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Liberty SiriusXM Group

(LSXMA/K)

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Find Me Value Investment Research

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What's Covered In this Deck?

- SIRI business, economics, valuation
- Overview of the re-attribution with FWON, why, and what that means going forward
- Brief overview of “Liberty” history in trackers and value creation (Greg Maffei / John Malone)
- NAV discount
- Valuation of SIRI, P, and LSXMA but using only market value for LYV assets (will be discussed in upcoming decks)
- Overview of other terms:
 - Call spreads
 - Exchangeable debt
 - Tracking stocks
- What is not covered here, but will be covered in upcoming decks:
 - Live Nation (LYV)
 - iHeart Radio (IHRT)
 - Music Labels
 - Spotify (SPOT)
 - Pandora (P) as a separate business

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SiriusXM Satellite Radio



SiriusXM Overview "SIRI"

Stock Price	\$	6.00	
Shares Outstanding		4,405.00	
Market Capitalization	\$	26,430	
Debt	\$	7,847	
Cash	\$	40	
Enterprise Value	\$	34,237	
Estimates	2020	2021	2022
Revenues	\$ 6,471	\$ 6,819	\$ 7,133
EBITDA	\$ 2,491	\$ 2,591	\$ 2,746
EBITDA Margin	39%	38%	39%
FCFF	\$ 2,179	\$ 2,201	\$ 1,935
FCFE	\$ 1,781	\$ 1,815	\$ 1,616
FCFE/sh.	\$ 0.40	\$ 0.43	\$ 0.41
Est. LSXM Ownership	75.0%	80.0%	81.6%
Subscribers (paying)	30,727	31,711	32,503
Enabled Fleet (mil)	139	154	170
CapEx	\$ 300	\$ 250	\$ 200
Capital Intensity	4.6%	3.7%	2.8%
Stock Performance	YTD 2020	3 Yr	5 Yr
SIRI	-16.8%	10.7%	59.0%
SPX	0.4%	30.5%	52.2%



SiriusXM Business Overview

- SiriusXM is an audio entertainment service that primarily offers talk, music, sports, comedy, news, and traffic distributed through XM or Sirius satellite radio systems. A majority of subscribers listen to the service inside their vehicle, where the SiriusXM hardware was installed by the auto manufacturers during.
- The primary source of revenue is subscription fees (> 80% of revenue, \$6.3bn TTM) via the SiriusXM product, which has 30.0m paying subscribers at an ARPU of ~ \$14/month.
- Churn levels are low for SIRI paying subscribers at an average range of 1.7% - 1.8% per month (compared to ~4.0% - 4.5% monthly churn for SPOT, reported Q2 2019)
- The competitive advantages SXM has are:
 - **Content** - differentiated versus just music, given the strong brands and people, also helping with an ability to have more scaled economics versus music platforms
 - **Auto OEM relationships** – shared economics with auto OEMs + long term relationships give SXM key placement inside the dashboard, as well as auto OEMs pushing for new car owners to have a 3 month – 1 year free trial of the SiriusXM product. SXM also is involved with the dashboard technology 3-5 years out and can adjust their service based on this. ~80% of new cars sold have SiriusXM installed during the manufacturing process.
 - **Satellite delivery** – improves the economics of the royalty rates, as well as providing a very low CapEx business model
 - **Scale** – With more than 30 million paying subscribers, and a ~80% penetration of new cars, along with declining cost curves, SAC per hardware install has declined substantially from \$60 - \$70 in 2008/2009 to just \$20 in Q1 2020. This makes the economics more favorable for increasing the penetration of new vehicles to lower-end models, as the average car turns over 3.2x, giving SXM 3 chances to win a customer over for a one time install cost.
 - **Cross selling with Pandora** – part of the Pandora acquisition was to leverage the massive enabled vehicle fleet SXM has already paid to have their hardware built in. With 128m vehicles currently, moving to >220m in the next decade, at some point the SiriusXM satellite product will be fully saturated and ~180m +/- vehicles on the road will have SXM installed but not a paying subscriber. The opportunity of still marketing to these owners a free ad-supported streaming service could provide some upside for Pandora's advertising revenue.

SiriusXM Business Overview

Will discuss Pandora more in upcoming decks. This deck is focused on SIRI / LSXM



SiriusXM (SIRI)

Sirius/ XM

The “cash cow” for the business: 80% of revenues (\$6.3bn), 90% of gross profits, 40% EBITDA margins

30m paying subscribers, 128m installed vehicles on the road in U.S.

Company formed through a merger between Sirius and XM in July 2008

Saved from bankruptcy < year after merger thanks to Liberty Media

Pandora (Audio Streaming Service)

<20% SIRI overall revenues, <10% of gross profit due to higher COGS

Acquired by SIRI in Q1 2019 for \$3.5bn in all-stock deal after previously investing \$480m in June 2017

Service will be used to attract non-SIRI paying subs, drive free ad-supported revenues, attract more content

61m MAUs (in decline) + 6.2m paying subscribers

SiriusXM Canada

2.7m subscribers

70% equity interest, 33% voting interest

SXM Canada pays SIRI 25% of gross revenues on a monthly basis + 5% of gross revenues on monthly basis for advisory fee

Podcast

Stitcher (acquired for \$325m in Q2/Q3 2020)

Simplecast (acquired 2020, undisclosed \$)

SoundCloud (2019 \$75m minority investment)

Connected Vehicle

~\$160m in revenues, SIRI has stated it is growing >10%, very profitable

Offered through “Automatic Labs” (subsidiary) consumers can connect an adapter to a mobile device, making it a connected vehicle. Helps connect drivers to the auto OEMs as well.

The “Story” for SXM / LSXM

- SXM has a high-functioning audio subscription services that largely caters towards above-average income earnings who are willing to pay for exclusive (largely non-music) audio content
- This business models has proven to be very stable, despite ebbs and flows from auto sales and competing audio services (like Pandora, Spotify, Apple Music, YouTube Music, etc.)
- SXM has exclusive relationships with the auto OEMs, and their agreement has been 10-15 years+ in the making, allowing them to have insight as to the technology and improvements inside future vehicle models 3-4 years or more in advance
- Given they focus less-so on music directly, they have a different cost structure versus streaming music providers, resulting in far more favorable economics (example: > 60% gross margins, ~40% EBITDA margins, low-middle single digit capital intensity)
- SIRI almost went into bankruptcy following the XM/SIRI merger and excessive debt load; Liberty (via John Malone, Greg Maffei) stepped in in 2009 with an investment that gave them conversion towards 40% equity ownership and de facto capital allocation decision making
- The strong business model, while not growing at a remarkable nor increasing pace (low-mid single digit top line), offers amplified equity returns due to the cost structure, minimal taxes for the next 1-2 years, low capital intensity (3-6% of revenues) alongside a capital allocation story of heavy equity buybacks that will eventually push Liberty Media ownership from 72.2% (Q1/20) to 80%+ and thereby shifting the capital allocation story more towards low-tax dividends to parent “LSXMA”, who should repurchase shares in LSXMA at a substantial discount to net asset value (NAV), which is currently ~36%, near the highest discrepancy since LSXM was created

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Content Offering

- One of the large components of the content offering for SXM is Howard Stern (The Howard Stern Show)
 - Signed to stay on air for 5 years in December 2015 as part of a 12 year deal
 - SXM also purchased the 12 year rights to Stern's audio and video performances from his 30 year
 - It was estimated his previous 5 year deal included \$500m in cash and stock (Macquarie Securities, Amy Yong)
 - Stern originally signed on with Sirius and began January 2006. At the time Sirius pegged his total production and operating costs of about \$100m per year. XM radio and SiriusXM had a combined 2.7m subscribers then, with Sirius having only 600k.

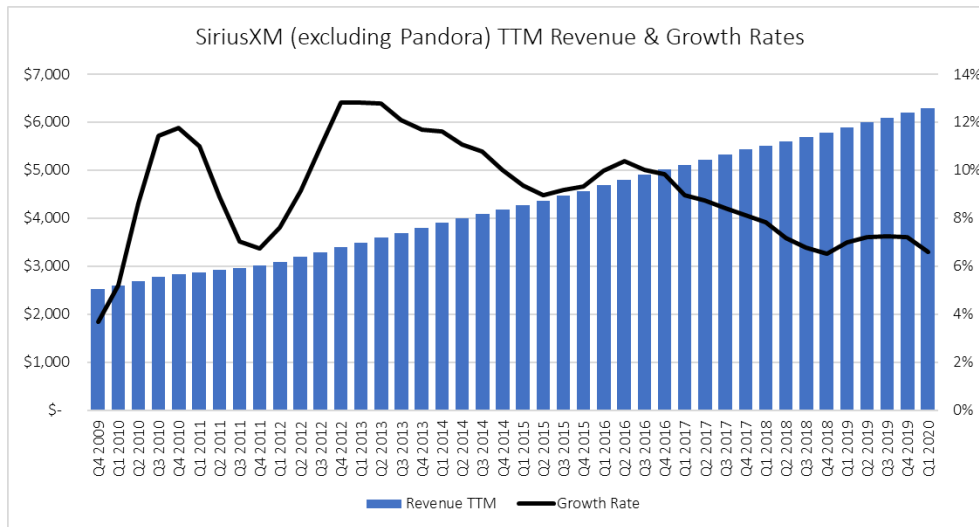


SiriusXM Revenue Breakdown

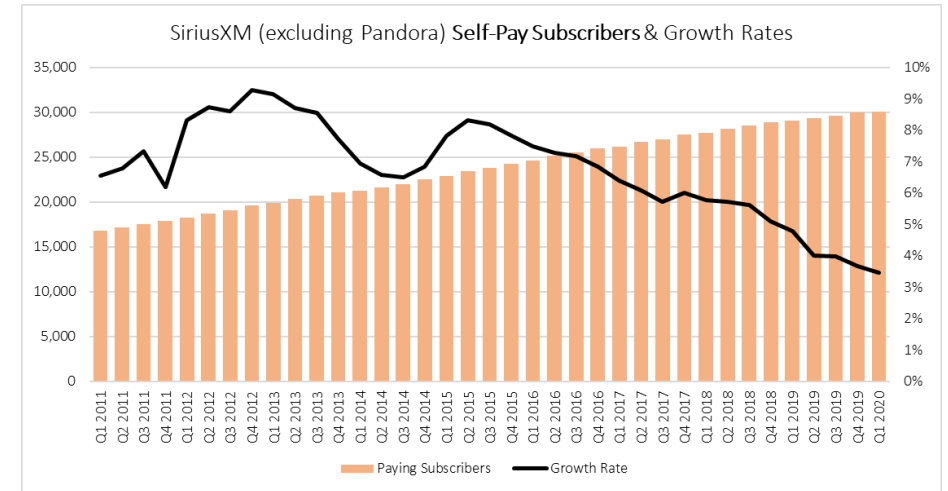
TTM revenue of \$6.3bn = 92% subscription / 8% advertising, other

Slowing revenue to 6.6% TTM due to lower subscriber (“volume”) growth rates, as the SiriusXM service gets more saturated and nears reaching saturation

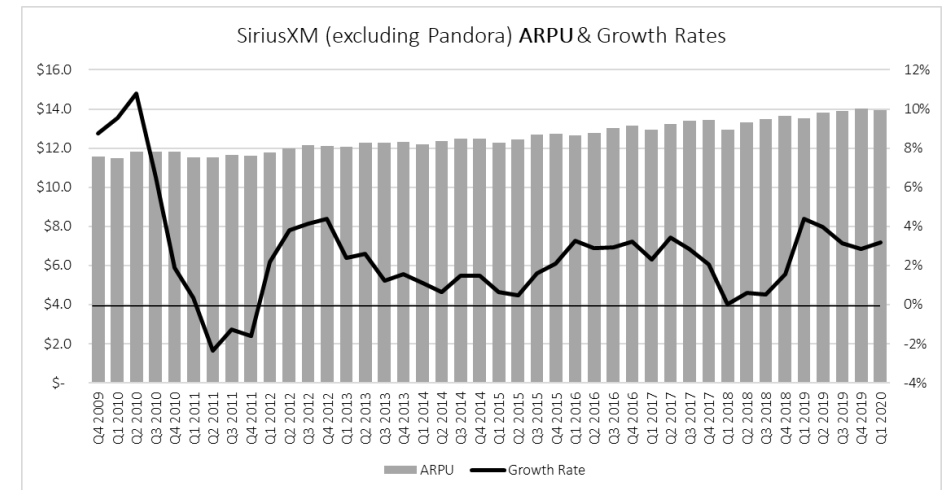
Pricing has and is expected to remain around CPI-ish levels, around 1-2% over time, despite ebbs and flows on an annual or quarterly basis



Volume



Pricing



Trends Affecting SXM's Business

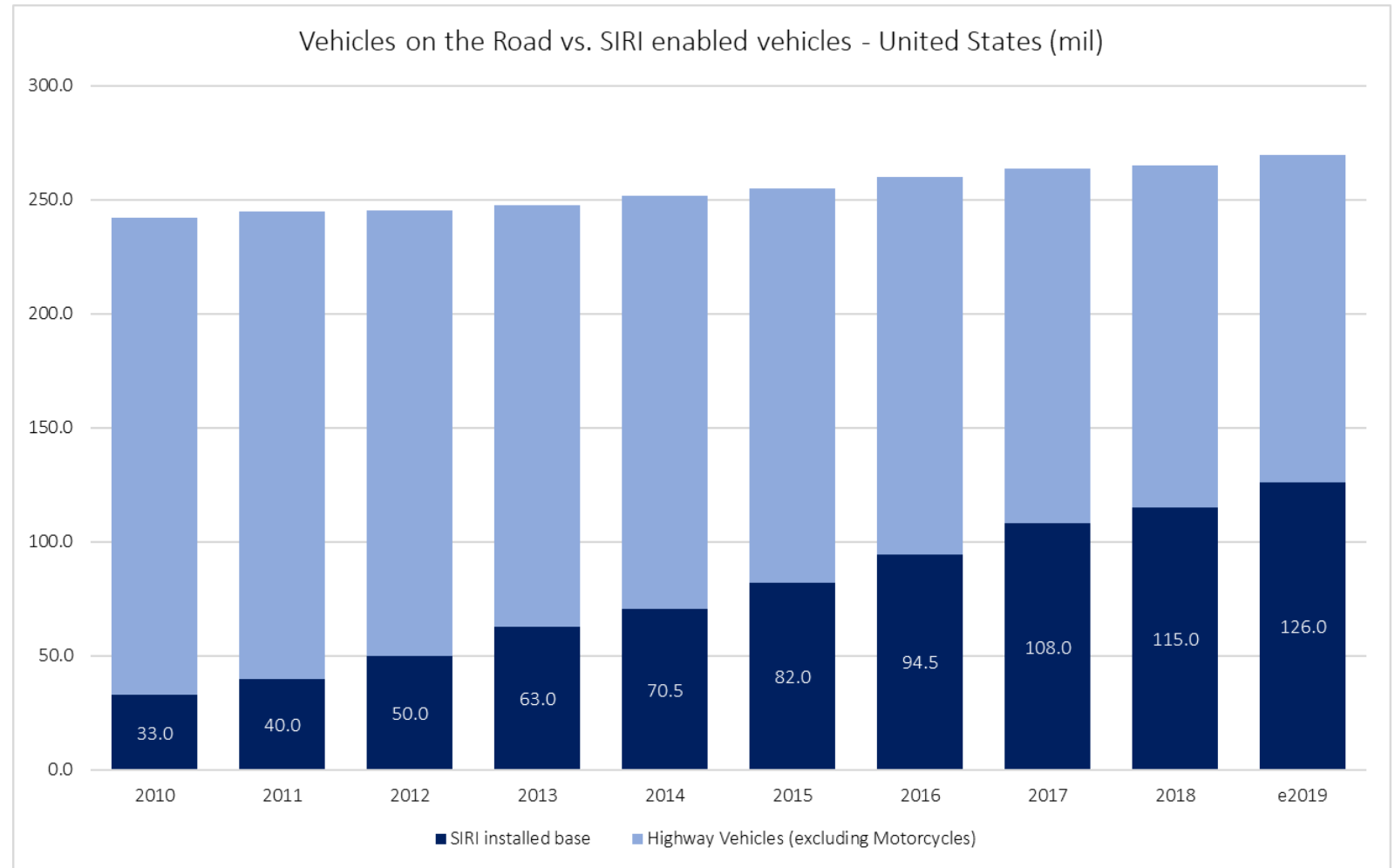


Trends Affecting SXM Business

- US SAAR – new vehicle sales & avg. pricing
- Trends around New Car Sales Activity, such as:
 - Average vehicle age on the road
 - Average price of a new vehicle
 - Financing for new vehicles
- Penetration of SXM-enabled hardware in new vehicles + overall enabled fleet in U.S.
- Used car sales + penetration of used car sales with SXM enabled hardware (which will eventually align with new car penetration %)
- Total miles driven in U.S. – SXM is a predominantly in-the-car audio service
- # of vehicles registered in the U.S. – SXM is enabled in ~75-80% of subsequently sold new vehicles. Over ~10 years the overall # of U.S. vehicles registered will have roughly ~75-80% of them with SXM installed, which represents the overall “installed base” which SXM paid to have installed, i.e. the opportunity for converting to subscribers
- Podcasting advertising revenue in U.S.

Vehicles Registered in the U.S.

- SXM pays auto OEMs to install the hardware inside the dashboard of a new vehicle
- Historically, SXM subscriber trends were heavily dependent on new car sales SAAR as only new vehicles had SXM installed as an option, and older vehicles did not (they had to purchase the aftermarket hardware)
- This represents some problems and opportunities:
 - The used car market in the U.S. is ~2x larger than the new car market
 - SXM pays an upfront SAC to have vehicles installed with SXM hardware, but then they sell this car ~6 years later, and the now-used vehicle has SXM built in, already installed, and has a new potential subscriber with the new owner
 - Out of ~270m vehicles registered in the U.S., ~95% are considered >1 year old, and thus SXM's heavy dependence on new car sales could diminish with penetration of the used car market
 - Incremental margins on converting a used car owner to become a subscriber is > 70%, compared with EBITDA margins for SXM of ~40%



Average Age of Light Vehicles in the U.S.

- Average age of light VIO (vehicles in operation) in US is **11.8 years** – IHS Markit
- From 2002-2007 average age rose by **3.5%**, post the great recession, from 2008-2013, the increase was **12.2%**
- People held on to their cars longer during a recession, attempting to extend the life longer
- From 2014-2019 average age is 4% growth
- “Better technology and overall vehicle quality improvements continue to be key drivers of the rising average vehicle age over time,” said Mark Seng, director, global automotive aftermarket practice at IHS Markit. “The 40% drop in new vehicle sales due to the recession created an acceleration in average age like we’ve never seen before. In the last couple of years, however, average age has returned to its more traditional rate of increase.”
- As people are purchasing SUVs and trucks, the average age of “light trucks” went up 0.1% yet passenger cars +2.2% in 2018-2019
- HIS Markit estimates 0-5 year old vehicles will grow 2% from 2018-2023, but 6-11 year old will grow 27% which is the sweet spot for repair shops and DIY, and 12-15 year old vehicles will decline 27% over same period
- Vehicles 16 years and older expected to grow 22% from 2018-2023 reaching 84m in 2023
- Source: <https://www.tirereview.com/average-age-cars-light-trucks/>

Liberty's Involvement



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SIRI Stock Chart & History



Liberty Media Investment

- In February 2009 Liberty Media announced they entered into an agreement in which they would invest an aggregate \$530m in the form of loans to SiriusXM to receive an interest in SiriusXM (SIRI) to help prevent SIRI from bankruptcy / takeover by DISH
- The terms: (based on the press release)
 - The first phase includes a \$280 million senior secured loan from Liberty to SIRIUS XM, \$250 million of which will be funded today. The proceeds of that loan will be used by SIRIUS XM to repay \$171.6 million of its maturing 2 1/2% Convertible Notes due February 17, 2009, and the balance will be used for general corporate purposes, including working capital and transaction costs. **The loan will bear interest at a rate of 15%**, mature in December 2012, and be secured by the assets securing SIRIUS XM's existing term credit agreement.
 - The second phase provides an additional loan of \$150 million to XM Satellite Radio, SIRIUS XM's wholly owned subsidiary. Liberty has also agreed to offer to purchase up to \$100 million of the loans outstanding under XM Satellite Radio's existing credit facilities from the lenders. (note: SIRI used this to repay a portion of its 10% convertible notes due December 2009)
- Upon completion of the 2nd phase, SXM will issue Liberty an aggregate 12.5m shares of preferred stock convertible into 40% of common stock of SiriusXM
- John Malone and Greg Maffei joined the Board of Directors at SXM
- At the time SiriusXM had 18.9m subscribers
- Essentially the investment rescued SiriusXM from default / takeover bid from DISH Network (DISH). DISH / Charlie Ergen bought \$300m of Sirius near term in an attempt to acquire some of its assets / take control if SIRI filed for bankruptcy
- XM Satellite Radio merged with Sirius in 2008 and was saddled with debt and declining auto sales in the U.S.

Liberty Involvement Timeline - *Early Days*

- With the investment in 2009, John Malone and Greg Maffei were put on the Board of Directors at SiriusXM
- Through the 2009 investment, Liberty (I refer to as either Liberty, LMCA, LSXM) held 12.5m Series B-1 Preferred Shares, conversion option to 40% of total shares outstanding
 - March 2012 - Liberty / John Malone – wanted to take control of SiriusXM through the conversion and subsequent ownership stake of 40% of SIRI, and requested to take control in a March 2012 request to the FCC, arguing they had de facto control with the 40% stake and board of director positions. Liberty's \$530m investment rose to ~ \$6bn by this time.
 - May 2012 - The FCC denied Liberty's take control request
 - Liberty responds they will get the ownership to > 50% if that helps get the request approved
 - May 2012 – days after the FCC denied request, Liberty Media raised its stake to as-converted 45.2% in a filing, buying 302m shares for \$2.15 each
 - Given the FCC seemed bent on denying Liberty “control”, with Liberty's investment and BOD positions, they eventually put Greg Maffei as Chairman
 - September 2012 – LMCA converts about half of the preferred shares, giving it a 32% actual equity ownership stake, and as-converted 49.5% if they converted remaining preferred stock
- Then 2012 SiriusXM CEO Mel Karmazin disliked the Liberty investment and oversight, urging the FCC to deny *de jure* control, and saying he didn't want Liberty as a “boss”.
- December 2012 – SiriusXM, under de facto control by LMCA, announced a special dividend (\$327m) and that they will begin a \$2bn share repurchase program. LMCA owned 49.8% of SIRI at this time.
- December 2012 - Maffei and Malone appoint Jim Meyer, previously President of Sales and Operations under Mel Karmazin, as CEO of Sirius XM, effectively firing Karmazin, who disliked Liberty's involvement and hands-on approach