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MAKING MONEY SELLING TELEVISIONS

TAG FOCUS:

- > No one agrees about whether consumer electronics retailers will be able to make money selling flat panel televisions as we enter the sweet spot in the life cycle. In our opinion, the retailers will in fact continue to generate increasing gross profit dollars due to greater unit and attachment (accessories/cables, audio, installation, and warranties) sales, despite declining gross margins.
- > Based on our assessment of the U.S. flat panel television market, we conclude that profits from the sale of attachments should easily offset any losses on the televisions resulting from expected gross margin erosion.
- > Our conservative base case assumptions yield blended (flat panel plus attachment sales) gross margins that fall short of the corporate average gross margins for the two big box consumer electronics retailers. However, our more optimistic “high” scenario, which is not overly aggressive, produces a blended gross margin that exceeds the corporate average.
- > We continue to favor Best Buy over Circuit City, but believe both will benefit from the hot, multi-product cycle.

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Executive Summary

Everyone agrees that flat panel televisions—liquid crystal display (LCD) and plasma—are amazing products that significantly enhance the way users watch television. Everyone agrees that they are sleek, stylish, and appealing, no matter how large the screen size. Everyone agrees that it is still very early in the life cycle of this innovative technology, with a current U.S. household penetration of flat panels in the low 20% area. Everyone agrees that prices continue to decrease, spurring sales of these hot items. Everyone also agrees that profit margins will continue to erode as prices drop and discounting at retailers is used to gain market share.

However, no one agrees about whether consumer electronics retailers will be able to make money selling flat panel televisions as we enter the sweet spot in the life cycle. In our opinion, the retailers will in fact continue to generate increasing gross profit dollars due to greater unit and attachment (accessories/cables, audio, installation, and warranties) sales, despite declining gross margins.

For perspective, we believe that the 2006 flat panel margin decline was precipitated by the high level of discounting that took place over the holiday season. We expect flat panel margin declines to moderate in 2007 and beyond, as the intensity of the price wars abate. In the case of Best Buy, we calculate this lost opportunity to be in the \$230 million area annually from 2007 to 2010. For Circuit City, we expect a loss of profits of about \$80 million per year over the same time period due to gross margin erosion. These amounts were calculated by deriving the difference between the estimated flat panel gross margin of the respective projected year and the gross margin had the rate of 2006 been maintained.

Our primary goal in writing this report was to understand the relationship between diminishing flat panel television gross profit and the sale of ancillary products and services, such as installation, warranties, audio components, and accessories/cables. We wanted to see if it was even realistic that the trade-off in margins, (lower television / higher attachments) could offset each other, and in the event that they could, what would be the mix of sales. Based on our assessment of the U.S. flat panel television market, we conclude that profits from the sale of attachments should offset television profit losses. For example, for Best Buy, we project attachment gross profits of \$342 million in 2006, essentially offsetting the television gross profit decline of \$97 million. Because of growth in attachment sales, which we estimate carry a blended gross margin of about 44% versus our base flat panel gross margin assumption of roughly 19% between 2007 and 2010, annual attachment profits are much greater than any lost profit from flat panel televisions. Circuit City's results are smaller in scale, but tell the same story, with projected attachment gross profit of \$127 million in 2006 making up for the television decrease of \$39 million.

Taking our thought process further, we analyzed the gross margin impact of the combined flat panel televisions and attachments relative to total U.S. division gross margins of the consumer electronics retailers. The quick answer is that our conservative base case assumptions yield results that fall short of the corporate average gross margins. However, an arguably more realistic "high" scenario produces a blended gross margin that exceeds the corporate average for the two big box electronics retailers. For example, in our base scenario, we estimate that Best Buy's 2006 blended flat panel and attachment gross margin came in at 24.1%, 60 basis points below our U.S. division gross margin projection of 24.7%. Note that our Best Buy high scenario gross margin of 27.6% in 2006 exceeded its U.S. average by 290 basis points. Our relatively conservative estimates through 2010 assume that Best Buy generates considerable gross profit from the sales of flat panel televisions and attachments, but the blended gross margin falls short of the total domestic gross margin by 100-170 basis points.

Circuit City's trends reveal a similar story. Aside from the fact that the sales and operational prowess of Circuit City lags Best Buy, the company still increases its gross profit through 2010 despite the gross margin shortfall relative to the total domestic division's gross margin. In 2006, we project a blended gross margin of 22.9% for Circuit City, in line with our estimate for the U.S. average. Between 2007 and 2010, our somewhat conservative blended television and attachment gross margin misses the domestic gross margin by 50-150 basis points.

After performing our analysis, we continue to believe in the strong flat panel television cycle and the consumer electronics retailers' abilities to make money selling these highly coveted items, albeit at a lower gross margin rate. Our conservative analysis reveals that attachment sales can in fact drive increased profit on a blended basis, largely making up for the gross margin erosion from the flat panel televisions. Moreover, our more optimistic scenario for attachments, which is not overly aggressive, indicates that Best Buy and Circuit City should be able to generate blended television and attachment gross margins that exceed the domestic gross margins at each company.

We continue to favor Best Buy over Circuit City, and believe both will benefit from the hot, multi-product cycle.

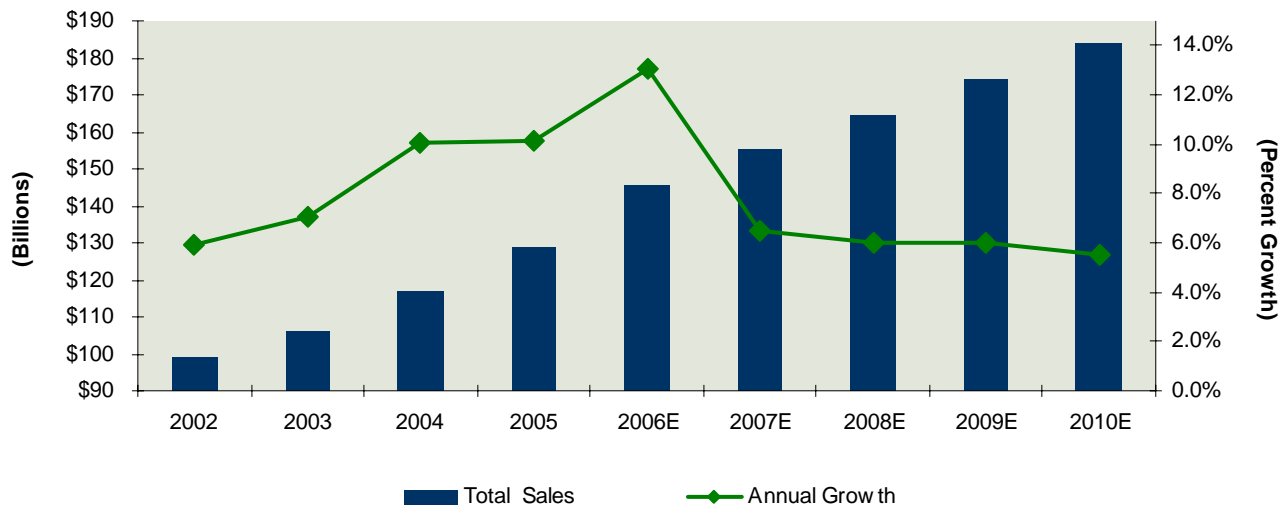
- > **Maintain 12-Month Price Target of \$64-\$66 on Best Buy.** The company remains a compelling investment for investors seeking solid high teens EPS growth within the framework of a world class franchise operating in a strong product cycle. Price declines and margin erosion will remain an issue for all consumer electronics retailers. However, Best Buy should continue to generate improvement in attachment rates of accessories and home theater installation, while controlling operating expenses to mitigate margin deterioration. The company should be able to continue to capture market share in a sector with an unprecedented product cycle, grow EPS by 17%-19% per year, and expand its high-teens ROIC. We continue to like the stock for the long term and assuming the shares trade in line with its historical P/E multiple and at the high end of its EPS growth rate, our 12-month price target range remains \$64-\$66.
- > **Maintain 12-Month Price Target of \$24-\$26 on Circuit City.** The company should be able to grow EPS in the mid-20% range for the next several years as it makes progress on its turnaround and capitalizes on the unprecedented consumer electronics product cycle. In addition, recent operational changes eliminated stores that were a drag on profits and reduced labor costs. Our 12-month price target of \$24-\$26 assumes that CC should be able to maintain a P/E multiple that is in line with our five-year EPS growth rate in the mid-20% area, and then applies it to our FY08 EPS estimate of \$0.85.

Market Overview

Demand for Consumer Electronics Remains Strong. Total U.S. consumer electronics sales (wholesale) rose at a compound annual growth rate (CAGR) of 9.2% between 2002 and 2005, well above the historic average annual growth rate of about 6%. According to the Consumer Electronics Association (CEA), 2006 was an even stronger year, with sales growth of 13.1% reaching approximately \$146 billion from \$129 billion in 2005. Sales growth is projected to moderate closer to historic levels at 6.5% in 2007, translating into total sales of more than \$155 billion. We believe the projected slower sales growth in 2007 is due largely to ongoing retail price decreases in flat panel televisions of 25%-35% per square inch of screen size as well as an expectation for slightly slower GDP growth in the 2.5%-3.5% range. Exhibit 1 reflects historical and projected annual consumer electronics (CE) sales for 2002-2010. For 2007-2010, we assume a more normalized annual industry growth rate of 5%-7%.

Exhibit 1

CONSUMER ELECTRONIC INDUSTRY GROWTH RATE NORMALIZES AS TV PRICES FALL



Source: Consumer Electronics Association (CEA) and TAG estimates.

Flat Panel Televisions Have Fueled Industry Growth. Total U.S. factory-to-dealer television sales (analog and digital) were an estimated \$25.1 billion, or 17.2% of all U.S. consumer electronics sales in 2006, versus \$19.0 billion, or 14.8% of industry sales in 2005. Although our expectations call for 5.9% total television category growth in 2007 due to further price declines, albeit in a more rational environment, we expect sales of flat panel televisions to increase by 28.8%. The strong 31.9% gain in total television sales in 2006 was fueled by flat panel television growth of 106.6% to \$14.2 billion versus \$6.9 billion in 2005. We expect total U.S. television sales growth to slow to the mid-single digit area through the end of the decade. However, we look for more robust flat panel television sales growth of 28.8% to \$18.3 billion in 2007, followed by moderating growth in 2008-2010.

Exhibit 2

LCD TV SALES GROWTH HAS OUTPACED ALL OTHER CATEGORIES

Category	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
LCD TV U.S. Factory-to-Dealer Sales (\$B)	\$0.2	\$0.7	\$1.6	\$3.3	\$8.5	\$12.2	\$15.1	\$17.7	\$19.8
% Change		169.9%	137.8%	106.3%	160.3%	44.2%	23.5%	17.5%	11.6%
% of U.S. Television Sales	1.8%	4.6%	9.4%	17.1%	33.8%	46.0%	53.4%	59.6%	64.5%
Units Sales (millions)	0.9	1.3	1.8	4.1	10.5	15.8	20.6	25.7	30.9
% Change		34.0%	47.0%	121.3%	157.5%	50.8%	30.0%	25.0%	20.0%
Plasma TV U.S. Factory-to-Dealer Sales (\$B)	\$0.5	\$1.6	\$2.3	\$3.6	\$5.7	\$6.0	\$6.0	\$5.8	\$5.5
% Change		208.7%	47.6%	53.8%	58.1%	5.9%	(1.4%)	(3.2%)	(5.0%)
% of U.S. Television Sales	3.8%	10.9%	14.0%	19.0%	22.7%	22.7%	21.1%	19.4%	17.8%
Units Sales (millions)	0.1	0.3	0.9	1.6	3.2	3.9	4.4	4.8	5.2
% Change		222.6%	154.4%	88.4%	96.9%	21.4%	12.0%	10.0%	8.0%
Flat Panel TV U.S. Factory-to-Dealer Sales (\$B)	\$0.8	\$2.3	\$3.9	\$6.9	\$14.2	\$18.3	\$21.1	\$23.5	\$25.3
% Change		196.2%	74.2%	74.9%	106.6%	28.8%	15.2%	11.6%	7.5%
% of U.S. Television Sales	5.6%	15.5%	23.4%	36.1%	56.5%	68.7%	74.5%	79.0%	82.3%
Units Sales (millions)	1.0	1.6	2.7	5.7	13.7	19.8	25.0	30.6	36.1
% Change		53.2%	70.0%	110.8%	140.2%	43.9%	26.4%	22.4%	18.1%
Other TV U.S. Factory-to-Dealer Sales (\$B)	\$12.9	\$12.3	\$12.9	\$12.2	\$10.9	\$8.3	\$7.2	\$6.2	\$5.4
% Change		(4.7%)	4.7%	(5.5%)	(10.3%)	(23.8%)	(13.4%)	(13.2%)	(13.0%)
% of U.S. Television Sales	94.4%	84.5%	76.6%	63.9%	43.5%	31.3%	25.5%	21.0%	17.7%
Units Sales (millions)	31.3	29.6	29.1	26.1	21.1	11.9	10.9	9.9	9.2
% Change		(5.7%)	(1.6%)	(10.4%)	(19.1%)	(43.3%)	(9.2%)	(8.4%)	(7.8%)
Total TV U.S. Factory-to-Dealer Sales (\$B)	\$13.6	\$14.5	\$16.8	\$19.0	\$25.1	\$26.6	\$28.2	\$29.8	\$30.7
% Change		6.5%	15.5%	13.3%	31.9%	5.9%	6.3%	5.3%	3.2%
% of Total Consumer Electronics Sales	13.7%	13.7%	14.3%	14.8%	17.2%	17.1%	17.2%	17.1%	16.7%
Units Sales (millions)	32.4	31.2	31.8	31.8	34.8	31.7	35.8	40.5	45.2
% Change		(3.8%)	2.1%	(0.1%)	9.5%	(9.0%)	13.0%	13.0%	11.7%
Consumer Electronics U.S. Factory-to-Dealer Sales (\$B)	\$99.3	\$106.3	\$117.0	\$128.9	\$145.7	\$155.2	\$164.5	\$174.4	\$184.0
% Change		7.1%	10.1%	10.1%	13.1%	6.5%	6.0%	6.0%	5.5%

Source: iSuppli, Consumer Electronics Association (CEA) and TAG estimates.

The CAGRs for LCD and plasma televisions more clearly show the disproportional growth relative to all televisions and the entire industry over the past four years. Although the established base for LCD and plasma was significantly smaller than the other categories in 2002, the scale in the differences of the sales growth rates certainly highlights the outperformance of the advanced television categories.

Exhibit 3

COMPARATIVE SALES CAGRS – 2002-2006E

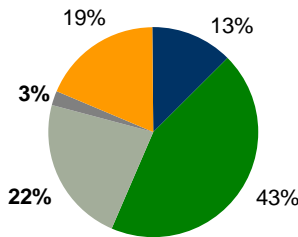
LCD	142.3%
Plasma	82.4%
Total Televisions	16.4%
Total Consumer Electronics	10.1%

Source: Consumer Electronics Association (CEA) and TAG estimates.

Flat Panel Technologies Are Becoming Dominant. The confluence of technological innovation, additional manufacturing capacity, and a highly competitive landscape has led to increased flat panel television affordability, driving sales of these hot items. The following pie charts reflect unit share by technology in 2002 and 2006. LCD televisions expanded to 47% of total digital televisions sold in 2006 from 22% in 2002 and 30% of all televisions sold in 2006 from 2% in 2002. Similarly, plasma televisions increased to 14% of digital television sales in 2006 from 3% in 2002 and 9% of total television sales from less than 1% in 2002.

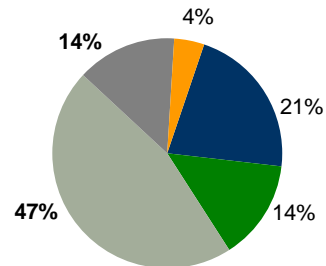
Exhibit 4

UNIT SALES AS A % OF ALL DIGITAL TVS – 2002



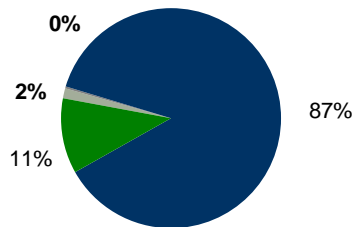
■ Direct ■ Projection ■ LCD ■ Plasma ■ Front Projection

UNIT SALES AS A % OF ALL DIGITAL TVS – 2006E



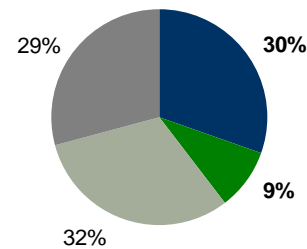
■ Direct ■ Projection ■ LCD ■ Plasma ■ Front Projection

UNIT SALES AS A % OF ALL TVS – 2002



■ LCD ■ Plasma ■ Analog ■ Other

UNIT SALES AS A % OF ALL TVS – 2006E



■ LCD ■ Plasma ■ Analog ■ Other

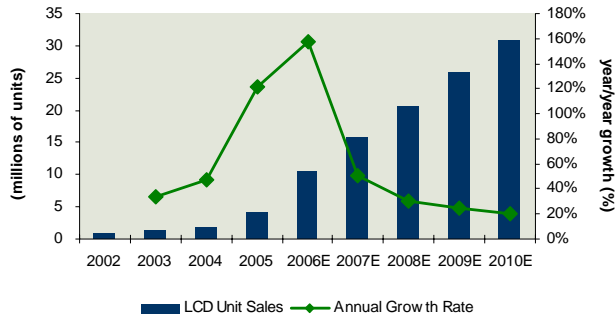
Source: Consumer Electronics Association (CEA) and TAG estimates.

Source: Consumer Electronics Association (CEA) and TAG estimates.

Unit Trends Reinforce Consumers' Preference For LCD Televisions. A closer look at the previous pie charts reflects the increasing dominance of LCD as the technology of choice. The two following charts show unit sales growth of LCD and plasma televisions from 2002 through our 2010 projections, underscoring the explosive sales during this decade. In addition, the unit trends reveal the growing consumer penchant for LCD over plasma as our estimates suggest approximately 25% annual LCD unit growth in 2007-2010, compared with 10% for plasma on a smaller base. The larger LCD screen sizes are encroaching on plasma's historic turf of 40 inches and above. Moreover, as LCD screen sizes push further into the greater than 40 inch area, they likely will continue to take flat panel market share, especially as manufacturers continue to enhance LCD technology. At this year's Consumer Electronics Show in early January, several manufacturers, including Samsung and Toshiba, showed off LCD flat panel televisions with much higher contrast ratios to produce purer blacks and frame refreshes at a speed of 120 mhz versus the current 60 mhz standard to reduce blurring of fast moving objects. These technological improvements will put further pressure on plasma.

Exhibit 5a

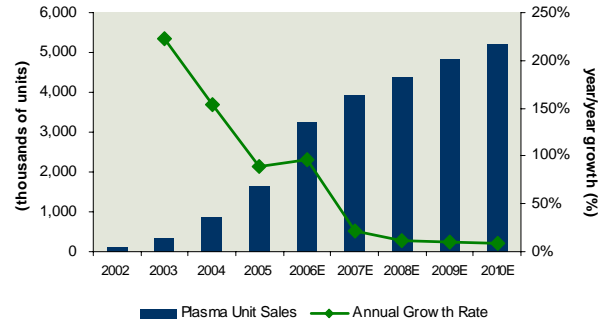
LCD UNIT SALES AND GROWTH



Source: Consumer Electronics Association (CEA) and TAG estimates.

Exhibit 5b

PLASMA UNIT SALES AND GROWTH



Source: Consumer Electronics Association (CEA) and TAG estimates.

LCD Sales Remain Hotly Contested. As the rate and unit volume of LCD television sales have rapidly increased over the last year, the battle for market share dominance has ensued, and in some cases differs from past markets. To be clear, not all LCD television brands manufacture the actual panel (the primary component) of the television, and therefore, there can be some overlap and resulting confusion in interpreting the data. The following data refers only to the companies that assemble the television for retail sales. Later in this report, we address flat panel manufacturing. Based on the data compiled by DigiTimes for iSuppli, we can make a number of observations that help define the LCD market that supplies the consumer electronics retailers.

Exhibit 6a

GLOBAL LCD TV MANUFACTURER SHIPMENT SHARE – 2006

Company	1Q06		2Q06		3Q06		4Q06		2006	
	Share	Rank	Share	Rank	Share	Rank	Share	Rank	Share	Rank
Samsung	12.4%	2	14.2%	2	13.5%	2	16.8%	1	14.6%	1
Philips	12.1%	4	12.4%	4	12.6%	3	15.1%	2	13.4%	2
Sharp	15.2%	1	14.5%	1	13.9%	1	11.4%	4	13.3%	3
Sony	12.3%	3	13.8%	3	11.6%	4	13.1%	3	12.7%	4
LGE	6.7%	5	8.4%	5	7.4%	5	7.8%	5	7.6%	5
Others	41.3%		36.7%		41.0%		35.8%		38.4%	

Source: iSuppli, February 2007.

Exhibit 6b

GLOBAL TV MANUFACTURER SHIPMENT SHARE – 2006

Company	2006	
	Share	Rank
Samsung	10.5%	1
LGE	9.8%	2
TCL	9.2%	3
Philips	8.1%	4
Panasonic	5.4%	5
Others	57.0%	

Source: iSuppli, February 2007.

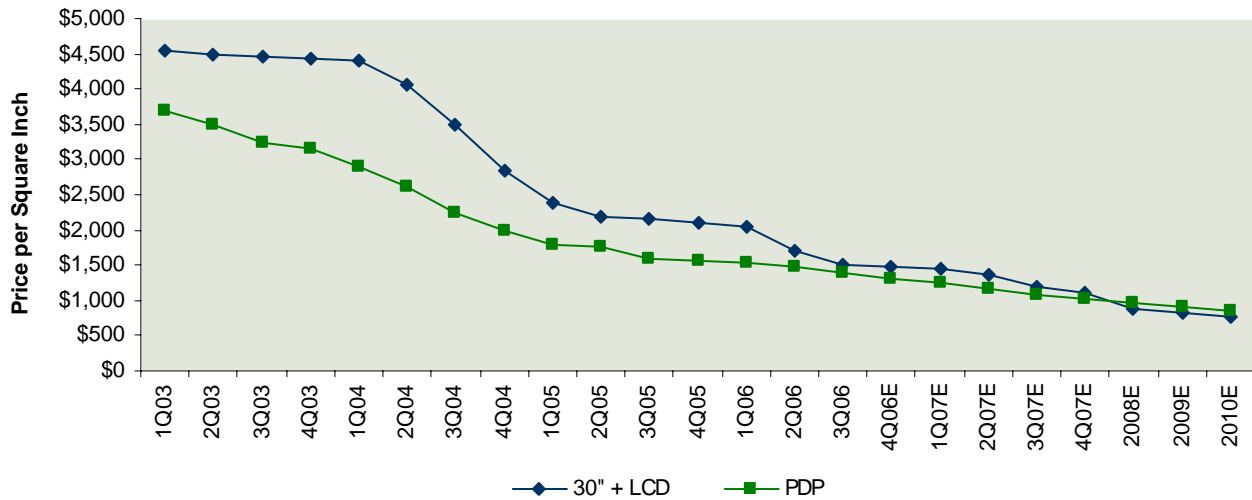
- > The LCD market is somewhat fragmented with the top five players holding a 62% share.
- > Samsung ended 2006 as the leader in LCD shipments. The 2006 quarterly trend points to a solidifying of the top two spots for Samsung and Philips and a clear drop in share for Sharp.
- > Relative to traditional television sales, the LCD television market is more consolidated, with the top five players holding 61.6% of the market share in 2006 versus 43.0% for total televisions. Currently, Samsung holds the top spot within the LCD and total television markets.

Price Declines Define Global and U.S. Flat Panel Market. Superior displays that reproduce images with amazing clarity and dimension, combined with falling prices, have been the primary drivers of advanced television sales. Since 2003, global retail prices per square inch of flat panel televisions 30 inches and above have decreased by approximately 25% per year, according to DisplaySearch. The following exhibit shows the global retail price trends for LCDs and plasma television panels (PDP) since the first quarter of 2003. Consistent with

other industry analysis, we believe that retail price compression will continue at a rate of about 25%-35% per square inch in 2007, moderating to the 20%-25% range in 2008-2010. Note that even though flat panel unit growth is projected to increase in the mid-20% area through 2010, the steady price decreases will pressure dollar growth, limiting sales growth to a mid to upper teens rate.

Exhibit 7

RETAIL PRICES PER SQUARE INCH DECLINES HAVE BEEN A MAJOR DRIVER OF CONSUMER INTEREST



Source: DisplaySearch and TAG estimates.

Black Friday 2006 Data Help Explain Flat Panel Trends. According to The NPD Group’s weekly point-of-sale data (Exhibits 8a and 8b), U.S. LCD television prices in aggregate are estimated to have decreased only 6.8% between Black Friday 2006 (day after Thanksgiving) and the prior year. This seems to conflict with other reports, but the biggest price drops were in plasma televisions, which declined 32.2% on a year-over-year basis. We believe the greater availability and strong demand for larger screen sizes in LCDs (40 and 46 inches this year versus 32 and 37 inches last year) offset the price declines in smaller-sized LCDs. In other words, screen sizes of LCDs “inched up” this year, while plasma screen sizes remained about the same, which translated into more significant plasma price decreases. Many more larger-sized LCDs sold in 2006 versus last year. On a screen size basis, there were dramatic price declines in LCD and plasma televisions. For example, the bellwether 40 inch LCD set sold for an average of \$1,606 in 2006 versus \$3,014 in 2005, a 46% decrease which is more consistent with the price declines seen in the press. For perspective, The NPD Group reported that LCDs above 30 inches experienced 209% sales and 297% unit growth on Black Friday 2006, while LCDs under 30 inches generated 26% sales and 86% unit increases. Plasmas saw a 63% jump in sales and a 140% rise in units.

Exhibit 8a

BLACK FRIDAY AVERAGE TV RETAIL PRICES 2006 VS. 2005

TV Type	2006	2005	% Change
LCD	\$558	\$599	(6.8%)
Projection	\$1,291	\$1,598	(19.2%)
Plasma	\$1,451	\$2,139	(32.2%)
Tube	\$165	\$189	(12.7%)
TV Combos	\$167	\$213	(21.6%)

Source: The NPD Group.

Exhibit 8b

BLACK FRIDAY TV UNIT SHARE 2006 VS. 2005

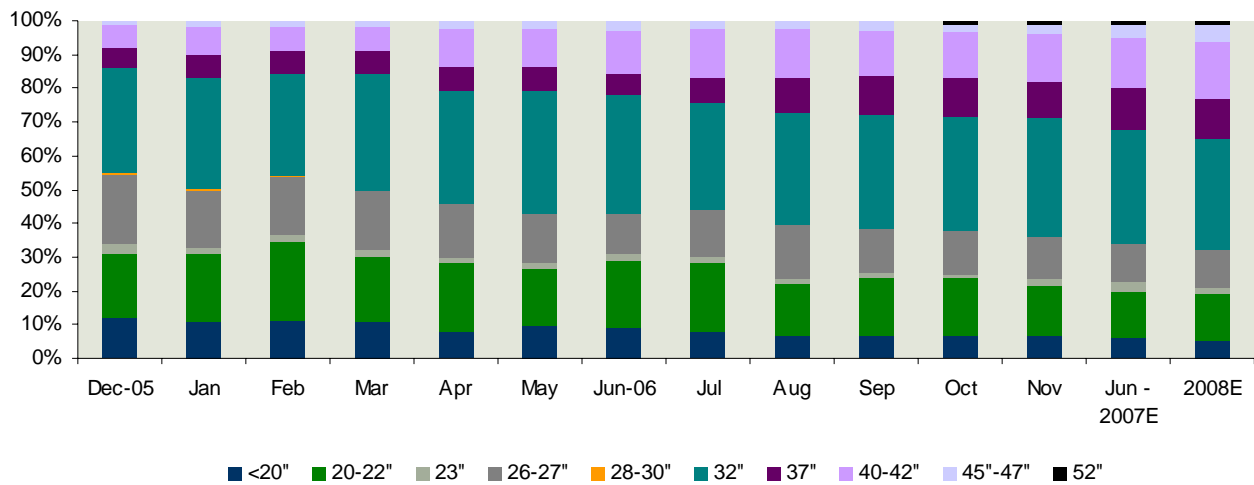
TV Type	2006	2005	% Change
LCD	48.9%	27.1%	80.2%
Projection	7.0%	8.0%	(13.0%)
Plasma	10.1%	5.4%	88.2%
Tube	21.0%	47.9%	(56.1%)
TV Combos	13.0%	11.6%	12.5%

Source: The NPD Group

Falling Prices Impact the Purchase of Larger Size Television. From our channel checks, management discussions, and research, we have found that consumers allotting certain amounts for the purchase of flat panel televisions have taken advantage of falling prices by maintaining their intended budget and trading up to bigger televisions. We believe that as price drops continue, screen sizes greater than 37 inches will grow in share to the mid-30% range by 2008 from approximately 29% in November 2006 and 14% in December 2005. Our mid-30% estimate by 2008 takes into consideration the slowing of price declines and growth over a larger base, and could prove to be conservative if prices fall faster than we anticipate. Importantly, as larger screen sizes with more innovative technologies become more affordable, we believe consumers will more readily purchase products and services that enhance their home entertainment experience, spurring sales of higher margin attachments.

Exhibit 9

LCD TV SIZE SHARE (UNIT BASIS)



Source: The NPD Group and TAG estimates.

Current Operating Environment

New Entrants Crowding the Market. Attempting to capitalize on growing demand for advanced televisions, non-traditional consumer electronics retailers have joined the selling fray. For example, this past holiday season, Home Depot offered a limited selection of flat panels in stores and a much more extensive selection online. We do not expect Home Depot to repeat this in the near future, based on our conversations with the company. Similarly, Office Depot entered the market with an in-store selection of 12 television models during the fourth quarter of 2006. There are several other examples of retailers introducing and/or expanding television departments. Wal-Mart, for example, continues to increase its focus on flat panel televisions, hoping to leverage unparalleled sourcing and distribution capabilities. In some cases, flat panels have been positioned as loss leaders—sold at little or no profit, used solely to capture market share as well as to generate store traffic and sales of other more profitable products. This strategy did not prove to be profitable for the consumer electronics retailers this past holiday season and they will have to do a better job of attaching higher margin sales to flat panel televisions. The crowded playing field could continue to precipitate price wars and compress margins in 2007 and beyond. In fact, less established brands, such as Apex and Vizio, continue to take market share. As previously mentioned, we believe that prices will continue to fall at a rate of about 25%-35% per square inch in 2007 due to manufacturing improvements, production increases, and pricing pressure.

Production and Technology Enhancements Drive Price Decreases. Flat panel television manufacturers have aggressively positioned themselves to participate in the extended product cycle. Manufacturing innovations have reduced time to market and assembly costs, resulting in flat panel production efficiencies and cost savings. Because of the short half-lives of television technology, retailers with excess inventory can be forced to discount prices in order to liquidate obsolete inventories. A recent example of this was the 2006 World Cup soccer tournament where it was believed the event would spur television sales. Demand was not as robust as anticipated, resulting in deep discounts aimed at eliminating the overhang.

The National Football League's Super Bowl on February 4 was the most recent viewing milestone. We tracked it closely to gain further insight into the state of the industry. We were pleased to see that the tenor of discounting was different than this past holiday season. Recent promoting was done through longer periods of zero interest rate financing rather than taking significant unit price cuts. Note that the cost of financing promotions is shared with the credit companies, helping to make this form of discounting have less severe an impact on profits. According to the Retail Advertising and Marketing Association's (RAMA) 2007 Super Bowl Intentions and Actions Survey, approximately 2.5 million consumers had planned to purchase a high definition television (the majority of which were flat panels) prior to the big game, up from roughly 1.7 million last year. Interestingly, sales in Indiana and Illinois, home states of the Indianapolis Colts and Chicago Bears, respectively, were up an estimated 67% and 27%, respectively. According to some reports, 42-inch high-definition sets for as little as \$1,000 were among the biggest sellers leading up to the Super Bowl. With additional costs of roughly \$200 for installation, \$100 for cables, a minimum of \$200 for five surround-sound speakers, and the price of a subscription to HDTV content, the final tab could come in close to \$2,000.

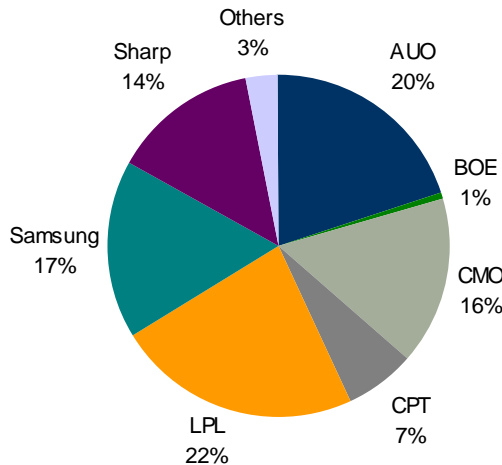
Manufacturing Discipline is Key to Price Support. In order to avoid the same rapid commoditized fate as DVD players, we believe manufacturing overcapacity must be rationalized. Even with discipline, flat panel televisions will continue to experience price declines as capacity and technology become cheaper. We expect to see some stabilization in 2007 given that only three new display facilities are scheduled to open in 2007 versus seven in 2006, according to glass manufacturer, Corning Inc. Another information source suggests that only two new facilities will open in 2007.

Despite the reduction in new facilities, production targets remain mixed in the near term. Some suppliers are posturing to increase capacity, while others reflect a more rational approach. LG Philips indicated that profitability and prudence will be a focus in 2007, implying that production cuts may be the plan. On the other hand, Samsung and Sharp have both indicated that factory utilization would not be trimmed, citing an improvement in annual demand prospects and limited capacity growth in seventh-generation (and above) panels. In December

2006, Sony boosted its 2007 LCD television sales target to ten million units from six million units. Similarly, in January 2007, Samsung projected it will sell 13.5 million flat panels (11 million LCDs and 2.5 million plasmas) units this year on top of 7.5 million last year (6.2 million LCDs and 1.3 million plasmas). The manufacturers would be wise to control growth to maintain pricing and profitability on a product cycle that can last many more years. Unfortunately, the rush to capture market share may cause history to repeat itself, leading to rapid price drops and razor-thin profit margins.

Exhibit 10a

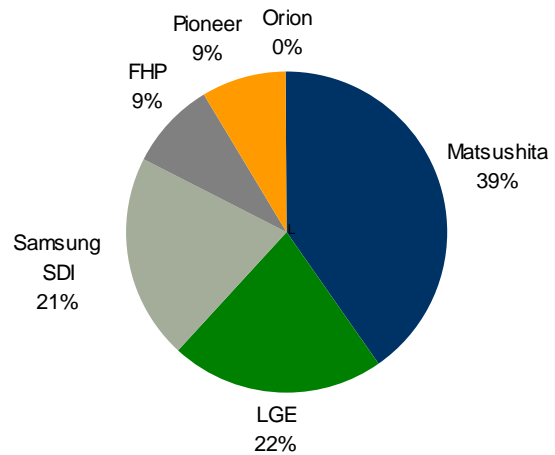
LCD TV SUPPLIER SHARE (UNITS)



Source Display Search and TAG estimates.

Exhibit 10b

PLASMA TV SUPPLIER SHARE (UNITS)



Source Display Search and TAG estimates.

Greater than Expected Price Drops During Holiday 2006. It was widely projected that overall (blended LCD and plasma) retail prices would decrease by roughly 30% on same size screens in 2006 with similar drops estimated for future years. However, price declines came closer to 40% on same size screens. A heightened focus on capturing market share by both the retailers and manufacturers drove the unprecedented discounting. The industry participants appear to have learned their lesson for the time being. The competitive environment before the Super Bowl was more rational, with stable pricing and the use of financing offers to drive traffic.

Attachment Rates Have Not Been as Good as Expected. Revenues from attachments of high margin accessories, services, extended warranties, and home theater components have been solid, but not as strong as planned, according to Best Buy and Circuit City. Part of the attachment shortfall was self-imposed, specifically on Black Friday, when the focus was on processing sales rather than adding on attachments. With the exception of accessories and cables, we did not see or hear many new flat panel television buyers being offered installation, warranties, or audio to complete their purchase. Short term profits were forgone for market share gains. However, as flat panel televisions become more affordable, priorities continue to evolve.

Based on a 2006 customer survey conducted by IDC, “price concerns towered over all others on the list including display technology, screen size, and even brand.” The survey also indicated that more than 60% of respondents (high income demographic) expect to pay less than \$2,000 for a new television. Given the price sensitivity of television buyers, we believe the consumer electronics retailer that is able to provide the most value through the simplest and most comprehensive solutions will see attachment rates outperform the competition. Moreover, we believe the higher the price and larger the screen size, the more likely a consumer will purchase a fuller complement of attachments. Anecdotal evidence points to roughly \$1,000 and 32-inch screen sizes as the breakpoints for when customers buy extended service plans and installation services.

Selection and Service Favor Consumer Electronics Retailers. We believe the consumer electronics retailers, particularly Best Buy and Circuit City, remain well-positioned because of an unmatched selection of flat panel television brands and sizes, knowledgeable associates, extended warranty offerings, home theater audio sales, installation capabilities, scope of ancillary products, and generally perceived better customer service. The aforementioned list helps to insulate the major consumer electronics retailers from discount and online retailers. Flat panel margins were expected to remain robust despite declining prices, but the desire for market share led to irrational pricing behavior this past holiday season.

The key question is whether sales of cables, power surge protectors, warranties, installation, and larger screen sizes will be enough to offset the margin erosion related to flat panel price decreases. The answer, in our opinion, is yes and is explored further in the next section.

Making Money Selling Flat Panel Televisions

Flat Panel Attachment Sales are the Key to Profitability. As LCD and plasma margins continue to decline, sales of related accessories and services become increasingly important to the profitability of Best Buy and Circuit City. It is important to understand that the retailers are not losing money selling flat panel televisions; rather the money they make on them is decreasing. Our goal is to understand the rate of profit decline on flat panel televisions and whether or not attachments of accessories and services will make up the shortfall. Because conversion rates and profit margins of ancillary sales are largely unknown, we attempt to forecast a number of scenarios aimed at framing the conversation.

CONTRIBUTION TO EARNINGS

Building Projections for Flat Panel Television Sales. On an aggregate basis, we start with our U.S. consumer electronics wholesale assumptions introduced earlier. Recall that we look for a return to a more normalized annual sales growth rate of 5%-7% in 2008 to 2010, as declining television prices crimp overall revenue expansion. We then estimate annual television unit volume and price changes for LCD, plasma, other digital, and analog televisions, resulting in sales for each category as well as total televisions. Building off the CEA's sales estimates through 2007, we project annual LCD unit growth of about 25% and wholesale price declines of 6% between 2008 and 2010. Our plasma television projections assume about 10% annual unit increases and 12% yearly wholesale price declines for the same period. Note that we expect LCD to increasingly take share in flat panel televisions through the end of the decade. Based on our unit and average price estimates, we believe U.S. wholesale LCD television unit sales will reach 30.9 million units and \$19.8 billion in sales, or 64.5% of the sales generated by total U.S. television market, in 2010 versus 10.5 million units and \$8.5 billion in sales, or 33.8% of the market's sales in 2006.

Exhibit 11

LCD AND PLASMA TELEVISION SALES AND AVERAGE PRICES

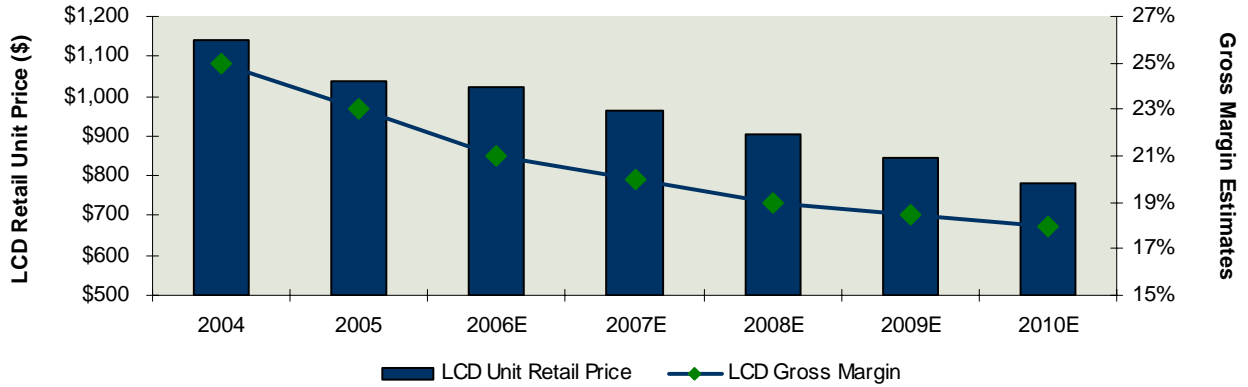
Year	LCD		LCD		LCD		Plasma		Plasma		Plasma	
	Unit Sales Thousands	% Change	Total Sales \$B	% Change	Average Price \$	% Change	Unit Sales Thousands	% Change	Total Sales \$B	% Change	Average Price \$	% Change
2002	935		\$0.2		\$263		106		\$515.0		\$4,858	
2003	1,253	34.0%	\$0.7	169.9%	\$530	101.4%	342	222.6%	\$1,590.0	208.7%	\$4,649	(4.3%)
2004	1,842	47.0%	\$1.6	137.8%	\$857	61.8%	870	154.4%	\$2,347.0	47.6%	\$2,698	(42.0%)
2005	4,077	121.3%	\$3.3	106.3%	\$799	(6.8%)	1,639	88.4%	\$3,609.0	53.8%	\$2,202	(18.4%)
2006E	10,500	157.5%	\$8.5	160.3%	\$808	1.1%	3,228	96.9%	\$5,705.0	58.1%	\$1,767	(19.7%)
2007E	15,831	50.8%	\$12.2	44.2%	\$772	(4.4%)	3,920	21.4%	\$6,044.0	5.9%	\$1,542	(12.8%)
2008E	20,580	30.0%	\$15.1	23.5%	\$734	(5.0%)	4,390	12.0%	\$5,957.0	(1.4%)	\$1,357	(12.0%)
2009E	25,725	25.0%	\$17.7	17.5%	\$690	(6.0%)	4,829	10.0%	\$5,766.3	(3.2%)	\$1,194	(12.0%)
2010E	30,870	20.0%	\$19.8	11.6%	\$641	(7.0%)	5,216	8.0%	\$5,480.3	(5.0%)	\$1,051	(12.0%)

Source: Consumer Electronics Association (CEA) and TAG estimates.

Grossing Up Wholesale Prices. In order to relate our wholesale industry assumptions to Best Buy's and Circuit City's retail operations, we marked up our wholesale unit price estimates by an average in the low 20% area. For LCD televisions, our estimated retail unit prices imply a gross margin of 18.0% in 2010, a 300 basis point decline from 21.0% in 2006. Our gross margin assumptions are based on our analysis of the sector and discussions with industry experts.

Exhibit 12

LCD AVERAGE UNIT RETAIL PRICES AND GROSS MARGINS – 2004-2010E

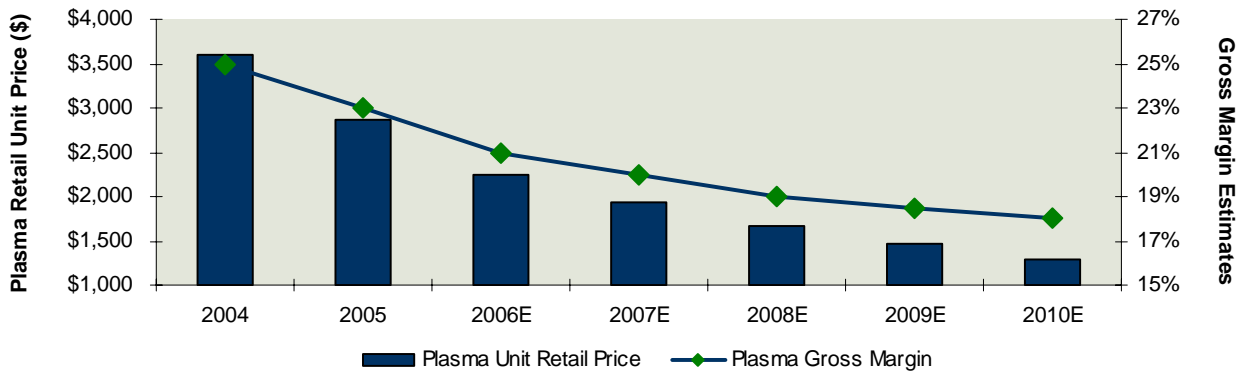


Source: Consumer Electronics Association (CEA) and TAG estimates.

Applying the same rationale to the mark-up process for plasma screens, we estimate gross margins average 18.5% in 2008-2010, down 250 basis points from approximately 21% in 2006, and materially lower than an estimated 25% in 2004.

Exhibit 13

PLASMA AVERAGE UNIT RETAIL PRICES AND GROSS MARGINS – 2004-2010E



Source: Consumer Electronics Association (CEA) and TAG estimates.

Projecting Best Buy's and Circuit City's Flat Panel Sales. Because our wholesale analysis considers only U.S. data, to maintain consistency, we looked only at domestic sales of both retailers. In Best Buy's case, we expect U.S. sales to expand to \$49.0 billion in 2010 (85% of total company sales) from an estimated \$30.6 billion in 2006 (86% of total sales). The slight decline in Best Buy's U.S. business as a percent of total sales in 2010 is due to the company's ongoing commitment to international expansion. Circuit City's domestic sales are more leveraged to the U.S. We project Circuit City's domestic sales will grow to \$17.4 billion (95.3% of total company sales) in 2010 from \$12.0 billion (94.8% of sales) in 2006. We then estimate the size of each company's consumer electronics sales based on the reported annual share of total revenues. For perspective, in 2006, we believe the consumer electronics category was in the mid-forty percent range of total revenues for the two companies.

In order to estimate Best Buy's and Circuit City's television sales, we assume 20%-29% share of each company's consumer electronics category (2002-2010) versus our calculated industry average of 13%-19%. Our assumptions are based on CEA data and our belief that both companies have an increased focus on television sales relative to other retailers. Finally, we use industry sales rates of LCD and plasma televisions (percent of total television sales) as a proxy to gauge revenue attributable to flat panel units. Again, due to the specialization factor of the respective businesses, we assume a higher ratio of advanced television sales versus the rest of the industry. We project Best Buy's sales of flat panel televisions will grow at a CAGR of 27.1% to \$12.7 billion in sales in 2010 from an estimated \$4.9 billion in 2006. Over the same time horizon, we expect Circuit City's flat panel television sales to increase at a CAGR of 23.6% to \$4.5 billion in 2010 from \$1.9 billion in 2006. Our detailed projections are highlighted in the Exhibits 14 and 15.

Exhibit 14

BEST BUY'S LCD AND PLASMA TELEVISION SALES

\$ in millions	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
Total Sales	\$20,946	\$24,548	\$26,940	\$30,848	\$35,634	\$40,230	\$45,411	\$51,187	\$57,478
% Change		17.2%	9.7%	14.5%	15.5%	12.9%	12.9%	12.7%	12.3%
U.S. Sales	\$19,303	\$22,228	\$24,124	\$27,380	\$30,643	\$34,464	\$38,779	\$43,626	\$48,858
% Change		15.2%	8.5%	13.5%	11.9%	12.5%	12.5%	12.5%	12.0%
% of Total BBY Sales	92.2%	90.5%	89.5%	88.8%	86.0%	85.7%	85.4%	85.2%	85.0%
% of Total U.S. Industry Sales	19.4%	20.9%	20.6%	21.2%	21.0%	22.2%	23.6%	25.0%	26.6%
U.S. Consumer Electronics Sales	\$7,142	\$8,447	\$9,408	\$11,773	\$14,096	\$15,853	\$17,838	\$20,068	\$22,475
% Change		18.3%	11.4%	25.1%	19.7%	12.5%	12.5%	12.5%	12.0%
% of Total BBY U.S. Sales	37.0%	38.0%	39.0%	43.0%	46.0%	46.0%	46.0%	46.0%	46.0%
U.S. Television Sales	\$3,928	\$4,646	\$5,363	\$6,946	\$8,599	\$9,829	\$11,202	\$12,643	\$14,226
% Change		18.3%	15.4%	29.5%	23.8%	14.3%	14.0%	12.9%	12.5%
% of Total BBY U.S. Sales	20.4%	20.9%	22.2%	25.4%	28.1%	28.5%	28.9%	29.0%	29.1%
Total Flat Panel Television Sales	\$219	\$721	\$1,254	\$2,508	\$4,862	\$7,042	\$9,145	\$10,962	\$12,705
% Change		229.0%	74.1%	99.9%	93.9%	44.8%	29.9%	19.9%	15.9%
% of Total U.S. Television Sales	5.6%	15.5%	23.4%	36.1%	56.5%	71.6%	81.6%	86.7%	89.3%
Unit Sales (Thousands)	216	372	650	1,607	3,717	6,094	8,752	11,543	14,768
LCD Television Sales	\$71	\$212	\$505	\$1,190	\$2,907	\$4,718	\$6,491	\$8,132	\$9,740
% Change		199.8%	137.6%	135.8%	144.3%	62.3%	37.6%	25.3%	19.8%
% of Total U.S. Television Sales	1.8%	4.6%	9.4%	17.1%	33.8%	48.0%	57.9%	64.3%	68.5%
Unit Sales (Thousands)	194	292	441	1,146	2,843	4,888	7,167	9,612	12,454
Plasma Television Sales	\$148	\$508	\$750	\$1,318	\$1,956	\$2,324	\$2,654	\$2,830	\$2,966
% Change		242.9%	47.5%	75.7%	48.4%	18.8%	14.2%	6.6%	4.8%
% of Total U.S. Television Sales	3.8%	10.9%	14.0%	19.0%	22.7%	23.6%	23.7%	22.4%	20.8%
Unit Sales (Thousands)	22	80	208	461	874	1,206	1,584	1,931	2,314

Source: Consumer Electronics Association (CEA), company reports, and TAG estimates.

Exhibit 15

CIRCUIT CITY'S LCD AND PLASMA TELEVISION SALES

\$ in millions	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
Total Sales	\$9,954	\$10,321	\$10,470	\$11,588	\$12,623	\$13,536	\$15,002	\$16,630	\$18,266
% Change		3.7%	1.4%	10.7%	8.9%	7.2%	10.8%	10.9%	9.8%
U.S. Sales	\$9,954	\$9,857	\$10,017	\$10,974	\$11,960	\$12,842	\$14,253	\$15,821	\$17,400
% Change		(1.0%)	1.6%	9.6%	9.0%	7.4%	11.0%	11.0%	10.0%
% of Total CC Sales	100.0%	95.5%	95.7%	94.7%	94.8%	94.9%	95.0%	95.1%	95.3%
% of Total U.S. Industry Sales	10.0%	9.3%	8.6%	8.5%	8.2%	8.3%	8.7%	9.1%	9.5%
U.S. Consumer Electronics Sales	\$3,981	\$4,041	\$4,207	\$4,829	\$5,502	\$5,907	\$6,556	\$7,278	\$8,004
% Change		1.5%	4.1%	14.8%	13.9%	7.4%	11.0%	11.0%	10.0%
% of Total CC U.S. Sales	40.0%	41.0%	42.0%	44.0%	46.0%	46.0%	46.0%	46.0%	46.0%
U.S. Television Sales	\$2,269	\$2,304	\$2,440	\$2,849	\$3,411	\$3,680	\$4,098	\$4,534	\$4,979
% Change		1.5%	5.9%	16.8%	19.7%	7.9%	11.3%	10.6%	9.8%
% of Total CC U.S. Sales	22.8%	23.4%	24.4%	26.0%	28.5%	28.7%	28.8%	28.7%	28.6%
Total Flat Panel Television Sales	\$127	\$357	\$571	\$1,028	\$1,929	\$2,567	\$3,374	\$3,922	\$4,496
% Change		182.3%	59.7%	80.2%	87.6%	33.1%	31.4%	16.3%	14.6%
% of Total U.S. Television Sales	5.6%	15.5%	23.4%	36.1%	56.5%	69.7%	82.3%	86.5%	90.3%
Unit Sales (Thousands)	125	185	296	659	1,475	2,207	3,229	4,129	5,232
LCD Television Sales	\$41	\$105	\$230	\$488	\$1,153	\$1,693	\$2,395	\$2,907	\$3,458
% Change		157.3%	118.0%	112.5%	136.3%	46.8%	41.5%	21.4%	18.9%
% of Total U.S. Television Sales	1.8%	4.6%	9.4%	17.1%	33.8%	46.0%	58.4%	64.1%	69.5%
Unit Sales (Thousands)	112	145	201	470	1,128	1,754	2,644	3,436	4,422
Plasma Television Sales	\$86	\$252	\$341	\$541	\$776	\$874	\$979	\$1,015	\$1,038
% Change		194.3%	35.3%	58.4%	43.5%	12.6%	12.0%	3.7%	2.3%
% of Total U.S. Television Sales	3.8%	10.9%	14.0%	19.0%	22.7%	23.7%	23.9%	22.4%	20.8%
Unit Sales (Thousands)	13	40	95	189	347	453	584	693	810

Source: Consumer Electronics Association (CEA), company reports, and TAG estimates.

Flat Panel Television Income Statements. Our attention then turned to the profitability of the advanced television segment with the intention to understand what percentage it was of each company's profits and how it would be attributed to LCD and plasma sales. We also wanted to identify how flat panel television profits trended over time, identifying periods of peak profitability and gauging each company's ability to offset declining margins with sales of ancillary products. Our major assumptions include:

- > We estimated that the gross margins for LCD and plasma televisions are about the same.
- > Best Buy's combined flat panel gross margin is estimated to reach 21% in 2006, 19% in 2008 and 18% in 2010. Circuit City's is projected to come in at 20% in 2006, 18% in 2008, and 17% in 2010.
- > We applied corporate SG&A rates to flat panel profits. For Best Buy, we estimate a domestic SG&A ratio of 18.7% in 2006 and gradual annual declines to 17.7% in 2008 and 16.9% in 2010. Similarly, our domestic SG&A ratio projection for Circuit City is 21.6% in 2006, with decreases to 20.9% in 2008 and 20.3% in 2010.
- > No allocation of interest income or expense in order to avoid unintentional benefit or penalty and maintain the operational focus on the business.

Best Buy's Flat Panel Television Contribution to EPS May Peak in 2007. We expect profits from Best Buy's flat panel television sales to reach 5.5% of annual EPS of \$3.29 in 2007, similar to our estimate of 5.5% of \$2.79 in 2006. Despite the CEA's belief that the average LCD television price declines another 4%-6% during 2007, we believe the mix of LCD unit sales and more affordable yet still profitable pricing will drive the year's results. In our Best Buy model, LCD and plasma television profits represent an estimated 3.7% and 1.8%, respectively of 2007 EPS. Interestingly, the share of profit from LCD televisions reaches its zenith in 2007, while plasma profit has been decreasing since 2005 due to increasing demand of LCD technology. Note that we did not strip out corporate general and administrative expenses—an estimated 2%-4% of total annual sales—from our analysis.

Exhibit 16

BEST BUY FLAT PANEL INCOME STATEMENT

\$ in millions, except per share data	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
LCD Sales	\$70.8	\$212.3	\$504.5	\$1,189.7	\$2,906.7	\$4,717.9	\$6,490.9	\$8,132.0	\$9,739.5
% Change		199.8%	137.6%	135.8%	144.3%	62.3%	37.6%	25.3%	19.8%
Plasma Sales	\$148.3	\$508.4	\$749.9	\$1,317.9	\$1,955.5	\$2,324.0	\$2,653.6	\$2,829.6	\$2,965.5
% Change		242.9%	47.5%	75.7%	48.4%	18.8%	14.2%	6.6%	4.8%
Total Flat Panel Sales	\$219.1	\$720.8	\$1,254.5	\$2,507.6	\$4,862.3	\$7,041.9	\$9,144.5	\$10,961.6	\$12,705.0
% Change		229.0%	74.1%	99.9%	93.9%	44.8%	29.9%	19.9%	15.9%
LCD Gross Profit	\$19.8	\$57.3	\$126.1	\$273.6	\$610.4	\$943.6	\$1,233.3	\$1,504.4	\$1,753.1
Plasma Gross Profit	\$41.5	\$137.3	\$187.5	\$303.1	\$410.7	\$464.8	\$504.2	\$523.5	\$533.8
Total Flat Panel Gross Profit	\$61.4	\$194.6	\$313.6	\$576.8	\$1,021.1	\$1,408.4	\$1,737.5	\$2,027.9	\$2,286.9
LCD Gross Margin Assumption	28.0%	27.0%	25.0%	23.0%	21.0%	20.0%	19.0%	18.5%	18.0%
Plasma Gross Margin Assumption	28.0%	27.0%	25.0%	23.0%	21.0%	20.0%	19.0%	18.5%	18.0%
Total Flat Panel Gross Margin Assumption	28.0%	27.0%	25.0%	23.0%	21.0%	20.0%	19.0%	18.5%	18.0%
LCD SG&A Expenses	\$14.0	\$39.0	\$91.9	\$232.2	\$542.8	\$852.4	\$1,148.6	\$1,407.7	\$1,649.4
Plasma SG&A Expenses	\$29.4	\$93.5	\$136.6	\$257.2	\$365.2	\$419.9	\$469.6	\$489.8	\$502.2
Total Flat Panel SG&A Expenses	\$43.4	\$132.5	\$228.6	\$489.4	\$908.0	\$1,272.3	\$1,618.2	\$1,897.6	\$2,151.6
Domestic SG&A Expense Ratio	19.8%	18.4%	18.2%	19.5%	18.7%	18.1%	17.7%	17.3%	16.9%
LCD Operating Income	\$5.8	\$18.3	\$34.2	\$41.4	\$67.6	\$91.2	\$84.7	\$96.7	\$103.7
Plasma Operating Income	\$12.2	\$43.8	\$50.8	\$45.9	\$45.5	\$44.9	\$34.6	\$33.6	\$31.6
Total Flat Panel Operating Income	\$18.0	\$62.1	\$85.1	\$87.4	\$113.1	\$136.1	\$119.3	\$130.3	\$135.3
LCD Operating Margin	8.2%	8.6%	6.8%	3.5%	2.3%	1.9%	1.3%	1.2%	1.1%
Plasma Operating Margin	8.2%	8.6%	6.8%	3.5%	2.3%	1.9%	1.3%	1.2%	1.1%
Total Flat Panel Operating Margin	8.2%	8.6%	6.8%	3.5%	2.3%	1.9%	1.3%	1.2%	1.1%
Tax Rate	38.7%	38.3%	35.3%	33.8%	33.2%	34.5%	34.5%	34.5%	34.5%
LCD Net Income	\$3.6	\$11.3	\$22.1	\$27.5	\$45.2	\$59.7	\$55.4	\$63.3	\$67.9
Plasma Net Income	\$7.4	\$27.1	\$32.9	\$30.4	\$30.4	\$29.4	\$22.7	\$22.0	\$20.7
Total Flat Panel Net Income	\$11.0	\$38.4	\$55.0	\$57.9	\$75.5	\$89.1	\$78.1	\$85.3	\$88.6
LCD EPS	\$0.01	\$0.02	\$0.04	\$0.05	\$0.09	\$0.12	\$0.11	\$0.13	\$0.14
Plasma EPS	\$0.02	\$0.05	\$0.07	\$0.06	\$0.06	\$0.06	\$0.05	\$0.05	\$0.04
Total Flat Panel EPS	\$0.02	\$0.08	\$0.11	\$0.11	\$0.15	\$0.18	\$0.16	\$0.18	\$0.18
Total EPS	\$1.27	\$1.60	\$1.80	\$2.25	\$2.79	\$3.29	\$3.88	\$4.58	\$5.38
LCD EPS	0.6%	1.4%	2.4%	2.4%	3.3%	3.7%	2.9%	2.8%	2.6%
Plasma EPS	1.2%	3.4%	3.6%	2.7%	2.2%	1.8%	1.2%	1.0%	0.8%
Total Flat Panel EPS	1.8%	4.8%	6.1%	5.1%	5.5%	5.5%	4.1%	3.8%	3.4%
Shares Outstanding	487.2	500.9	504.9	506.9	496.2	490.6	487.8	485.8	483.8

Source: Consumer Electronics Association (CEA), company reports, and TAG estimates.

Circuit City's Flat Panel Profits Could Have Been the Highest in 2003. Based on our assumptions, Circuit City has struggled to achieve breakeven EPS selling flat panels, mainly because the company's gross margin is lower than Best Buy due to retailing the items at a lower price and it has a higher expense structure. Note that we fully allocated the SG&A expense ratio to the flat panel television business and did not attempt to strip out corporate general and administrative expenses, which amounts to about 2.5% of total sales. The company came close to breakeven in 2005. However, the accelerated promotional environment in 2006 led to gross margin erosion. We estimate that flat panel televisions may have dragged down EPS by about \$0.12 in 2006. Although Circuit City should continue to generate gross profit dollars by selling flat panel televisions, we project continued gross margin erosion, leading to flat panel television losses at the EPS level in 2007 and beyond.

Exhibit 17

CIRCUIT CITY FLAT PANEL INCOME STATEMENT

\$ in millions, except per share data	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
LCD Sales	\$40.9	\$105.3	\$229.6	\$487.9	\$1,153.1	\$1,692.9	\$2,394.8	\$2,907.3	\$3,458.2
% Change		157.3%	118.0%	112.5%	136.3%	46.8%	41.5%	21.4%	18.9%
Plasma Sales	\$85.7	\$252.1	\$341.2	\$540.5	\$775.8	\$873.8	\$978.8	\$1,014.8	\$1,037.8
% Change		194.3%	35.3%	58.4%	43.5%	12.6%	12.0%	3.7%	2.3%
Total Flat Panel Sales	\$126.6	\$357.4	\$570.8	\$1,028.4	\$1,928.9	\$2,566.7	\$3,373.6	\$3,922.1	\$4,496.0
% Change		182.3%	59.7%	80.2%	87.6%	33.1%	31.4%	16.3%	14.6%
LCD Gross Profit	\$11.0	\$27.4	\$55.1	\$107.3	\$230.6	\$321.6	\$431.1	\$508.8	\$587.9
Plasma Gross Profit	\$23.1	\$65.5	\$81.9	\$118.9	\$155.2	\$166.0	\$176.2	\$177.6	\$176.4
Total Flat Panel Gross Profit	\$34.2	\$92.9	\$137.0	\$226.3	\$385.8	\$487.7	\$607.3	\$686.4	\$764.3
LCD Gross Margin Assumption	27.0%	26.0%	24.0%	22.0%	20.0%	19.0%	18.0%	17.5%	17.0%
Plasma Gross Margin Assumption	27.0%	26.0%	24.0%	22.0%	20.0%	19.0%	18.0%	17.5%	17.0%
Total Flat Panel Gross Margin Assumption	27.0%	26.0%	24.0%	22.0%	20.0%	19.0%	18.0%	17.5%	17.0%
LCD SG&A Expenses	\$9.8	\$24.8	\$56.9	\$108.7	\$249.2	\$358.8	\$500.4	\$598.8	\$701.9
Plasma SG&A Expenses	\$20.6	\$59.4	\$84.6	\$120.4	\$167.6	\$185.2	\$204.6	\$209.0	\$210.6
Total Flat Panel SG&A Expenses	\$30.4	\$84.2	\$141.5	\$229.1	\$416.8	\$544.1	\$705.0	\$807.8	\$912.6
Domestic SG&A Expense Ratio	24.0%	23.6%	24.8%	22.3%	21.6%	21.2%	20.9%	20.6%	20.3%
LCD Operating Income	\$1.2	\$2.6	(\$1.8)	(\$1.3)	(\$18.6)	(\$37.2)	(\$69.4)	(\$90.0)	(\$114.0)
Plasma Operating Income	\$2.6	\$6.1	(\$2.7)	(\$1.5)	(\$12.5)	(\$19.2)	(\$28.4)	(\$31.4)	(\$34.2)
Total Flat Panel Operating Income	\$3.8	\$8.7	(\$4.5)	(\$2.8)	(\$31.1)	(\$56.4)	(\$97.7)	(\$121.5)	(\$148.2)
LCD Operating Margin	3.0%	2.4%	(0.8%)	(0.3%)	(1.6%)	(2.2%)	(2.9%)	(3.1%)	(3.3%)
Plasma Operating Margin	3.0%	2.4%	(0.8%)	(0.3%)	(1.6%)	(2.2%)	(2.9%)	(3.1%)	(3.3%)
Total Flat Panel Operating Margin	3.0%	2.4%	(0.8%)	(0.3%)	(1.6%)	(2.2%)	(2.9%)	(3.1%)	(3.3%)
Tax Rate	37.0%	35.9%	37.4%	36.6%	35.8%	37.6%	36.8%	36.8%	36.8%
LCD Net Income (Loss)	\$0.8	\$1.6	(\$1.1)	(\$0.9)	(\$11.9)	(\$23.2)	(\$43.9)	(\$56.9)	(\$72.1)
Plasma Net Income (Loss)	\$1.6	\$3.9	(\$1.7)	(\$0.9)	(\$8.0)	(\$12.0)	(\$17.9)	(\$19.9)	(\$21.6)
Total Flat Panel Net Income (Loss)	\$2.4	\$5.6	(\$2.8)	(\$1.8)	(\$19.9)	(\$35.2)	(\$61.8)	(\$76.8)	(\$93.7)
LCD EPS	\$0.00	\$0.01	(\$0.01)	(\$0.00)	(\$0.07)	(\$0.14)	(\$0.27)	(\$0.36)	(\$0.47)
Plasma EPS	\$0.01	\$0.02	(\$0.01)	(\$0.01)	(\$0.05)	(\$0.07)	(\$0.11)	(\$0.13)	(\$0.14)
Total Flat Panel EPS	\$0.01	\$0.03	(\$0.01)	(\$0.01)	(\$0.12)	(\$0.21)	(\$0.39)	(\$0.49)	(\$0.61)
Total EPS	(\$0.03)	(\$0.00)	\$0.33	\$0.81	\$0.67	\$0.84	\$1.11	\$1.41	\$1.76
LCD EPS	NM	NM	(1.8%)	(0.6%)	(10.6%)	(16.7%)	(24.7%)	(25.8%)	(26.9%)
Plasma EPS	NM	NM	(2.6%)	(0.6%)	(7.1%)	(8.6%)	(10.1%)	(9.0%)	(8.1%)
Total Flat Panel EPS	NM	NM	(4.4%)	(1.2%)	(17.7%)	(25.4%)	(34.8%)	(34.9%)	(35.0%)
Shares Outstanding	207.2	205.9	196.2	180.7	168.7	164.1	160.3	156.4	152.6

Source: Consumer Electronics Association (CEA), company reports, and TAG estimates.

Profitability Analysis Highlights the Importance of Attachment Sales. Despite differences between Best Buy's and Circuit City's operating models, the two cases reveal the challenges that lay ahead in the flat panel television business. Both companies have laid out lofty goals for operating improvement. Best Buy aims to increase its operating margin to 7% by 2010 from an estimated 5.5% in 2006. Similarly, Circuit City is working to achieve a 5% earnings before taxes (EBT) margin by 2010-2012 from a projected 1.4% in 2006. In order to meet these defined goals, the organizations must maintain, or at least come close to maintaining, their corporate gross margins (BBY 24.7% in 2006E; Circuit City 23.3% in 2006E).

ATTACHMENT ANALYSIS

We set out to understand if sales of related television products could counter the eroding margins on the units themselves. Our primary market and financial assumptions include:

Market Assumptions

- > A healthy demand for services based on the increasing complexity of home theater solutions.
- > The propensity of consumers to insure their purchases and buy complementary products as the average unit price of televisions bought increases.
- > Favorable demographic trends as baby boomers that have accumulated wealth, and are nearing retirement, drive the ongoing shift to do-it-for-me (DIFM) from do-it-yourself (DIY).

Financial Assumptions

- > In order to understand our assumed annual flat panel television gross margin declines in dollar terms, we compared the annual difference in gross profits of estimated sales and gross profits (lower) with the sales and gross margins of 2006 (higher).
- > Attachment sales fall under four categories: installation, warranties, audio, and accessories/cables.

Exhibit 18

BASE CASE ASSUMPTIONS BY TYPE OF ATTACHMENT

Category	Average Price	Unit Attachment Rates	Gross Margin
Installation	\$225	25%	33%-35%
Warranties	\$275	2.8% of sales	50%
Audio	\$300	10%	22%-23%
Accessories/Cables	\$100	85%	50%-55%

Source: TAG estimates.

Growth of Attachment Profits Can Offset Declining Television Profits at Best Buy. We calculated the gross profit lost each year by assuming that Best Buy maintained its 2006 estimated gross margin through 2010 and compared it to the projected gross profit assuming ongoing gross margin erosion. This exercise, in Exhibit 19, indicated that the company would forego \$70 million in gross profit in 2007 and the foregone profit would amount to \$381 million in 2010. We then looked at the four major attachments to flat panel television sales to determine if the profit gained from those sales could offset the annual profit drain from the sale of the actual flat panel television. Our estimates indicate that attachment sales (based on our outlined assumptions) produce \$535 million of profits in 2007, more than exceeding the \$70 million decline from flat panel television gross margin degradation. Our projections through 2010 show attachment profit consistently exceeds the drop in television profit.

We also looked at Best Buy's ability to maintain or grow its total domestic gross margin in spite of the pressure from its flat panel television business. We found that despite the decline in flat panel television profits relative to the total domestic gross margin, Best Buy was able to easily exceed the profit shortfall through the sale of related attachments. However, Best Buy's blended flat panel gross margin (televisions plus attachments) likely will continue to fall short of its total domestic gross margin by 100-170 basis points between 2007 and 2010.

Exhibit 19

BEST BUY ATTACHMENT ANALYSIS

\$ in millions	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
Flat Panel Sales	\$219	\$721	\$1,254	\$2,508	\$4,862	\$7,042	\$9,145	\$10,962	\$12,705
Unit Sales (Thousands)	216	372	650	1,607	3,717	6,094	8,752	11,543	14,768
Gross Profit	\$61	\$195	\$314	\$577	\$1,021	\$1,408	\$1,737	\$2,028	\$2,287
YOY Change in Gross Profit		\$133	\$119	\$263	\$444	\$387	\$329	\$290	\$259
Gross Margin	28.0%	27.0%	25.0%	23.0%	21.0%	20.0%	19.0%	18.5%	18.0%
Gross Profit based on Prior Year / 2006E Gross Margin					\$1,118	\$1,479	\$1,920	\$2,302	\$2,668
YOY Change in Gross Profit due to GM Erosion					(\$97)	(\$70)	(\$183)	(\$274)	(\$381)
Gross Profit based on Total Domestic Gross Margin	\$55	\$174	\$299	\$635	\$1,202	\$1,724	\$2,228	\$2,659	\$3,070
Total Domestic Gross Margin	25.0%	24.1%	23.8%	25.3%	24.7%	24.5%	24.4%	24.3%	24.2%
Flat Panel Gross Profit minus Total Domestic	\$7	\$21	\$15	(\$58)	(\$181)	(\$315)	(\$490)	(\$631)	(\$783)
Installation									
Installation Average Retail Price	\$250	\$250	\$250	\$250	\$250	\$225	\$200	\$175	\$150
Installation Attachment Rate	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Installation Units	54	93	162	402	929	1,523	2,188	2,886	3,692
Installation Sales	\$13	\$23	\$41	\$100	\$232	\$343	\$438	\$505	\$554
Installation Gross Margin	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%
Installation Gross Profit	\$5	\$8	\$14	\$35	\$81	\$120	\$153	\$177	\$194
YOY Change in Gross Profit		\$3	\$6	\$21	\$46	\$39	\$33	\$24	\$17
Warranties									
Warranty Average Retail Price	\$300	\$300	\$300	\$300	\$300	\$275	\$250	\$225	\$200
Warranty Attachment Rate	11.8%	22.6%	19.3%	15.6%	10.9%	10.5%	10.4%	10.6%	10.8%
Warranty Units	26	84	125	251	405	640	914	1,218	1,588
Warranty Sales	\$8	\$25	\$38	\$75	\$122	\$176	\$229	\$274	\$318
Warranty % of Total Sales	3.5%	3.5%	3.0%	3.0%	2.5%	2.5%	2.5%	2.5%	2.5%
Warranty Gross Margin	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%
Warranty Gross Profit	\$4	\$13	\$19	\$38	\$61	\$88	\$114	\$137	\$159
YOY Change in Gross Profit		\$9	\$6	\$19	\$23	\$27	\$26	\$23	\$22
Audio									
Audio Average Retail Price	\$300	\$300	\$300	\$300	\$300	\$300	\$300	\$300	\$300
Audio Attachment Rate	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
Audio Units	22	37	65	161	372	609	875	1,154	1,477
Audio Sales	\$6	\$11	\$19	\$48	\$112	\$183	\$263	\$346	\$443
Audio Gross Margin	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%
Audio Gross Profit	\$1	\$3	\$4	\$11	\$26	\$42	\$60	\$80	\$102
YOY Change in Gross Profit		\$1	\$2	\$7	\$15	\$16	\$18	\$19	\$22
Accessories/Cables									
Accessories/Cables Average Retail Price	\$100	\$100	\$100	\$100	\$100	\$100	\$100	\$100	\$100
Accessories/Cables Attachment Rate	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%
Accessories/Cables Units	183	316	552	1,366	3,160	5,180	7,439	9,812	12,553
Accessories/Cables Sales	\$18	\$32	\$55	\$137	\$316	\$518	\$744	\$981	\$1,255
Accessories/Cables Gross Margin	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%	55.0%
Accessories/Cables Gross Profit	\$10	\$17	\$30	\$75	\$174	\$285	\$409	\$540	\$690
YOY Change in Gross Profit		\$7	\$13	\$45	\$99	\$111	\$124	\$131	\$151
Total Attachments									
Attachments Sales	\$46	\$91	\$153	\$361	\$781	\$1,220	\$1,673	\$2,107	\$2,570
Attachments Gross Margin	43.8%	44.6%	44.4%	44.1%	43.7%	43.9%	44.1%	44.3%	44.6%
Attachments Gross Profit	\$20	\$41	\$68	\$159	\$342	\$535	\$737	\$933	\$1,145
YOY Change in Gross Profit		\$21	\$27	\$91	\$183	\$193	\$202	\$196	\$212
Attachments + FP TVs = YOY Change in Gross Profit		\$41	\$68	\$159	\$244	\$465	\$554	\$659	\$764
Attachments + (FP TV - Total Domestic) = Net Gross Profit		\$62	\$83	\$101	\$161	\$220	\$247	\$302	\$362
Attachments Gross Margin			44.4%	44.1%	43.7%	43.9%	44.1%	44.3%	44.6%
Flat Panel Gross Margin			25.0%	23.0%	21.0%	20.0%	19.0%	18.5%	18.0%
Blended Flat Panel + Attachment Gross Margin			27.1%	25.7%	24.1%	23.5%	22.9%	22.7%	22.5%
Total Domestic Gross Margin			23.8%	25.3%	24.7%	24.5%	24.4%	24.3%	24.2%
Difference			3.3%	0.3%	(0.6%)	(1.0%)	(1.5%)	(1.6%)	(1.7%)

Source: TAG estimates.

Best Buy's Attachment Rate Sensitivity Analysis. For clarity and ease, we present our attachment rate sensitivity analysis findings in the following table. Our methodology employs a "good, better, best" set of scenarios to add some perspective to the potential earnings power that can be generated from the sale of flat panel televisions and complementary products. Our "High" scenario uses the highest levels of margins and attachment rates, our "Base" analysis is the base case presented in the prior analysis, and our "Low" estimates are most conservative. We used our 2007 estimates because they are forward looking, topical, and timely.

The key takeaway from our attachment rate sensitivity for Best Buy is that that the company should be able to sustain its profit, despite gross margin erosion. Moreover, our medium and low scenarios are on the conservative side and one could argue that our high scenario is a more realistic view of the attachments. This implies that the blended gross margin may in fact exceed the corporate average gross margin.

Exhibit 20

BEST BUY ATTACHMENT SENSITIVITY ANALYSIS, 2007E

Assumption	High	Base	Low
Installation	\$350	\$225	\$175
Unit Attachment Rate	30%	25%	20%
Gross Margin	40%	35%	30%
Warranty	\$350	\$275	\$200
Unit Attachment Rate	13%	11%	9%
Gross Margin	60%	50%	40%
Audio	\$400	\$300	\$200
Unit Attachment Rate	13%	10%	7%
Gross Margin	25%	23%	21%
Accessories / Cables	\$200	\$100	\$75
Unit Attachment Rate	90%	85%	80%
Gross Margin	60%	55%	50%
Attachments Gross Profit	\$1,162	\$535	\$444
Attachments Gross Margin	49.8%	43.9%	39.9%
Attachments + FP TV's = YOY Change in Gross Profit	\$1,092	\$465	\$261
Attachments + (FP TV – Total Domestic) = Net Gross Profit	\$847	\$220	(\$46)
Attachments Gross Margin	49.8%	43.9%	39.9%
Flat Panel Gross Margin	20.0%	20.0%	20.0%
Blended Flat Panel + Attachment Gross Margin	27.4%	23.5%	22.0%
Total Domestic Gross Margin	24.5%	24.5%	24.5%
Difference	2.9%	(1.0%)	(2.5%)

Source: TAG estimates.

Attachment Sales are Likely to Contribute to Circuit City's Profits. We applied the same analysis to Circuit City; however, we used gross margins that are 100 basis points lower than Best Buy due to the more aggressive pricing policy at Circuit City. Directionally, we found the same trend as Best Buy: attachment profits more than offset the flat panel television margin decline. Our analysis indicates that Circuit City's gross profit would be \$26 million less in 2007 than it would if the gross margin remained at the 2006 level and \$135 million less in 2010. When looking at attachments to flat panel television sales, our estimates indicate that attachments may produce \$181 million of profits in 2007, more than exceeding the \$26 million loss from flat panel television gross margin degradation. Our projections through 2010 also show attachment profit more than making up for the television profit decline.

Similar to our analysis of Best Buy, we also looked at Circuit City's ability to maintain or grow its total domestic gross margin in the face of declining flat panel television gross margins. We found that despite the decline in flat panel television profits relative to the total domestic gross margin, Circuit City more than offset the profit shortfall through the sale of related attachments. However, Circuit City's blended flat panel gross margin (televisions plus attachments) likely will continue to fall short of its total domestic gross margin by 50-150 basis points between 2007 and 2010.

Exhibit 21

CIRCUIT CITY ATTACHMENT ANALYSIS

\$ in millions	2002	2003	2004	2005	2006E	2007E	2008E	2009E	2010E
Flat Panel Sales	\$127	\$357	\$571	\$1,028	\$1,929	\$2,567	\$3,374	\$3,922	\$4,496
Unit Sales (Thousands)	125	185	296	659	1,475	2,207	3,229	4,129	5,232
Gross Profit	\$34	\$93	\$137	\$226	\$386	\$488	\$607	\$686	\$764
YOY Change in Gross Profit		\$59	\$44	\$89	\$160	\$102	\$120	\$79	\$78
Gross Margin	27.0%	26.0%	24.0%	22.0%	20.0%	19.0%	18.0%	17.5%	17.0%
Gross Profit based on Prior Year / 2006E Gross Margin					\$424	\$513	\$675	\$784	\$899
YOY Change in Gross Profit due to GM Erosion					(\$39)	(\$26)	(\$67)	(\$98)	(\$135)
Gross Profit based on Total Domestic Gross Margin	\$30	\$83	\$146	\$264	\$441	\$583	\$765	\$886	\$1,013
Total Domestic Gross Margin	23.6%	23.2%	25.6%	25.7%	22.9%	22.7%	22.7%	22.6%	22.5%
Flat Panel Gross Profit minus Total Domestic	\$4	\$10	(\$9)	(\$38)	(\$55)	(\$95)	(\$157)	(\$200)	(\$249)
Installation									
Installation Average Retail Price	\$250	\$250	\$250	\$250	\$250	\$225	\$200	\$175	\$150
Installation Attachment Rate	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Installation Units	31	46	74	165	369	552	807	1,032	1,308
Installation Sales	\$8	\$12	\$18	\$41	\$92	\$124	\$161	\$181	\$196
Installation Gross Margin	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%
Installation Gross Profit	\$3	\$4	\$6	\$14	\$30	\$41	\$53	\$60	\$65
YOY Change in Gross Profit		\$1	\$2	\$7	\$17	\$11	\$12	\$6	\$5
Warranties									
Warranty Average Retail Price	\$300	\$300	\$300	\$300	\$300	\$275	\$250	\$225	\$200
Warranty Attachment Rate	11.8%	22.6%	19.3%	15.6%	10.9%	10.6%	10.4%	10.6%	10.7%
Warranty Units	15	42	57	103	161	233	337	436	562
Warranty Sales	\$4	\$13	\$17	\$31	\$48	\$64	\$84	\$98	\$112
Warranty % of Total Sales	3.5%	3.5%	3.0%	3.0%	2.5%	2.5%	2.5%	2.5%	2.5%
Warranty Gross Margin	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%
Warranty Gross Profit	\$2	\$6	\$9	\$15	\$24	\$32	\$42	\$49	\$56
YOY Change in Gross Profit		\$4	\$2	\$7	\$9	\$8	\$10	\$7	\$7
Audio									
Audio Average Retail Price	\$300	\$300	\$300	\$300	\$300	\$300	\$300	\$300	\$300
Audio Attachment Rate	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
Audio Units	12	18	30	66	147	221	323	413	523
Audio Sales	\$4	\$6	\$9	\$20	\$44	\$66	\$97	\$124	\$157
Audio Gross Margin	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%
Audio Gross Profit	\$1	\$1	\$2	\$4	\$10	\$15	\$21	\$27	\$35
YOY Change in Gross Profit		\$0	\$1	\$2	\$5	\$5	\$7	\$6	\$7
Accessories/Cables									
Accessories/Cables Average Retail Price	\$100	\$100	\$100	\$100	\$100	\$100	\$100	\$100	\$100
Accessories/Cables Attachment Rate	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%	85.0%
Accessories/Cables Units	106	157	251	560	1,254	1,876	2,744	3,510	4,447
Accessories/Cables Sales	\$11	\$16	\$25	\$56	\$125	\$188	\$274	\$351	\$445
Accessories/Cables Gross Margin	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%	50.0%
Accessories/Cables Gross Profit	\$5	\$8	\$13	\$28	\$63	\$94	\$137	\$175	\$222
YOY Change in Gross Profit		\$3	\$5	\$15	\$35	\$31	\$43	\$38	\$47
Total Attachments									
Attachments Sales	\$27	\$45	\$70	\$148	\$310	\$442	\$617	\$754	\$910
Attachments Gross Margin	41.1%	42.2%	41.9%	41.5%	40.9%	41.0%	41.2%	41.3%	41.5%
Attachments Gross Profit	\$11	\$19	\$29	\$61	\$127	\$181	\$254	\$311	\$378
YOY Change in Gross Profit		\$8	\$10	\$32	\$66	\$55	\$73	\$57	\$66
Attachments + FP TVs = YOY Change in Gross Profit		\$19	\$29	\$61	\$88	\$156	\$187	\$213	\$243
Attachments + (FP TV - Total Domestic) = Net Gross Profit		\$29	\$20	\$24	\$72	\$86	\$97	\$111	\$129
Attachments Gross Margin			41.9%	41.5%	40.9%	41.0%	41.2%	41.3%	41.5%
Flat Panel Gross Margin			24.0%	22.0%	20.0%	19.0%	18.0%	17.5%	17.0%
Blended Flat Panel + Attachment Gross Margin			25.9%	24.5%	22.9%	22.2%	21.6%	21.3%	21.1%
Total Domestic Gross Margin			25.6%	25.7%	22.9%	22.7%	22.7%	22.6%	22.5%
Difference			0.3%	(1.2%)	0.0%	(0.5%)	(1.1%)	(1.3%)	(1.4%)

Source: TAG estimates.

Circuit City's Attachment Rate Sensitivity Analysis. Although Circuit City's sales are about one-third of Best Buy's, the economics still point toward profitability via flat-panel ancillary sales. For clarification, our methodology employs "good, better, best" scenarios to add some perspective of the potential earnings power that can be generated from the sale of flat panel televisions and complementary products. Our "High" scenario uses the highest levels of margins and attachment rates, our "Base" analysis is the base case presented in the prior analysis, and our "Low" estimates are most conservative. We used our 2007 projections because they are forward looking, topical, and timely.

The key takeaway from our attachment rate sensitivity for Circuit City is the same as for Best Buy. Based on our assumptions, Circuit City should be able to sustain its profit even in our conservative scenario. In addition, Circuit City may be able to achieve a blended flat panel plus attachment gross margin above the corporate average assuming the gross margins on the four attachments are slightly higher than our conservative medium scenario.

Exhibit 22

CIRCUIT CITY ATTACHMENT SENSITIVITY ANALYSIS, 2007E

Assumption	High	Base	Low
Installation	\$350	\$225	\$175
Unit Attachment Rate	30%	25%	20%
Gross Margin	40%	33%	30%
Warranty	\$400	\$275	\$200
Unit Attachment Rate	12%	11%	10%
Gross Margin	60%	50%	40%
Audio	\$400	\$300	\$200
Unit Attachment Rate	13%	10%	7%
Gross Margin	25%	22%	21%
Accessories / Cables	\$200	\$100	\$75
Unit Attachment Rate	90%	80%	80%
Gross Margin	60%	50%	45%
Attachments Gross Profit	\$421	\$181	\$107
Attachments Gross Margin	49.8%	41.0%	37.6%
Attachments + FP TV's = YOY Change in Gross Profit	\$396	\$156	\$82
Attachments + (FP TV – Total Domestic) = Net Gross Profit	\$326	\$86	\$12
Attachments Gross Margin	49.8%	41.0%	37.6%
Flat Panel Gross Margin	19.0%	19.0%	19.0%
Blended Flat Panel + Attachment Gross Margin	26.6%	22.2%	20.9%
Total Domestic Gross Margin	22.7%	22.7%	22.7%
Difference	3.9%	(0.5%)	(1.9%)

Source: TAG estimates.

Glossary

Black Friday. Considered one of the most important retail sales days of the year, this is the Friday after Thanksgiving. Robust performance on this day is crucial to executing strong holiday results and is often used as an early data point in terms of estimating growth in total holiday sales.

Consumer Electronics Association (CEA). Two thousand companies currently make up the CEA member community. CEA Market Research is an authoritative source for consumer technology research, providing actionable information and intelligence on all aspects of the CE industry, including hardware, software, services and infrastructure.

Flat Panel Televisions. The general term that encompasses both LCD and plasma televisions.

Liquid Crystal Display (LCD). This technology consists of two layers of transparent material, polarized, and then glued together. One layer is coated with a special polymer that holds the individual liquid crystals. Current is passed through individual crystals, allowing the crystal to either block or pass light through to create the image. An external light source is needed for the LCD image to be viewed.

Plasma. This is based primarily on fluorescent light bulb technology with the screen composed of cells. Within the cells, two glass panels are separated by a gap where neon-xenon gas sits (placed there during manufacture). While the television is in use, the gas in the cells charge the red, green, and blue phosphors (pixels), resulting in an image. While the technology allows for the thinness of flat panel, some drawbacks include excess heat generation and screen burn.

ADDENDUM**Important Disclosures:**

Valuation Method for Target Price: Price-to-Earnings, price-to-EBITDA, P/E to growth, price to free cash flow, and discounted cash flow analysis.

Investment Risks: Slower consumer spending, rising interest rates, weaker consumer confidence, rising unemployment, supply chain disruptions, fashion misses, and excessive markdowns.

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Joseph Feldman and Michael Cohen

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