

# The Goldman Guide

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## In This Issue

Penn State Scandal: We Look at the Financials

Obsolescence vs. Innovation

Buy eBay (NASDAQ:EBAY)

## Penn State Scandal: We Look at the Financials

Anyone with a heartbeat knows the tragic, unfathomable Penn State University story that has dominated headlines and conversation for a week. It is a sad reminder of many of man's worst qualities: fear, greed, power, arrogance, and self-preservation. After sifting through Penn State's financials, we also conclude, it's all about money.

There is a story that hit the *Financial Times* over the weekend that Moody's is considering reviewing the rating on Penn State's bonds. Interestingly it notes that Penn State athletics accounts for only 2% of the University's \$4.6 billion in FY 2011 in operating revenue. Pretty close to the *stated* number, but way off.

According to a 2008 Penn State commissioned independent study produced by Tripp Umbach and Associates, Penn State contributes more to Pennsylvania's economy than any industry. In fact, the figure cited is that Penn State contributes \$17 billion annually to the Commonwealth of Pennsylvania.

We drilled down further on operating revenue sources which were revealing. PSU is one of very few universities to have an athletics department that generates profit. Based on recent figures, it looks as if PSU athletics generates operating profit of 15% annually, of which a portion is contributed to help fund other parts of the PSU system.

Back to the core of the issue. We have a sick man, a pedophile using his power, influence, and position to run amok---for years after he was dismissed. There is a story out that he was recruiting players to PSU this year!

Clearly, this has been swept under the rug. A blind eye turned, all to save the brand.

I am not here to say that Joe Paterno and PSU football has been the driving force behind the PSU brand and its success as an academic institution. But, let's face it. He was.

He was the model of consistency, decency, success, longevity. He was the man and role model many wished to be. He instilled pride and passion into the university. While he "only" was the head coach of the school's football team, let's be real. For all intents he was the face and tacit leader of the institution itself.

There is a reason why Penn State has the largest dues-paying alumni association of any university in the world.

And it ain't cause of the liberal arts department, or the business school.

It's all about the money and the brand. Self-preservation.

## Obsolescence vs. Innovation

It is said that the more things change the more they stay the same. In the technology world, nothing could be further from the truth. In the consumer world, trends come and go, for products and services. If companies are not quick to change, they will be left behind. How many venerable retail chains have closed down in the past 20 years due to the rise of Wal-Mart and Target, not to mention dollar stores? Are malls still relevant?

In the technology world, previously innovative companies grew complacent and did not change quickly enough. Their products became irrelevant. Obsolescence reared its ugly head.

Here is a link to a great article on technology company obsolescence. <http://www.foxnews.com/scitech/2011/11/12/heavyweight-to-scrap-heap-whats-future-for-rim/>

One of the featured companies is Research in Motion, which we have mentioned as a troubled company that may be acquired, since it likely cannot survive as a stand-alone firm for much longer.

Interesting how there can be both hardware and software obsolescence.

## Buy eBay

We are less than two weeks from Black Friday and we will discuss companies in the commerce and retail business for the next few weeks, as a result of the upcoming holiday season.

These stocks tend to become more popular (volume-wise) as, like their businesses, the stock performance and interest is somewhat seasonal.

While we typically stick to our knitting in small caps, we sense an interesting trend brewing in e-commerce. When one thinks of e-commerce, Amazon, the 800-pound gorilla, comes to mind. In our view, eBay (NASDAQ: EBAY -\$31.76) may be the better play.

While most of us think eBay as an auction site, or somewhat of an online mall, in truth, eBay is much more. Over the past 5 years, eBay has acquired no fewer than 15 companies. All of these firms have unique technology that enables some aspect of e-commerce, fulfillment, advertising, etc. The cornerstone of these transactions was the purchase of GSI Commerce 5 months ago. GSI Commerce, which creates and runs online shopping sites for major brick and mortar companies, should contribute nicely to eBay this year.

The Company's PayPal unit, which acquired BillMeLater is one of the Firm's biggest acquisitions, and continues to flourish. Importantly, innovation, both through acquisition and R&D should begin to come out from behind the shadows in the coming months.

eBay is trading at a reasonable P/E of 14x next year's EPS consensus estimate of \$2.31, which has been trending higher in recent months. eBay is not a high-flyer, nor is it an also-ran, as expectations are for 25% top-line and 15% bottom line growth (which we think are conservative expectations.)

In our view, eBay is about the safest play in e-commerce and a way to enjoy the innovation of e-commerce. There is also great technical support at current levels and just a small move upward could move the trend much higher. Expect more M&A and cool new offerings in the Mobile App arena next year. And, of course, good deals in its auctions.

Until next week....



### **Analyst: Robert Goldman**

Rob Goldman has over 20 years of investment and company research experience as a senior research analyst and as a portfolio and mutual fund manager. During his tenure as a sell-side analyst, Rob was a senior member of Piper Jaffray's Technology and Communications teams. Prior to joining Piper, Rob led Josephthal & Co.'s Washington-based Emerging Growth Research Group. In addition to his sell-side experience Rob served as Chief Investment Officer of a boutique investment management firm and Blue and White Investment Management, where he managed Small Cap Growth portfolios and *The Blue and White Fund*.

### **Analyst Certification**

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