



The Silver Word

EmergingGrowth.com, Inc.
The Satellite Radio Industry

What is Satellite Radio?

If you are one of the twenty-five million die-hard listeners of Howard Stern, then you are well aware that he has been threatening to call it quits to enter the world of satellite radio. For most of us fans, this is an enormous let down, however situations such as this, prompt immediate interest in this new medium.

Satellite Radio is a subscriber based radio service that is broadcast directly from satellites. Subscribers are able to receive up to 100 radio channels featuring compact disk digital quality music, news, weather, sports or talk radio. Satellite radio is not limited by the geographic boundaries that govern regular radio stations. With the potential to reach people across the country, even channels of relatively narrow interest can be expected to attract a large enough audience to justify their existence.

In 1992, the FCC allocated a portion of the "S" band for nationwide radio broadcast in the US of satellite based Digital Audio Radio Service and in 1997, the FCC awarded 8-year radio broadcast licenses to two companies, Sirius Satellite Radio Inc. ("Sirius") and XM Satellite Radio ("XM") and satellite radio became available in 2001.

To receive satellite radio broadcasts, one must subscribe by paying a monthly fee and purchasing a radio receiver or an adapter for an existing radio that is capable of receiving the Sirius or XM satellite broadcast. One can subscribe through thousands of different national, regional and local retail stores, over the Internet, or through automobile dealers. Since Sirius and XM have developed slightly different technologies, one needs only to purchase a radio capable of receiving satellite broadcasts from one company or the other, but not both; however, Sirius and XM have agreed to develop a unified standard for satellite

radios. This "second generation" satellite radio will allow a single radio to receive broadcasts from either company.¹

Industry Outlook

While the ultimate size of this market is difficult to predict, it is likely that twenty million U.S. consumers - the same number currently subscribing to satellite television - might subscribe to a satellite radio service. This estimate might be conservative, considering that the majority of radio listening is done in the car, and there are 200 million registered automobiles in the United States.

Long term success is tentative at this point. There is a lot of uncertainty about how quickly consumers will adopt to this new technology. Even more uncertain is how much it will cost Sirius and XM to convert radio listeners to satellite technology. In addition, the facts that a digital alternative to satellite already exists and that local FM radio operators plan to broadcast digitally do not bode well for the industry.

Although sharp growth has been reflected in the dramatic increase in subscribers for both Sirius and XM, neither company is currently profitable. Both Sirius and XM skirted with financial disaster in 2002, as funding nearly ran out before enough subscribers could be signed on to meet expenses. With minimal differentiation between the two services, customer-acquisition costs may remain high for many years.

XM and Sirius are employing similar strategies to attract subscribers. Both emphasize that they offer channels that are unavailable on the traditional AM and FM bands. XM and Sirius have different approaches to dealing with commercials, as some XM music channels are commercial free, while none of Sirius' music channels have commercial interruptions. But avoiding advertising entirely comes at a price for subscribers: Sirius's monthly charge is \$12.95 and XM's fee is \$9.95.

Both companies have relationships with virtually all the major automakers that call for dozens of car models to come equipped with factory or dealer-installed satellite radio receivers. The idea is that the cost of a satellite receiver can be rolled into a vehicle's price. Most subscribers thus far have acquired their satellite radios in the aftermarket, either for their vehicles or to use at home.

¹ <http://www.digitalaudioguide.com/faq/satellite/faq.htm>
<http://www.howstuffworks.com/satellite-radio.htm>

Clearly, satellite radio is attractive to investors since stock in Sirius and XM is up considerably this year, although both companies lost most of their market value when the technology bubble burst and remain well below all-time highs.²

The Facts on Sirius

Launched on July 1, 2002, Sirius provides listeners with over 120 channels of commercial-free music, sports, information and entertainment with digital quality sound, broadcast daily from New York City, Los Angeles, Nashville, New Orleans, Houston and Daytona. Sirius offers 65 channels of 100% commercial-free music, featuring multiple categories of pop, rock, country, hip-hop, R&B, dance, jazz, classical and Latin music, along with more than 50 channels of world-class sports, news, talk entertainment, traffic and weather. Sirius also broadcasts live play-by-play games of the NHL and is the official satellite radio partner of the NFL.

Sirius-Ready receivers are manufactured to meet the needs of all subscribers, and come in versions for cars, trucks, recreational vehicles, boats, aircraft, offices and stores. The company's exclusive automotive partners are DaimlerChrysler, Ford Motor Company and BMW, which represent over 40% of new cars and light trucks sold annually in the US. In 2004, Sirius radios are expected to be available in over 80 different car models.

The Company's primary source of revenue is subscription fees but also derives revenue from activation fees, the sale of advertising on its non-music channels and the direct sale of Sirius radios. As of June 30, 2004, Sirius had 480,341 subscribers. This was a record for the company with net additions of 37% or 128,678 subscribers during the second quarter of this year. The company reaffirms its forecast of one million subscribers by year-end. For the second quarter of 2004, average monthly revenue per subscriber was \$10.54, reflecting an increase of 33% from the year ago quarter of \$7.91 and a 6% increase over the previous quarter at \$9.92.

Sirius recognized second quarter 2004 revenue of \$13.2 million, compared to \$2.1 million for the year ago quarter. Sirius reported a loss \$137 million, or a loss of \$0.11 per share, compared to a loss from operations of \$112 million or a loss of \$0.12 per share for the second quarter of 2003. Compared to the previous quarter, revenues were 42% higher, while earnings were relatively flat at a loss of \$0.12 per share. Sirius maintains a strong cash position, ending the second quarter with \$640 million in cash, cash equivalents, and marketable securities.

²http://www.space.com/business/technology/satcom_radio_industry_031112.html

Interest in the stock is heating up on Wall Street, as it is currently covered by twenty-seven brokerage houses and in 2004, the following seven firms initiated coverage: Banc of America Securities, William Blair, Fulcrum, Legg Mason, Wachovia, JP Morgan and IRG Research.

Investment Outlook

Buying into Sirius is a purely speculative investment strategy. Sirius must overcome numerous obstacles before its business model is proved successful. First, it remains uncertain is how much it will cost Sirius to convert radio listeners to satellite and persuade satellite listeners to choose it over XM. Despite spending hundreds of million of dollars for advertising and marketing, Sirius had 1.6 million fewer subscribers than XM at the end of the second quarter this year. Second, due to technical problems, Sirius was delayed in launching its service and in order to catch up, Sirius will need to make its service more appealing than its competitor. Suffice to say, the company's competition with XM is fierce, and there's no guarantee that both companies will survive over the long run. Third, Sirius is a young company with a very high sales growth rate but the company doesn't have earnings. However, if Sirius perpetually trails XM in subscribers, the total economic pie may be large enough to satisfy both satellite radio operators.

Company: Sirius Satellite Radio Inc.								
Symbol:	NASDAQ: SIRI							
Price (As of 8/6/04):	\$2.33							
52-Week Range:	\$1.40 - \$4.20							
Market Cap: (B)	\$2.89							
Shares Out. (M):	1,240							
Avg. Daily Volume:	35,052,363							
FINANCIALS								
(In \$ Thousands)								
	2003	2002	1Q03	2Q03	3Q03	4Q03	1Q04	2Q04
Revenues	\$12,872	\$805	\$1,591	\$2,073	\$4,258	\$4,950	\$9,291	\$13,230
Total Expenses	\$450,402	\$313,932	\$100,719	\$111,871	\$107,745	\$130,067	\$128,799	\$146,215
Operating Loss	(\$437,530)	(\$313,127)	(\$99,128)	(\$109,798)	(\$103,487)	(\$125,117)	(\$119,508)	(\$132,985)
Realized Gains/Losses	\$168,330	(\$54,433)	\$168,330	\$0	\$0	\$0	(\$2,521)	(\$489)
Interest	(\$45,223)	(\$100,906)	(\$17,322)	(\$2,038)	(\$3,202)	(\$22,661)	(\$22,030)	(\$3,323)
Net Income	(\$314,423)	(\$468,466)	\$51,880	(\$111,836)	(\$106,689)	(\$147,778)	(\$144,059)	(\$136,797)
Weighted Avg. Shares (M)	827,186.0	76,394.0	327.8	931.7	998.2	1,041.4	1,217,608.0	1,235,920.0
EPS	(\$0.38)	(\$6.13)	\$0.16	(\$0.12)	(\$0.11)	(\$0.14)	(\$0.12)	(\$0.11)
Cash & Cash Equivalents	\$520,979	\$18,375	\$254,180	\$554,535	\$450,508	\$520,979	\$701,056	\$639,599
Total Assets	\$1,617,317	\$1,340,940	\$1,420,985	\$1,660,830	\$1,568,301	\$1,617,317	\$1,887,019	\$1,800,871
Long-term Debt	\$194,803	\$670,357	\$58,205	\$259,570	\$259,686	\$194,803	\$425,920	\$426,037
Total Liabilities	\$292,123	\$772,941	\$117,744	\$324,855	\$336,705	\$292,123	\$538,402	\$573,525
Stockholders' Equity	\$1,325,194	\$567,999	\$1,303,241	\$1,335,975	\$1,231,596	\$1,325,194	\$1,348,617	\$1,227,346
Long-term Debt/Equity	15%	118%	4%	19%	21%	15%	32%	35%
Total Subscribers	261,061	29,947	68,059	105,186	149,612	261,061	351,663	480,341
Revenue per Subscriber	\$9.39	\$7.47	\$10.94	\$7.91	\$11.20	\$8.50	\$9.92	\$10.54

Source: SEC Filings, Company Earnings Releases

The Facts on XM

Launched on September 25, 2001, XM transmits over 120 nationwide radio channels of music, news, talk, sports and children's programming. XM's ESPN Radio channel includes play-by-play NBA and Major League Baseball games, including the all-star games, playoffs, championships and World Series.

XM's powerful strategic and equity partners are leaders in their respective industries: General Motors, Honda Motors, Clear Channel, Pioneer, Alpine, Sony, and electronics retailers such as Walmart, Best Buy, Circuit City, Sears and Radio Shack. These alliances favorably position XM Radio within the reach of millions of consumers.

The XM Radio system is capable of providing high-quality satellite services to XM radios in automobiles, trucks and recreation vehicles as well as to fixed or portable XM radios in the home, or office. The company transmits XM content throughout the continental United States to vehicle, portable, home and plug-and-play radios.

In August of this year, XM announced that they have entered into an exclusive, multi-year strategic marketing alliance with Starbucks Coffee Company. As part of the agreement, the "Starbucks Hear Music" channel, featuring music programming from Hear Music, the voice of music at Starbucks, will debut this fall for XM Radio's subscribers. In addition, in 2005 millions of Starbucks customers will be able to listen to the "Starbucks Hear Music" channel programming and be exposed to XM in more than 4,000 Starbucks locations nationwide. In October XM will feature Opie & Anthony in the morning and afternoon drive times on both coasts. This is an extremely popular and controversial show targeted for the male age 18-49 audience.

XM announced that it finished the second quarter of 2004 with more than 2.1 million subscribers. XM added more than 25%, or 418,000 new subscribers in the quarter. As a result of this significant subscriber growth, and an improving outlook for both the retail aftermarket and new car business in the second half of the year, XM is increasing year-end 2004 subscriber guidance from 2.8 million subscribers to 3.1 million subscribers. For the second quarter of 2004, average monthly revenue per subscriber was \$9.40, reflecting a decrease of 11% from the year ago quarter of \$10.60 but a 9% gain over the previous quarter at \$8.66.

For second quarter of 2004, XM reported quarterly revenues of \$53 million, nearly tripling the \$18.3 million reported in the second quarter 2003 and represented a 23% increase over the first quarter 2004. XM reported a loss of \$168 million or earnings loss of \$0.84 per share for the second quarter 2004, compared to a loss of \$165 million and an earnings loss of \$1.38 per share for the second quarter 2003. This was still an improvement over the first quarter with net income at a loss of \$173 million and earnings loss of \$0.96 per share.

At the end of the second quarter 2004, XM had total cash and short-term investments of \$377 million and capacity under the Revolving Credit and Equity Facilities from GM of \$126 million. XM updated 2004 revenue guidance to \$220

million and an EBITDA loss of \$300 million. XM continues to maintain its leadership position with an 81% market share. The stock is currently covered by 28 brokers with the following eight firms initiating coverage this year: Banc of America Securities, William Blair, Fulcrum, Legg Mason, Barrington Research, Wachovia, JP Morgan, IRG Research.

Investment Outlook

XM has spent the past few years investing in the infrastructure necessary to operate its business. The company is focused on adding as many subscribers as possible through extensive marketing and strategic alliances. Relationships with automotive companies are important to subscriber growth and XM has the biggest automaker, General Motors, signed up through 2012. Thanks to its large equity stake and profit-sharing, General Motors has been a very motivated partner. Growth is expected to continue although XM has still not made a profit, as it continues to burn through cash.

Company: XM Satellite Radio Holdings							
Symbol:	NASDAQ: XMSR						
Price (As of 8/6/04):	\$24.43						
52-Week Range:	\$10.02 - \$30.96						
Market Cap: (B)	\$4.69						
Shares Out. (M):	191.8						
Avg. Daily Volume:	4,406,715						
FINANCIALS							
(In \$ Thousands)							
	2003	2002	1Q03	2Q03	3Q03	4Q03	1Q04
Revenues	\$91,781	\$20,181	\$13,052	\$18,321	\$26,913	\$33,495	\$42,965
Total Expenses	\$546,239	\$458,961	\$119,822	\$135,151	\$126,988	\$164,278	\$160,815
Operating Loss	(\$454,458)	(\$438,780)	(\$106,770)	(\$116,830)	(\$100,075)	(\$130,783)	(\$117,850)
Realized Gains/Losses	(\$43,139)	(\$18,629)	\$5,553	(\$21,458)	(\$15,986)	(\$11,248)	(\$27,542)
Interest	(\$107,283)	(\$58,462)	(\$23,247)	(\$26,316)	(\$29,556)	(\$28,164)	(\$27,042)
Net Income	(\$604,880)	(\$515,871)	(\$124,464)	(\$164,604)	(\$145,617)	(\$170,195)	(\$172,434)
Weighted Avg. Shares (M)	125.2	86.7	98.7	119.4	129.7	152	178.9
EPS	(\$4.83)	(\$5.95)	(\$1.26)	(\$1.38)	(\$1.12)	(\$1.12)	(\$0.96)
Cash & Cash Equivalents	\$418,307	\$32,818	\$418,307	\$345,868	\$456,632	\$418,307	\$385,191
Total Assets	\$1,526,782	\$1,160,280	\$1,526,782	\$1,493,142	\$1,591,787	\$1,526,782	\$1,567,744
Long-term Debt	\$601,363	\$412,540	\$567,606	\$621,805	\$639,299	\$601,363	\$567,606
Total Liabilities	\$993,894	\$567,969	\$993,894	\$873,961	\$939,718	\$993,894	\$950,466
Stockholders' Equity	\$532,888	\$592,311	\$532,888	\$619,181	\$652,069	\$532,888	\$617,278
Long-term Debt/Equity	113%	70%	107%	98%	113%	113%	92%
Total Subscribers	1,360,228	3,472	483,075	692,253	929,648	1,360,228	1,681,903
Revenue per Subscriber	\$10.52	\$11.64	\$9.34	\$10.60	\$8.84	\$10.12	\$8.66

Source: SEC Filings, Company Earnings Releases