

Merriam Report Focus List: Earnings Update for Dec. 15, 2009

BEST BUY (BBY)

Merriam Rating: AVOID

For the third qtr. ended Nov. 28, Best Buy reported a profit of \$227 million, or 53 cents a share, up from \$52 million, or 13 cents, a year earlier. Although the results beat analyst' estimates, shares took a hit on a warning by the company that this quarter's margins should be lower than anticipated due to sales of lower priced netbooks and televisions.

In our Oct. 29th Merriam Report for BBY, we suggested avoiding this stock due to deteriorating dual-cash flow trends, high goodwill levels and contrasting capital productivity and revenue metrics.



Although we're impressed with the 4.6% bump in sales (Y-to-Y), the decline in gross margins for the latest qtr. in addition to management's warning of potential further margin erosion in the current period isn't surprising.

At the time we issued our report, BBY shares were changing hands at \$40. In the six weeks since and leading up to Q3 earnings, investors bid the stock up to \$45, only to see the shares get hammered almost 10% following the earnings release.

Congratulations to traders smart enough to sell before earnings were announced. However, we remain very cautious on BBY and believe fair value is closer to \$35.