

Sigma Designs

(SIGM^{5,8} \$15.00) BUYJohn Vinh
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- **Initiating coverage of Sigma Designs (SIGM) with a Buy rating and \$22 price target.** SIGM produces media processor microchips for IPTV set-top boxes and is well poised to benefit from the anticipated ramp in IPTV deployments over the next several years. Our price target is based on 21x our fiscal 2008 (Jan) EPS estimate of \$1.03.
- **We expect Telco's aggressive push to offer consumers "triple-play" services to drive strong ramp in IPTV services.** As telecommunication providers attempt to compete against cable and satellite providers, it is clear that the battleground will be fought over the coveted "triple-play" package, which includes voice, broadband, and video. We expect that telcos will look to offer consumer video services through IPTV offerings and believe that this will be a significant catalyst for Sigma Designs moving forward.
- **Expect SIGM to benefit from strong growth in IPTV set-top boxes.** With multiple telcos currently in the process of ramping IPTV services, we expect growth in IPTV set-top boxes to be a growth driver for SIGM in 2H06 and into 2007. Current industry forecasts from Gartner indicates that production of digital IP set-top boxes is expected to grow from 2.8M units in 2005 to 4.5M units in 2006 (64% y/y) and to grow to 11.1M units in 2010 at an estimated 32% CAGR (between 2005-10).
- **Strategic partnership with Microsoft provides SIGM with a first mover advantage.** Due to the company's existing relationship with Microsoft and work on previous MSFT projects, it has allowed SIGM to be one of the first vendors in production with a media processor that supports Microsoft's VC-1 codec and IPTV platform. We expect Microsoft to be the dominant middleware platform for IPTV moving forward. At this point, ST Micro is the only other vendor that has a production-ready chip that supports Microsoft IPTV. However, no IPTV deployments to date have been deployed with it.
- **Expect early design wins in Blu-Ray to help sustain longer-term growth.** Being one of the first providers to release decoder chips that support both H.264 and VC-1, video codecs required by HD DVD and Blu-ray, has allowed Sigma Designs to secure multiple design wins in the high definition DVD market. We expect moderate growth in this market in the near term as consumers await a winner in the high definition DVD format wars. We ultimately believe that SIGM will benefit from strong design win activity in BD, as we believe Blu-ray disk will ultimately prevail over HD DVD.
- **Risks factors include:** 1) Competition from larger companies such as Broadcom and STMicroelectronics; 2) Uncertainty related to the ramp of worldwide IPTV deployments; 3) ASP and gross margin pressures associated with intense competition in the marketplace; 4) Uncertainty related to the outcome of the company's investigation into its internal option grant practices; risk of NASDAQ delisting as it has not yet filed its 10Q due to its internal option investigation.

Key Data

52-Week Range	\$7.99 - \$17.05
Weighted Average Shares (MM)	22.6
Float (MM)	22.1
% Held Institutionally	41.3%
Market Capitalization (MM)	\$339
Average Daily Volume (000)	637.8
Revenues - LTM (MM)	\$53.9
Total Debt (MM)	\$0.02
Cash per Share	\$0.67
Long-Term Growth Rate	20%
12-Month Price Target	\$22.00

Fiscal Year Ends: Jan.	<u>2006A</u>	<u>2007E</u>	<u>2008E</u>
Revenue (MM)	\$33.3	\$83.8	\$130
Earnings per Share			
Q1	\$(0.03)	\$(0.03)	\$0.18
Q2	\$0.01	\$0.06	\$0.24
Q3	\$0.08	\$0.12	\$0.28
Q4	<u>\$0.02</u>	<u>\$0.17</u>	<u>\$0.32</u>
Year	\$0.07	\$0.32	\$1.03
P/E	214x	46.9x	14.6x
Shares Fully Diluted (MM)	23.7	22.7	23.4



Sigma Designs is a supplier of digital media processor microchips for consumer electronic devices. The company's microchip decoder products are focused on five main consumer end markets including IPTV set-top boxes, high definition DVD players, portable media devices, digital media adapters, and HDTV.

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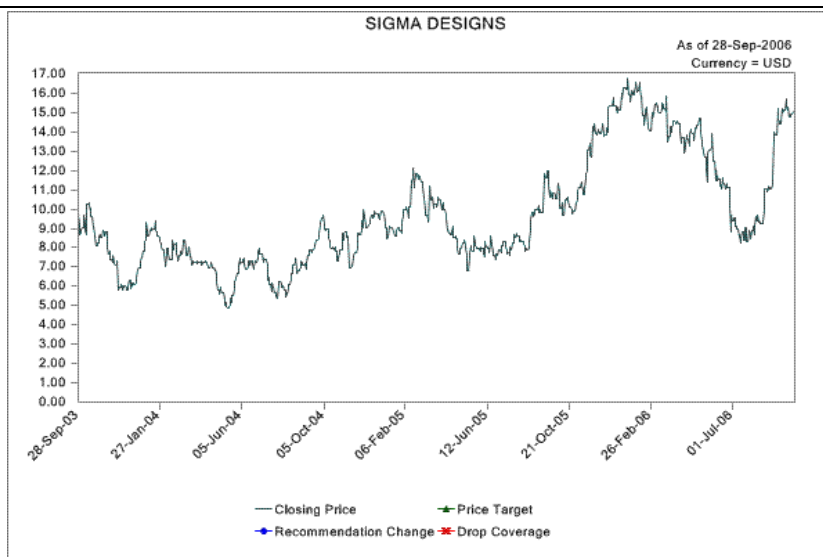
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SIGMA DESIGNS

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
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	% of CEUT Universe with this rating	% of rating tier for which CEUT provided IB services
Buy	57%	80%
Market Perform	39%	20%
Under Perform	4%	0%

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