

# EQUITY RESEARCH

## Monthly Stock Monitor

August 3, 2007



### HIGHLIGHTS

Disney.....Lowered rating  
Dominion Resources.....Selling assets and buying stock/debt  
First Community Bancshares .....2Q07 earnings growth  
GlobalSCAPE.....Initiated coverage  
Massey Energy.....Earnings rebound  
PriceSmart, Inc.....Lowered rating  
Sirius Satellite Radio.....Good earnings report, awaiting merger approval  
Union Bankshares.....Lower earnings, but at nadir?

### COMMENTS AND UPDATES

#### Disney (DIS--\$33.90)

We lowered our rating on DIS from OUTPERFORM to NEUTRAL since the stock achieved our \$34/share price target established when we began coverage of this company in 2004 with its stock at \$26.27/share. Our \$34/share target price was based on new CEO, Robert Iger, turning around the company and improving DIS's operating cash flow, thus leading to higher earnings in subsequent years. Mr. Iger was successful in this objective evidenced by Disney's yearly earnings improvement since 2004. Given the recent appreciation in its stock, it appears most of the good news surrounding the turnaround at DIS begun 3 years ago is reflected currently in its share price. DIS reported 3Q07 earnings increased 14% to \$0.57/share versus \$0.53/share during 3Q06. Revenues on a quarter-to-quarter basis rose to \$9.05 billion from \$8.47 billion. Media Networks/Broadcasting revenues were higher at \$3.82 billion versus \$3.59 billion, while segment operating income increased to \$1.39 billion from \$1.11 billion. Broadcasting income rose due to fewer sports programming hours and strong international/domestic syndication sales of ABC Studio productions. Parks and Resorts revenues grew to \$2.90 billion from \$2.73 billion and income increased to \$621 million from \$549 million. Consumer Product revenues rose to \$549 million from \$445 million as operating income grew to \$118 million from \$105 million due to growth in earned royalties across multiple marketing lines. Studio revenues rose 4% to \$1.78 billion from \$1.71 billion. (SFM)

#### Dominion Resources (D--\$84.00)

It has been a busy period for Dominion Resources during the past few months. First, Chairman of the Board, Thomas E. Capps, retired and was succeeded in that position by current CEO/President, Thomas F. Farrell II. Second, the company began exiting its oil and gas exploration/production to focus on its core operations. The company sold its offshore Gulf of Mexico, Canadian, other onshore operations for approximately \$14 billion. D said it will use these proceeds to repurchase its common stock, reduce debt, and for general corporate purposes. To this end, the company

***For Important Disclosure information regarding the Firm's rating system, valuation methods and potential conflicts of interest, please refer page 4 of this report.***

707 East Main Street, 20th Floor ■ Richmond, Virginia 23219  
P.O. Box 1459 ■ Richmond, Virginia 23218-1459

804.643.2400 ■ 800.767.2424  
Fax: 804.343.3308

[www.AndersonStrudwick.com](http://www.AndersonStrudwick.com)

is conducting a \$55 million "Dutch Auction" of its common stock and repurchased \$2.5 billion of debt. D announced 2Q07 operating income of \$0.89/share compared to \$0.80/share during 2Q06. The improvement came from an increase in electric and natural gas utility sales due to warmer weather compared to last year's quarter. Also, the improved operating income was derived from increased results from its merchant generation/producer services businesses and higher prices from D's oil/natural gas units. These increases offset higher unrecovered Virginia fuel expenses, lower natural gas/oil production, increased DD&A expense from D's E&P units, and higher interest expense. During its 2Q07 earnings release D management gave 2008 profit guidance of \$6.00/share and annual 4-6% earnings growth in the following years. These shares are rated NEUTRAL. (SFM)

### **First Community Bancshares (FCBC--\$27.12)**

FCBC has been pro-active in dealing with the industry wide challenges of rising deposit costs and a slowing real estate market evidenced by its 2Q07 earnings report. The bank reported 2Q07 earnings of \$0.66/share versus \$0.64/share during 2Q06. The 2.2% improvement in earnings, on a quarter to quarter basis, was due to increased amounts of earning assets and lower operating expenses. Total interest income rose 6.5% to \$31.98 million from \$30.03 million due to higher interest earning assets. Total non-interest income increased to \$5.55 million from \$5.52 million. Total interest expense rose to \$15.0 million from \$11.9 million resulting from higher deposit funding costs. FCBC plans to open branches in Richmond VA, Mechanicsville VA, Daniels WV, Summersville WV, and a convenience center in Glade Springs WV. FCBC shares, like most bank stocks, have come under selling pressure due to industry wide concerns over sub prime loans market and a slowing real estate market. Given FCBC's lack of sub prime exposure, low price to book ratio of 1.5, and a 4% dividend yield these shares are recommended for growth/income investors. While the majority of Wall Street is negative on bank stocks, these shares offer upside potential when investors return to this currently out-of-favor industry. FCBC is rated OUTPERFORM. (SFM)

### **GlobalSCAPE (GSB--\$4.53)**

We recently initiated coverage of GSB with an OUTPERFORM rating. The stock appreciated 42% in 10 days after being listed on the AMEX. Profit taking followed and the stock has since settled to what we believe is an attractive entry point. GlobalSCAPE's file transfer products provide for the privacy of critical personal information such as medical records, financial data, customer files and other similar documents. In addition, these products provide for compliance with government regulations relating to the protection of information while allowing users to reduce IT costs, increase efficiency, track and audit transactions and automate processes. GSB's customer base includes individual consumers, small to medium-sized businesses, as well as some of the largest corporations in the world. The company has penetrated 94 of the Fortune 100 including: Mayo Clinic, Cleveland Clinic, Sentara, Citi, Experian, HSBC Holdings (HBC--\$91.42), Microsoft (MSFT--\$28.96), DELL (DELL--\$27.15), Circuit City (CC--\$11.13), XM Satellite Radio (XMSR--\$10.94), Gap (GPS--\$16.44), Dish Network (DISH--\$41.30), US Army, Lockheed Martin (LMT--\$99.37), Australian Government, SAIC (SAI--\$16.97), US Navy and Northrop Grumman (NOC--\$78.03). Based on the company's guidance of \$20 million in revenues for 2007 and plans of continued 40% internal growth, we believe the stock could appreciate to \$8 during the next 12 months, or 25X our \$0.33 taxed estimate for 2008. These shares are rated OUTPERFORM and are recommended for speculative/aggressive investors. (STT, Jr.)

### **Massey Energy (MEE--\$19.00)**

Massey Energy reported 2Q07 earnings of \$0.43/share vs \$0.04/share during 2Q06. The improved results came from higher produced coal revenues generated by a rise in prices on new supply contracts for 2007 and better overall product mix. Total revenues rose to \$617.8 million from \$556.1 million while EBITDA increased 55% to \$120.3 million from \$77.5 million. On a quarter-to-quarter comparison, produced coal revenues were \$516.2 million vs \$492.5 million and the price per ton rose to \$42.68 from \$41.92. On a per ton basis, the operating cash margin increased 36% to \$8.72 vs \$6.42. Metallurgical coal sales in tons sold increased 11% and revenues per ton rose 10%. MEE's work face situation stabilized during the current quarter as voluntary employee turnover rates decreased 15% during the 1H07 compared to 1H06. Legal hurdles remain for MEE as management announced its intention to appeal a recent jury decision in the Wheeling Pittsburgh Steel contract lawsuit. Additionally, MEE believes it can favorably resolve the EPA lawsuit against the company regarding alleging violations of the Clean Water Act. MEE's shares, as

have other coal companies, have come under selling pressure over concerns of rising operating costs. This could be a good entry point for MEE shares, trading at a multi-year low, for contrarian investors. Higher coal prices and lower operating costs could improve the company's overall profit margins and lead to an increase in earnings during the next 12-18 months. These shares are rated OUTPERFORM. (SFM)

### **PriceSmart Inc. (PSMT--\$22.25)**

Upon release of the company's 3Q07 earning announcement, we downgraded the stock to NEUTRAL based on valuation. The stock had run up nearly 50% in almost three months nearing our 12-month target of \$26. Should PSMT's stock decline further or, consolidate at current levels, we would consider revisiting the story. PriceSmart was spun off from Price Enterprises in 1997 at about \$18 after Price Company merged with Costco. The company owns and operates U.S.- style membership shopping warehouse clubs in Latin America and the Caribbean (the clubs are about half the square footage of a typical Costco warehouse). The model is identical to Costco's layout. High quality merchandise is sold at low prices, to both individuals and businesses. By offering low prices on brand name and private label merchandise, the warehouse clubs seek to generate sufficient sales volumes to operate profitably at relative low gross profit margins. PriceSmart operates 23 warehouse clubs in 11 countries and one U.S. territory. PriceSmart believes it is well positioned to profit from the growth in developing markets due to its purchasing power and the experience with membership warehouse clubs in these areas. (STT, Jr.)

### **Sirius Satellite Radio (SIRI--\$2.90)**

Sirius Satellite Radio reported better than expected 2Q07 earnings of (\$0.09)/share vs. (\$0.17)/share during 2Q06. The improvement was due to higher retail and automotive subscriber growth. SIRI added 561,493 subscribers during the past quarter bringing its total to 7.1 million. The bulk of these additions came from the automotive side which added 431,650 new subscribers. Revenue, on a quarter-to-quarter, rose 51% to \$226.4 million from \$150.1 million. Subscriber acquisition costs (SAC) declined to \$108 from \$131 during 2Q06. Going forward, SIRI management reaffirmed its 2007 guidance of \$1 billion in revenues, 8 million subscribers, and SAC approaching \$100. The primary story for SIRI is its agreement to merge with XM Satellite Radio (XMSR-\$10.94). XMSR has over 8 million subscribers and a merger with SIRI would give the combined entity over 15 million customers. The merger has generated a lot of controversy in Washington DC as the Department of Justice (DOJ) and Federal Communications Commission (FCC) must give approval for this deal to be completed. As a result, the final decision is likely to be determined by the lobbying efforts from the SIRI/XMSR group and the National Association of Broadcasters who are opposed to this merger. SIRI believes a final DOJ/FCC decision could occur during 12/07. Until this time SIRI's stock may trade sideways as investors await the decision on its merger with XMSR. Potentially, approval of the merger would be bullish for SIRI/XMSR, while a denial could put pressure on both stocks. SIRI is rated Outperform and recommended for aggressive/speculative investors. (SFM)

### **Union Bankshares (UBSH--\$19.40)**

UBSH reported 2Q07 earnings of \$0.42/share versus \$0.50/share during 2Q06. The decline came from higher interest expense, increased non-interest expense, and lower non-interest income, offsetting a rise in interest income. Interest expense rose 28% to \$15.9 million from \$12.4 million resulting from higher deposit costs. Non-interest expense increased 2.9% to \$17.7 million from \$17.2 million as UBSH opened 2 new branches, relocated 2 others, spent for infrastructure improvement, and moved into its new operations center. Total assets increased to \$2.2 billion from \$2.1 billion, loans grew to \$1.64 billion from \$1.51 billion, and deposits rose to \$1.65 billion from \$1.62 billion. Book value per share increased to \$15.28 from \$14.09. When comparing 2Q07 results to 2Q06 results, UBSH's earnings give investors little reason for excitement. However, on a sequential quarter basis, UBSH showed improvement in some of its operating ratios. 2Q07's net interest margin improved to 4.20% from 4.09% during 1Q07. Also, ROA rose to 1.06% from 1.00% and ROE increased to 11.07% from 10.38%. Potentially, this could be the nadir for UBSH's business if interest rates decline (lowering interest expense) and the real estate industry slowdown cause minimal problems for the banking industry's loan portfolios. UBSH's shares look inexpensive trading at 1.27x book value and paying a 3.6% dividend yield. UBSH is rated OUTPERFORM. (SFM)

Steven F. Marascia  
Research Analyst  
(804) 344-3806 / (800) 767-2424  
[smarascia@andersonstrudwick.com](mailto:smarascia@andersonstrudwick.com)

S. Taylor Tompkins, Jr.  
Institutional Sales and Research  
(804) 643-2400 / (800) 767-2424  
[ttompkins@andersonstrudwick.com](mailto:ttompkins@andersonstrudwick.com)

## Important Disclosures

Steve Marascia and Taylor Tompkins certify, with respect to the companies or securities that he analyzes, that (1) the views expressed in this report accurately reflect his personal views about all of the subject companies and securities and (2) no part of his compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

Anderson & Strudwick makes a market in First Community Bancshares.

Anderson & Strudwick makes a market in Union Bancshares.

Anderson & Strudwick makes a market in Sirius Satellite Radio.

Anderson & Strudwick makes a market in PriceSmart Inc.

Steve Marascia owns shares of Dominion Resources and Sirius Satellite Radio.

Taylor Tompkins owns shares of GlobalSCAPE Inc.

Anderson & Strudwick beneficially owns more than 1% of outstanding shares of Supertel Hospitality.

Stock ratings used in this report are defined as follows:

- (1) Outperform – The stock's total return including dividends is expected to exceed the industry or market average by at least 10% over the next twelve months.
- (2) Neutral – The stock's total return including dividends is expected to be in line with the industry or market average of +/- 10% over the next twelve months.
- (3) Underperform – The Stock's total return including dividends is expected to be below the industry or market average by 10% or more over the next twelve months.

The distribution of investment ratings for all companies in our coverage universe is as follows: (1) 46%, (2) 53%, (3) 1%

The distribution of investment ratings used for companies whom we have performed banking services in the last 12 months are: (1) 60%, (2) 40%, (3) 0%

For regulatory purposes, our ratings of Outperform, Neutral and Underperform most closely correspond to Buy, Hold and Sell, respectively.

## Other Disclosures

This report is not directed to, or intended for distribution to or use by any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject Anderson & Strudwick or its affiliates to any registration or licensing requirement within such jurisdiction.

The information presented in this report is provided to you for information purposes only and is not to be used or considered as an offer or the solicitation of an offer to sell or buy or subscribe for securities or other financial instruments. Anderson & Strudwick may not have taken any steps to ensure that the securities referred to in this report are suitable for any particular investor. Anderson & Strudwick will not treat recipients of this report as its customers by virtue of their receiving this report. The investments and services contained or referred to in this report may not be suitable for you and it is recommended that you consult an independent investment advisor if you are in doubt about such investments or investment services. Nothing in this report constitutes investment, legal, accounting or tax advice, or a representation that any investment or strategy is suitable or appropriate to your individual circumstances, or otherwise constitutes a personal recommendation to you. Anderson & Strudwick does not advise on the tax consequences of investments and you are advised to contact an independent tax advisor. Information and opinions presented in this report have been obtained or derived from sources believed by Anderson & Strudwick to be reliable, but Anderson & Strudwick makes no representation as to their accuracy or completeness. This report is not to be relied upon in substitution for the exercise of independent judgment. Anderson & Strudwick may have issued, and may in the future issue, other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. Information, opinions and estimates contained in this report reflect a judgment at its original date of publication by Anderson & Strudwick and are subject to change without notice. The price, value of and income from any of the securities mentioned in this report can fall as well as rise.

***For more information on this report, please contact us at 800-767-2424 or write to Anderson & Strudwick 707 E. Main Street 20<sup>th</sup> Floor, Richmond, VA 23219.***