Goldman SMALL CAP RESEARCH

The Goldman Guide

VOLUME 4 | ISSUE 6 | JUNE 9, 2013

INSIDE THIS ISSUE:

KEY TAKEAWAYS

- ⇒ *Millenials could have a huge impact on the future of small stocks in the coming ears*
- ⇒ *2Q13 earnings in trouble?*
- ⇒ *This sector could absolutely rock the house in 2H13*
- ⇒ *This stock could be a train wreck or a huge hit. Which one will it be?*

KEY STATISTICS

Index	Close	2013
DJIA	15248	15.4%
S&P 500	1643	14.4%
NASDAQ	3469	14.4%
Russell 2K	988	15.9%

(figures are rounded)

The Future of Small Stock Investors

This is the time of year when graduations and graduation parties are aplenty. It is also the time of year I try to squeeze insights regarding investing and investments out of parents, friends and family members. This year, I elected to take a completely different approach and gleaned some potentially dramatic information regarding the future of stocks. Most of my conversations were with the millennial generation (mostly children of baby boomers and the bulk of my target group were in their late 20's). Frankly, the takeaways were well, cool.

Work, let alone career paths with meaningful incomes remain hard to find, by and large. A fair number remain at home with parents with few contemplating buying homes. Car purchases and any kind of technology and high-end mobile devices are very important. Socialization in groups in restaurants and bars remain huge with few contemplating settling down. So, they buy cars devices and go out, with home-buying not really in the cards for a while. That bodes well for consumer stocks. Health care? A non-issue or important topic. (That's for old people.)

Most important, many view investing and saving with disdain and indifference, with some citing major losses by parents as reasons why they largely plan to do it themselves....down the road. Interestingly, their consumer spending is largely conducted via research online and through peer reviews, and it is likely that this will be the method they use collectively ad individually, going forward.

From what we gather, this demographic could embrace stocks over funds, versus their parents, but seek out index funds. Since they experienced with their own eyes the explosion of small firms into powerhouses, this group could gravitate toward small stocks to a greater degree than their predecessors, and marry it with index funds in a core and satellite approach.

If they can get older real fast, we can get some big $ into this space...lol.

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Keep An Eye On This

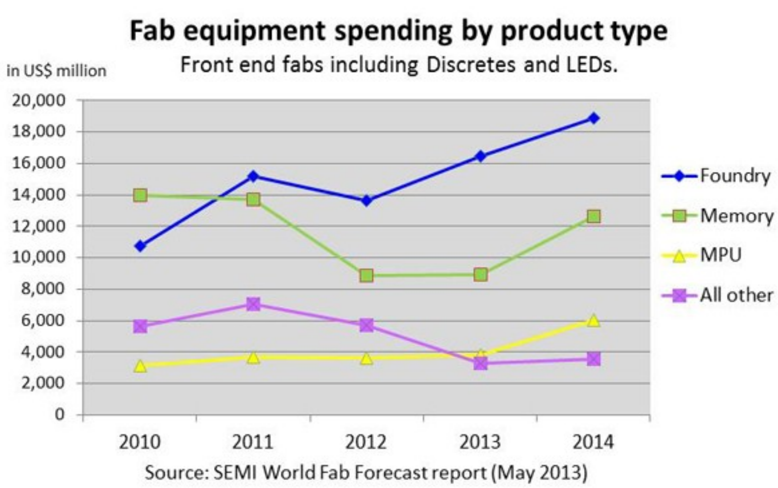
We are over three-fourths through 2Q13 and investors have high hopes not just for this period but especially the second half of 2013. Do not be surprised to see some negative earnings pre-announcements rear their ugly heads later this week and especially into next week. Remember to follow along as to why the shortfall is occurring and if it is a secular set of reasons other stocks could get hurt as well. If it is company-specific, other stocks will likely emerge relatively unscathed. The market is skittish as is, so the slightest bit of negative news could crush a stock. It is not unusual for 40-50% of revenue to be pushed through the next couple of weeks so this is the real turning point and a harbinger for 2H13 for many companies. Be wary, be cautious, and be quick to act.

<u>Could Semis Be The Place To Be?</u>

Semiconductor stocks haven't exactly set the world on fire and certainly have not reached the valuations and lofty growth since 2009 and 2010. Could this cyclical business be nearing a big turn? For the semiconductor capital equipment industry, We say yes, and here is why.

According to the latest forecast by industry group SEMI.org:

"Fab equipment spending will grow two percent year-over-year (US$ 32.5 billion) for 2013 and 23 to 27 percent in 2014 ($41 billion). The 2nd half of 2013 is expected to be much stronger with a 32 percent growth rate or $18.5 billion compared to 1st half of 2013 ($13.9 billion). The equipment spending increase in the second half is attributed to growing semiconductor demand and improving average selling price for chips. 2014 is expected to have 23 to 27 percent growth of $41 billion year-over-year (YoY), which would be an all-time record.



Demand keeps increasing such as media tables and smart phones, ASP for chips are expected to improve and many revenue predictions for 2013 are in the strong single digits. Overall, the scenario remains cautious but more optimistic than in prior forecasts."

Stocks tend to trade based on expectations four to six months out, so we could start to see moves even this summer, although it is more probable that the sector has a kick-ass fall season. With this in mind, expect us to profile a semi stock or two in the not too distant future.

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Like Volatile? You Will Love This

The following stock will either be a complete and total train wreck or a huge hit. Here is the story from 30,000 feet:

Orchard Supply Hardware Stores Corp. (NASDAQ – OSH - $3.03) operates 89 neighborhood hardware and garden stores in California. The 52-week high for the stock is $20.41 and the year low is $1.41, which was reached just six weeks ago. OSH is not for the faint of heart. Since its close of $2.37 on May 31st, the stock reached $4.60 only to drop to $2.31 and return to north of the $3.00 level---all in a matter of days.

From what we can gather, the Company has had horrific financial results in recent quarters, which has resulted in major losses due to restructuring and poor operating performance. Thus, a sell-off ensued which was exacerbated by short sellers selling short 25% of the thin public float of 3.8M shares.

For those that are chartists, we should note that the recent positive trading activity is likely a result of 2 things. First, after the stock collapsed a second time, a "cup" chart formation occurred, with buyers driving the shares higher on very heavy volume. Second, we believe some shorts elected to cover their positions which prompted an even greater rise. For example, earlier this week, the trading volume in one day was nearly equivalent to the public float.

Clearly, OSH is a tough call. The current market cap for the Company is a paltry $19M compared to its $600M annual revenue run-rate. Surely, despite the losses and terrible balance sheet with only $6M in cash, the company would be worth much greater than $19M in a sale? Obviously Home Depot (NYSE – HD) and Lowe's (NYSE – LOW) are hurting it but perhaps the stock is oversold, even after the run-up. If I were the Company's investment banker I would be gearing it up for sale on at least a break-up value basis given that there is real value in the large inventory level ($170M) and its property values likely offset much of the non-operating debt on its books. From this vantage point, a double from here would seem very reasonable.

However, given the schizophrenic nature of its trading activity and the thin float, the stock is fraught with trading risk let alone operating risk just in case management cannot right the ship. To highlight this, at midnight on Friday a story came out on Bloomberg citing sources that the Company could file for bankruptcy this week. The stock is off 26% in after-hours trading. Still, the Company is working on restructuring debt including covenants that expire on June 30.

Seems like it could be decent speculation along the way if you have ridiculous courage but Lord knows...it could get clobbered from jump street. What I do know is that this will not be boring.

Until next week...

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