Research Note

April 27, 2007

Price (as of close 4/26/07)
$11.78

Rating
HOLD

12- Month Target Price
$14

William Kidd
(213) 688-6698
william.kidd@wedbush.com

Jung Hwang, CPA
(213) 688-4557
jung.hwang@wedbush.com

XM Satellite Radio (XMSR)

Q1 Results Meet Lowered Expectations

52-Week Range	$9.63 - 23.56	Market Capitalization	$3.8 billion
Shares Outstanding	337.8 million	Enterprise Value	$5.2 billion
Insider/Institutional	20% / 91%	Debt	$1.3 billion
Public Float	242.1 million	EBITDA	$(450.4) million
Short Interest	31.2 million	Subscribers	7.6 million

FYE DEC	2006A	2007E		2008E	
EPS($)	ACTUAL	CURRENT	PREVIOUS	CURRENT	PREVIOUS
Q1 Mar	$(0.60)	$(0.40)A		$(0.31)E	$(0.30)E
Q2 Jun	(0.87)	(0.47)E	(0.47)E	(0.21)E	(0.22)E
Q3 Sep	(0.32)	(0.41)E	(0.39)E	(0.11)E	(0.11)E
Q4 Dec	(0.90)	(0.57)E	(0.54)E	(0.20)E	(0.18)E
Year*	**$(2.70)**	**$(1.85)E**	**$(1.83)E**	**$(0.83)E**	**$(0.81)E**
P/E Ratio	N/A	N/A	N/A	N/A	N/A
Change					

FYE DEC	2006A	2007E		2008E	
Revenue ($ mil.)	ACTUAL	CURRENT	PREVIOUS	CURRENT	PREVIOUS
Q1 Mar	$208.0	$264.1A		$322.6E	$329.3E
Q2 Jun	227.9	270.4E	274.9E	353.6E	355.0E
Q3 Sep	240.4	280.6E	287.1E	377.6E	381.3E
Q4 Dec	257.1	293.8E	301.2E	402.9E	406.2E
Year*	**$933.4**	**$1,108.9E**	**$1,126.4E**	**$1,456.7E**	**$1,471.7E**
Change	67%	19%	21%	31%	31%

** Numbers may not add up due to rounding.*

Company Description

XM Satellite Radio was incorporated in 1992 and is based in Washington, D.C. The company operates in a duopoly, as one of two FCC licensed providers of satellite radio. Its service offers over 140 channels of commercial free music and talk channels on a coast-to-coast basis for $12 95 per month

- **Q1 results in line with low expectations as retail softness continues from last year.** Subscriber growth, still considered the most important bogey for satellite radio companies, was spot on, with the company adding 285k subscribers (vs. 569k in 1Q06), consistent with our ~294k net adds estimate. Buried in subscriber figures was the quarter's biggest positive—XM started to win back retail market (roughly 5-10 points in some months), which we believe is reflective of both XM's commitment to win back lost ground (e.g., higher SAC) as well as a diminished Howard Stern effect. XM reported EPS of ($0.40), in line with our ($0.44) estimate and the ($0.39) consensus estimate. The loss narrowed considerably from last year, as fewer gross additions (865k in 1Q07 vs. ~1mn 1Q06) accounted for much of the improvement.
- **XM's subscriber results should generally improve from Q1 levels throughout most of the year.** OEM sales continue to build sequentially while the severity of the retail hit softens and the company approaches easier comparisons. Secondly, skepticism regarding the merger's likelihood is already well priced in, making that a moot issue, at least relative to present price levels.
- **With guidance, sometimes no change is good news.** XM management did not change any of its subscriber guidance, but did augment its expectations for CPGA (e.g., SAC) and its adjusted operating loss. Although we consider the amended guidance (e.g., higher SAC, $4-14mn higher operating loss) to be a small incremental negative, we think the market was more relieved to see XM maintain its year-end subscriber range. Even so, we think the year-end subscriber guidance looks implausible on the high end and reasonable on the low end.
- **Minor model revisions shave a dollar off our price target.** We are lowering our price target from $15 to $14 due mostly to modest ARPU assumption changes to our DCF model, specifically around advertising revenue.
- **We still favor Sirius given its competitive strengths and our perception that the proposed merger's approval is unlikely.** The advantage XM seems to have at the moment is that success, such as its market share gains, is relatively unexpected, making it easy to exceed low expectations. However, if one were more optimistic than us about the merger's likelihood of achieving regulatory approval, we could see how the optionality that the merger creates could make XM an extremely interesting holding.

Media

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- Risks to attainment of our share price target include shortfalls in subscriber growth; increased competition whether from XM; AM/FM radio, HD Radio, or streaming-media services; new/increased government regulation; a prolonged and/or failed merger attempt; an inability to renew key content and OEM contracts; satellite anomalies; and an unfavorable outcome in the ongoing arbitration process with record labels over royalty rates.

ANALYSIS

Don't Expect Retail Subscriber Shortcomings to Overshadow 2007

In Q1, gross additions fell to 868k from 1,017k last year, as the modest pickup in OEM gross adds was insufficient to offset the roughly 36% decline in retail gross additions. We think the biggest challenge satellite radio is facing is competition from digital television sets and to a lesser extent iPods. The reality is that consumer dollars are finite and they cannot buy every product available in a given month or quarter. And for the moment, digital television sets, whether flat or projected, seem to be what is most on consumer minds. Also, 1Q06 was Howard Stern's first quarter at Sirius, which created a lot of one-time demand, even if most of that incremental demand favored Sirius. Thus, the comparisons for the category are a bit distorted as a result. Having said that, when retail sales first started to soften, which we believe was near the end of summer 2006, the market was able to dismiss some of the weakness because of an FCC-driven recall on select satellite radio devices occurring at the time. The FCC had been scrutinizing various aftermarket satellite radio devices for interference, causing some units to be fixed/adjusted and thus negatively affecting retail inventories. Naturally, both companies tuned down marketing during the issue, also contributing to the weaker showing.

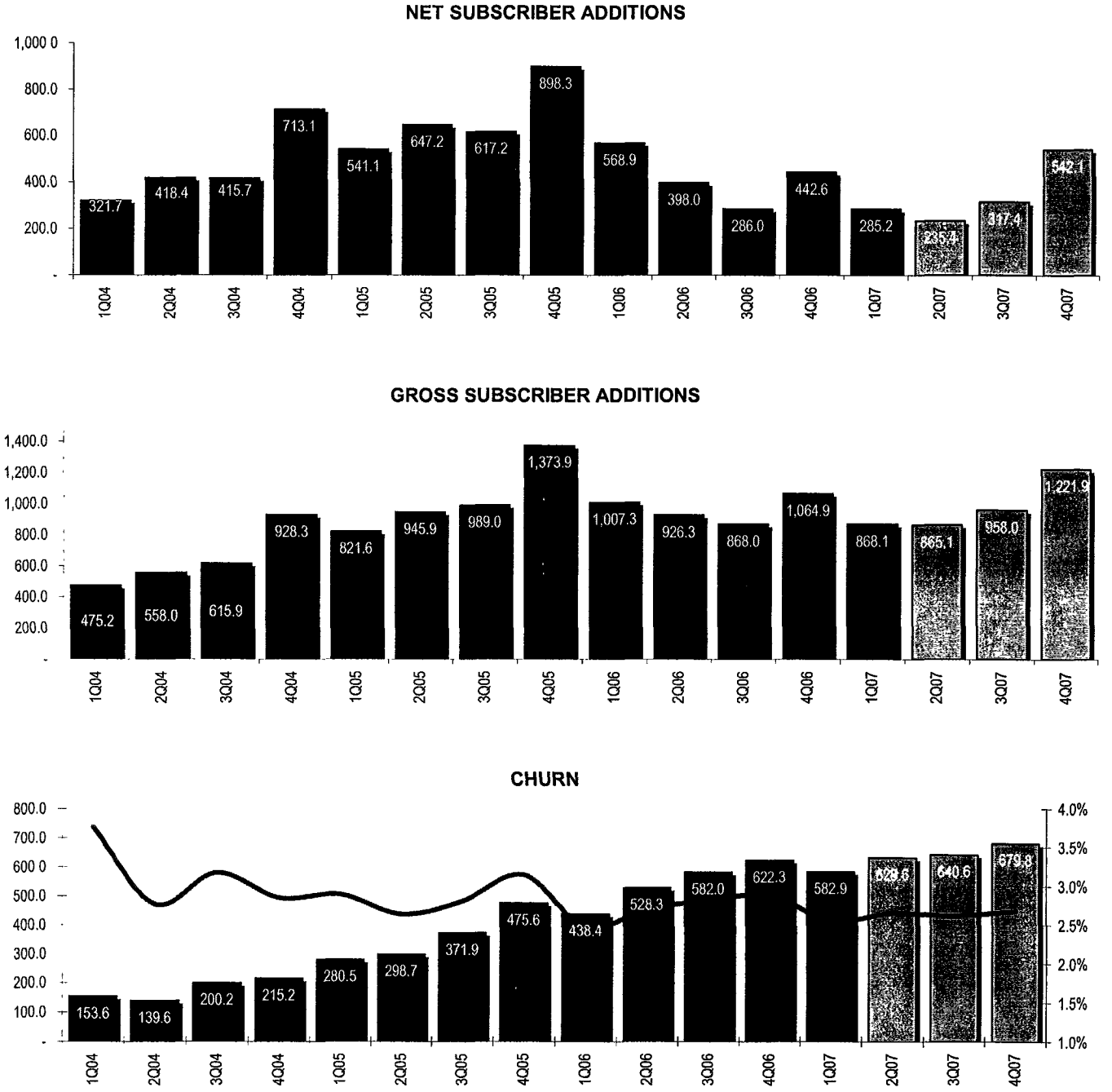
We made channel checks following the 1Q07 and learned that both companies were vigilant with retailers in terms of educating them about the merger in order to prevent consumer confusion. We also confirmed that both companies did not have much in the way of new receivers on retail shelves, which was a negative. The slight positive was that what was available was older and typically quite affordable.

Looking forward over the next couple quarters, we expect the magnitude of the retail losses to lessen, particularly as we near summer, since the comparisons with last year will get considerably easier. XM will also benefit from the fact that its 2006 market levels, particularly in the second half, were anemic, which will also likely contribute to an easier 2007 comparison. However, the real story for XM and satellite radio in general should not continue to be retail apathy. Rather, improving OEM demand should be the focus, since ultimately, satellite radio needs strong OEM commitment to reach a level of success sufficient to justify even higher share prices.

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Figure 1. XM Subscriber Growth and Churn Trends

($000's)



Note: Projected figures are shaded lightly.
Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
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Guidance: ***what was affirmed was more than what was changed***

In its Q1 earnings call, XM reaffirmed its 2007 guidance on total subscribers and subscription revenue. In addition, the company refined its CPGA guidance to $111-114 from its previous flat-to-higher guidance with respect to the prior year's CPGA of $105. We believe that the increase in CPGA amounts to the company's elevated focus on gaining back market share from Sirius. NPD data suggests XM's market share to be 44% and 47% for February and March, respectively. This compares to XM's 37% market share for 4Q06, a significant difference from current market share levels.

In terms of adjusted operating loss, the company updated its guidance to a range of $170-180 million. The change from its prior guidance is small ($4-14mn) and thus we do put much weight on the guidance change.

The company also reaffirmed its guidance to positive 2008 full-year CFO. The company did not comment on positive CFO for 2007 but guided to an improved CFO in 2007. Such optimism may be in response to Sirius' hype on being FCF positive in 4Q06.

Figure 2. XM 2007 Guidance

		2007 Guidance	Updated Guidance	WMS 2007E
Total Subs	7.63	9-9.2	affirmed	9.01
Subscription revenue	826	~ 1,000	affirmed	984
Adjusted EBITDA	(166)	Flat	(170)-(180)	-
EBITDA	(234)	-	N/A	(226)
CPGA	105	Flat-to-Higher	111-114	115
Positive 2007 CFO	NA	no	N/A	no
Positive 2008 CFO	NA	yes	affirmed	yes
Date Issued	NA	2/26/2007	4/26/2007	NA

Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

The good news for XM is that its OEM commitments continue to strengthen. However, differences in subscriber accounting may push some of the gains to late 2007 and early 2008.

During the quarter, XM announced three major milestones with carmakers:

(1) Infiniti announced that it would make XM a factory-installed standard on every 2008 model. Although the press release does not state that Infiniti's commitment will extend into future years, we presume that the commitment will remain so long as its contract with XM is on-going and satellite radio remains a product desired by its customers.

(2) Honda announced that it would extend its agreement with XM by 10 years, putting the end date at 2016.

(3) Similarly, Toyota also announced that it would extend its agreement with XM by 10 years, putting the end date at 2017.

However, even before these recent announcements, we were expecting XM to show considerable progress in 2007 due to continued step-ups in OEM production commitments, particularly with 2008 and 2009 model years. Summer and early fall are the periods when new models are introduced. And thus, it is natural to have high expectations for OEM gross adds in the second half of 2007. However, we note that the full effect of the OEM productions commitments will not be realized so immediately. First, older car models, without satellite radio, are still being sold in conjunction with the newer models that offer satellite radio. Thus, it will take time for the mix to heavily favor new cars, which are increasingly skewed to satellite radio. In addition, differences in subscriber accounting will push some OEM gross add recognition further back. GM and Honda pay for the three-month trial period and thus subscribers through these carmakers are recognized immediately. However, for other car dealers, XM subsidizes the trial period and does not receive any payment. Subscribers from these dealers can only be recognized after the three-month trial period and only if the subscribers convert into paying customers. We believe that the strength of OEMs for the second half of 2007 may be overestimated, as gross additions may be further pushed back. Nevertheless, the more important trend is that OEM production commitments are on the rise, and whether it occurs in three, six, or nine months after production, subscribers tallies should naturally benefit.

XM - Automaker Round-up

Hyundai 4/5/07	Hyundai adds XM as standard feature on all-new Veracruz and future premium sports sedan. XM Radio is already a standard, factory-installed feature on all 2007 Azera, Elantra, Santa Fe and Sonata audio systems.
Lexus 4/4/07	XM Radio and XM NavTraffic capability will be standard factory-installed features on the all-new Lexus LX 570.
Infiniti 4/4/07	As the **exclusive satellite radio service** for Infiniti, **XM will be a standard factory-installed feature on every 2008 Infiniti model**, including the G, M, FX and QX.
Toyota 1/31/07	Toyota extended its agreement with XM for Toyota and Lexus through model-year 2017. **Toyota's annual factory production of XM-equipped vehicles is expected to exceed one million by 2010.** Toyota, like most of XM's other auto OEM deals gives car purchasers a three-month trial, paid for by the automaker. XM typically recognizes a portion of the 3-month commitment as deferred revenue. Sirius only works with Toyota/Lexus at the dealer level, making XM

the sole provider of factory-installed radios.

Honda
1/30/07

Honda extended its **exclusive relationship** with XM as part of a new 10-year agreement that runs through 2016. An original strategic partner in the launch of XM, American Honda introduced its first factory-installed XM vehicles in 2003 and is **projecting production of 650,000 factory-installed XM units for 2007 model vehicles.** American Honda has produced more than 1.5 million cars with XM factory-installed to date.

General Motors
10/05/06

General Motors, **an exclusive XM partner, plans to build over 1.8 million vehicles with factory-installed XM Satellite Radio in 2007**. GM was the world's first automaker to offer satellite radio when it introduced XM as a factory-installed feature on Cadillac Seville and Deville models in 2001 and continues to lead all automakers in offering factory- installed satellite radio.

Porsche
10/30/06

Porsche and XM announced a new long-term agreement to equip Porsche vehicles for the U.S. market with XM, beginning in 2007. XM has been available as a popular factory-installed feature for Cayenne models since 2005 and will be the exclusive satellite radio option in the future.

Hyundai
10/03/06

Hyundai announced the production of the first Hyundai vehicles with standard, factory-installed XM Satellite Radio. The Santa Fe is the first of four Hyundai models to add XM Satellite Radio as a standard feature to all audio systems this year. Others include the 2007 Sonata, Azera and Elantra. **These vehicles mark the beginning of Hyundai's aggressive rollout of XM Radio as a standard feature in all audio systems of its U.S. vehicles**, boding well for XM and the sector if others started to think similarly.

Nissan
11/2/05

Nissan selected XM Satellite Radio as its factory-installed satellite radio solution for Infiniti and Nissan vehicles beginning with the 2008 model year. **More than five hundred thousand Nissan and Infiniti vehicles with factory-installed XM Satellite Radio are projected to be produced for the 2008 model year with more than one million annually by model-year 2010.**

Suzuki
8/23/05

Suzuki offered XM Radio for the first time in the 2006 model year with Suzuki Grand Vitara and Suzuki XL-7 sport utility vehicles arriving XM-Ready at U.S. dealerships.

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Figure 3. Automobile OEM Production Commitments

OEM	2006 Car Sales	Sirius	XM	OEM Market Share Sirius	OEM Market Share XM	Production Notes by Model Year 2006 MY	2007 MY	2008 MY	2009 MY	Exclusivity
BMW	313,939	✓		1 9%	0.0%					Aug-08
BMW		✓					8 lines			...
Mini		✓					Dealer Only			...
Rolls Royce		✓					All Lines			Exclusive
DaimlerChrysler	2,390,585	✓		14 4%	0.0%	30%	40%			Sep-12
Chrysler		✓					6 lines			...
Dodge		✓					10 lines			...
Jeep		✓					6 lines			...
Maybach		✓					1 line			...
Mercedes-Benz		✓					80%	90%	>90%	...
Ford Motor Co	2,901,090	✓		17.5%	0.0%		21 lines	90%		Jan-09
Aston Martin		✓								...
Ford		✓								...
Jaguar		✓				3 lines				...
Land Rover		✓				2 lines				...
Lincoln		✓						90%		...
Mercury		✓								...
Volvo		✓								...
General Motors	4,065,341		✓	0 0%	24.5%		~45% / 1.8mn			
Buick			✓				5 lines			...
Chevrolet			✓				15 lines			...
Cadillac			✓				6 lines			...
GMC			✓				6 lines			...
Hummer			✓				2 lines			...
Pontiac			✓				6 lines			...
SAAB			✓				3 lines			...
Saturn			✓				5 lines			...
Honda	1,509,358		✓	0.0%	9.1%	~35%	~45% / 650k			YE2016
Acura			✓				5 lines			...
Honda			✓				12 lines			...
Hyundai Group	749,822	✓		4.5%	4.5%					
Hyundai			✓				4 lines			...
Kia		✓							All Lines	YE2014
Isuzu	8,614		✓	0.0%	0.1%		1 line			...
Mazda	268,786	✓		1.6%	0.0%		7 lines			...
Mitsubishi	118,558	✓		0.7%	0.0%		4 lines	All Lines		...
Nissan	1,019,249	✓	✓	0.0%	6.2%					XM Exclusive MY08
Infiniti		✓	✓				5 lines	All Lines		...
Nissan		✓	✓				10 lines			...
Porsche	34,227		✓	0.0%	0.2%		1 line			Exclusive
Subaru	200,703	✓	✓	0.0%	1.2%		6 lines			...
Suzuki	100,990		✓	0.0%	0.6%		3 lines			...
Toyota	2,542,525		✓	0.0%	15.4%				+1mn	YE2017
Lexus			✓				10 lines			...
Toyota			✓				9 lines			...
Scion			✓				3 lines			...
VW	329,112	✓		2.0%	0.0%					2012 MY
Audi		✓								2012 MY
Bently		✓								...
VW		✓					80%			2012 MY
Other OEMs	6,726			0.0%	0.0%					
Ferrari										...
Lamborghini										...
Lotus			✓				1 line			...
Mini								2 lines		
U.S. Car Sales	**16,559,625**			**42.7%**	**61.8%**					

Source: Automotive News Data Center, Wedbush Morgan Securities

William Kidd (213) 688-6698
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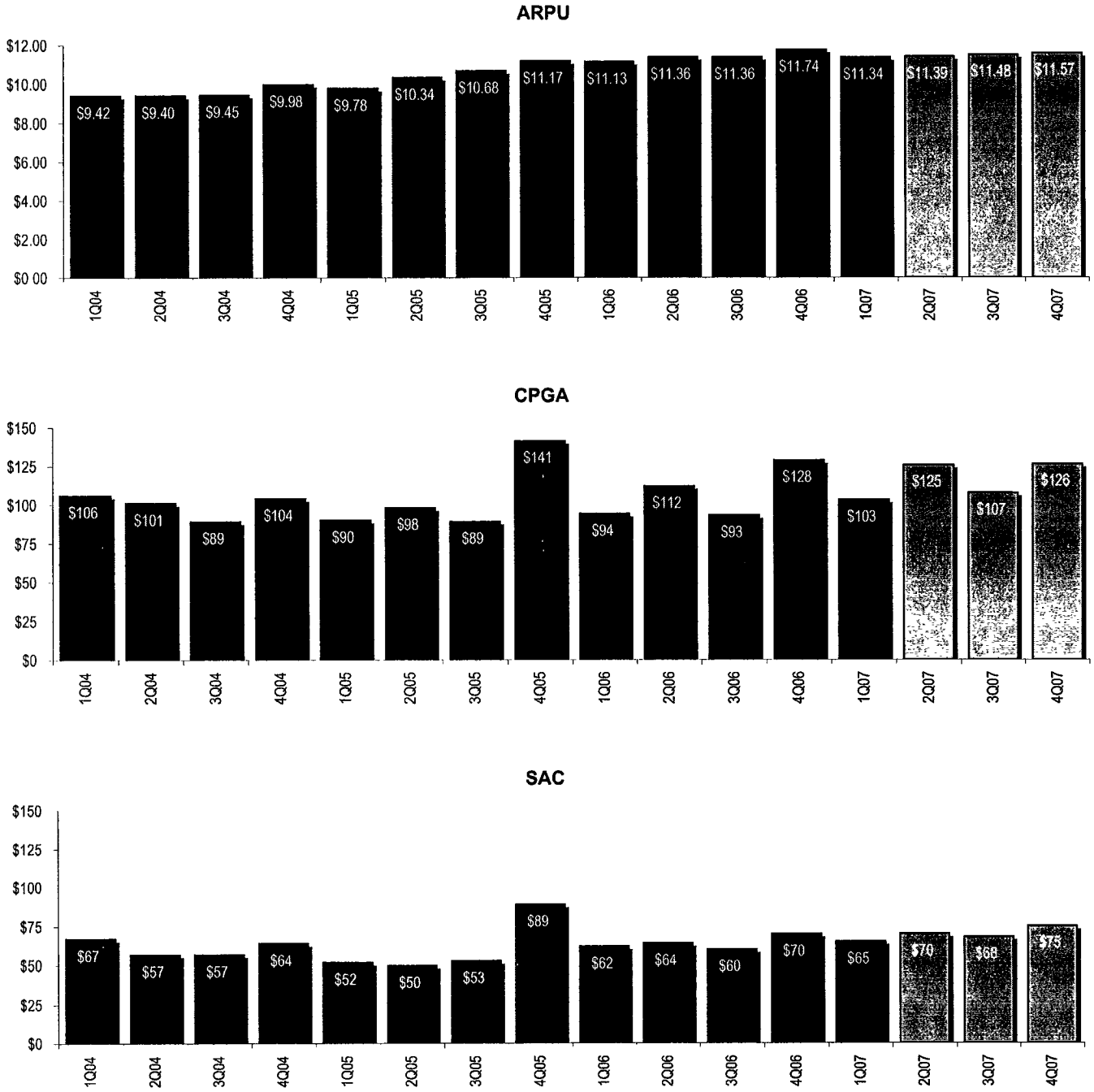
Figure 4. XM Quarterly Results Comparison

(millions)	1Q06	4Q06	1Q07	1Q07 % change Y-o-Y	1Q07 % change Q-o-Q	WMS 1Q07 Estimates	WMS Variance
Net Subscriber Additions	569	443	285	(49.9%)	(35.6%)	294	(2.9%)
Total Subscribers	6,502	7,629	7,914	21.7%	3.7%	7,922	(0.1%)
Revenue:							
Subscription	188,102	220,542	236,486	25.7%	7.2%	230,459	2.6%
Activation	3,579	4,459	4,654	30.0%	4.4%	4,643	0.2%
Equipment	3,551	10,076	5,297	49.2%	(47.4%)	4,577	15.7%
Net Ad Sales	6,518	11,045	7,478	14.7%	(32.3%)	12,714	(41.2%)
Other	6,216	11,000	10,197	64.0%	(7.3%)	11,110	(8.2%)
Total Revenue	**207,966**	**257,122**	**264,112**	27.0%	2.7%	**263,502**	0.2%
Cost of Revenue:							
Revenue Share & Royalties	34,276	43,405	47,426	38.4%	9.3%	46,190	2.7%
Customer Care & Billing	22,455	28,850	27,928	24.4%	(3.2%)	27,463	1.7%
Cost of Equipment	7,993	20,525	18,277	128.7%	(11.0%)	13,731	33.1%
Ad Sales	3,356	4,768	3,385	0.9%	(29.0%)	6,357	(46.8%)
Satellite & Terrestrial	13,049	12,729	13,882	6.4%	9.1%	12,793	8.5%
Broadcast & Operations	14,739	15,033	16,260	10.3%	8.2%	15,517	4.8%
Programming & Content	37,643	46,427	43,952	16.8%	(5.3%)	39,091	12.4%
Total Cost of Revenue	**133,511**	**171,737**	**171,110**	28.2%	(0.4%)	**161,142**	6.2%
Research & Development	10,981	9,080	7,310	(33.4%)	(19.5%)	9,171	(20.3%)
General & Administrative	17,630	30,327	34,185	93.9%	12.7%	30,630	11.6%
Marketing:							
Retention & Support	8,047	9,064	9,756	21.2%	7.6%	9,424	3.5%
Subsidies & Distribution	59,732	73,464	43,602	(27.0%)	(40.6%)	62,718	(30.5%)
Advertising & Marketing	29,666	52,789	32,809	10.6%	(37.8%)	30,111	9.0%
Amortization of GM Liability	9,313	6,504	6,504	(30.2%)	0.0%	6,504	0.0%
Total Marketing	**106,758**	**141,821**	**92,671**	(13.2%)	(34.7%)	**108,757**	(14.8%)
Depreciation & Amortization	39,882	44,043	46,882	17.6%	6.4%	47,988	(2.3%)
Total Operating Expenses	**308,762**	**397,008**	**352,158**	14.1%	(11.3%)	**357,688**	(1.5%)
Operating Profit (Loss)	**(100,796)**	**(139,886)**	**(88,046)**	(12.6%)	(37.1%)	**(94,186)**	(6.5%)
Interest Income	6,573	3,499	3,544	(46.1%)	1.3%	1,285	nmf
Interest Expense	(33,236)	(34,958)	(27,609)	(16.9%)	(21.0%)	(40,069)	(31.1%)
Other Income (Expense)	(22,630)	(84,142)	(9,643)	(57.4%)	nmf	-	nmf
Pre-Tax Income	(150,089)	(255,487)	(121,754)	(18.9%)	(52.3%)	(132,970)	(8.4%)
Taxes	868	(1,237)	(684)	nmf	nmf	(579)	18.1%
Net Income (Loss)	**(149,221)**	**(256,724)**	**(122,438)**	(17.9%)	(52.3%)	**(133,549)**	(8.3%)
8.25% Series B & C Preferred Stock Dividend	(2,149)	(530)	-	nmf	nmf	(515)	nmf
Series B Preferred Stock Retirement Gain	-	-	-	nmf	nmf	-	nmf
Series C Preferred Stock Retirement Loss	-	(5,938)	-	nmf	nmf	-	nmf
Net Income (Loss) to Common Shareholders	**(151,370)**	**(263,192)**	**(122,438)**	(19.1%)	(53.5%)	**(134,063)**	(8.7%)
Basic & Diluted EPS	**($0.60)**	**($0.90)**	**($0.40)**	(33.0%)	(55.3%)	**($0.44)**	(8.7%)
Basic & Diluted Shares Outstanding	253,213	293,797	305,878	20.8%	4.1%	305,669	0.1%

Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Figure 5. XM ARPU, Adjusted SAC, and SAC Trends



Note: Projected figures are shaded lightly.
Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Figure 6. XM Discounted Cash Flow (DCF) Valuation

(000's)		2006	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E
XM Subscribers		7,629	9,009	10,354	11,617	12,812	13,866	14,781	15,581	16,417	17,127
Discounted Cash Flow											
EBITDA		(166,172)	(212,206)	26,352	196,930	323,890	400,905	493,687	607,170	750,787	829,743
Unlevered Taxes		14	(2,421)	(2,316)	(2,316)	(2,316)	(2,316)	(2,316)	(2,316)	(2,316)	(2,316)
CapEx		(253,131)	(384,608)	(179,286)	11,049	(60,000)	(60,000)	(60,000)	(60,000)	(60,000)	(60,000)
Change in Working Capital		(285,614)	285,745	180,951	115,958	172,828	119,334	181,491	84,929	225,381	93,582
Unlevered Cash Flow		(704,903)	(313,491)	25,701	321,620	434,402	457,923	612,861	629,783	913,852	861,009
PV of Cash Flows			2,437,653	2,675,828							
PV of Terminal Value			3,697,149	4,097,366							
Private Market Value			6,134,803	6,773,194							
Private-to-Public Discount			-	-							
Public Enterprise Value			6,134,803	6,773,194							
Add Cash			75,539	66,842							
Less. Debt (excl in-the-money preferreds)			1,519,979	1,569,171							
Add. Proceeds from Warrants/Options			67,398	67,398							
Add Face Value, In-the-money 10% Convert			33,000	33,000							
Add: Public Inv.- XM Canada, Worldspace			66,649	66,649							
Market Capitalization			4,857,410	5,437,912							
Shares Outstanding			337,805	337,805							
Fair Value per Share (Year-end)			**$14.38**	$16.10							
Current Price			$11.78	$11.78							
Implied Upside			22.1%	36.7%							
Valuation Multiples											
EV/EBITDA	@ $14.38	NA	NA	232.8x	31.2x	18.9x	15.3x	12.4x	10.1x	8.2x	7.4x
P/E	@ $14.38	NA	NA	NA	NA	39.7x	25.9x	17.4x	11.7x	9.2x	8.6x
P/FCF	@ $14.38	NA	NA	NA	22.0x	13.3x	13.0x	9.5x	8.8x	6.3x	6.9x
P/BV	@ $14.38	NA	NA	NA	NA	NA	NA	NA	NA	17.0x	6.1x
EV/SUB	@ $14.38	804	681	592	528	479	442	415	394	374	358
EV/EBITDA	@ $11.78	NA	NA	151.0x	20.2x	12.3x	9.9x	8.1x	6.6x	5.3x	4.8x
P/E	@ $11.78	NA	NA	NA	NA	35.1x	22.9x	15.3x	10.3x	8.1x	7.6x
P/FCF	@ $11.78	NA	NA	NA	18.0x	10.9x	10.7x	7.8x	7.2x	5.1x	5.7x
P/BV	@ $11.78	NA	NA	NA	NA	NA	NA	NA	NA	14.0x	5.0x
EV/SUB	@ $11.78	$522	$442	$384	$343	$311	$287	$269	$255	$242	$232

Cost of Equity	11.5%
After-tax Cost of Debt	7.0%
WACC	10.8%
Terminal Growth	2.9%
Debt/Capitalization	15.0%
Implied TV Multiple	12.98x
TV/15 EBITDA	10.14x
Private-to-Public Discount	0.0%

Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Earnings Model

Figure 7. XM Annual Subscriber Forecast (4Q05-4Q07E)

(000's)	2003	2004	2005	2006	2007E	2008E	2009E	2010E
Gross Additions (WMS estimates)								
Retail	-	-	2,195	1,761	1,461	1,555	1,662	1,733
OEM	-	-	1,891	2,074	2,403	2,782	2,914	3,069
Rental	-	-	25	11	26	12	11	11
Data Services	-	-	19	20	22	25	27	30
Total Gross Additions	**1,167**	**2,577**	**4,130**	**3,866**	**3,913**	**4,374**	**4,614**	**4,843**
% Change - Gross Additions (yoy)								
Retail	-	-	-	(6.9%)	(17.0%)	6.4%	6.9%	4.3%
OEM	-	-	-	(5.5%)	15.9%	15.8%	4.8%	5.3%
Rental	-	-	-	(55.7%)	130.7%	(54.2%)	(7.6%)	0.0%
Data Services	-	-	-	5.3%	10.0%	10.0%	10.0%	10.0%
% Change (yoy)	**242.0%**	**120.8%**	**60.3%**	**(6.4%)**	**1.2%**	**11.8%**	**5.5%**	**5.0%**
Churn								
Retail	-	-	500	963	1,069	1,115	1,159	1,207
OEM	-	-	918	1,152	1,449	1,894	2,171	2,418
Rental	-	-	8	50	6	7	7	8
Data Services	-	-	0	7	9	12	14	16
Total Churn	**154**	**709**	**1,427**	**2,171**	**2,533**	**3,028**	**3,351**	**3,648**
Churn Rate (Monthly)								
Retail	-	-	1.8%	2.1%	2.0%	1.9%	1.8%	1.7%
OEM	-	-	4.4%	3.6%	3.4%	3.5%	3.4%	3.4%
Rental	-	-	1.8%	11.6%	2.5%	1.9%	1.8%	1.7%
Data Services	-	-	-	2.3%	2.0%	1.9%	1.8%	1.7%
Churn Rate	**2.1%**	**3.1%**	**2.9%**	**2.7%**	**2.6%**	**2.7%**	**2.6%**	**2.5%**
Net Additions								
Retail	-	-	1,694	798	392	440	502	527
OEM	-	-	973	922	955	888	743	651
Rental	-	-	17	(38)	20	5	4	3
Data Services	-	-	19	14	13	13	13	14
Total Net Additions	**1,013**	**1,869**	**2,704**	**1,696**	**1,380**	**1,346**	**1,263**	**1,195**
Subscribers								
Retail	-	1,887	3,582	4,380	4,772	5,212	5,714	6,241
OEM	-	1,315	2,288	3,210	4,165	5,053	5,796	6,447
Rental	-	27	44	5	26	31	35	38
Data Services	-	-	19	33	46	59	72	86
Total Subscribers	**1,360**	**3,229**	**5,933**	**7,629**	**9,009**	**10,354**	**11,617**	**12,812**
Average Subscribers	727	2,125	4,400	6,817	8,073	9,423	10,699	11,927
Subscriber Distribution (%)								
Retail		58.5%	60.4%	57.4%	53.0%	50.3%	49.2%	48.7%
OEM		40.7%	38.6%	42.1%	46.2%	48.8%	49.9%	50.3%
Rental		0.8%	0.7%	0.1%	0.3%	0.3%	0.3%	0.3%
Data Services		0.0%	0.3%	0.4%	0.5%	0.6%	0.6%	0.7%
Total		**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**
Net Additions Distribution (%)								
Retail		-	62.7%	47.1%	28.4%	32.7%	39.8%	44.1%
OEM		-	36.0%	54.4%	69.2%	66.0%	58.9%	54.5%
Rental		-	0.6%	(2.3%)	1.5%	0.4%	0.3%	0.3%
Data Services		-	0.7%	0.8%	1.0%	1.0%	1.0%	1.2%
Total		**-**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Figure 8. XM Annual P&L (2003-2010E)

(000's)	2003	2004	2005	2006	2007E	2008E	2009E	2010E
Revenue:								
Subscription	78,275	221,073	502,612	825,626	983,690	1,291,539	1,560,423	1,829,791
Activation	1,868	4,814	10,066	16,193	19,370	20,575	20,647	23,357
Equipment	6,692	7,262	18,182	21,719	20,015	22,615	25,678	28,626
Net Ad Sales	4,065	8,485	20,103	35,330	44,438	78,916	130,174	152,897
Other	881	2,811	7,303	34,549	41,404	43,085	44,835	46,655
Total Revenue	**91,781**	**244,445**	**558,266**	**933,417**	**1,108,916**	**1,456,730**	**1,781,757**	**2,081,325**
Cost of Revenue:								
Revenue Share & Royalties	26,440	50,676	93,874	149,010	181,728	248,176	309,625	364,828
Customer Care & Billing	25,945	40,887	76,222	104,871	124,935	148,752	172,217	195,793
Cost of Equipment	9,797	11,557	40,707	48,949	62,430	56,538	64,195	62,977
Ad Sales	3,257	6,165	10,058	15,961	21,865	39,458	65,087	76,449
Satellite & Terrestrial	39,692	35,922	42,356	49,019	55,946	57,073	58,223	59,396
Broadcast & Operations:								
Broadcast	*7,689*	*10,848*	*16,610*	*23,049*	*26,972*	*29,195*	*31,602*	*34,207*
Operations	*12,023*	*13,192*	*24,459*	*34,683*	*41,259*	*46,848*	*50,709*	*54,889*
Broadcast & Operations	19,712	24,040	41,069	57,732	68,230	76,043	82,311	89,096
Programming & Content	23,109	32,698	101,008	165,196	173,169	204,682	249,209	314,693
Total Cost of Revenue	**147,952**	**201,945**	**405,294**	**590,738**	**688,303**	**830,722**	**1,000,867**	**1,163,233**
Research & Development	12,285	23,514	31,218	37,428	29,682	30,887	32,141	33,446
General & Administrative	27,418	28,555	43,864	88,626	138,805	83,737	94,756	98,604
Marketing:								
Retention & Support	7,873	13,259	22,275	31,842	40,270	46,071	51,274	56,027
Subsidies & Distribution	92,521	165,705	264,719	241,601	260,945	263,227	231,550	233,369
Advertising & Marketing	64,309	88,090	163,312	147,639	151,232	149,720	148,222	146,740
Amortization of GM Liability	35,564	37,252	37,252	29,761	26,016	26,016	26,016	26,016
Total Marketing	**200,267**	**304,306**	**487,558**	**450,843**	**478,463**	**485,033**	**457,062**	**462,152**
Impairment of Goodwill	-	-	-	-	-	-	-	-
Depreciation & Amortization	158,317	147,165	145,869	168,881	190,471	135,021	128,503	132,061
Total Operating Expenses	**546,239**	**705,485**	**1,113,803**	**1,336,516**	**1,525,723**	**1,565,399**	**1,713,330**	**1,889,496**
Pre-Marketing Cash Flow	*(139,311)*	*(60,080)*	*18,363*	*155,022*	*185,840*	*439,298*	*576,702*	*704,000*
PMCF Margin	-	-	*3.3%*	*16.6%*	*16.8%*	*30.2%*	*32.4%*	*33.8%*
Operating Profit (Loss)	**(454,458)**	**(461,040)**	**(555,537)**	**(403,099)**	**(416,808)**	**(108,669)**	**68,427**	**191,829**
Interest Income	3,066	6,238	23,586	21,664	6,213	2,982	3,015	3,197
Interest Expense	(110,349)	(85,757)	(107,791)	(121,305)	(148,954)	(158,113)	(124,640)	(73,202)
Other Income (Expense)	(22,794)	(74,492)	(24,645)	(216,148)	(9,643)	-	-	-
Pre-Tax Income	(584,535)	(615,051)	(664,387)	(718,887)	(569,192)	(263,801)	(53,199)	121,824
Taxes	-	(27,317)	(2,330)	14	(2,421)	(2,316)	(2,316)	(2,316)
Effective Tax Rate	-	(4.4)%	(0.4)%	0.0%	(0.4)%	(0.9)%	(4.4)%	1.9%
Net Income (Loss)	**(584,535)**	**(642,368)**	**(666,717)**	**(718,874)**	**(571,613)**	**(266,117)**	**(55,515)**	**119,508**
8.25% Series B & C Preferred Stock Dividend	(17,569)	(8,802)	(8,597)	(6,127)	(1,544)	(2,059)	(2,059)	(2,059)
Series B Preferred Stock Retirement Gain (Loss)	8,761	-	-	(755)	-	-	-	-
Series C Preferred Stock Retirement Gain (Loss)	(11,537)	-	-	(5,938)	-	-	-	-
Net Income (Loss) to Common Shareholders	**(604,880)**	**(651,170)**	**(675,314)**	**(731,694)**	**(573,157)**	**(268,176)**	**(57,574)**	**117,449**
Basic & Diluted EPS	**($4.83)**	**($3.30)**	**($3.07)**	**($2.71)**	**($1.85)**	**($0.83)**	**($0.17)**	**$0.34**
Basic & Diluted Shares Outstanding	125,176	197,318	219,620	270,368	310,496	323,104	336,223	349,875

Source: Wedbush Morgan Securities, Company Reports

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Figure 9. XM Quarterly Subscriber Forecast (4Q05-4Q07E)

(000's)	4Q05	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07E	3Q07E	4Q07E
Gross Additions (WMS estimates)									
Retail	916.4	512.3	402.5	310.3	535.6	326.4	293.9	289.3	551.7
OEM	433.8	495.0	510.6	552.5	516.1	518.2	561.6	663.0	660.6
Rental	4.4	(4.1)	7.0	-	8.3	19.0	2.7	-	4.3
Data Services	19.3	4.1	6.2	5.2	4.8	4.5	6.8	5.8	5.3
Total Gross Additions	**1,373.9**	**1,007.3**	**926.3**	**868.0**	**1,064.9**	**868.1**	**865.1**	**958.0**	**1,221.9**
% Change - Gross Additions (yoy)									
Retail	-	23.0%	(4.6%)	(29.5%)	(41.5%)	(36.3%)	(27.0%)	(6.8%)	3.0%
OEM	-	25.7%	(0.8%)	0.7%	19.0%	4.7%	10.0%	20.0%	28.0%
Rental	-	(135.6%)	(25.1%)	(100.0%)	90.0%	(563.6%)	(62.1%)	(110.2%)	(48.4%)
Data Services	-	-	-	-	-	10.0%	10.0%	10.0%	10.0%
% Change (yoy)	**48.0%**	**22.6%**	**(2.1%)**	**(12.2%)**	**(22.5%)**	**(13.8%)**	**(6.6%)**	**10.4%**	**14.7%**
Churn									
Retail	153.3	211.6	238.8	245.0	267.1	268.6	266.3	256.9	277.6
OEM	319.7	223.0	285.7	313.9	329.1	310.8	359.9	380.1	398.1
Rental	2.6	2.6	2.3	21.3	23.4	1.5	1.4	1.4	1.4
Data Services	-	1.2	1.4	1.7	2.6	2.0	2.1	2.3	2.7
Total Churn	**475.6**	**438.4**	**528.3**	**582.0**	**622.3**	**582.9**	**629.6**	**640.6**	**679.8**
Churn Rate (Monthly)									
Retail	1.8%	2.0%	2.1%	2.0%	2.2%	2.0%	2.0%	1.9%	2.1%
OEM	4.9%	3.2%	3.7%	3.8%	3.6%	3.2%	3.5%	3.5%	3.4%
Rental	2.0%	2.0%	2.1%	17.0%	38.1%	9.2%	2.0%	1.9%	2.1%
Data Services	-	2.0%	2.1%	2.1%	2.9%	2.1%	2.0%	1.9%	2.1%
Churn Rate	**3.1%**	**2.5%**	**2.7%**	**2.8%**	**2.9%**	**2.5%**	**2.7%**	**2.6%**	**2.7%**
Net Additions									
Retail	763.1	300.7	163.7	65.2	268.5	57.8	27.7	32.4	274.1
OEM	114.1	272.0	224.9	238.6	187.0	207.4	201.7	282.9	262.5
Rental	1.8	(6.7)	4.7	(21.3)	(15.1)	17.5	1.3	(1.4)	2.9
Data Services	19.3	2.9	4.8	3.6	2.2	2.5	4.7	3.5	2.6
Total Net Additions	**898.3**	**568.9**	**398.0**	**286.0**	**442.6**	**285.2**	**235.4**	**317.4**	**542.1**
Subscribers									
Retail	3,581.6	3,882.3	4,046.0	4,111.2	4,379.8	4,437.6	4,465.3	4,497.7	4,771.8
OEM	2,288.0	2,560.1	2,785.0	3,023.5	3,210.5	3,417.9	3,619.6	3,902.6	4,165.1
Rental	43.9	37.2	41.8	20.5	5.4	22.9	24.2	22.8	25.7
Data Services	19.3	22.3	27.1	30.6	32.9	35.3	40.1	43.5	46.1
Total Subscribers	**5,933.0**	**6,501.9**	**6,899.9**	**7,185.9**	**7,628.6**	**7,913.7**	**8,149.2**	**8,466.5**	**9,008.7**
Average Subscribers	5,284.0	6,228.8	6,684.9	7,054.3	7,300.3	7,763.4	7,913.7	8,149.2	8,466.5
Subscriber Distribution (%)									
Retail	60.4%	59.7%	58.6%	57.2%	57.4%	56.1%	54.8%	53.1%	53.0%
OEM	38.6%	39.4%	40.4%	42.1%	42.1%	43.2%	44.4%	46.1%	46.2%
Rental	0.7%	0.6%	0.6%	0.3%	0.1%	0.3%	0.3%	0.3%	0.3%
Data Services	0.3%	0.3%	0.4%	0.4%	0.4%	0.4%	0.5%	0.5%	0.5%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**
Net Additions Distribution (%)									
Retail	84.9%	52.9%	41.1%	22.8%	60.7%	20.3%	11.8%	10.2%	50.6%
OEM	12.7%	47.8%	56.5%	83.4%	42.2%	72.7%	85.7%	89.1%	48.4%
Rental	0.2%	(1.2)%	1.2%	(7.5)%	(3.4)%	6.1%	0.5%	(0.4)%	0.5%
Data Services	2.2%	0.5%	1.2%	1.2%	0.5%	0.9%	2.0%	1.1%	0.5%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Source: Wedbush Morgan Securities

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Figure 10. XM Quarterly P&L (4Q05-4Q07E)

(000's)	4Q05	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07E	3Q07E	4Q07E
Revenue:									
Subscription	156,251	188,102	202,165	214,817	220,542	236,486	241,064	248,236	257,904
Activation	3,079	3,579	3,942	4,213	4,459	4,654	4,749	4,893	5,074
Equipment	8,627	3,551	4,928	3,164	10,076	5,297	4,748	4,889	5,080
Net Ad Sales	7,283	6,518	8,982	8,786	11,045	7,478	9,496	12,224	15,240
Other	1,895	6,216	7,869	9,464	11,000	10,197	10,299	10,402	10,506
Total Revenue	**177,135**	**207,966**	**227,886**	**240,444**	**257,122**	**264,112**	**270,357**	**280,644**	**293,803**
Cost of Revenue:									
Revenue Share & Royalties	27,889	34,276	37,923	33,406	43,405	47,426	48,240	41,412	44,650
Customer Care & Billing	24,560	22,455	26,395	27,171	28,850	27,928	30,864	32,016	34,128
Cost of Equipment	22,267	7,993	10,254	10,177	20,525	18,277	14,245	14,668	15,240
Ad Sales	3,644	3,356	4,460	3,378	4,768	3,385	4,748	6,112	7,620
Satellite & Terrestrial	11,353	13,049	11,571	11,670	12,729	13,882	13,951	14,021	14,091
Broadcast & Operations:									
Broadcast	*4,707*	*5,852*	*5,169*	*6,158*	*5,869*	*6,544*	*6,675*	*6,808*	*6,945*
Operations	*6,851*	*8,887*	*8,805*	*7,827*	*9,164*	*9,716*	*10,105*	*10,509*	*10,929*
Broadcast & Operations	11,558	14,739	13,974	13,985	15,033	16,260	16,780	17,317	17,874
Programming & Content	30,551	37,643	42,253	38,873	46,427	43,952	40,949	42,876	45,392
Total Cost of Revenue	**131,822**	**133,511**	**146,830**	**138,660**	**171,737**	**171,110**	**169,777**	**168,422**	**178,995**
Research & Development	10,248	10,981	8,518	8,849	9,080	7,310	7,383	7,457	7,532
General & Administrative	13,213	17,630	18,672	21,997	30,327	34,185	34,527	34,872	35,221
Marketing:									
Retention & Support	6,584	8,047	7,443	7,288	9,064	9,756	9,895	10,139	10,481
Subsidies & Distribution	113,852	59,732	61,126	47,279	73,464	43,602	60,554	65,147	91,643
Advertising & Marketing	66,703	29,666	37,666	27,518	52,789	32,809	38,231	27,931	52,261
Amortization of GM Liability	9,313	9,313	7,440	6,504	6,504	6,504	6,504	6,504	6,504
Total Marketing	**196,452**	**106,758**	**113,675**	**88,589**	**141,821**	**92,671**	**115,184**	**109,720**	**160,888**
Impairment of Goodwill	-	-	-	-	-	-	-	-	-
Depreciation & Amortization	39,028	39,882	41,847	43,109	44,043	46,882	47,925	47,863	47,800
Total Operating Expenses	**390,763**	**308,762**	**329,542**	**301,204**	**397,008**	**352,158**	**374,796**	**368,334**	**430,436**
Pre-Marketing Cash Flow	*21,852*	*45,844*	*53,866*	*70,938*	*45,978*	*51,507*	*58,670*	*69,893*	*72,056*
PMCF Margin	*12.3%*	*22.0%*	*23.6%*	*29.5%*	*17.9%*	*19.5%*	*21.7%*	*24.9%*	*24.5%*
Operating Profit (Loss)	**(213,628)**	**(100,796)**	**(101,656)**	**(60,760)**	**(139,886)**	**(88,046)**	**(104,439)**	**(87,690)**	**(136,633)**
Interest Income	7,218	6,573	6,376	5,216	3,499	3,544	1,103	726	840
Interest Expense	(36,557)	(33,236)	(29,317)	(23,794)	(34,958)	(27,609)	(40,037)	(40,005)	(41,303)
Other Income (Expense)	(24,766)	(22,630)	(105,689)	(3,687)	(84,142)	(9,643)	-	-	-
Pre-Tax Income	(267,733)	(150,089)	(230,286)	(83,025)	(255,487)	(121,754)	(143,373)	(126,969)	(177,095)
Taxes	(593)	868	1,177	(794)	(1,237)	(684)	(579)	(579)	(579)
Effective Tax Rate	0.2%	(0.6)%	(0.5)%	1.0%	0.5%	0.6%	0.4%	0.5%	0.3%
Net Income (Loss)	**(268,326)**	**(149,221)**	**(229,109)**	**(83,819)**	**(256,724)**	**(122,438)**	**(143,952)**	**(127,548)**	**(177,674)**
8.25% Series B & C Preferred Stock Dividend	(2,149)	(2,149)	(1,814)	(1,634)	(530)	-	(515)	(515)	(515)
Series B Preferred Stock Retirement Gain (Loss)	-	-	(755)	-	-	-	-	-	-
Series C Preferred Stock Retirement Gain (Loss)	-	-	-	-	(5,938)	-	-	-	-
Net Income (Loss) to Common Shareholders	**(270,475)**	**(151,370)**	**(231,678)**	**(85,453)**	**(263,192)**	**(122,438)**	**(144,467)**	**(128,063)**	**(178,189)**
Basic & Diluted EPS	**($1.22)**	**($0.60)**	**($0.87)**	**($0.32)**	**($0.90)**	**($0.40)**	**($0.47)**	**($0.41)**	**($0.57)**
Basic & Diluted Shares Outstanding	221,929	253,213	266,099	268,363	293,797	305,878	308,936	312,026	315,146

Source: Wedbush Morgan Securities, Company Reports

William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

Public Companies Mentioned in this Report (priced as of close 4/26/07)

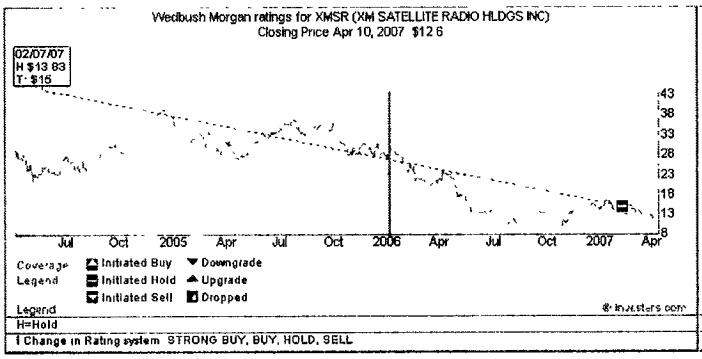
COMPANY	TICKER	RATING	PRICE	PRICE TARGET
Sirius Satellite Radio	SIRI	BUY	$2.96	$5

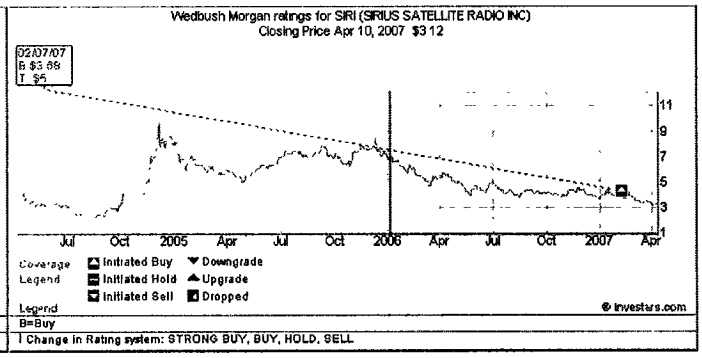
William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

ANALYST CERTIFICATION

I, William Kidd, certify that the views expressed in this report accurately reflect my personal opinion and that I have not and will not, directly or indirectly, receive compensation or other payments in connection with my specific recommendations or views contained in this report.

IMPORTANT DISCLOSURES





INVESTMENT RATINGS

STRONG BUY – The stock is expected to return at least 20% over the next 6-12 months.
BUY – The stock is expected to return at least 15% over the next 12 months.
HOLD – The stock is expected to return between -15% and +15% over the next 12 months.
SELL – The stock is expected to decline by at least 15% over the next 12 months.

DISTRIBUTION OF RATINGS (as of March 30, 2007)

BUY – 55% (3% of this rating category were investment banking clients within the last 12 months).
HOLD – 41% (3% of this rating category were investment banking clients within the last 12 months).
SELL – 4% (0% of this rating category were investment banking clients within the last 12 months).

The analysts responsible for preparing research reports do not receive compensation based on specific investment banking activity. The analysts receive compensation that is based upon various factors including WMS's total revenues, a portion of which are generated by WMS's investment banking activities.

WMS makes a market in the securities mentioned herein.

WMS changed its rating system from (BUY/ HOLD/SELL) to (STRONG BUY/BUY/HOLD/SELL) on January 5, 2006.

Additional information is available upon request.

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William Kidd (213) 688-6698
Jung Hwang, CPA (213) 688-4557

WEDBUSH MORGAN SECURITIES
RESEARCH DEPARTMENT

(213) 688-4520 / (866) 855-4529

DIRECTOR OF RESEARCH
Steven B. Gerber, M.D. (213) 688-4530

MANAGER, RESEARCH OPERATIONS AND BUSINESS CONDUCT
Vincent J. Moy (213) 688-4528

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Basic Industries and Business Services
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Edward Woo, CFA ..... (213) 688-4382

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Edward Woo, CFA.... ..... (213) 688-4382

Media
William Kidd.... ..... (213) 688-6698
Jung Hwang, CPA..... (213) 688-4557

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Ariel Sokol..... (212) 668-9874

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Nick Setyan ..... (213) 688-4519

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Craig Berger, CFA CPA..... (213) 688-4343
Steve Park..... (213) 688-4380

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Rohit Chopra ..... (212) 668-9871
Chris Rolland ..... (212) 938-9923

Telecommunications Software
Scott P. Sutherland, CFA ..... (213) 688-4522
Kerry Rice, CPA ..... (213) 688-4538

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CORPORATE HEADQUARTERS

1000 Wilshire Blvd., Los Angeles, CA 90017-2465
Tel: (213) 688-8000
www.wedbush.com

ALASKA
Anchorage ..... (907) 273-2300
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Cherry Creek ..... (303) 377-7327
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