Goldman Small Cap Research

The Goldman Guide

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Financials: A Lesson Learned

Last week's Jefferies Group and Leucadia National Corp fiasco reminds us that that you have to have your head examined if you are buying financials right now. Investors forget that financials are not like "regular" stocks. Beyond the macro picture, there is no thematic magic or catalyst that provides one with a favorable risk/reward in this environment except some short term gains or M&A from time to time. One must have a true understanding of financial institution operations, accounting, and how to assess leverage, regulatory compliance, and risk.

There was a time when you could make some real money buying small cap and midcap bank stocks in anticipation of M&A. That is certainly not the case now. Let's review what happened with Jefferies and Leucadia because we can learn a lot from this situation.

A couple of weeks ago, an investment firm headed by former U.S. Senator and New Jersey Governor Jon Corzine had, well, some issues. Corzine, a former head of Goldman Sachs, led the firm's efforts to become a trading powerhouse both for its own trading account as well as on behalf of clients.

Unfortunately, MF Global really F'd up. The Company recently filed for bankruptcy as it came to light that it owed billions in loans to banks after lousy bets on European sovereign debt. Seems it took some serious risk in not only the subject countries in Europe, but reportedly used a leverage ratio of 30:1. So, when the value of the bonds came crashing down, well, you get the story.

Now it seems that MF Global F'd its clients by allegedly commingling client assets with these principal trades, as a not-so inconsequential sum of money is missing. What a putz.

People want to talk about risk in low-priced, illiquid stocks? Buying debt isn't a riskless transaction and the level of risk can be exponential when arbitrage and leverage are involved.

What is maddening is that this is reminiscent of the demise of hedge fund Long Term Capital Management 12-13 years ago after it lost almost $5 billion in 4 months following the Russian financial crisis and debt default. This situation now reeks of plain stupidity, greed, and clear lack of oversight.

That brings us to Jefferies and Leucadia. Jefferies is an investment bank/brokerage/trading firm, with heavy roots in debt underwriting and trading, especially in junk bonds.

With MF Global as the first major U.S. firm to collapse due to the European financial crisis, investors sought out other problem children as well with which to sell, sell short, or avoid. Jefferies' debt was downgraded to junk (by a little known ratings agency) shortly after the MF Global mess, as it was disclosed that they had exposure as well.

What happened? Jefferies' stock traded sharply lower on huge volume and was actually halted twice after management issued 2 separate releases citing that it had very limited exposure. Since Leucadia owned 28% of Jefferies it got smacked too.

What do we take away from all of this?

On a global level, financials are linked, thus if something happens in one country, it can and will have a carryover effect with financial institutions here. On a basic level, time will tell what happens with Jefferies. Some believe management, some do not.

For better or for worse, I tend to believe management, but only time will tell if that credibility and belief is misplaced.

Regardless of the outcome, this scenario should be a reminder to monitor the large stakes public entities may hold in one another. Oftentimes, slow growth firms may find that their book value or major asset composition is dominated by these outside holdings. While it can provide the appearance that by investing in the holder, you are getting the holder's actual business for free, that works only if the investee company is doing well as the true value may yet be realized at some point. If the investee firm stumbles, the risk is like the Jefferies/Leucadia scenario.

It is also another example of how quickly risk is assessed across industries. Be sure you are aware of what type of businesses and strategies and investments in which your stocks may engage. Especially financials, where it can be more difficult to read between the lines.

With a mess here and there, and everywhere, financials still carry great risk, be they big money-center banks, mammoth global powerhouses, regionals, investment firms, etc.

If you do decide to venture here, use the Peter Lynch method and ensure you understand it and can describe the business in an elevator. I caution to stick with those firms that have "stuck to their knitting" and have little exposure to economically sensitive businesses.

Perhaps around year-end some of the risk will abate and we can discuss some ideas. For now, stay away and stick with stocks that are on the upside of the curve. For example….

Mimvi: Like Buying Google in 1998

Today we are introducing what may be the best opportunity we have come across in two years. Hands down. It's like buying Google in 1998. In our view, <u>it is a must-own stock that will be driven much higher in the coming weeks and later be acquired at a huge premium.</u>

The name of the Company is Mimvi, Inc. (OTCQB:MIMV) and it is considered the Google of Mobile Application (Mobile App) search engines. If you have a smartphone, then you how the Mobile Apps market is huge! Here are some Mimvi highlights:

Mimvi is the <u>ONLY</u> pure-play, publicly-traded Mobile App search entity and the only firm that offers Google-like search results with Amazon-like recommendations. Plus, Mimvi has the most comprehensive search and index results in the space and is one of only a few search engines that can be used across multiple mobile devices and platforms.

The Mobile App market is driving the Mobile search market, and the Mobile App market is booming, making Mimvi's search engine critical. Industry research suggests that the number of <u>Mobile App downloads will approach 100 billion in 2015 and research suggests that Mobile App download revenue will exceed $100B by 2017</u>.

Mimvi's estimated 2-year technology lead over the competition should result in multiple revenue streams in 2012.

Management has a history of success in search engine development and operation. The founder's previous search firm generated 250M searches and 50M monthly unique visitors.

Mimvi has just signed an LOI with First Wall Street Capital Corp. to assist it in raising $5M in financing.

Buying Mimvi stock in 2011 is akin to buying into a privately held Google in 1998. We liken this rare situation to buying Web search engine stocks in the mid-1990's that were later acquired for huge premiums and deem that Mimvi will emerge as *THE* M&A target in the next 12-18 months, as the business model is executed. <u>In the short term, all of the infrastructure is in place and the stock is set to soar in the coming weeks as major traffic comes on line and new products and financing are introduced before year-end.</u> Our $1.50 price target is based upon 30x FY13 our low-end net income estimate. We rate Mimvi Speculative Buy.

Until next week….

<u>Analyst: Robert Goldman</u>

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*.

<u>Analyst Certification</u>

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