

McIntire Investment Institute

At the University of Virginia



Long Pitch: GeoEye Inc. (NASDAQ: GEOY)

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Business Overview I

- A. Dulles, VA-based company that operates satellites, mapping aircraft, and a network of ground stations that provide aerial and geospatial imagery to the US Government, Google, and commercial enterprises.
- B. Satellites
 - I. OrbView-2
 - I. Fully depreciated; 12 years old but still operational
 - II. Ikonos
 - I. Fully depreciated; expected to remain operational through 2010
 - III. GeoEye-2
 - I. Optical equipment has been ordered from ITT
 - II. Scheduled for launch in 2010

Business Overview II

A. GeoEye-1

- I. Expected cost of \$502 million, of which \$466.5 has been expended
- II. Will provide the world's highest resolution, most accurate commercial satellite imagery in either color or black and white
 - I. This is a significant competitive advantage
- III. Launched on 9/6/08 and has a design life of seven years, with fuel for two more; will orbit the Earth 15 times a day
- IV. It was not fully operational for five months after launch due to calibration and software problems
- V. GEOY announced on 2/5/09 that performance objectives were met and images were submitted to the NGA for approval



Business Overview III

The following image was taken 423 miles above Washington D.C. by GeoEye-1



<http://venturebeat.com/2009/01/20/pictures-president-obamas-inauguration-as-seen-from-space/>



Stock Overview

- 52-week range: \$14.75 to \$35.14
- 2/9 Close: \$19.77 (down 8.43% on the day)
- Market Capitalization: 361.6M
- P/E: 10.69
- % of Float Short: 15.05
- ROE: 18.20%
- Insider Action: 9,000 shares sold in early December and 14,250 shares bought from Dec. 19 to Dec. 22
- Farallon and Deephaven each own nearly 5% stakes
- Q4 08 revenue to be released 3/9; analyst estimate range is -\$0.10 to \$0.06



52-Week Stock Chart



Thesis Points

A. Business Model

B. Strong Financials

C. Industry Trends

Business Model I

A. Relationship with US Gov.

I. Special Status

- I. In March 2003 the National Geospatial Intelligence Agency (NGA) began supporting the commercial satellite imagery industry by sharing engineering, construction, and launch costs of satellites
- II. This program is meant to ensure that the NGA has access to commercial satellite images to support intelligence gathering
- III. Because of its financial support, NGA has priority in ordering images from GEOY's satellites

II. Service Level Agreement (SLA)

- I. GEOY is negotiating a SLA with the NGA. Once GeoEye-1 images are approved by the NGA, a SLA worth \$12.5 million per month for the next year will be completed.
- II. Previously GEOY had a pay-by-image arrangement with the NGA



Business Model II

A. US Government, Cont.

- I. The government has supported the construction of GeoEye-1 with \$237 in research funding
- II. The government accounts for 40-50% of GEOY's revenue depending on the quarter
- III. The federal government guarantees to purchase GEOY images if its satellites meet NGA requirements
- IV. Satellite imagery is a cheap way to gain intelligence
- V. The government desires commercial satellite companies that can supplement its military hardware
 - I. Additionally, the commercial sector aids innovation



Business Model III

A. Relationship with Google

I. Contract

- I. In September 2008, Google signed an exclusive deal with GeoEye to gain access to its images for use on Google Earth and Google Maps
 - I. Google Earth 5.0 was recently released
- II. Google has begun experimenting with advertisements on Google Maps and Google Earth
 - I. As potential revenue sources, these features are more important for Google's strategy and will indirectly benefit GeoEye
 - II. GeoEye-1 images could greatly enhance Google Earth and draw more users



Strong Financials I

A. Financial Position

- I. Quick Ratio of 1.45
- II. Total Debt/Total Capital Ratio of 51.90%
- III. Despite large expenditures for the final construction and launch of GeoEye-1, GEOY has a strong financial position
- IV. According to recent SEC statements, GEOY has \$146,066,000 in cash and cash equivalents, current liabilities of \$134,104,000, and long-term debt of \$247,324,000



Strong Financials II

A. Profit Margins

- I. GEOY has high fixed costs (satellite construction and launch expenses) but very low marginal costs
- II. Although it relies on the US government for a plurality of revenues, GeoEye has strong pricing power and favorable profit margins
- III. Margins:
 - I. Gross Profit Margin of 48.66%
 - II. Net Profit Margin of 24.73%



Industry Trends I

A. Barriers to Entry

I. Difficulties designing and launching a satellite

I. Cost considerations (GeoEye-1 cost \$500+ million)

II. Technological barriers

III. Difficulties raising venture capital in this environment

IV. US government has shown no desire to establish another commercial satellite operator

II. Government Export Restrictions

I. Due to national security concerns, the US government places strict restrictions on the export of satellite hardware and software. This impedes foreign competition from developing.



Industry Trends II

A. Lack of Competitors

I. GeoEye's main US competitor is DigitalGlobe, which also contracts with NGA and sells images to commercial users

II. Image Comparison

I. http://www.digitalglobe.com/downloads/DG_2009_P_residential_Inauguration.pdf

II. <http://news.cnet.com/photos-obama-inauguration-viewed-from-space/>



Industry Trends III

A. Emerging Opportunities

I. Obama Inauguration

II. Commercial Applications

I. GeoEye images will be used in Tom Clancy's upcoming HAWX air combat video game

II. Commercial fishers, miners, oil and gas drillers could all use geospatial imagery to assist them in exploration

III. Search and Rescue Missions

I. GeoEye imagery used to locate the Sirius Star

II. Also used to find wreckage of Steve Fossett's plane



Value Added Research (VAR)

- I. Robert E. Lindberg, Research Professor, National Institute of Aerospace
- II. James C. McDaniel, UVa Engineering Professor
- III. Christopher P. Goyne, Director, UVa Aerospace Research Laboratory
- IV. Jason Bates, Editor, *Satellite Today*
- V. Video Game Designer

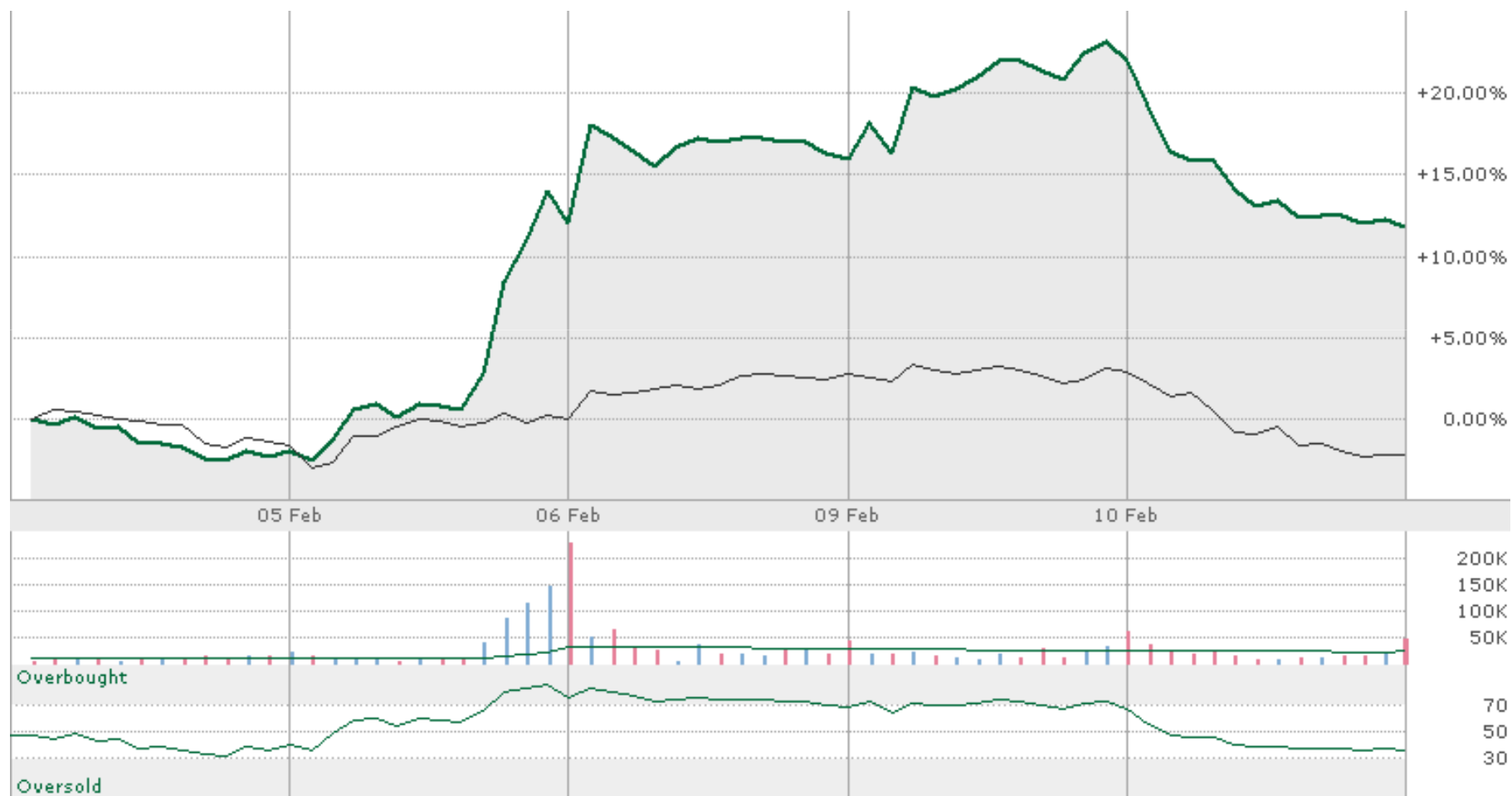


Catalysts

- I. NGA certification granted
 - I. NGA has invested over \$225 million on satellite
 - II. satellite images are operational and examples have been shown
 - III. NGA issued a press release titled “NGA Celebrates Successful Launch of GeoEye-1” on 9/8/08 and posted a link to the 2/5/09 article in which GeoEye announced it submitted images for NGA approval
- II. Possible short squeeze
- III. Acquisition by Google
- IV. Higher quarterly revenue year-over-year



Five Day Stock Chart



Risks

- I. GeoEye-1 imagery does not gain NGA certification
- II. A satellite has irreparable technical problems, leaves orbit, etc.
- III. Higher 2009 earnings expectations
- IV. New CFO and past accounting problems
- V. Connection with Google and MII portfolio risk



Summary

- Recommendation:
 - If we are willing to take on the risk, do a scaled (2.5% buy in) immediately followed by additional 2.5% buy in if GeoEye-1 images gain NGA approval
 - If we feel the GeoEye-1 situation is too risky, wait and see how it develops. If the satellite's imagery gains NGA approval, purchase a 5% stake in GEOY
- Disclosure: The analyst is long GEOY in his personal account

