Goldman SMALL CAP RESEARCH

The Goldman Guide

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Two Oversold Stocks

KEY TAKEAWAYS

⇒ *Year-end selling has commenced and is nearing a conclusion*

⇒ *This annual phenomenon creates oversold opportunities for mall cap and microcap stocks that tend to make big moves in late December and early January*

⇒ *There are hundreds of small caps down 50% or more year to date, especially in energy and biotech*

⇒ *Some oil and gas and tech stocks are already oversold and offer upside relative to EPS and/or revenue growth in 2015*

KEY STATISTICS

Index	Close	2014
DJIA	17959	8.3%
S&P 500	2075	12.2%
NASDAQ	4781	14.5%
Russell 2000	1182	1.5%

(figures are rounded)

The Next Big Winners

This is the time of year that sets apart the men from the boys. By the end of next week, the majority of year-end selling will have occurred. That means that the big losers of 2014 will reach or near their 52 week lows. With the exception of those stocks whose companies are likely closing their doors, thus taking the value effectively to zero, a year-end bounce in these names is right around the corner.

Nowhere is it more likely to occur (as it does every year) but in the small cap and microcap segment. With a YTD return of under 2% for the Russell 2000 Index as compared with the nearly 15% rise in the NASDAQ Composite, small stocks have lagged for much of the year. This year's losers stand a strong chance of becoming next year's winners, especially when taking into account the fact that inherent upside is likely greater with small stocks.

With this in mind, where does one go from here? A quick performance review illustrates that there are about 300 sub-$2 billion market cap stocks trading on NASDAQ or the NYSE that are down more than 50% for the year and currently trade below $10 per share. It is a great list in which to draw candidates, although I caution that there are some trends that could make it a bit difficult. The larger the market cap, the more likely that the stock is oil and gas heavy, for obvious reasons, and has analyst coverage. In the sub-$50M arena, there is a meaningful percentage of biotech stocks.

Both sectors contain risk for different reasons but could portend that they will also be strong industry performers next year. Since volume is higher and coverage exists, we have elected to profile 3 stocks in the slightly larger market cap segment of the small cap arena.

Two Oversold Stocks

It has been widely opined that oil and gas could see another 50% decline. It is certainly possible and would have a negative impact on stocks in the segment. Still, if ever there was a near term oversold group it might be this one. We caution that it might be too early to step in but you would be remiss if you didn't at least closely follow this gem.

Gastar Exploration Inc. (NASDAQ—GAST—$2.85) is an independent energy company engaged in the exploration, development and production of oil, condensate, natural gas and natural gas liquids in the United States. Gastar's principal business activities include the identification, acquisition, and subsequent exploration and development of oil and natural gas properties with an emphasis on unconventional reserves, such as shale resource plays and the company has had significant success of late. In Oklahoma, Gastar is developing the primarily oil-bearing reservoirs of the Hunton Limestone horizontal play and expects to test other prospective formations on the same acreage, including the Woodford Shale and the Meramec Shale (middle Mississippi Lime), which Gastar refers to as the Mid-Continent Stack Play. In West Virginia, Gastar is developing liquids-rich natural gas in the Marcellus Shale and has drilled its first successful dry gas Utica Shale/Point Pleasant well on its acreage.

The company is hitting on all cylinders, as evidenced by its recent releases and although 2015 financial guidance may have to be reduced to some degree, it appears to already be reflected in the stock price. For example, at current levels, the stock trades 69% below its 52-week high achieved in June. Yet, Wall Street expects revenue to rise by 33% next year and EPS to essentially double from $0.22 to $0.43. Moreover, the stock trades at a ridiculous 6.6x P/E on FY15E EPS. The current price is just a hair above the 52 week low and even though oil and gas stocks are woefully out of favor, this stock could be a big winner in late December/early January.

InterCloud Systems, Inc. (NASDAQ—$3.23) has some similarities with GST above. The stock trades 83% below its year-high and 10% above its 52 week low. As with GST, the Street estimates that revenue will jump by 33% next year and they have been awarded a series of new contracts of late, demonstrating strong top-line growth. Granted, EPS is on the decline to its aggressive growth stance, but even if Street EPS estimates of $0.41 are too high, we do not believe it would materially drop from the $0.41 projection. At current levels, this cloud and enterprise network virtualization provider trades under 8x FY15E EPS.

Interestingly, the stock trades at a big discount to other industry peers that have been smacked. **e2open, Inc. (NASDAQ—EOPN)** trades over 2x next year's revenue forecast while ICLD, which is forecast to grow revenue at a higher pace (albeit to a different market and audience) trades at a paltry .5x net year's revenue estimate. In our view, this is an example of why ICLD offers greater upside.

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