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Film and Entertainment

Technology May Revolutionize Media Consumption, but Don't Expect Consumers to Shun the Cinema

- Cyclical sector with long history of growth.** Although the theatrical exhibition industry has had its issues with over expansion in the past, demand has generally been an industry strength. Over the past 20 years, box office has grown at a 4.7% CAGR, with attendance growth of 1.78% outpacing population growth of 1.11%. Although technology has expanded consumer entertainment choice, consumers consistently return to mainstream media with their pocketbooks whether in the theatre, retail store, home, or Internet. Consumers also are showing, through their continued theatre attendance that home theatre, pay-per-view, DVDs, and streaming media may be increasingly close substitutes for a movie watching experience, but they are not substitutes for an evening out. We also believe that much of the continued strength in traditional media, whether measured in theatre attendance, TV watching or radio listening suggests that consumers are not substituting new emerging media for traditional media, but rather, increased their overall consumption of media.
- Strong film slate should drive another year of growth: we expect 2007 box office to follow in 2006's footsteps.** In 2006, the U.S. box office improved 5.5% to \$9.5 billion. The year was important because it challenged the pessimism of critics as well as reversed a 3-year period of falling box office and attendance. The industry is now able to convincingly argue that it is not just the proliferation of home theatre, on-demand pay television, piracy, and inexpensive DVDs that weigh on box/film performance, but also film quality. This is an important point since film quality can improve, while the other technology trends are generally expected to work against exhibitors. The reality is that film slates matter, which we think will be again proven in 2007. Our analysis of 2007's slate, which includes three highly anticipated third-installments—*Spiderman*, *Shrek*, and *The Pirates of the Caribbean*, makes us confident that the upward trend in the film industry will continue and another year of attendance growth will continue. For 2007, we project a box office increase of 5.2%, supported by attendance growth of 2.8%. This should push the box office to \$9.98 billion, making it the best year on record. Based on the release schedule, expect May to make or break the year. For 2008 through 2010, we are forecasting modest gains in the box office, driven by higher ticket prices (~2.7% per annum). Over the same period, we are forecasting attendance to drop off by 0.6% per year as consumers continue to find more ways to access Hollywood content.
- Expect individual film performance records to be challenged, if not broken.** We expect at least a few of this year's films to ultimately rank in the top 20 highest grossing films of all time. Our level of confidence is high, given that most of this year's top films will likely come from very established movie franchises, where predictability is better. The movie *300* already put the year on a good track, delivering the strongest March opening on record and the third highest ever for an R-rated film in any month. The year also should benefit from a strong animation slate, featuring a Pixar release, *Ratatouille*, and the return of *Shrek*.
- The pressure remains on exhibitors to innovate and find new ways of capturing consumer interest: digital cinema is next logical step in industry progression.** Through digital cinema and sound, improved in-theatre advertising, and other emerging technologies such as 3-D cinema, exhibitors are making a continual effort to refine and develop their offerings. Recent progress in establishing digital standards as well as continued growth in the number of available digital feature releases suggests that studios and exhibitors may finally be coming together to make digital cinema a reality. The good news for exhibitors is that we expect studios to finance a great deal of the cost, given they accrue most of the benefit from digital conversion.

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Theatrical Exhibition Industry Introduction

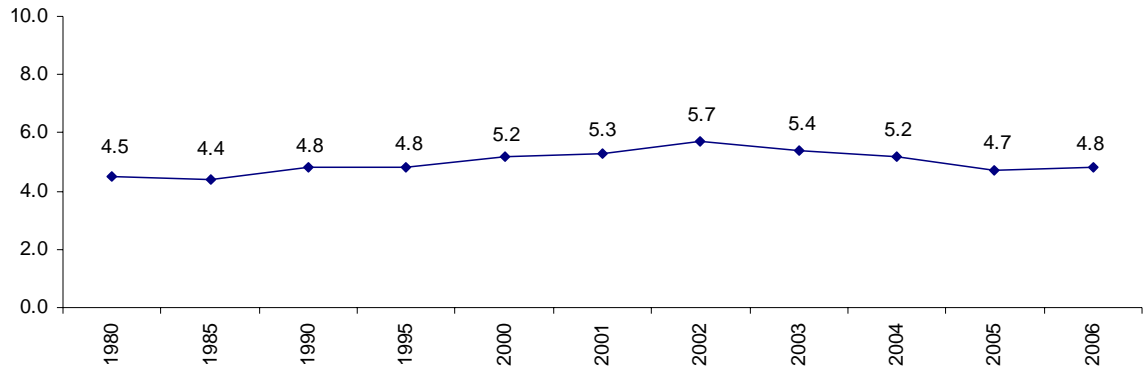
The Setting

The importance of filmed entertainment to consumers continues to grow steadily. Technological innovation, vis-à-vis DVDs, video-on-demand (VOD), home theatre, and the Internet, has only managed to increase the value of such content by making content more accessible than ever before. Growth in theatre screens and sites, which has facilitated more choice and show times, has also contributed to consumer dependence on entertainment in general and satisfaction with cinema specifically. Consequently, in recent years, studios have flourished as their content has found more avenues to satiate consumer wants.

The movie exhibition industry has benefited from increased consumer interest in film content. By our count, attendance growth has outpaced population growth, growing at a 20-year CAGR of 1.78% through 2006 vs. 1.11% for the U.S. population. Coupled with higher ticket prices, the box office has grown at an average rate of 4.7% over the same duration. However, over the past decade and even more pronounced over the last five years, the fortunes of movie exhibitors and studios have started to diverge. Most notably, from 2003-2005, movie attendance fell for three consecutive years, causing many to portend doom for exhibitors. Most pundits attributed the exhibition industry's divergence and its ills to the proliferation of home theatre systems, the ascension of the DVD, and the ever-shortening DVD release window. Amongst a number of concerns, VOD loomed largely in the backdrop, though it is more of a future problem than a present one. Undoubtedly, these developments explained much of the causal factors behind the problems that theatres were facing. But since technology rarely stands still or backtracks, the outlook for the movie exhibition industry became quite pessimistic. In hindsight, the view was too pessimistic because it did not account for how film quality could play a role in magnifying, and later countering, the industry's woes.

At the onset of 2006, before the strength of the film slate became evident, many industry followers had a hard time seeing how exhibition industry revenues, largely comprised of box office, could rebound given that the negative technology trends were hardly going to abate in 2006 if ever. Thus, many were surprised that in 2006, movie attendance grew 3.3% on an improved film slate, helped by a host of family friendly animation films. And for 2007, we expect the release of three highly anticipated third-installments—*Spiderman*, *Shrek*, and the *Pirates of the Caribbean*—to go a long way towards driving another year of attendance growth. We acknowledge that the competition for a consumer's entertainment dollars is only going to get more competitive with time. But even so, consumers are showing, through their continued attendance, that pay-per-view, DVDs, and streaming media may be increasingly close substitutes for a movie watching experience, but they are not as close of a substitute for an evening out. According to Nielsen/Entertainment/NRG in January 2007, 80% of moviegoers who saw at least movie in 2006 believed the experience was time and money well spent, versus the 16% who preferred watching a DVD and 4% who regretted the experience. Nearly half of these moviegoers indicated that they plan to buy the movie on DVD (MPAA, March 2007). Despite the challenges, we believe the fact remains that going to the movies remains one of the most popular out-of-home entertainment experiences in the U.S., supported by the audio/visual quality of the theatre presentation as well as its convenience and affordability.

Figure 1. U.S. Theatre Admissions per Capita



Source: MPAA, PricewaterhouseCoopers

Evolution

Today, theatre chains are increasingly relying on large megaplex theatres. The megaplex format has only been around since 1988, when Kinopolis of Belgium opened what is widely considered to be the first megaplex with 25 screens and stadium seating in Brussels. Although the definition of a megaplex varies, the most common definition is a theatre with 20-plus screens. Consumers quickly embraced the format, as the larger screen counts at these sites made it easier for consumers to find both movies and show times. Added amenities including more comfortable chairs, stadium seating, and better concessions (e.g., restaurant-style appetizers, coffee, ice cream bars, etc.) also contributed to an improved movie-going experience.

Most credit AMC Entertainment with bringing the megaplex format to the U.S. in 1995, when it opened the Grand 24 in Dallas. By the early nineties, there were already at least a couple examples of large multiplexes that featured roughly 20 screens and comparable amenities, so the distinction between first megaplex and large multiplex is a bit blurry in our mind. For instance, in 1987, Cineplex Oden opened its Universal City, California cinema with 17 screens plus an IMAX. This theatre later became the cornerstone of Universal’s “City Walk” development when it officially opened in May 1993. As an aside, the City Walk venue helped show the advantage of grouping a megaplex-type theatre as an anchor tenant with newer, trendy restaurants and shopping to create an entertainment center. This increasingly ubiquitous real estate format is sometimes referred to as an outdoor mall or outdoor shopping destination. Interestingly, “Stanley Durwood of American Multi-Cinema (which became AMC Theatres) pioneered what would become the multiplex in 1963 after realizing that he could operate several attached auditoriums with the same staff needed for one through careful management of the start times for each movie,” per wikipedia.

During the mid-to-late nineties, the success of these large cinema formats set off a construction wave in the U.S. This construction boom that went with the exhibition industry’s affinity for megaplexes is what caused the bankruptcy wave that plagued the industry in the late nineties and the early part of this decade. The problem was that megaplexes were so popular that they cannibalized attendance of nearby smaller, older theatres. This was problematic given that industry capital expenditures were precariously high at the time. The bankruptcy wave affected major circuit operators and small independents alike. The aftermath also contributed to industry consolidation, as bankruptcies not only lowered prices, but also made once closely held assets readily acquirable. Case in point, the nation’s largest operator, Regal Entertainment, is a roll-up of three 2001 bankruptcies—Regal Cinemas, Edwards and United Artists—by billionaire and majority shareholder Philip Anschutz.

Consolidation & Industry Structure

After a period of over-expansion in the late 1990's, the exhibition industry has experienced significant consolidation and circuit rationalization. We suspect the relative maturation of box office revenues has undoubtedly been a motivating factor to increase scale and drive greater bottom-line efficiencies. The effects of such consolidation are pronounced. The top four exhibitors now account for 55% of box office revenues compared to 29% in 1995, per a recent AMC S-1 filing.

Consolidation has created some meaningful differences in the competitive landscape. For instance, the largest theatre circuit operators—Regal, AMC and Cinemark—tend to have national networks and increasingly prefer megaplexes and large multiplexes, whereas their smaller rivals tend to be regional and operate smaller multiplexes on average.

Figure 2. Top 10 U.S. and Canadian Movie Theatre Circuits

	Theatre Chain	Screens		Screens per Site		
		Screens	Sites	Screens per Site	Site	
1	Regal Entertainment Group	6,413	17%	544	9%	11.8
2	AMC	4,597	12%	321	5%	14.3
3	Cinemark (Pro Forma Century)*	3,471	9%	285	5%	12.2
4	Carmike Cinemas	2,221	6%	291	5%	7.6
5	Cineplex Entertainment LP	1,275	3%	130	2%	9.8
6	National Amusements	1,082	3%	89	1%	12.2
7	Kerasotes Theatres	634	2%	77	1%	8.2
8	Hollywood Theatres	536	1%	55	1%	9.7
9	Marcus Theatres	504	1%	45	1%	11.2
10	Empire Theaters Limited	403	1%	55	1%	7.3
	Other Theatres	17,724	46%	4,367	70%	4.1
	Total**	38,860	100%	6,259	100%	6.2

*Reflects August 2006 acquisition. **Chart as of June 15, 2006

Source: NATO, Wedbush Morgan Securities

Figure 3. Summary Comparison of Publicly Traded Theatre Operators

Company Ticker	Regal RGC	AMC ¹ AC	Cinemark ² CNK	Carmikes CKEC	IMAX IMAX
Financial Data	12/31/2006	12/28/2006	12/31/2005	12/31/2005	12/31/2005
Attendance ('000s)	247,404	214,753	212,197	57,866	NA
Attendance per Theatre ('000s)	459	562	553	192	NA
Attendance per Screen ('000s)	39	40	49	23	NA
Theatres	539	382	384	301	266
Screens	6,403	5,340	4,324	2,475	266
Screens per Theatre	12	14	11	8	NA
Admissions (mn)	1,727.1		982.7	309	17.5
Concessions (mn)	696.7		457.2		
Other (mn)	174.3		74.6	159.5	127.4
Total Revenue (mn)	2,598.1	2,379.7	1,514.4	468.9	144.9
Revenue per Theatre ('000s)	4,820.2	6,229.6	3,943.9	1,557.8	544.8
Revenue per Screen ('000s)	405.8	445.6	350.2	189.5	544.8
Revenue per Attendee ('000s)	10.5	11.1	7.1	8.1	NA
EBITDA (mn)	505.6	392.8	323.8	78.5	47.2
EBITDA Margin	19.5%	16.5%	21.4%	16.7%	32.6%
Debt (mn)	1,987.9	1,913.1	2,022.0	30.9	160.0
Debt-to-EBITDA	3.9x	4.9x	6.2x	0.4x	3.4x
Debt-to-Capital	1.0x	0.6x	0.8x	0.1x	1.2x

(1) AMC per the company's February 2007 amended S-1. Figures presented are pro forma Lowes acquisition and NCM IPO; (2) Figures presented are pro forma Century acquisition. Debt is pro forma as of 9/30/06. Other figures 12/31/2005

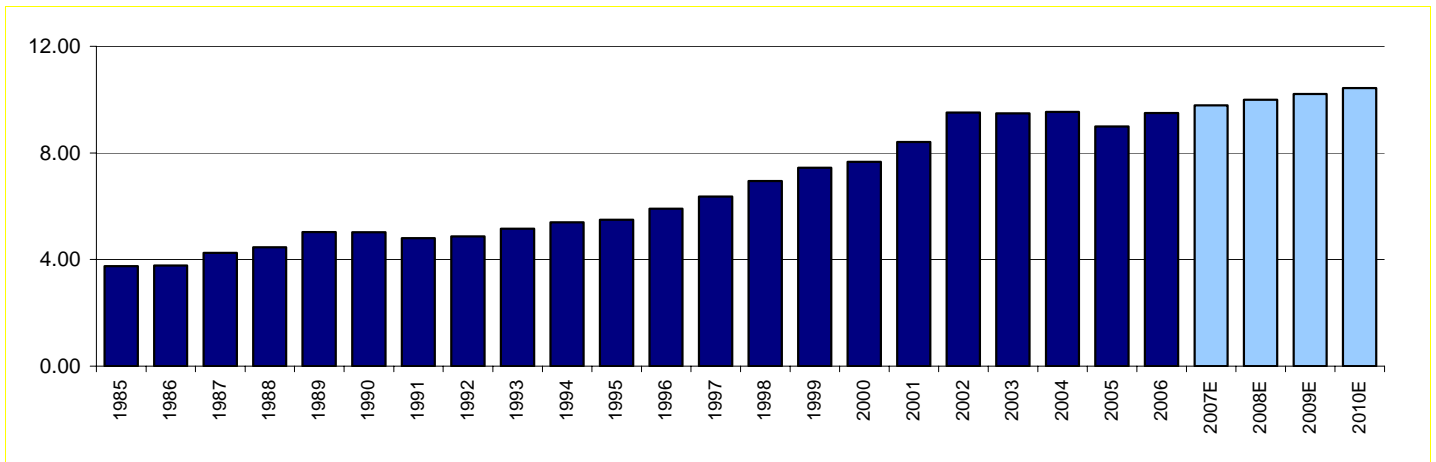
Source: Wedbush Morgan Securities, Company Reports

Industry Forecast

Box Office Forecast

In 2006, the U.S. box office improved 5.5% from the prior year, generating approximately \$9.5 billion, while movie attendance increased 3.3% to 1.45 billion. The improvement in box office and attendance was very important for the industry as it followed three years of consecutive attendance declines. The 2006 improvement allowed the industry to successfully argue that factors in addition to the proliferation of home theatres, on-demand pay television, piracy, and inexpensive DVDs impacted box/film performance.

Figure 4. U.S. Box Office (1985-2010E)



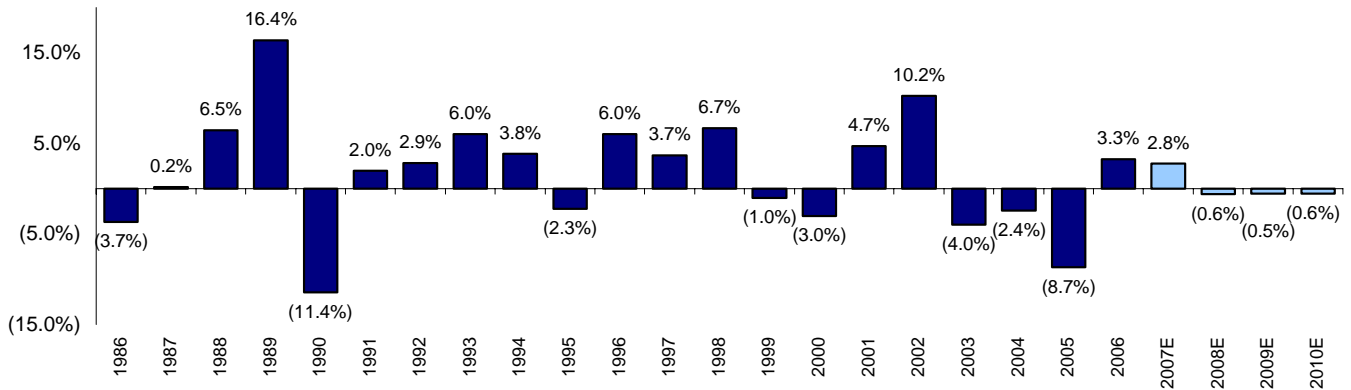
Note: Projected figures are lightly shaded
 Source: MPAA, Wedbush Morgan Securities

We believe the recovery and growth in the box office helps support our argument that prior box office weakness was at least partially attributable to weak film slates in those years, as measured by the less than stellar performances of the largest films of 2003-2005. By the same token, we also believe that the 2006 recovery in box office was also supported by an improvement in film quality. Consider that the negatives facing exhibitors did not suddenly abate in 2006. Prior to the 2006 recovery, we had seen anecdotal signs that film quality was playing a factor in cinema's troubles, including weaker composite film-critic ratings for 2003-2005. Similar sympathy in the international box office figures also support the claim on quality, as international markets were not facing the same sort of comparable technologies risks that were purportedly plaguing the domestic film results. Thus, when the international markets struggled in tandem with the domestic markets, we felt it was an overt sign that film quality was an issue. That said, most pundits ignored such factors in favor of the easier story to tell—that technology was making the theatre obsolete.

We think 2007 is poised to be a very strong year. In qualitative terms, we expect opening weekend records to at least be challenged, if not broken at least a few of this year, to ultimately rank in the top 20 best grossing films of all time. Our level of confidence is high, given that most of this year's top films will likely come from very established movie franchises such as *Spiderman* and *the Pirates of the Caribbean*, where predictability is better. The year also should benefit from a strong animation slate that not only has breadth, but also features a Pixar release, *Ratatouille*, and the return of Shrek. Pixar and Shrek were both absent in 2006. In terms of our industry outlook, we are forecasting a box office increase of 5.2% (to \$9.98 billion), facilitated by attendance growth of 2.8%. At \$9.98 billion, 2007 would be the best year on record, surpassing 2004's high of \$9.54 billion. In addition to the yoy Q1 box office change of 6.6%, we are expecting the proceeding quarterly box office changes to be as follows: Q2 +9.2%; Q3 +5.0%; and Q4 0.0%. The rationale behind our quarterly forecast is detailed in the following section of this report. Please note that our

quarterly changes are based on “calendar box office” meaning they include just the revenues actually generated in the quarterly period, as opposed to the total box generated by films released in that quarter.

Figure 5. % Change in U.S. Theatre Admissions (1986-2010E)



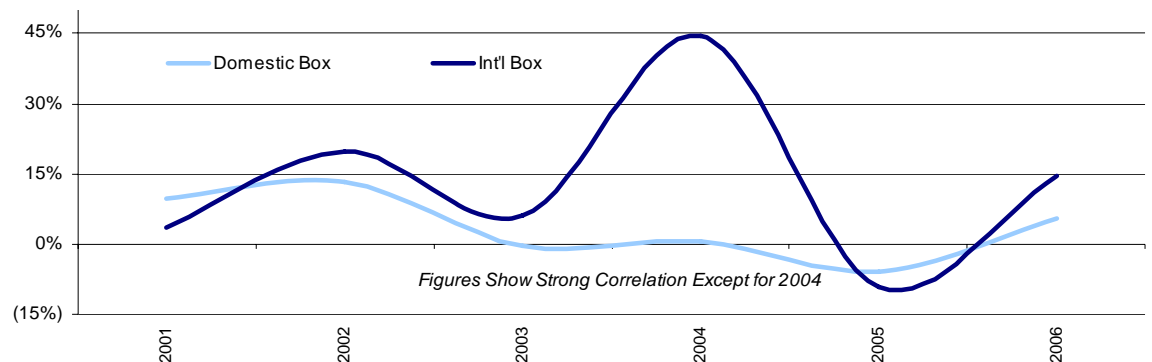
Note: Projected figures are lightly shaded
 Source: MPAA, Wedbush Morgan Securities

For 2008 through 2010, we are forecasting modest gains in the box office, driven by higher ticket prices (~2.7% per annum). Over the same period, we are forecasting attendance to drop off by 0.6% per year as consumers continue to find more ways to access Hollywood content.

For exhibitors, the overall box office tallies along with concessions, loyalty payments, and advertising to comprise their total industry revenue. In recent years, the box office has represented about 65% of total exhibitor revenue, whereas concessions typically represent another 25%-30% (combined 90-95%).

For studios, the box office represents about 25% of their revenue stream from a given film, though the level of box office success generally dictates the level of success garnered by the other ancillary revenue streams, such as DVD sales, pay-per-view, and pay-TV rights.

Figure 6. Domestic & International Box Office Changes



Source: MPAA. 2006 figures are Wedbush Morgan Securities estimates

Quarterly Film Slate Analysis: 2007 vs. 2006

To gage the strength of the 2007 movie slate and box office potential, we performed a quarter-by-quarter analysis of anticipated 2007 releases vs. actual 2006 releases. The top ten quarterly releases, like those presented in the following figures, typically account for 35-55% of a quarter's total box office, whereas for an entire year, the top ten performing releases typically account for about 25-29%.

Thus, our quarterly box office analysis is predicated on comparing the major films of 2007 vs. 2006 by quarter, which we believe adds precision to our annual forecast. We realize that it is possible that in a given quarter, the performance of major films as well as small releases can differ materially from expectations. Even so, we believe the process film slate comparison is still worthwhile and helpful more times than fruitless. Unfortunately, an additional challenge exists for more distant time periods. By 4Q07, it becomes increasingly difficult to incorporate the strength of the film slate into our overall box office forecast, since less is known about the potential strength of future film offerings.

Given that it is our belief that film quality is one of the chief determinants of not only a film's individual box office performance, but also the industry's box office, we believe a quarterly analysis is especially helpful where possible. For longer-term horizons (e.g., beyond one year), we realize that it is difficult, if not impossible, to perform an analysis comparable to what we detail below. Thus, the biggest potential positive—film quality—tends to be the most difficult to forecast long-term. The weak film slates in the few years prior to 2006 clearly indicate the danger in being positive about the industry without a solid basis. And as a result, from our perspective, it is harder to be as bullish longer-term on the exhibition industry, since most of the other more predictable and better-understood factors influencing long-term demand/attendance tend to be more negative than positive.

Figure 7. Top Performing Films Often Dictate the Direction of Overall Box Office

Box Office: Top 10 Films (\$mn)						
	2001	2002	2003	2004	2005	2006
1	317.6	403.7	377.0	441.2	380.3	423.3
2	313.4	339.8	339.7	373.6	291.7	244.1
3	267.7	302.2	305.4	370.3	290.0	234.4
4	255.9	262.0	281.6	279.3	234.3	232.1
5	226.2	241.4	242.9	261.4	218.1	217.5
6	202.0	228.0	214.9	249.5	209.3	200.1
7	198.5	213.3	173.4	186.7	206.5	195.3
8	183.4	190.4	150.4	176.2	205.3	193.4
9	181.2	176.4	139.3	173.0	193.6	165.9
10	180.0	170.7	138.6	162.8	186.3	160.5
Top 10 Films Total	2,325.8	2,530.0	2,360.0	2,675.0	2,415.3	2,266.6
% change		8.8%	(6.7%)	13.3%	(9.7%)	(6.2%)
% of Total Box		26.6%	24.9%	28.0%	26.9%	23.9%
Total Box Office	8,412.5	9,519.6	9,488.5	9,539.2	8,991.2	9,490.0
% change		13.2%	(0.3%)	0.5%	(5.7%)	5.5%

Note: Green arrows (2002-2005) represent positive correlations. Red arrows (2006) represent no correlation.
 Source: Box Office Mojo, MPAA, Wedbush Morgan Securities

Figure 8. Q1 Top Box Office Film Slate Comparison

1Q06			
Movie	Studio	Comments	Gross (mns)
The Lion, the Witch and the Wardrobe	Disney	Spillover from 2005	81.5
The Pink Panther	Sony	Starring Steve Martin, Kevin Kline, Beyonce Knowles	81.4
Eight Below	Disney		78.5
Brokeback Mountain	Focus	Directed by Ang Lee. Starring Heath Ledger, Jake Gyllenhaal	70.3
Big Momma's House 2	Fox	Starring Martin Lawrence	69.0
Failure to Launch	Par.	Starring Matthew McConaughey, Sarah Jessica Parker	68.8
Tyler Perry's Madea's Family Reunion	LGF		62.5
Underworld: Evolution	SGem	Starring Kate Beckinsale	62.3
King Kong	Uni.	Directed by Peter Jackson. Starring Naomi Watts, Adrien Brody	59.3
Curious George	Uni.	Animation-voices of Will Ferrell and Drew Barrymore	57.3
			690.9

1Q07			
Movie	Studio	Comments	Gross (mns)
300	WB	300 Spartans fight to the death against Xerxes and Persian army.	176.6
Wild Hogs	Disney	Starring John Travolta, Tim Allen, Martin Lawrence, William H. Macy	133.4
Night at the Museum	Fox	Starring Ben Stiller	131.3
Ghost Rider	Sony	Starring Nicolas Cage, Eva Mendes	113.7
Norbit	DW	Starring Eddie Murphy	94.3
Bridge to Terabithia	Disney	Based on popular Newbery Award-winning novel	80.1
Dreamgirls	DW	Starring Jamie Foxx, Beyonce Knowles, Eddie Murphy	66.0
The Pursuit of Happyness	Sony	Starring Will Smith	65.2
Stomp the Yard	SGem	Troubled youth helps step team win the championship	61.4
Music and Lyrics	WB	Starring Hugh Grant and Drew Barrymore	49.5
			971.3

Source: Box Office Mojo , Wedbush Morgan Securities

Q1: Strong holiday spillovers gave the box office an early lead, which was sustained as a result of an unexpected sprint near the finish. To start the year, *Night at the Museum*, *The Pursuit of Happiness*, and *Dreamgirls* pushed \$262.4 million over to 2007. In the year prior, holiday spillovers into Q1 amounted to just \$211 million. Most of the quarter was fairly neutral, at least in terms of yoy box office comparisons. But with a few weeks left in the quarter, the surprising strength of *Wild Hogs* and *300* was enough to bring Q1's box office tally up to \$2.156 billion, 6.6% higher than 1Q06 box office of \$2.022 billion. *300* was particularly strong with an opening weekend box office of \$70.9 million, which included \$3.4 million from 62 IMAX theatres, a record opening weekend for the large-screen format.

Figure 9. Q2 Top Box Office Film Slate Comparison

2006			
Movie	Studio	Comments	Gross (mns)
X-Men: The Last Stand	Fox	Directed by Brett Ratner. Starring Hugh Jackman, Halle Berry	227.1
The Da Vinci Code	Sony	Starring Tom Hanks	208.1
Cars	Pixar/Dis	Animation-voices of Own Wilson, Paul Newman	172.1
Ice Age: The Meltdown	Fox	Animation-voices of Ray Romano, Queen Latifah	171.9
Over the Hedge	DW	Animation-voices of Bruce Willis, Steve Carrell	146.8
Mission: Impossible III	Par.	Starring Tom Cruise	132.0
The Break-Up	Uni.	Starring Vince Vaughn, Jennifer Aniston	108.1
Scary Movie 4	W/Dim.		90.0
RV	Sony	Starring Robin Williams	67.5
Click	SonR	Starring Adam Sandler	64.7
			1,388.3

2007			
Movie	Studio	Comments	Rel. Date
Teenage Mutant Ninja Turtles	WB	Animation	3/27/2007
Spider-Man 3	Sony	Last release \$374mn	5/4/2007
Shrek the Third	DW	Last release \$441mn	5/18/2007
Pirates of the Caribbean: At World's End	Disney	Last release \$423mn	5/25/2007
Ocean's Thirteen	WB	Last release \$126mn	6/8/2007
Fantastic Four	Fox	Last release \$155mn	6/15/2007
Evan Almighty	Uni.	Last release-Bruce Almighty \$243mn	6/22/2007

Source: Box Office Mojo , Wedbush Morgan Securities

Q2: Film slate has the potential to make Q2 one of the strongest quarters on record.

Although third installments usually underperform their sequels, the three third installments slated for release in May 2007 are based on some of the most successful predecessor films of all time: *Shrek*, *Spider-Man*, and *Pirates of the Caribbean*. All three of the prior releases for these films topped \$350 million in box office revenues. And even if we assume some drop off in their prior box office performances from their prior release, we think all three third installments are likely to post higher box office tallies than any film in the comparable 2006 period. This coming quarter also benefits from other noteworthy sequels including *Ocean's Thirteen*, *Fantastic Four 2*, and *Evan Almighty* (sequel to Bruce Almighty). 2Q06 was jam packed with sequels and subsequent installments of X-Men, Ice Age, Mission Impossible, and Scary Movie, not to mention other box office hits including The Da Vinci Code and Cars. Impressive, yes, but we note that none of these 2006 releases or any of their previous releases were close to breaking the \$300 million box office mark. Consequently, we are very excited about Q2's potential. We believe quarterly box office could climb as much as 9.2% yoy. We suspect our forecast is likely a few percentage points above the consensus.

One gating factor on the industry box is the overlapping release windows of this quarter's major releases, which are only separated by a week each. Thus, we have some concern that the consumer might be a bit overwhelmed, given that we could see the biggest opening of all time set in the quarter. We believe even avid moviegoers could find it difficult to go to the movies for six weeks straight to support what we believe are six sequential strong releases. And we realize that this might be a high-class problem for exhibitors. But without a doubt, the openings will be large and will command considerable consumer attention.

Figure 10. Q3 Top Box Office Film Slate Comparison

3Q06			
Movie	Studio	Comments	Gross (mns)
Pirates of the Caribbean: Dead Man's Chest	Disney	Starring Johnny Depp, Orlando Bloom, Keira Knightley	420.2
Superman Returns	WB		150.4
Talladega Nights: The Ballad of Ricky Bobby	Sony	Starring Will Ferrell	147.3
The Devil Wears Prada	Fox	Starring Meryl Streep, Anne Hathaway	114.4
You, Me and Dupree	Uni.	Starring Owen Wilson, Kate Hudson, Matt Dillon, Michael Douglas	75.6
Click	SonR	Starring Adam Sandler	72.6
Monster House	Sony		72.5
Cars	Pixar/Dis	Animation-voices of Own Wilson, Paul Newman	71.6
Barnyard: The Original Party Animals	Par.		71.1
World Trade Center	Par.	Starring Nicolas Cage	70.0
			1,265.8

3Q07			
Movie	Studio	Comments	Rel. Date
Ratatouille	Pixar/Dis	Pixar Animation	6/29/2007
Transformers	DW	Action/Sci-Fi	7/4/2007
Harry Potter and the Order of the Phoenix	WB	Last release \$290mn	7/13/2007
I Now Pronounce You Chuck and Larry	Uni.	Starring Adam Sandler	7/20/2007
The Simpsons Movie	Fox		7/27/2007
Bourne Ultimatum	Uni.	Last release \$176mn	8/3/2007
Rush Hour 3	NL	Last release \$226mn	8/10/2007

Source: Box Office Mojo , Wedbush Morgan Securities

Q3: Sequels continue to take over and face no sequel match from 3Q06 other than Pirates of the Caribbean. With *Pirates of the Caribbean: Dead Man's Chest* bringing home \$420 million last summer, the comparative 2007 period would normally be no walk in the park particularly in a hits-driven business like film. However, we expect Q3 to be solid with the return of *Harry Potter*, *Bourne Ultimatum*, and *Rush Hour 3*, whose last releases generated a combined box office total of \$692 million. The new releases are also exciting with *Ratatouille* (a Pixar Film), *The Simpson's Movie*, and *Transformers* leading the line-up. We believe that such releases are a comparable match for 3Q06's strong releases, which included *Superman Returns* (not considered a sequel by our standards as the last release was back in 1987), *Talladega Nights*, and *The Devil Wears Prada*. All three topped \$100 million and we believe that Q3's major new releases have potential to do the same. The net result is that we are forecasting a 5.0% increase for Q3.

Figure 11. Q4 Top Box Office Film Slate Comparison

4Q06			
Movie	Studio	Comments	Gross (mns)
Happy Feet	WB	Animation-voices of Elijah Wood, Robin Williams	176.0
Casino Royale	Sony	Starring Daniel Craig	153.5
Borat	Fox		125.6
The Departed	WB	Starring Leonardo DiCaprio, Matt Damon, Jack Nicholson	120.4
Night at the Museum	Fox	Starring Ben Stiller	115.8
The Pursuit of Happyness	Sony	Starring Will Smith	98.4
The Santa Clause 3: The Escape Clause	Disney	Starring Tim Allen	83.5
Saw III	LGF		80.2
Open Season	Sony	Animation-voices of Martin Lawrence, Ashton Kutcher	67.9
Flushed Away	DW	Animation-voices of Hugh Jackman, Kate Winslet	62.0
			1,083.4

4Q07			
Movie	Studio	Comments	Rel. Date
His Dark Materials: The Golden Compass	NL	Starring Nicole Kidman-Adventure/Fantasy Movie	12/7/2007
I am Legend	WB	Starring Will Smith-Sci-Fi Horror/Vampire Movie	12/14/2007
National Treasure 2	Disney	Last release \$173mn. Starring Nicholas Cage	12/21/2007

Source: Box Office Mojo , Wedbush Morgan Securities

Q4: Fourth quarter comparisons are hard to make, as the slate is still a bit hazy. We can say that based on a solid 4Q06 with five movies (almost six movies) topping \$100mn, comps are going to be competitive. This is why we are projecting a flat quarter, at least until we have a better handle on the quality of the schedule. Some movies set for release in Q4 with blockbuster potential include *The Golden Compass* starring Nicole Kidman, *I am Legend* starring Will Smith, and *National Treasure 2* starring Nicholas Cage.

Figure 12. Forecast Box Office of Major 2007 Film Releases

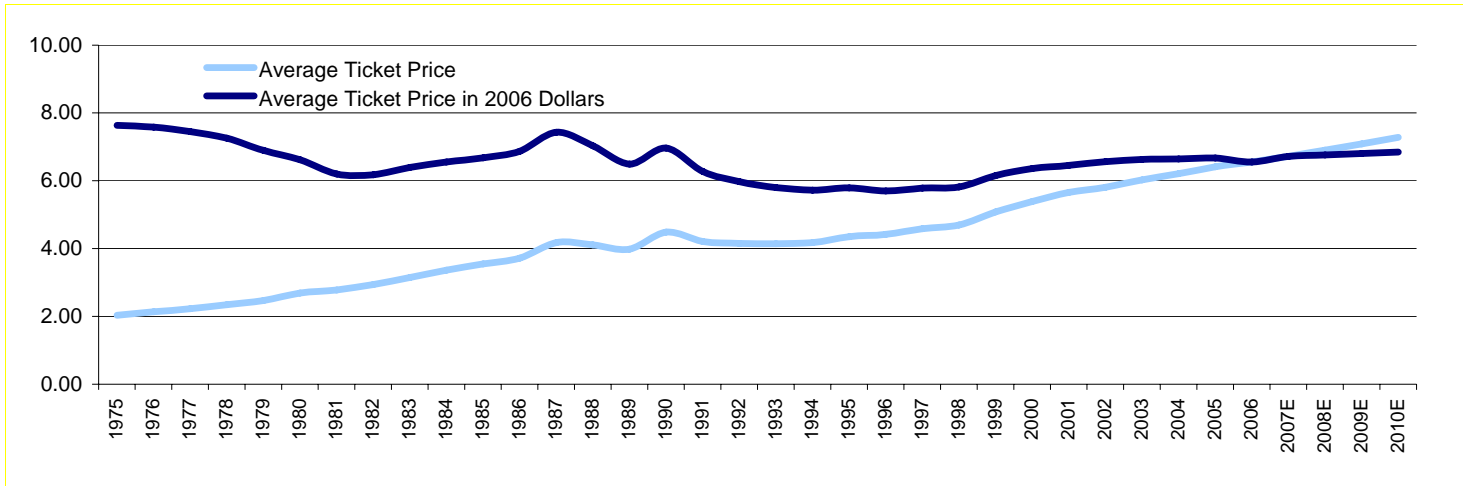
2007 Release	Studio	Movie	Comments	Proj. Box Office	
				HSX	WMS
May	Sony	Spider-Man 3	Last release (6/30/04) earned \$374mn	329	381
May	DW	Shrek the 3rd	Last release (5/19/04) earned \$441mn	296	353
May	Disney	Pirates of the Caribbean: At World's End	Last release (7/7/06) earned \$423mn	329	317
June	WB	Ocean's 13	Last release (12/10/04) earned \$126mn	101	-
June	Fox	Fantastic Four	Last release (7/8/05) earned \$155mn	160	-
June	Uni.	Evan Almighty	Bruce Almighty (5/23/05) earned \$243mn	107	-
June	Pixar/Dis.	Ratatouille	Animation	147	-
July	SW	Transformer	Action/Sci-Fi	170	-
July	WB	Harry Potter	Last release (11/18/05) earned \$290mn	247	-
July	Fox	The Simpsons Movie	Animation	126	-
Aug	Uni.	Bourne Ultimatum	Last release (7/23/04) earned \$176mn	141	-
Aug	NL	Rush Hour 3	Last release (8/3/01) earned \$226mn	137	-

Source: Wedbush Morgan Securities. HSX figures reports Hollywood Stock Exchange values as of March 6, 2007

Movie Ticket Prices

Consumers are often critical of high movie ticket prices. In nominal dollars, ticket prices have increased over the years. However, the figure below of average ticket prices from 1975-2010, adjusted for inflation, shows that real ticket prices have not increased over the thirty-year horizon presented and only modestly over the past decade. For example, 2006’s average ticket price of \$6.55 is in the range of inflation-adjusted historical real prices—\$5.70 in 1996 and \$7.63 in 1975. Thus, we believe that real ticket prices have not noticeably changed.

Figure 13. Average Movie Ticket Price (1975-2010E) in Nominal and 2006 Dollars



Source: NATO, Wedbush Morgan Securities

We believe ticket prices are relatively inelastic. We would also argue that although substitutes/competition exists, such as DVDs and VOD, we do not perceive them as very close substitutes because of the unique qualities of cinema, namely the earlier, exclusive release window and presentation venue. Clearly, if movies were simultaneously released to the big screen, DVD and VOD, the substitutes would serve as even closer substitutes, given that a key-differentiating feature would be eliminated. Fortunately for exhibitors, we are skeptical that studios will make such a move in the foreseeable future.

The fact that theatre prices are so dissimilar from its competition is also evidence that the competition may serve a substitute, but not a close substitute. With DVD rentals and pay-per view at \$3-4 and DVDs at \$12-18, an entire family or group can view a movie from the comforts of their homes for a modest expenditure. For a family of four to attend a theatre, the cost to attend a theatre could easily be in excess of \$20 in most instances. Moreover, in some cases and in some specific regional markets, the cost for that same family of four to attend a theatre could be in excess of \$40. This shows that in some cases, the cost of some substitutes can be dramatically lower than cinema. These substitutes also mean that consumers who are very cost conscious or simply prefer a particular medium over another have likely already voted with their dollars and probably are not especially likely to reverse their spending pattern as a result of a small exhibitor price change. Consequently, we believe that lowering movie ticket prices will not bring dramatically more viewers to the theatres due to an already great price differential with movie theatre’s closest substitutes.

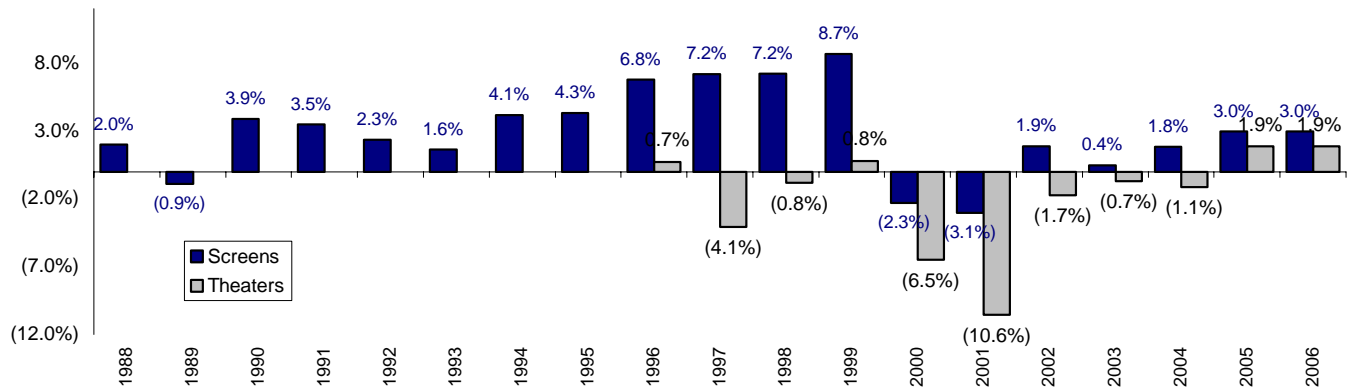
As an aside, we note that in addition to revenue from ticket sales, theatres receive a substantial amount of concessions revenue, which was approximately \$2.82 per attendee in 2006 per Regal’s data (we don’t have industry-wide data for concessions). Thus, average revenue per attendee is approximately \$9-10 per attendee, excluding advertising and licensing revenues.

Theatre Screen/Site Supply

As a result of the industry's maturity, the theatre industry has seen only marginal growth (if not a decline) in theatre sites and screens over the past few years. We think the lack of supply growth suggests that most regional/local markets are adequately served. Consequently, the risk of excessive or harmful supply growth does not seem to be a meaningful industry concern, particularly against the overall competitive media backdrop.

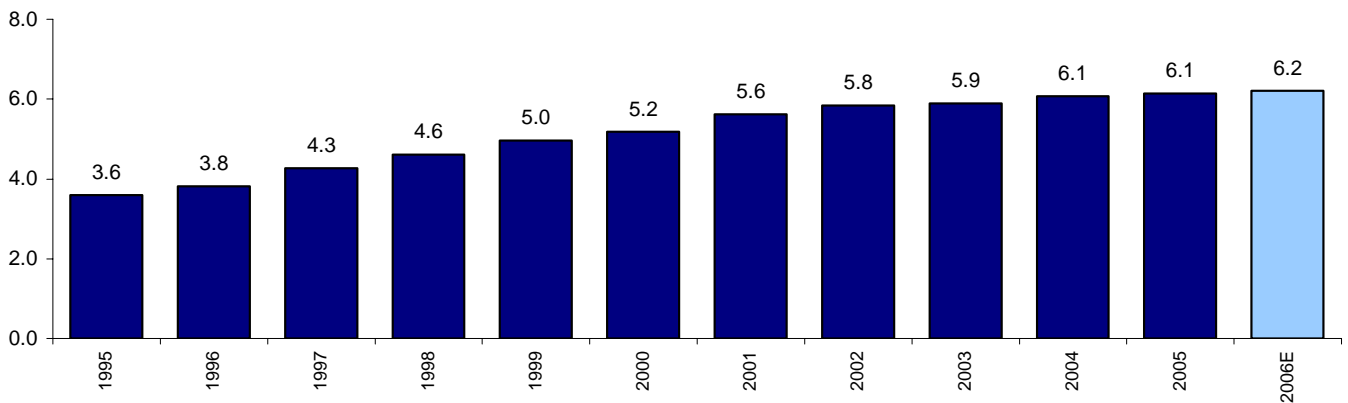
The data on supply/screen trends suggest that exhibitors have increasingly chosen to serve existing markets with newer, larger theatres, while closing down some of their smaller, weaker theatres. The net effect has been modest screen growth in recent years, even though site growth has been modestly declining. Over the past decade, screens have increased noticeably, which has had an affect on film performance and consumer behavior. The biggest difference is that consumers are now better able to find and access movies, allowing exhibitors to reduce the release window per film from months some decades ago to weeks. This in turn has made opening weekends more meaningful as a percentage of a film's overall box office.

Figure 14. % Change in U.S. Theatres and Screens (1988-2006)



Source: NATO

Figure 15. Screens per Theatre (1988-2006)



Note: Projected figures are lightly shaded. 2006 screen per theatre not available through NATO at 4/9/07

Source: NATO, Wedbush Morgan Securities

Industry Dynamics

The Digital Cinema Dilemma

Digital Cinema was born in March 2002 with *Star Wars Episode 2*, the first major motion picture release to be shot without film. Years earlier, when the decision was made to shoot Episode 2 entirely in digital, *Star Wars Episode 1* was nearing its theatrical release date. At the time, George saw an opportunity and had Episode 1 transferred to a digital print format before its release in June 1999 in 4 digital cinemas (2 in Los Angeles and 2 in New York), alongside its wide release, to test audience reaction. According to Texas Instruments, the early audience reactions were overwhelmingly positive. Anecdotally, it's interesting that these early digital experiments utilized projectors that we believe were roughly 1280x1024 in terms of resolution, making them comparable to a typical HD broadcast, which is generally at 1280x1080i. HD broadcast quality typically does not get much worse than 1280x720 or better than 1920x1080i. Note that HD broadcast quality varies by pay television provider as well as by channel.

The resolution of a "2K" digital cinema projector is 2048x1080 and is double for a "4K" projector (4096x2160). Most theatres presently opt for 2K projectors, though the higher cost 4K projectors are available. A 2K projector is essentially on par with Blu-Ray or HD DVD that are at 1920x1080p, though actual Blu-Ray movies are dramatically more compressed (e.g. lower quality) than the digital print shown on a 2K projector. Although true celluloid film does not have pixels and is of higher quality than digital, some pundits would argue that the noticeable benefits of a 2K projector, such as consistency and sound, offset some subtle detail loss. Also bear in mind, that many digital film presentations were shot on film than converted to a digital format, meaning that the digital presentation is not going to be better than film in many key respects. That being said, we think that 4K projectors are closer to the bounds of what is visually perceptible in terms of pixels on a big screen.

We believe the cost of a digital projector is roughly \$100,000 per screen. Reports suggest that cost could be as high as \$125,000 depending on the camera as well as other associated network costs. This contrasts with about \$30,000 to \$35,000 for a 35mm projector, though these projectors do not often need replacing. We believe these figures imply that the total digital projector conversion cost could be in the \$1.5-2 billion range, assuming that the prices of such projectors would fall with volume. Consequently, digital cinema is a conundrum for exhibitors, since consumers generally would like a digital product, perceiving it to be superior although arguably the benefits of digital to a theatre do not exceed its costs.

Some notable directors/filmmakers have seemed to embrace digital. We think their interest stems from the fact that the digital presentation is consistent from screen to screen, whereas a film presentation can vary by the camera or by usage. Specifically, a film print can lose quality, developing lines, cracks, pops, and hisses that can detract from the presentation.

Forgetting exhibitor balance sheets that indicate a general lack of capacity for widespread digital conversions, it is hard for most exhibitors to rationalize such investments. Much of the technical improvements could be imperceptible, and picture detail could possibly be worse. That said, one minor exhibitor benefit from the conversion to digital is that the digital projector can be used for events other than film presentations, like concerts and sports broadcasts. As a result, many exhibitors do not believe they should bear the cost of the conversions, when most of the economic benefits of the conversion fall on the studio.

The chief benefit to the studio is the reduction in film print costs. For a wide release that opens on 4,000 screens, it could cost a studio/distributor \$5 million (assuming \$1,200 per print) for just the domestic prints. We estimate that film prints could cost studios/distributors in the neighborhood of \$600 million annually for domestic prints alone, based on the following assumptions: ~440k prints at \$1,350 per print. Others estimate the cost of prints to run as high as \$700 million domestically. Screen Digest estimates that the worldwide cost of film prints exceeds \$2 billion (Business Week, June 2005). Given the disparity in where the benefits fall, exhibitors and studios continue to ponder creative means by which studios share the reduction in print costs with exhibitors or entrepreneurs in order to encourage greater digital installations. In March 2006, AMC, Cinemark, and Regal

announced the formation of such a company, Digital Cinema Implementation Partners, saying that the entity would work with studios to arrange financing for digital conversions.

We think it's more reasonable to think of these cost reductions as studio benefits than distributor benefits. Digital distribution could facilitate studio distribution without the need of significant infrastructure. So it's not entirely clear if pure distributors would be the ultimate beneficiaries. Continuing on this point, consider that these relatively large per film print costs can be especially problematic for smaller studios and their generally smaller budget films. If such studios existed in a world where exhibitors were all digital, it would be far easier for those studios to distribute their films, perhaps without even the need for a distributor. These smaller independent studios could send their films directly to exhibitors, saving not just print costs, but also recapturing distribution margins. Digital also facilitates the showing of such small films. Theatres would have the ability to easily offer a unique showing of a particular film, given that a few clicks of a mouse could change what's playing on a given screen. Thus, the digital conversion process has not only big implications for exhibitors but also on the margins of large and small studios. The process could make it especially easier for smaller studios to find a market for their films.

The Present State of Digital

The conversion to digital has gone very slow. The problem is that most of the benefits of going digital benefit the studio, while the cost of projectors have historically fell on exhibitors. Most of the major theatre chains still seem to be relying on studio assistance for their rollouts, which continues to slow down the process. Some smaller operators have seemed to make incrementally greater commitments to digital, though generally still very small as a percentage of their networks. Case in point, "As of June 2006 there were 841 2K digital screens compared with 112 at the end of 2005...In the U.S., Carmike Cinemas leads the digital cinema charge with more than 350 screens already converted — the largest 2K digital network worldwide." (Variety, Oct. 2006) Given that the U.S. has almost 40,000 screens, the process is moving slowly, but obviously accelerating.

For exhibitors, the lack of digital content has also been an issue. However, Hollywood is moving much faster here to fix the issue. The same Variety report indicated that 49 films were released in digital format to exhibitors through Sep. 2006, up from 23 for full-year 2005. We don't suspect that content will be a gating factor for long, given that digital conversions are in the best interest of studios.

One issue that may have been contributing to the slow uptake of both digital content and hardware has been the lack of standards. Digital film content and digital projectors need to speak the same language for the process to run smoothly. Studios realized this issue and formed an organization called the Digital Cinema Initiative (DCI). DCI, formed in 2002, is a joint venture of Disney, Fox, Paramount, Sony Pictures Entertainment, Universal, and Warner Bros. In July 1995 an important milestone was reached in digital's history, DCI released final standards (2K and 4K) that would allow digital films and theatrical projectors to be compatible. This achievement should not only bring down the cost of hardware, but it will also dramatically increase Hollywood's willingness to provide digital content. And finally, it allows exhibitors to commit to digital without significant obsolescence risk.

Digital Advertising

At least a few of the major chains already have large digital networks already in place for in-theater advertising (sans trailers), such networks typically use relatively inexpensive digital projectors. Case in point, National CineMedia's digital network spans over 11,000 AMC, Cinemark and Regal screens. However, these inexpensive digital projectors (representative model, Christie L6) typically have 1K resolution as opposed to the 2K minimum that most exhibitors require for feature digital presentations. Thus, these specific theatres have generally two projectors, one digital for pre-show advertising and one analog 35mm for trailers and the theatrical presentation. Consequently, these digital projectors do not show up in tallies of industry digital screen counts.

Given its size, Regal's digital rollout status is also helpful in putting the industry digital screen counts in better perspective. Today, Regal has roughly 6,400 screens, of which 95% feature a digital projector solely for advertising purposes. However, for feature presentations, the company has just 115 digital screens, of which 109 are Real-D systems (3D systems typically capable of "2K" resolution), 5 are 2K test projectors and 1 is a 4K test projector. These tallies should increase rapidly over the next few years given the company's recent formation of its Digital Cinema Implementation Partners joint venture.

Animation Brought the Family Back to Theatres

When Disney's *Snow White* started the animated feature film genre back in 1937, early forays, particularly the Disney ones, were typically met with success. However, by the nineties and particularly in the post Katzenberg era, the Disney formula was no longer resonating with movie audiences. Naturally, the number of animation releases contracted. The digital animation releases, which Pixar (*Toy Story*, *Monsters, Inc*, *Finding Nemo*) and DreamWorks (*Shrek*, *Shark Tale*) largely pioneered in the mid-nineties, were the exception to animation's troubles. These new digital release from new studios also came with an edgier sense of comedy, and thus had broader appeal. Over the last ten years, the digital animation formula gained headway, built on the continued box office success often at unprecedented levels. The high cost to make these films and the complexity of the technology behind the scenes, which Steve Jobs would also likely argue, have managed to keep smaller independents largely out of the market. Even so, Warner Brothers (*Happy Feet*) and Fox (*Robots*, *Ice Age*) are managing to slowly encroach on the Pixar and DreamWorks fiefdoms, but the process will take time.

What we can say is that film is very much a copycat business. And with so much recent success in digital animation, the animation slate in 2006 and 2007 seem to be at all time highs. Competition has surely reached its peak in the animation world, making us skeptical that the average animation film will continue to be able to deliver impressive results. Actual 2006 results may be an indication that our thinking is right. In totality, we suspect animation will continue to reign as an important film segment; animation is very family friendly, giving major films a unique drawing power particularly over a typical major R-Rated release. Perhaps the deluge in animation films is a bit extreme. As returns start to fall on lesser releases, we suspect that studios will again get the message and become more disciplined with their animation line-ups. That said, from an exhibitor point of view, the large animation line-up gives us confidence that families will at least be going to the movies in numbers, though such a statement is not meant to serve as assurance that studios will see strong returns from such films.

As an aside, feature animation films are approaching another technological inflection point. In March 2007, DreamWorks announced its intention to produce all of its films in stereoscopic 3-D starting in 2009. DreamWorks has already started production on its first film in this format, *Monsters vs. Aliens* (working title), intended for release in the summer of 2009. Thus it would not surprise us if other studios were to follow suit. REAL D, the leading provider of digital 3-D projectors and technology, claims that over 700 3-D screens in 14 countries are currently deployed and approximately 1000 screens are expected later this year.

Figure 16. Feature Animation Releases (2007E)

Movie	Studio	2007	
		Comments	Rel. Date
1 Arthur and the Invisibles	MGM/W	\$14.3mn as of 3/4/07	12/29/2006
2 Happily N' Ever After	LGF	\$15.6mn as of 3/4/07	1/5/2007
3 Teenage Mutant Ninja Turtles	WB	Turtle power!	3/27/2007
4 Meet the Robinsons	Disney	Lewis meets boy from future and travels forward in time	3/30/2007
5 Shrek the Third	DW	Last release \$441mn	5/18/2007
6 Surf's Up	Sony	Penguins go surfing	6/8/2007
7 Ratatouille	Pixar/Dis.	Rat dreams of becoming a great French chef	6/29/2007
8 The Simpsons Movie	Fox	Homer and the gang finally come to the big screen	7/27/2007
9 Bee Movie	DW	Bee to sue humans after he finds out they actually steal honey	11/2/2007
10 Beowulf	Sony	6th century-warrior battles monster	11/16/2007
11 Foodfight!	LGF	Food comes to life after supermarketlights are turned off	11/16/2007
12 Enchanted	Disney	Live action/animation about a fairytale princess thrust into NYC	11/21/2007

Source: Box Office Mojo, Wedbush Morgan Securities

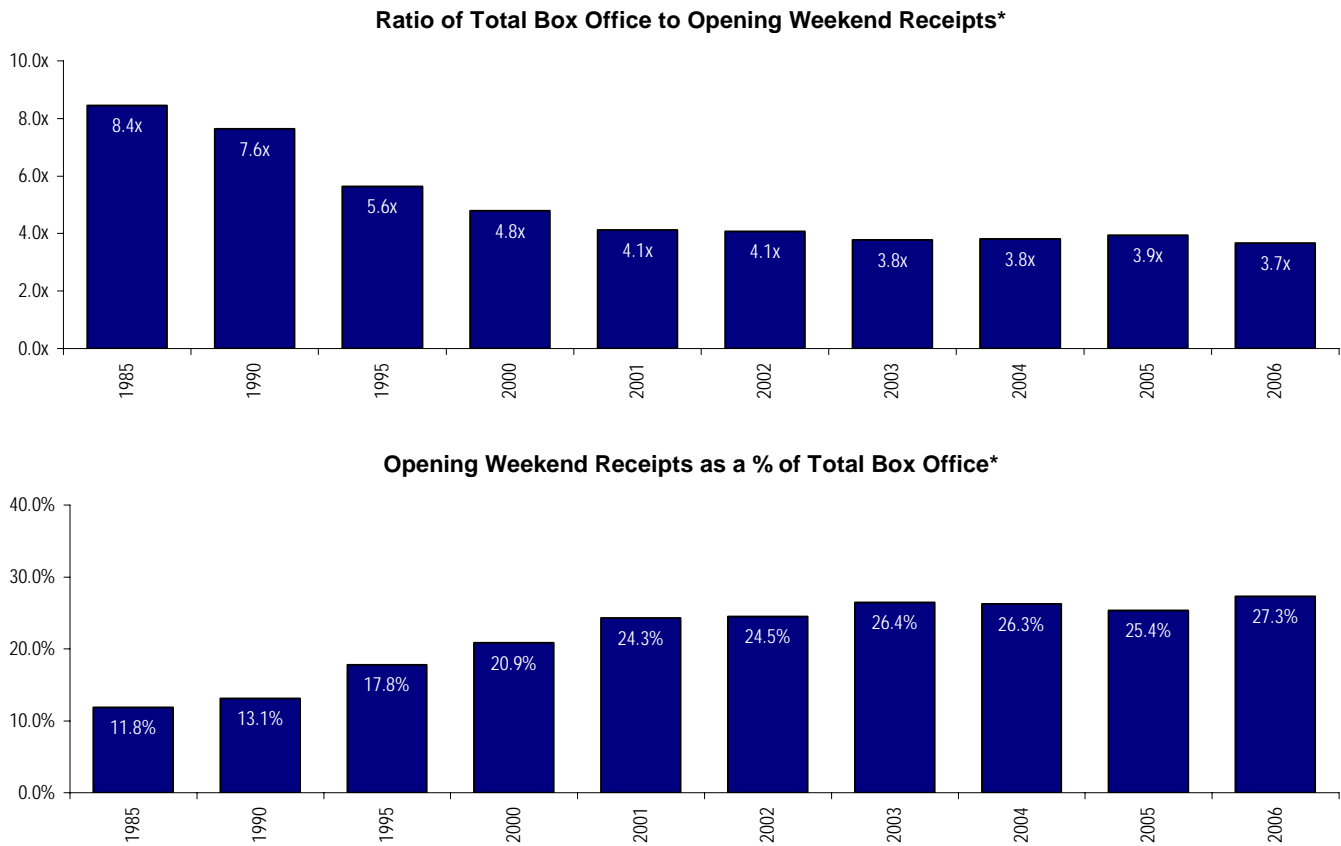
Figure 17. Feature Animation Releases (2003-2006)

2003			
Movie	Studio	Comments	Gross (mns)
1 Finding Nemo	Pixar/Dis.	A father-son underwater adventure featuring Nemo, a boy clownfish	339.7
2 Brother Bear	Disney	A young Inuit hunter is magically changed into a bear	82.6
3 The Jungle Book 2	Disney	Jungle boy decides to leave civilized village life for the wild	47.9
4 Rugrats Go Wild	Par.	Follows the adventures of the whole Rugrats gang all grown up	39.4
5 Sinbad: Legend of the Seven Seas	DW	Sailor is framed by the goddess Eris as the theft of the Book of Peace	26.5
6 Piglet's Big Movie	Disney	Piglet disappears and his pals must use scrapbook map to find him	23.1
7 Looney Tunes: Back in Action	WB	The Looney Tunes search for a man's missing father	20.4
			579.6
			% of Total Box Office 6.3%
			Average Box per Animation Release 82.8
2004			
Movie	Studio	Comments	Gross (mns)
1 Shrek 2	DW	Newlywed ogres' story continues	441.2
2 The Incredibles	Pixar/Dis.	A family of undercover superheroes	248.9
3 Shark Tale	DW	Son of shark mob boss found dead. Oscar is found at the scene	160.5
4 The Polar Express	WB	Doubting boy boards a magical train headed to the North Pole	151.6
5 The SpongeBob SquarePants Movie	Par.	SpongeBob tracks down King Neptune's stolen crown	81.1
6 Home on the Range	Disney	Animals go hunting for a notorious outlaw to save farm	50.0
7 Yu-Gi-Oh! The Movie	WB	Yugi, a small high school student, becomes Game King	19.8
8 Teacher's Pet	Disney	Spot the dog poses as a boy and sneaks into school	6.5
			1,159.7
			% of Total Box Office 12.3%
			Average Box per Animation Release 145.0
2005			
Movie	Studio	Comments	Gross (mns)
1 Madagascar	DW	Story of four animals in Central Park Zoo, NYC	193.6
2 Chicken Little	Disney	After ruining his reputation, chicken must rescue fellow citizens	131.7
3 Robots	Fox	Idealistic inventor moves to metropolis of Robot City	128.2
4 Wallace and Gromit: The Curse of the Were-Rabbit	DW	Wallace and loyal dog set out to uncover garden sabotage	56.0
5 Tim Burton's Corpse Bride	WB	Corpse rises from grave assuming shy groom wants to marry her	53.4
6 Valiant	Disney	Lowly wood pigeon overcomes his small size to become a hero	19.5
7 Pooh's Heffalump Movie	Disney		18.1
8 Howl's Moving Castle	Disney		4.7
9 The SpongeBob SquarePants Movie	Par.		4.3
			609.5
			% of Total Box Office 6.9%
			Average Box per Animation Release 67.7
2006			
Movie	Studio	Comments	Gross (mns)
1 Cars	Pixar/Dis.	Rookie race car finds the true meaning of friendship	244.1
2 Ice Age: The Meltdown	Fox	Sequel to the Ice Age which earned \$176.3	195.3
3 Happy Feet	WB	Penguin cannot sing; but he sure can tap dance	176.0
4 Over the Hedge	DW	Raccoon tricks forest creatures but soon learns value of friendship	155.0
5 Open Season	Sony	Grizzly bear stranded in the woods 3 days before Open Season	84.3
6 Monster House	Sony	Three teens discover that neighbor's house is a scary monster	73.7
7 Barnyard: The Original Party Animals	Par.	Animals play when farmer is away	72.6
8 Flushed Away	DW	Uptown rat that gets flushed down the toilet	62.0
9 Curious George	Uni.	Inquisitive monkey with insatiable taste for adventure	58.4
10 Hoodwinked	Wein.	Little Red Riding Hood with a twist	51.4
11 The Wild	Disney	Adolescent lion accidentally shipped from New York Zoo to Africa	37.4
12 The Ant Bully	WB	After flooding an ant colony, boy is shrunken down to insect size	28.1
13 Everyone's Hero	Fox		14.5
14 Tim Burton's The Nightmare Before Christmas in 3-D	Disney		8.7
15 Doogal	Wein.		7.4
			1,268.9
			% of Total Box Office 13.8%
			Average Box per Animation Release 84.6

Source: Box Office Mojo, Wedbush Morgan Securities

Opening Weekends Matter More

Figure 18. The Significance of Opening Weekends Continues to Increase



* Statistics based on the top-25 movies in a given year.
Source: Box Office Mojo, Wedbush Morgan Securities

Although we touched on the growing importance of opening weekends earlier herein, we feel we should present additional detail on how the change in structure of the theatre industry, particularly in its evolution of screens and sites, has affected film performance. We also think our analysis can provide a better basis to interpret future opening-weekend box office results.

When movies were offered with less frequency (not to mention that there were arguably fewer screens available to consumers), movies needed to stay in theatres longer in order to give consumers a chance to see the film. However, as megaplexes and large multiplexes changed the landscape, they also changed the way movies were released, not just watched. One of the primary implications of the past decade's screen growth were shorter theatrical release windows for films, which in turn allowed studios to be able to release more movies as a result of the improved turnover.

The figure above shows that opening weekends accounted for 27.3% of total box office receipts in 2006 versus just 11.8% in 1985. By using such trends, we point out that one can use such data as a simplistic means of forecasting total box office from opening weekend receipts. Thus, in 2006, we could have multiplied a given film's opening by roughly 4x and calculated a reasonable estimation of its total domestic box office. For perspective on the variance, most films are going to be near 4x, but it is not uncommon to see multiples near 2.5x on the low range and near 8x on the high range.

As an aside, piracy has also contributed to international opening being more coordinated with the domestic opening, whereas years ago, it was more common for there to be a considerable separation in order to allow the film to be well promoted by the film's talent.

Competitive Challenges

Digital Cable/VOD

VOD is slowly transforming a subscriber's cable box into a video server. Before VOD, subscribers were able to watch films, whether on pay-per-view or a premium movie channel, though the process was still very much like traditional TV, except with more choice. Theoretically, VOD eliminates the TV schedule from a subscriber life while giving them unprecedented choice—movie access with the mere click of a remote button.

The competition that exhibitors will face from VOD will grow in coming years as cable/VOD penetration rise. It will take time for consumer familiarity and comfort with VOD to build as well as for operator glitches to subside and content choices to continue to expand. Already with most VOD offerings, subscribers have on-demand access, at no additional cost, to movies and shows from HBO, Showtime, Cinemax, and Starz, so long as they subscribe to that network's traditional premium services. Subscribers also generally have on demand, pay-per-view access to typically 50-200 new movies.

Though a theoretical competitor to exhibitors, we suspect VOD may ultimately have a bigger impact on the home video market and DVD sales than new box office receipts. The home video market naturally has some exposure to VOD because VOD has comparative advantages on both convenience and quality, particularly if the on-demand broadcast is in HD. The same is true for DVD sales. We suspect that home theatres owners buy DVDs, not just because they are fond of a particular movie and it is affordable; we suspect an important element of that purchase is that the consumer often perceives that DVD video quality is high, and thus worthy/appropriate for their home theatre setup. We point out that DVD quality argument is quickly dissolving, since DVDs are inferior to HD broadcasts. Thus, if HD and VOD penetration rates accelerate faster than Blu-Ray and HD-DVD penetration rates, consumers may for once have an alternative (e.g., HD content from cable/satellite) that supersedes DVDs in quality, which at some point could have negative implications for both DVD rentals and sales.

Figure 19. Digital Cable Penetration Rates

	2002A	2003A	2004A	2005A	2006A
Digital Penetration (of basic subs)					
Comcast	31.1%	35.7%	40.2%	45.6%	52.4%
Time Warner	34.3%	39.8%	44.2%	49.3%	54.2%
Cablevision	7.3%	30.8%	50.1%	64.8%	78.3%
Charter	40.8%	41.5%	44.6%	47.5%	51.7%
Insight	26.0%	31.1%	35.5%	40.5%	-
Mediacom	23.3%	24.8%	27.2%	34.7%	38.3%
	31.4%	36.9%	42.0%	47.8%	54.1%

Source: Wedbush Morgan Securities

For exhibitors, the growth in VOD is another example of how technology is giving consumers another means of accessing theatrical film content in an affordable and convenient manner. The only solace for exhibitors remains their exclusive theatrical release window, which means that if someone wants to watch a new movie on VOD, they are often going to have to wait for more than 140 days from the theatrical release. Such difference in film release windows allows for very minimal direct competition amongst the various distribution forms. We note that in terms of indirect competition, VOD affects theatrical distribution to an even lesser extent than DVDs, as DVDs have an earlier release window (see figure 20). By the time VOD is available, many people may have already opted to buy or rent the film.

Figure 20. Film Release Windows

Release Period*	Months After Initial Release	Approximate Release Period
Theatrical	—	0-3 months
Home video/ DVD (1st cycle)	3-6 months	1-3 months
Pay-per-transaction (pay per-view and video-on-demand)	4-8 months	3-4 months
Pay television	9-12 months **	18 months
Network or basic cable	21-28 months	18-60 months
Syndication	48-70 months	12-36 months
Licensing and merchandising	Concurrent	Ongoing
All international releasing	Concurrent	Ongoing

* These patterns may not be applicable to every film and may change with new technologies.

** First pay television window

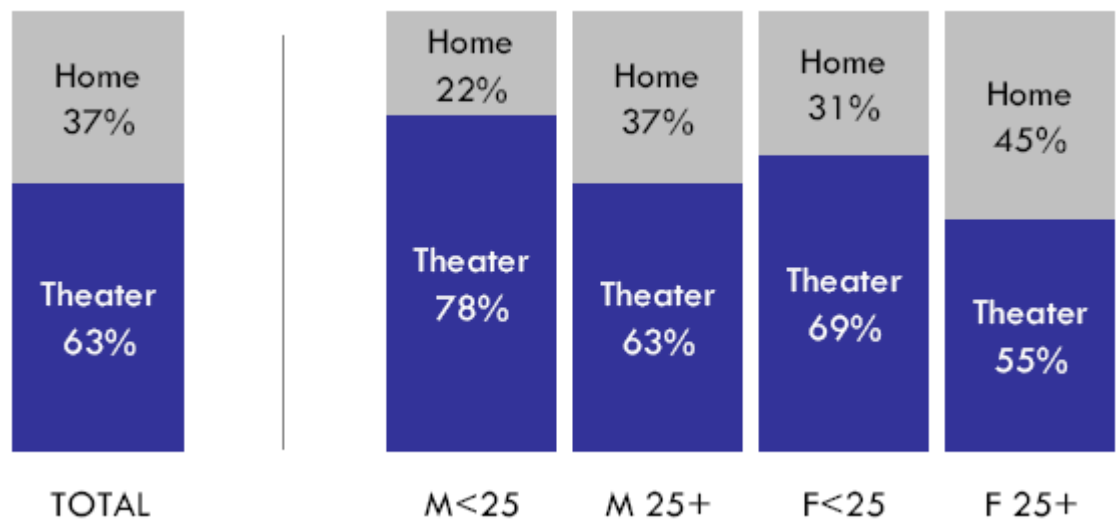
Source: Lionsgate

Home Theatre: *The Palace at Home*

Home Theatre is the lynchpin that makes pay television and DVD potentially far more effective substitutes for cinema. While the technology that comes together to make a home theatre system work can vary, we would expect a cutting-edge, high-end home theatre system to include a home theatre receiver (a stereo that is also capable of up-scaling video to 1080p) with a surround-sound speaker system and a large TV of some sort, preferably 1080p capable. The media that would power such a system would likely be a HD-cable or satellite set-top box and/or a Blu-Ray or HD DVD player.

The technological gains in the visual and audio quality of home presentations not only deter some from visiting theatres, but also pressure exhibitors to innovate. The push for digital projectors somewhat reflects this pressure to innovate, in addition to concepts like stadium seating, IMAX, and 3D-Cinema. It is definitely not helpful to theatre attendance if consumers increasingly believe that their in-home experience is comparable or equivalent to a theatrical release in a theatre. Fortunately, the vast majority of consumers do not believe the home experience (37%) is better than the theatre (67%), per the figure below. However, there is little assurance that the present preference levels won't change.

Figure 21. What is the Ultimate Movie-Watching Experience?

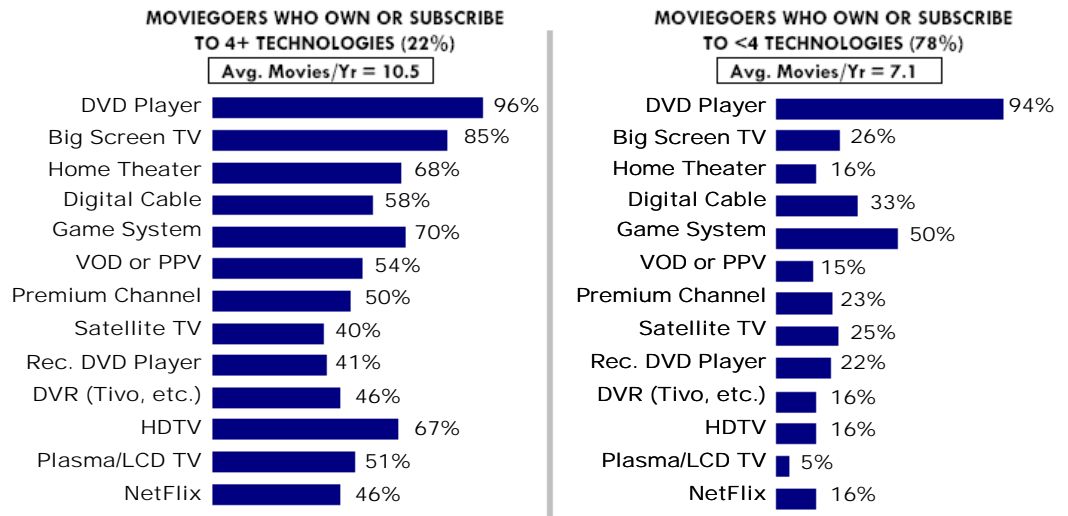


Source: Nielsen Entertainment/NRG (MPAA, 2006 U.S. Theatrical Market Statistics)

The other theory at work against exhibitors is that with higher penetration rates of media substitutes, whether home theatre, VOD, or almost anything else, it could spell doom for theatre attendance. Given that consumer media choices have risen for well beyond a decade, not just the past three to five years, and theatres still have relatively strong attendance, we believe this should give some indication that the pessimistic theory is somewhat flawed. We believe it's appropriate to be concerned about the future, but it is also important to put the past in proper perspective to truly understand consumer behavior. Consequently, we believe the Nielsen Entertainment study (see figure below) that shows that moviegoers with more technology choices actually go to more movies than consumers with fewer options is quiet interesting.

The analysis below seems to suggest that media substitutes and other new technologies are not that big of a problem for exhibitors. At some level, this research is also consistent with our perception that consumers have dramatically increased their consumption of Internet media, with only a modest decrease in their consumption of other media outlets, like TV and radio.

Figure 22. More Media/Tech Choices Equals More Movies, Not Less



Source: Nielsen Entertainment/NRG (MPAA, 2006 U.S. Theatrical Market Statistics)

All that said, we point out that one possible flaw with this analysis is that it is not adjusted for an income bias. Rather, the study seems to actually imply a socio-economic difference between the two camps. We suspect that if we could segment the two camps, one being moviegoers who own or subscribe to 4+ technologies and those with less than 4, into two smaller subsets divided by income, we are doubtful that the results would be as compelling. We suspect that for an equivalent socioeconomic level, the results for both moviegoers who own more than 4 technologies and for those that own less than 4 would be as supportive. In other words, it's possible that the difference in results is more a function of income than how many technologies/subscriptions a consumer owns. Nevertheless, this data has utility, because it could be used to argue that income has more of an impact on movie attendance than technology. While not particularly positive, it would still help show that technology is not the overwhelming factor that drives attendance and continue to support our argument that theatre attendance predictions need to account for more than just all the potential negatives.

Shrinking DVD Release Windows

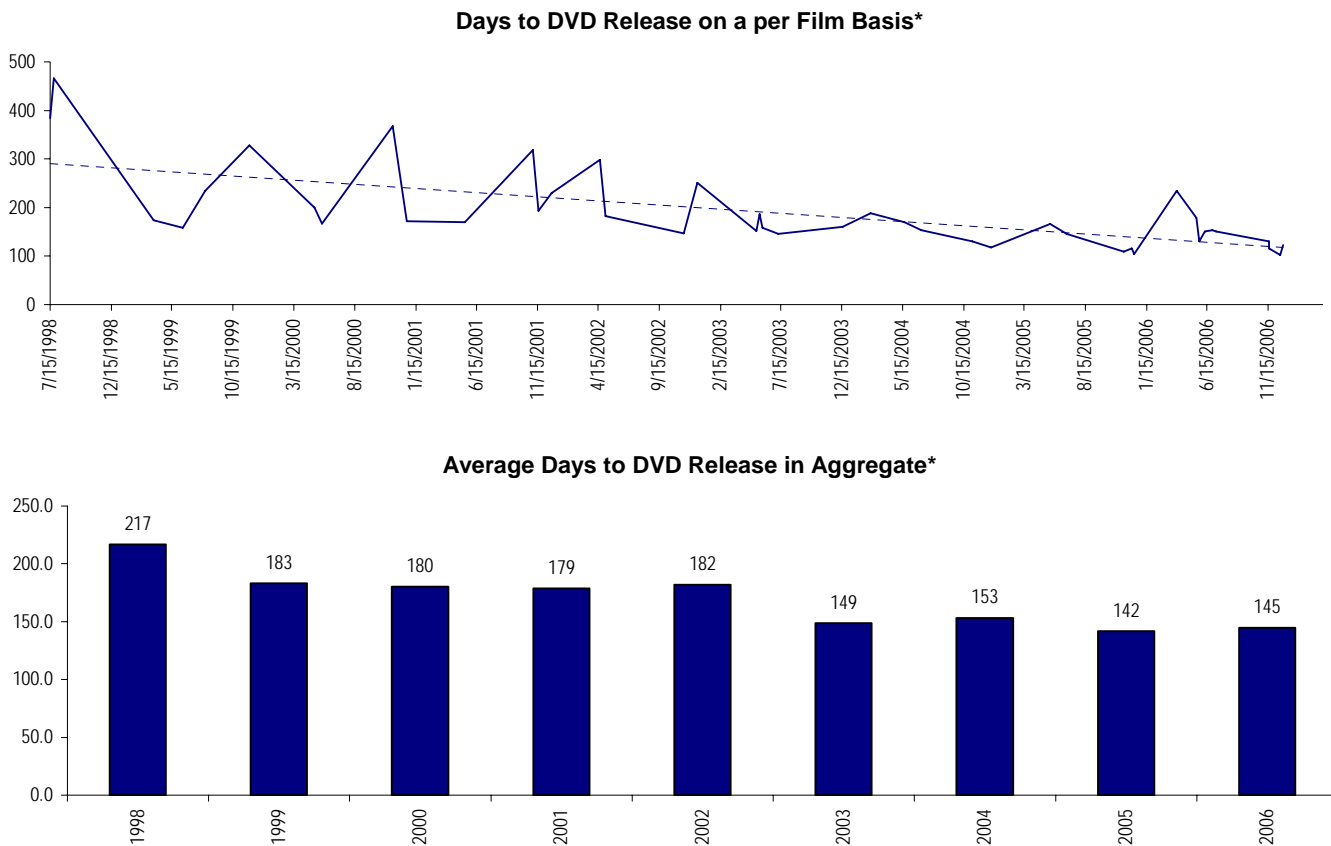
Even before the DVD, when there was just VHS, the theatre industry has been protected from direct competition with home video. Movies are first exclusively released to theatres, and then some months later, are released to home video and other media avenues, such pay-per-view, airplanes, etc. This exclusive window means that consumers must go to a theatre if they want to see a movie when it's released.

Studios constantly evaluate how to maximize their revenue. And in recent years, they have tinkered with the length of the exclusivity window. Many have argued that a shorter theatre to DVD release window would allow DVD sales to piggy back and capitalize on the marketing of a film's theatrical release. And for the most part, the window has been compressed, giving theatres a smaller and smaller period, but still well in excess of the four to eight weeks most movies need to garner the vast majority of their domestic box office revenues. The compression has caused some to argue that the already compressed window is negatively impacting box office results, which we doubt. Others are concerned that the exclusive window might someday be totally eliminated, which clearly would be a problem for at least exhibitors.

Based on our sample, it took approximately 180 days for a movie to reach DVD between 1998-2002. However, in more recent years, movies are making quicker transitions to DVD. The exclusivity window has generally hovered between 140-150 days for the past 3 years. We note that days to DVD release may deviate from this range, particularly if a quicker or delayed release would better enable the movie to capitalize on seasonal selling periods. Theatrical releases tend to become congested from Memorial Day to Labor Day, pushing some releases into late July/early August. Thus, the DVDs for these July/early August films are often released in time for the December holiday season, even though this would equate to a 100 day or so release. For example, *Dukes of Hazzard*, which was released in theatres on 8/5/05, hit DVD on 12/6/05 for a 123-days release window.

The following tables show DVD release windows for select top box office movies on a per film basis and the average window of select top box office movies in aggregate. We note that less popular movies tend to hit DVDs faster than movies booming at the box office. Thus other comparable studies might show a shorter exclusivity window if their sample includes more films with lower box office.

Figure 23. The Shrinking DVD Release Windows



* Both charts are based on data this represents a subset of major film releases in a given year.
Source: Wedbush Morgan Securities

The bad news surely is that the window has compressed; the good news is there has been some stabilization. Even amidst what seems to be a stabilizing DVD release window, the debate has not subsided. There is still ample industry chatter on the matter, spanning from varying DVD release windows by the type of film to completely eliminating the DVD window and simultaneously releasing DVDs with the theatrical showing.

Modest Window Changes Are Not a Concern

Some observers have suggested that children’s movies could benefit from a shorter window, allowing studios to cater to a younger audience’s immediate demands. Disney’s head, Robert Iger, has even said, “One idea is to sell ‘Chicken Little’ DVDs in the theatre. So you’ve seen the movie and just as when you go to a play on Broadway or a concert, you can buy the DVD. That’s when people are feeling best about it, and you cut the theatre owner in to the video sale.” Such ideas have not played out, even for Mr. Iger, considering that Chicken Little’s DVD release took 137 days. However, the idea is novel at the least.

We do not consider modest changes in release windows a significant exhibitor concern. That said, we believe the elimination of the exclusive window would be a far more serious problem. A few

movies have ventured new grounds in simultaneous releases of movies in both the theatre and in the home. In July 2005, UK/US micro-budget indie film *EMR* directed by James Erskine and Danny McCullough became the first simultaneous release. Soon after, in January 2006, Steven Soderbergh's "Bubble" hit theatres and cable TV simultaneously, with the DVDs coming four days later. None of these early examples were successful in the box office, so they did not make for especially good proxies or experiments. And until the simultaneous experiment is conducted with better test subjects, the implications will remain speculative. Exhibitors must be comforted that studios do not seem to be experimenting with this notion in any meaningful way and many of the studio heads have spoken out publicly against the elimination of the window, realizing that such a move would not only impair exhibitors but probably their golden goose—DVD sales.

The Exclusive Theatrical Window is Here to Stay

One of the arguments for elimination of the exclusivity window is that it would better combat piracy. Given that bootlegged DVDs can be available in the streets even before a film's theatrical debut, the reduction in piracy that may come with the elimination of the window might not be as pronounced as some think. We also doubt that the vast majority of bootleg purchasers would have ever bought the DVD, since these consumers are not buying DVDs for quality since these versions often have very low picture/audio quality. We tend to think that purchasers of bootlegs tend to do so because they sell for considerably less than DVDs. DVD piracy, particularly abroad, takes off once digital versions become available.

Another argument for DVD window elimination is the possibility of increasing a studio's potential revenue by charging a premium for simultaneous DVD releases. Many argue that by eliminating the exclusivity window, the shortfall in box office receipts can be more than made up by higher margins on DVDs, assuming DVDs were priced even higher at initial release. While an interesting theory, we continue to believe that the tremendous media coverage that films receive with theatrical debut is invaluable to DVD sales as well as every other film ancillary market. Such exposure typically encompasses not just TV and print, but every conceivable media outlet. The media attention is often at no charge, not to mention the word of mouth benefits that come with exposure to large theatre audiences. But most importantly, this argument fails because studios know that a significant portion of their DVD sales come from moviegoers who are only motivated to buy the DVD because they liked the movie on the big screen.

Clearly, we are very skeptical that studios will some day come to the realization that the elimination of the theatrical release window serves their best interest. However, if such an event were to happen, our concern would not just be limited to the DVD window. We would naturally wonder if studios would similarly compress the pay-per-view/VOD windows. Given that DVD releases precede on-demand releases, it may be even harder for the studios to address VOD/PPV windows in isolation. At most, we believe it is conceivable that some day VOD/PPV could share the same window as DVD sales & rentals. Even so, we think the likelihood of that shift occurring is low, but not out of the question. That said, in March 2007, Warner Brothers teamed up with Time Warner Cable to experiment with the release window that separates DVD and VOD, selling movies on demand the same day they are released on DVD in two specific markets—Austin, TX and Columbus, OH. No major plans for expansion into other markets have been announced.

Emerging Online Film Downloads Represent New Competition

The marketplace around movie downloading seems to be growing rapidly. Initially, it was MovieLink (July 1999) and Cinemanow (November 2002). But in the past year, Amazon, GUBA, iTunes, Netflix and Wal-Mart have all either launched their own services or plan to do so imminently. Most of these services sell 24-hour rentals for \$3-\$4. They are also quickly trying to offer online sales of movies in which the user either downloads the film to their hard disk or burns a copy of the title on their own DVD. However, the technology driving online sales (particularly the DVD burning) are still in the early stages. Content availability is also limited online. Prices for online sales typically range from \$14.95 and up, making them comparable to a DVD.

With feature films, most of the surrounding technological innovation has come in the form of picture/sound quality (e.g. Blu-Ray, HD-DVD and HD), convenience (e.g., VOD, Movie downloads), or both (HD VOD). For the most part, the content remains the same, though DVDs can feature added commentaries and special versions of the film. Given that consumers are increasingly spending more hours online, it stands to reason that some may want to consume traditional media via their PC. Clearly, in the case of say college students or travelers, the usefulness of such online delivery of film is clear.

For exhibitors, we think the threat from online delivery is minimal:

- (1) We do not expect online delivery to ultimately challenge its larger direct competitors in market share. We define online delivery's direct competitors as DVD sales, home video rental and pay-per-view, since they share an overlapping release window.
- (2) The exclusive theatrical release window afforded exhibitors still gives them considerable protection, as it does versus DVDs and pay-per-view.
- (3) For most individuals, we are doubtful that they would prefer/want to use their computer as a means of viewing theatrical releases. Preferring a PC over TV would almost be tantamount to working backwards from the home theatre concept. For considerably older movies and TV shows, PC delivery is easier to understand. In such cases, the content is not as easily accessible through traditional media outlets, such as your cable or satellite provider.
- (4) Online downloads also have other drawbacks that make them less attractive, such as downloads aren't portable (you can't start watching in one room, move to another, and so on), and can't be lent to friends, given away, or sold back. Thus, they're less valuable than DVDs.
- (5) Resolution of online downloads today typically hover around 640x480, making them close but inferior to DVDs and well below Blu-Ray and HD DVDs. Having said that, online downloads have some potential to cannibalize DVD sales. However, unless resolution improves or the market share of online downloads rises dramatically, we would argue that the new higher definition DVD sales should not be materially impacted.

However, there are some early signs of online success. In February 2007, after just recently permitting iTunes to feature its theatrical releases, the Walt Disney Corp. indicated in a Financial Times interview that it sold 1.3 million movies via Apple's iTunes in a matter of months. The company also said that it sold 20 million television shows through iTunes over the past year.

Online Piracy

For studios, the threat from piracy remains great. An MPAA commissioned report in 2005 estimated that domestic studios lost more than \$6 billion per year as a result of both online and hard goods piracy, with 80% of the loss coming from overseas. Studio losses as a result of Internet piracy were estimated at \$447 million, which we would construe is considerably skewed to lost DVD sales and pay-per-views as opposed to lost movie ticket sales.

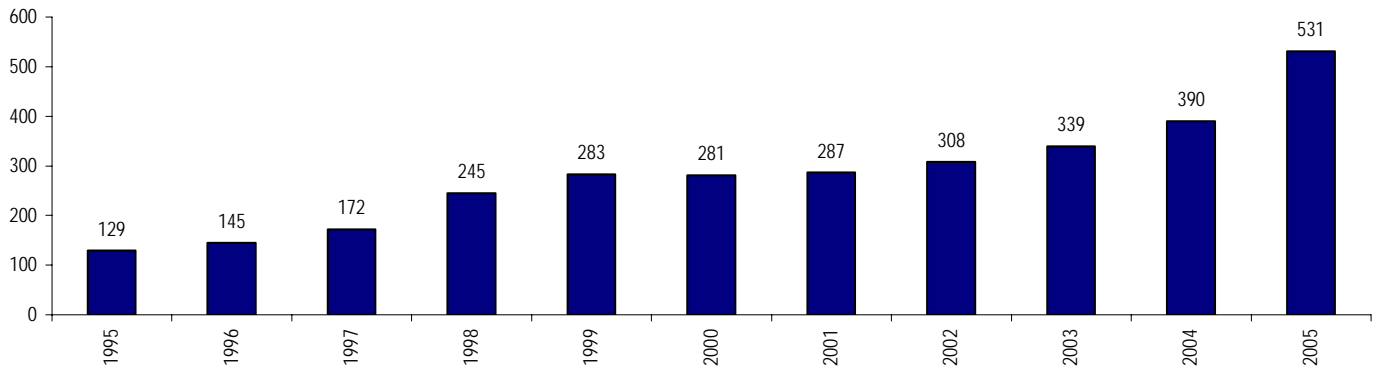
For exhibitors, the domestic threat from piracy is relatively small. Most online piracy typically does not occur until the DVD is released, which is well after the theatrical release window. Granted, there are numerous cases of films being illegally available online in tandem with the theatrical

release. But in totality, it is rare for a high quality digital copy to be available prior to the DVD release. If there is online piracy, it is likely to be handycam quality. We are doubtful that the individuals who would be satisfied watching handycam versions are typical moviegoers, which again contributes to the online piracy issue being small in our minds at least from an exhibitor's point of view. With international markets, exhibitors are exposed to considerably more piracy risk, especially if the international theatrical release date trails the domestic release, as opposed to being simultaneous.

Too Much Choice? Non-Film Content is on the Rise

Many critics of the film industry contend that it is not just movie content that is becoming more accessible through new technologies. Like VOD and online downloading, other content alternatives such as cable networks, pod casts, and user-created video clips are also growing. The figure below shows that it's just not the ease of access that has improved as a result of digital cable/VOD for instance, but also the number of viewing choices (e.g., channels) that consumers have.

Figure 24. Cable TV Channel Growth Continues to Expand

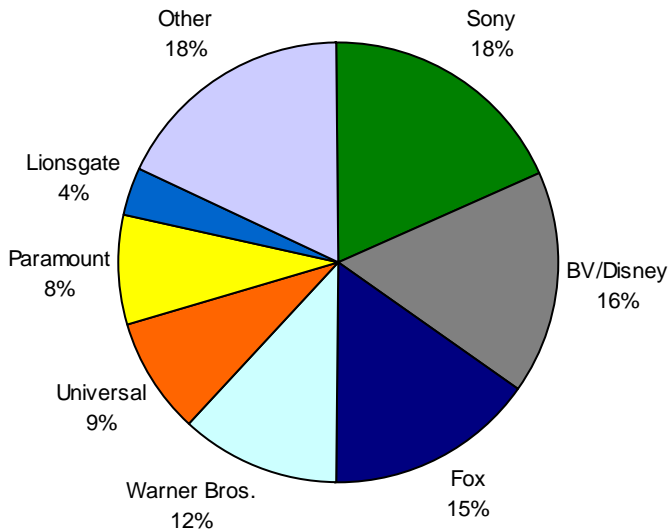


Source: FCC

We believe statistics like these indicate that the competition for an individual's time and dollars is only increasing. While it's intuitive that such a dynamic is playing out nationally, what is not as intuitive is the impact of such trends. In recent years, we believe the most dramatic change for a typical individual has been the amount of time spent on Internet. We believe most time-spent analyses will show that TV viewing, radio listening, and even movie attendance have not change that significantly, even though the penetration of broadband as well as the time spent on such services is up dramatically over the past 10 years. Our point is that it is clearly true that the world has become more competitive. The interesting aspect is that the average person has not really substituted the Internet or these other new emerging mediums for other media, especially traditional media, but rather has increased their overall consumption of media. That said, we are concerned, in the context of forecasting exhibitor's revenues and attendance, about the continued success of home theatre and VOD as well as emerging threats, like online movie distribution. Nevertheless, we believe for the more visible, immediate future, we are not anticipating any negative disruptive events. Our forecast is that attendance could erode modestly in a given year, if Hollywood does not step up with excellent entertainment choices. But in most years, we expect inflation to be sufficient to cover such losses. The more distant future for cinema is obviously even more challenging given that these competitive challenges will only continue to grow in significance. Thus, the pressure is on exhibitors to see if they can find new ways to capture consumer interest; hopefully, exhibitors will be able to do this through quality films and their own emerging technologies, like 3-D cinema, or new offerings such as concerts and sports.

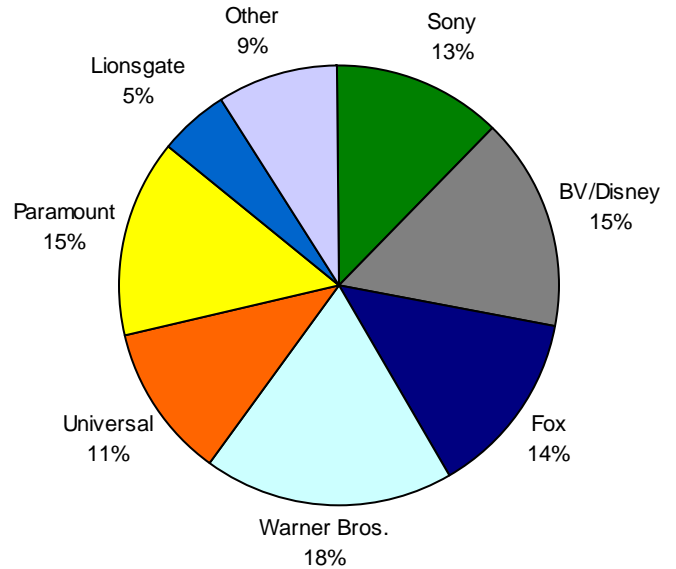
Appendix

Figure 25. Box Office Market Share by Studio
2006 Box Office by Studio-Total \$9.2 billion



Source: Wedbush Morgan Securities Data: Box Office Mojo

Figure 26. Home Video Market Share by Studio
2006 Home Video Sales/Rentals-Total \$23.6 billion



Source: Home Video Business

Figure 27. Top 20 Film Openings of All Time

Rank	Movie	Studio	Opening*	Total Gross*	Date
1	Pirates of the Caribbean: Dead Man's Chest	Disney	135.6	423.3	7/7/2006
2	Spider-Man	Sony	114.8	403.7	5/3/2002
3	Spider-Man 3	Sony	112.2	381.5	5/4/2007
4	Star Wars: Episode III - Revenge of the Sith	Fox	108.4	380.3	5/19/2005
5	Shrek 2	DW	108.0	441.2	5/19/2004
6	X-Men: The Last Stand	Fox	102.8	234.4	5/26/2006
7	Harry Potter and the Goblet of Fire	WB	102.7	290.0	11/18/2005
8	Pirates of the Caribbean: At World's End	Disney	101.7	317.3	5/25/2007
9	Harry Potter and the Prisoner of Azkaban	WB	93.7	249.5	6/4/2004
10	The Matrix Reloaded	WB	91.8	281.6	5/15/2003
11	Harry Potter and the Sorcerer's Stone	WB	90.3	317.6	11/16/2001
12	Harry Potter and the Chamber of Secrets	WB	88.4	262.0	11/15/2002
13	Spider-Man 2	Sony	88.2	373.6	6/30/2004
14	Shrek the Third	DW	86.4	352.8	5/18/2007
15	X2: X-Men United	Fox	85.6	214.9	5/2/2003
16	The Passion of the Christ	NM	83.8	370.3	2/25/2004
17	Star Wars: Episode II - Attack of the Clones	Fox	80.0	302.2	5/16/2002
18	The Da Vinci Code	Sony	77.1	217.5	5/19/2006
19	Austin Powers in Goldmember	NL	73.1	213.3	7/26/2002
20	The Lord of the Rings: The Return of the King	NL	72.6	377.0	12/17/2003

* Data in millions. Note that projected figures are lightly shaded
Source: Box Office Mojo, Wedbush Morgan Securities

Figure 28. Theatre Industry Data (1948-2006E)

	U.S. Box Office (bn)			Worldwide Box Office (bn)	Admissions (bn)			U.S. Avg Ticket Price			Total Sites	Total Screens	Avg. Film Cost (mn)
	MPAA	NATO	Box Office Mojo	MPAA	MPAA	NATO	Box Office Mojo	MPAA	NATO	Box Office Mojo	NATO	NATO	Box Office Mojo
2006	9.49	9.48	9.21	25.82	1.45	1.45	1.40	6.55	6.55	6.58	6,259*	38,860*	-
2005	8.99	8.99	8.84	23.24	1.40	1.40	1.38	6.41	6.41	6.40	6,144	37,740	-
2004	9.54	9.53	9.42	25.23	1.54	1.53	1.52	6.21	6.21	6.21	6,031	36,652	-
2003	9.49	9.49	9.19	20.34	1.57	1.57	1.52	6.03	6.03	6.03	6,100	35,995	63.8
2002	9.52	9.52	9.17	19.76	1.64	1.63	1.58	5.81	5.80	5.81	6,144	35,836	58.8
2001	8.41	8.41	8.41	16.96	1.49	1.49	1.49	5.66	5.65	5.66	6,253	35,173	47.7
2000	7.66	7.67	7.66	15.92	1.42	1.42	1.42	5.39	5.39	5.39	6,992	36,280	54.8
1999	7.45	7.45	7.45		1.47	1.47	1.47	5.08	5.06	5.08	7,477	37,131	51.5
1998	6.95	6.95	6.95		1.48	1.48	1.48	4.69	4.69	4.69	7,418	34,168	52.7
1997	6.37	6.37	6.37		1.39	1.39	1.39	4.59	4.59	4.59	7,480	31,865	53.4
1996	5.91	5.91	5.91		1.34	1.34	1.34	4.42	4.42	4.42	7,798	29,731	39.8
1995	5.49	5.49	5.49		1.26	1.26	1.26	4.35	4.35	4.35	7,744	27,843	36.4
1994	5.40	5.40	5.40		1.29	1.29	1.29	4.18	4.08	4.18		26,689	34.3
1993	5.15	5.15	5.15		1.24	1.24	1.24	4.14	4.14	4.14		25,626	29.9
1992	4.87	4.87	4.87		1.17	1.17	1.17	4.15	4.15	4.15		25,214	28.9
1991	4.80	4.80	4.80		1.14	1.14	1.14	4.21	4.21	4.21		24,639	26.1
1990	5.02	5.02	5.02		1.12	1.19	1.19	4.49	4.22	4.22		23,814	26.8
1989	5.03	5.03	5.03		1.26	1.26	1.26	3.99	3.99	3.99		22,921	23.5
1988	4.46	4.46	4.46		1.08	1.08	1.08	4.11	4.11	4.11		23,129	18.1
1987	4.25	4.25	4.26		1.02	1.09	1.09	4.17	3.91	3.91		22,679	20.1
1986	3.78		3.78		1.02		1.02	3.71	3.71	3.71			17.5
1985	3.75		3.75		1.06		1.06	3.55	3.55	3.55			16.8
1984			4.03				1.20		3.36	3.36			14.4
1983			3.77				1.20		3.15	3.15			11.9
1982			3.45				1.18		2.94	2.94			11.8
1981			2.97				1.07		2.78	2.78			11.3
1980			2.75				1.02		2.69	2.69			9.4
1979									2.47				
1978									2.34				
1977									2.23				
1976									2.13				
1975									2.03				
1974									1.89				
1973													
1972													
1971									1.65				
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1954									0.49				
1953													
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1951													
1950													
1949													
1948									0.36				

* WMS estimates. 2006 screen and theatre figures were not available through NATO at 3/8/07

Source: MPAA, NATO, Box Office Mojo, Wedbush Morgan Securities

Figure 29. 2005 Top 10 Films by Quarter

		2005		
	Movie	Studio	Comments	Gross (mns)
Q1				
1	Hitch	Sony	Starring Will Smith, Eva Mendes	168.4
2	Meet the Fockers	Uni.	Starring Owen Wilson, Robert DeNiro, Ben Stiller, Dustin Hoffman	145.0
3	Robots	Fox	Animation-voices of Ewan McGregor, Halle Berry, Robin Williams	94.6
4	Million Dollar Baby	WB	Directed by Clint Eastwood. Starring Hilary Swank, Morgan Freeman	94.4
5	The Pacifier	Disney	Starring Vin Diesel	90.3
6	Are We There Yet?	SonR	Starring Ice Cube, Nia Long	80.4
7	The Aviator	Mira.	Starring Leonardo DiCaprio, Cate Blanchett, Kate Beckinsale	77.4
8	Constantine	WB	Starring Keanu Reeves, Rachel Weisz	73.2
9	Coach Carter	Par.	Starring Samuel L. Jackson	66.9
10	The Ring Two	DW	Written by Ehren Kruger. Starring Naomi Watts	62.4
				<hr/> 952.8
Q2				
1	Star Wars: Episode III	Fox	Directed by George Lucas	361.5
2	Madagascar	DW	Animation-voices of Ben Stiller, Chris Rock	165.4
3	The Longest Yard	Par.	Starring Adam Sandler, Chris Rock	144.7
4	Batman Begins	WB	Directed by Christopher Nolan	135.5
5	Mr. & Mrs. Smith	Fox	Starring Brad Pitt, Angelina Jolie	133.4
6	Monster-in-Law	NL	Starring Jennifer Lopez, Jane Fonda	80.1
7	Sin City	Dim.	Starring Bruce Willis, Mickey Rourke, Jessica Alba	73.7
8	The Interpreter	Uni.	Starring Nicole Kidman, Sean Penn	71.9
9	Sahara	Par.	Starring Matthew McConaughey	68.1
10	The Amityville Horror (2005)	MGM	Starring Ryan Reynolds	65.2
				<hr/> 1,299.5
Q3				
1	Wedding Crashers	NL	Starring Owen Wilson, Vince Vaughn	206.1
2	Charlie and the Chocolate Factory	WB	Directed by Tim Burton. Starring Johnny Depp	204.3
3	War of the Worlds	Par.	Directed by Steven Spielberg. Starring Tom Cruise	197.6
4	Fantastic Four	Fox		153.9
5	The 40-Year-Old Virgin	Uni.		99.2
6	The Dukes of Hazzard	WB	Starring Johnny Knoxville, Seann William Scott, Jessica Simpson	79.6
7	March of the Penguins	WIP	Narrated by Morgan Freeman	73.5
8	Four Brothers	Par.	Starring Mark Wahlberg	73.0
9	Batman Begins	WB	Directed by Christopher Nolan	69.5
10	The Exorcism of Emily Rose	SGem		65.5
				<hr/> 1,222.2
Q4				
1	Harry Potter and the Goblet of Fire	WB	Starring Daniel Radcliffe, Emma Watson, Rupert Grint	273.3
2	The Lion, the Witch and the Wardrobe	Disney	Directed by Andrew Adamson	209.4
3	King Kong	Uni.	Directed by Peter Jackson. Starring Naomi Watts, Adrien Brody	158.7
4	Chicken Little	Disney	Animation	131.7
5	Walk the Line	Fox	Starring Joaquin Phoenix, Reese Witherspoon	90.9
6	Saw II	Lions		87.0
7	Jarhead	Uni.	Starring Jake Gyllenhaal, Peter Sarsgaard, Jamie Foxx	62.4
8	The Curse of the Were-Rabbit	DW	Animation	56.0
9	Fun with Dick and Jane	Sony	Starring Jim Carrey	54.1
10	Flightplan	Disney	Starring Jodie Foster	53.5
				<hr/> 1,177.0

Source: Box Office Mojo, Wedbush Morgan Securities

Figure 30. 2006 Top 10 Films by Quarter

		2006		
	Movie	Studio	Comments	Gross (mns)
Q1				
1	The Lion, the Witch and the Wardrobe	Disney	Spillover from 2005	81.5
2	The Pink Panther	Sony	Starring Steve Martin, Kevin Kline, Beyonce Knowles	81.4
3	Eight Below	Disney		78.5
4	Brokeback Mountain	Focus	Spillover from 2005	70.3
5	Big Momma's House 2	Fox	Starring Martin Lawrence	69.0
6	Failure to Launch	Par.	Starring Matthew McConaughey, Sarah Jessica Parker	68.8
7	Tyler Perry's Madea's Family Reunion	LGF		62.5
8	Underworld: Evolution	SGem	Starring Kate Beckinsale	62.3
9	King Kong	Uni.	Spillover from 2005	59.3
10	Curious George	Uni.	Animation-voices of Will Ferrell and Drew Barrymore	57.3
				<u>690.9</u>
Q2				
1	X-Men: The Last Stand	Fox	Directed by Brett Ratner. Starring Hugh Jackman, Halle Berry	227.1
2	The Da Vinci Code	Sony	Starring Tom Hanks	208.1
3	Cars	Pixar/Dis.	Animation-voices of Own Wilson, Paul Newman	172.1
4	Ice Age: The Meltdown	Fox	Animation-voices of Ray Romano, Queen Latifah	171.9
5	Over the Hedge	DW	Animation-voices of Bruce Willis, Steve Carrell	146.8
6	Mission: Impossible III	Par.	Starring Tom Cruise	132.0
7	The Break-Up	Uni.	Starring Vince Vaughn, Jennifer Aniston	108.1
8	Scary Movie 4	W/Dim.		90.0
9	RV	Sony	Starring Robin Williams	67.5
10	Click	SonR	Starring Adam Sandler	64.7
				<u>1,388.3</u>
Q3				
1	Pirates of the Caribbean: Dead Man's Chest	Disney	Starring Johnny Depp, Orlando Bloom, Keira Knightley	420.2
2	Superman Returns	WB		150.4
3	Talladega Nights: The Ballad of Ricky Bobby	Sony	Starring Will Ferrell	147.3
4	The Devil Wears Prada	Fox	Starring Meryl Streep, Anne Hathaway	114.4
5	You, Me and Dupree	Uni.	Starring Owen Wilson, Kate Hudson, Matt Dillon, Michael Douglas	75.6
6	Click	SonR	Starring Adam Sandler	72.6
7	Monster House	Sony		72.5
8	Cars	Pixar/Dis.	Animation-voices of Own Wilson, Paul Newman	71.6
9	Barnyard: The Original Party Animals	Par.		71.1
10	World Trade Center	Par.	Starring Nicolas Cage	70.0
				<u>1,265.8</u>
Q4				
1	Happy Feet	WB	Animation-voices of Elijah Wood, Robin Williams	176.0
2	Casino Royale	Sony	Starring Daniel Craig	153.5
3	Borat	Fox		125.6
4	The Departed	WB	Starring Leonardo DiCaprio, Matt Damon, Jack Nicholson	120.4
5	Night at the Museum	Fox	Starring Ben Stiller	115.8
6	The Pursuit of Happyness	Sony	Starring Will Smith	98.4
7	The Santa Clause 3: The Escape Clause	Disney	Starring Tim Allen	83.5
8	Saw III	LGF		80.2
9	Open Season	Sony	Animation-voices of Martin Lawrence, Ashton Kutcher	67.9
10	Flushed Away	DW	Animation-voices of Hugh Jackman, Kate Winslet	62.0
				<u>1,083.4</u>

Source: Box Office Mojo, Wedbush Morgan Securities

Figure 31. 2007 Top Expected Films by Quarter

		2007		
	Movie	Studio	Comments	Release Date
Q1				
1	The Pursuit of Happyness	Sony	Starring Will Smith	12/15/2006
2	Dreamgirls	DW	Starring Jamie Foxx, Beyonce Knowles, Eddie Murphy	12/15/2006
3	Night at the Museum	Fox	Starring Ben Stiller	12/22/2006
4	Stomp the Yard	SGem	Troubled youth helps step team win the championship	1/12/2007
5	Norbit	DW	Starring Eddie Murphy	2/9/2007
6	Ghost Rider	Sony	Starring Nicolas Cage, Eva Mendes	2/16/2007
7	Bridge to Terabithia	Disney	Based on popular Newbery Award-winning novel	2/16/2007
8	Wild Hogs	Disney	Starring John Travolta, Tim Allen, Martin Lawrence, William H. Macy	3/2/2007
9	300	WB	300 Spartans fight to the death against Xerxes and Persian army.	3/9/2007
Q2				
1	Teenage Mutant Ninja Turtles	WB	Animation	3/27/2007
2	Spider-Man 3	Sony	Last release \$374mn	5/4/2007
3	Shrek the Third	DW	Last release \$441mn	5/18/2007
4	Pirates of the Caribbean: At World's End	Disney	Last release \$423mn	5/25/2007
5	Ocean's Thirteen	WB	Last release \$126mn	6/8/2007
6	Fantastic Four	Fox	Last release \$155mn	6/15/2007
7	Evan Almighty	Uni.	Last release-Bruce Almighty \$243mn	6/22/2007
Q3				
1	Ratatouille	Pixar/Dis.	Pixar Animation	6/29/2007
2	Transformers	DW	Action/Sci-Fi	7/4/2007
3	Harry Potter and the Order of the Phoenix	WB	Last release \$290mn	7/13/2007
4	I Now Pronounce You Chuck and Larry	Uni.	Starring Adam Sandler	7/20/2007
5	The Simpsons Movie	Fox		7/27/2007
6	Bourne Ultimatum	Uni.	Last release \$176mn	8/3/2007
7	Rush Hour 3	NL	Last release \$226mn	8/10/2007
Q4				
1	His Dark Materials: The Golden Compass	NL	Starring Nicole Kidman-Adventure/Fantasy Movie	12/7/2007
2	I am Legend	WB	Starring Will Smith-Sci-Fi Horror/Vampire Movie	12/14/2007
3	National Treasure 2	Disney	Last release \$173mn. Starring Nicholas Cage	12/21/2007

Source: Box Office Mojo, Wedbush Morgan Securities

Figure 32. Examples of Select DVD Release Windows

Picture	Film Release	DVD Release	DVD Days to Rel.
There's Something About Mary	7/15/1998	8/3/1999	384
Saving Private Ryan	7/24/1998	11/2/1999	466
The Matrix	3/31/1999	9/21/1999	174
Austin Powers: The Spy Who Shagged Me	6/11/1999	11/16/1999	158
The Sixth Sense	8/6/1999	3/28/2000	235
Toy Story 2	11/24/1999	10/17/2000	328
Gladiator	5/5/2000	11/21/2000	200
Mission: Impossible II	5/24/2000	11/7/2000	167
How the Grinch Stole Christmas	11/17/2000	11/20/2001	368
Cast Away	12/22/2000	6/12/2001	172
Shrek	5/16/2001	11/2/2001	170
Monsters, Inc.	11/2/2001	9/17/2002	319
Harry Potter and the Sorcerer's Stone	11/16/2001	5/28/2002	193
The Lord of the Rings: The Fellowship of the Ring	12/19/2001	8/6/2002	230
My Big Fat Greek Wedding	4/19/2002	2/11/2003	298
Spider-Man	5/3/2002	11/1/2002	182
Harry Potter and the Chamber of Secrets	11/15/2002	4/11/2003	147
The Lord of the Rings: The Two Towers	12/18/2002	8/26/2003	251
The Matrix Reloaded	5/15/2003	10/14/2003	152
Bruce Almighty	5/23/2003	11/25/2003	186
Finding Nemo	5/30/2003	11/4/2003	158
Pirates of the Caribbean: The Curse of the Black Pearl	7/9/2003	12/2/2003	146
The Lord of the Rings: The Return of the King	12/17/2003	5/25/2004	160
The Passion of the Christ	2/25/2004	8/31/2004	188
Shrek 2	5/19/2004	11/5/2004	170
Spider-Man 2	6/30/2004	11/30/2004	153
The Incredibles	11/5/2004	3/15/2005	130
Meet the Fockers	12/22/2004	4/19/2005	118
Star Wars: Episode III - Revenge of the Sith	5/19/2005	11/1/2005	166
War of the Worlds	6/29/2005	11/22/2005	146
Harry Potter and the Goblet of Fire	11/18/2005	3/7/2006	109
The Chronicles of Narnia: The Lion, the Witch and the Wardrobe	12/9/2005	4/4/2006	116
King Kong	12/14/2005	3/28/2006	104
Ice Age: The Meltdown	3/31/2006	11/21/2006	235
The Da Vinci Code	5/19/2006	11/14/2006	179
X-Men: The Last Stand	5/26/2006	10/3/2006	130
Cars	6/9/2006	11/7/2006	151
Superman Returns	6/28/2006	11/28/2006	153
Pirates of the Caribbean: Dead Man's Chest	7/7/2006	12/5/2006	151
Happy Feet	11/17/2006	3/27/2007	130
Casino Royale	11/17/2006	3/13/2007	116
The Pursuit of Happyness	12/15/2006	3/27/2007	102
Night at the Museum	12/22/2006	4/24/2007	123

Source: Wedbush Morgan Securities

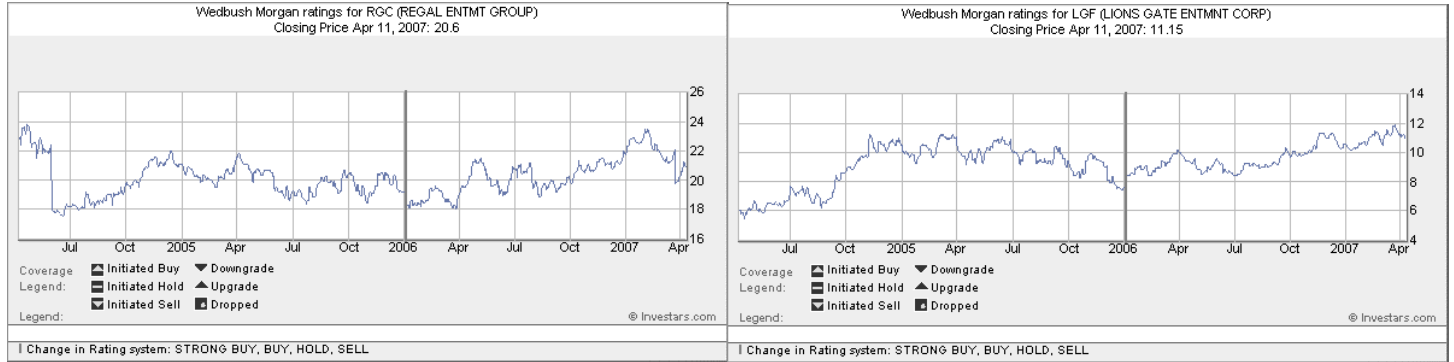
Public Companies Mentioned in this Report (priced as of close 4/11/07)

COMPANY	TICKER	RATING	PRICE	PRICE TARGET
Amazon.com Inc.	AMZN	NR	\$41.68	N/A
Apple Inc.	AAPL	NR	92.59	N/A
Carmike Cinemas, Inc.	CKEC	NR	24.87	N/A
Dreamworks Animation SKA	DWA	NR	28.82	N/A
IMAX Inc.	IMAX	NR	4.30	N/A
Lionsgate	LGF	BUY	11.15	\$13
National CineMedia, Inc.	NCM	NR	25.84	N/A
Regal Entertainment Group	RGC	BUY	20.60	24
Sony Corporation	SNE	NR	53.36	N/A
Texas Instruments, Inc.	TXN	NR	30.78	N/A
Walt Disney Co.	DIS	NR	34.59	N/A
Wal-Mart Stores, Inc.	WMT	NR	47.27	N/A

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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.

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