	26.75%	6.95	27.69%	3.55	14.07%	13.37
Pearson	13.62	17.46	6.81%	1.74	10.44%	1.52	7.86%	9.12
Moody's	69.7	29.79	31.26%	65.38	178.91%	11.66	3.24%	20.42

	P/E forward	5-year Exp. Growth	P/BV mrq	ROE ttm	P/S ttm	Net Margin	EV/EBITDA
Averages w/o FDS	21.673333	0.252412462	15.09667	0.4552	4.526667	0.0973972	14.1906402
Avg's w/o FDS & Moody's	20.05	0.24	5.04	0.19	3.10	0.11	12.94

Actuals						
FDS Equity Value:	2,102	1796.50	1351.27	1211.82		2205.08
Shares Outstanding:	48.68	49.68	51.68	53.68		55.68
FDS Stock Price:	43.18	36.16	26.15	22.58		39.60

FDS Target Capitalization:	1641.17
FDS Target Price:	31.12



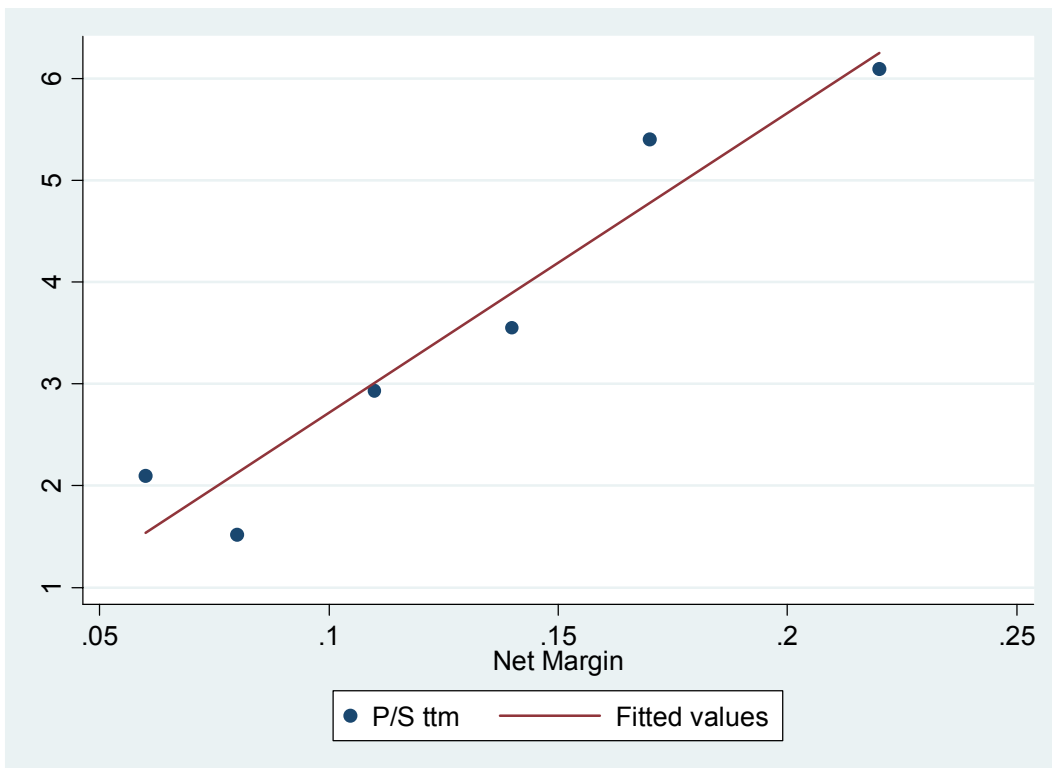
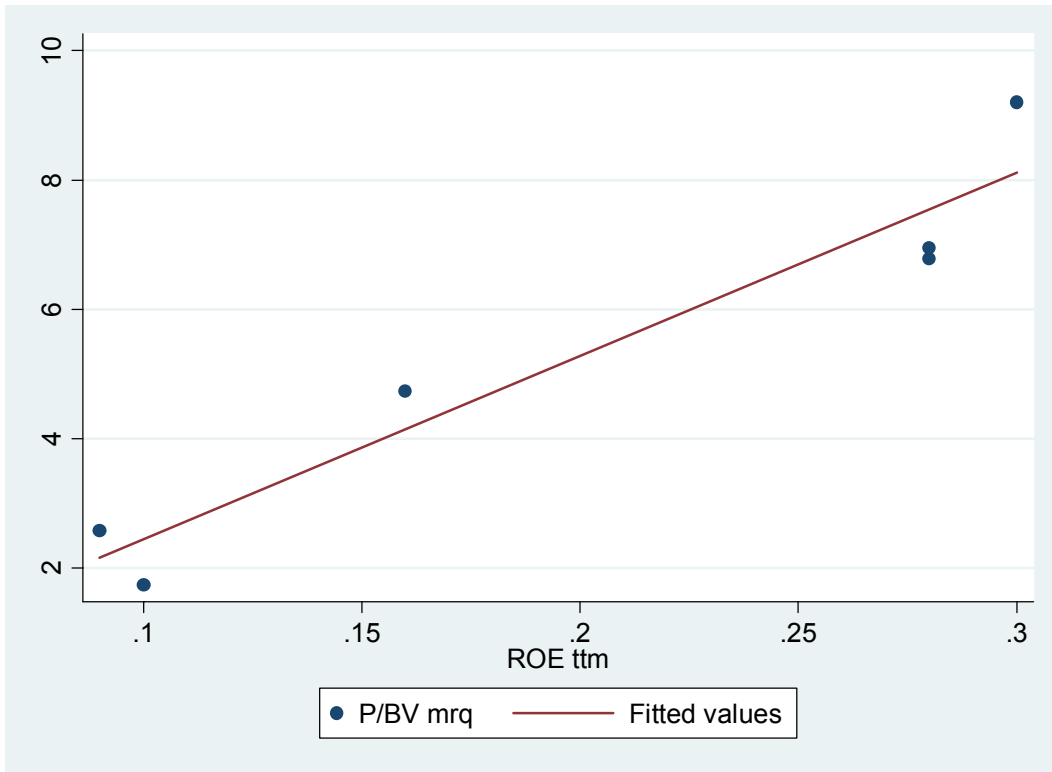




Exhibit 4 – Management

Directors

Philip A. Hadley

Chairman of the Board,
Chief Executive Officer

Charles J. Snyder

Vice Chairman of the Board,
Retired President

Michael F. DiChristina

President,
Chief Operating Officer

Scott A. Billeadeau

Senior Vice President,
Senior Portfolio Manager
Fifth Third Asset Management
Minneapolis, Minnesota

Joseph E. Laird, Jr.

Chairman,
Chief Executive Officer
Laird Squared, LLC
New York, New York

James J. McGonigle

Lead Independent Director,
Chairman
The Corporate Executive Board
Washington, D.C.

Walter F. Siebecker

President
Burgess Consulting LLC
New York, New York

Management

Philip A. Hadley

Chairman of the Board,
Chief Executive Officer

Michael F. DiChristina

President,
Chief Operating Officer

Michael D. Frankenfield

Senior Vice President,
Director of U.S.
Investment Management Services

Townsend Thomas

Senior Vice President,
Chief Content Officer

Peter G. Walsh

Senior Vice President,
Chief Financial Officer,
Treasurer

Scott L. Beyer

Senior Vice President,
Director of International Operations

Chris Ellis

Senior Vice President,
Director of Portfolio Analytics

Mark J. Hale

Senior Vice President,
Director of Software Engineering

Kieran M. Kennedy

Senior Vice President,
Director of Investment Banking and
Brokerage Services

Laura C. Ruhe

Senior Vice President,
Director of U.S.
Investment Management
Product Development

Jeff Young

Senior Vice President,
Chief Technology Officer

Source: FactSet



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