

ALGORITHM CAPITAL

INVESTMENT RESEARCH

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TRANSMETA (TMTA \$15.04) Rating: Buy

Price Target	\$23.40	Shares Outstanding (MM)	12.3
52 Week Range	\$4.10 - \$15.70	Market Value (MM)	\$185
P/E Ratio (Forward)	7.3	Beta	1.8
Price/Sales Ratio (Forward)	6.3	Average Volume	140,900
Cash Per Share	\$12.65	Insider Holdings	23.0%
Book Value	\$0.19	Institutional Ownership	27.0%

Company description: Based in Santa Clara, CA., Transmeta develops and licenses computing, microprocessor, and semiconductor technologies and related intellectual property. The company focuses on developing and licensing advanced power management technologies for controlling leakage and increasing power efficiency in semiconductor and computing devices.

Investment Update

Transmeta reported second quarter revenue of \$366,000, all of which was from licensing. This compares to \$240,000 in license revenues during the first quarter of 2008. Net income was \$214,000, or \$0.02 per share, vs. a net loss of \$410,000 or \$0.0 per share in 1Q08.

Transmeta's transition to a established licensor of intellectual property took another step forward with the announcement of a \$25 million agreement with NVIDIA for LongRun2 Technologies.

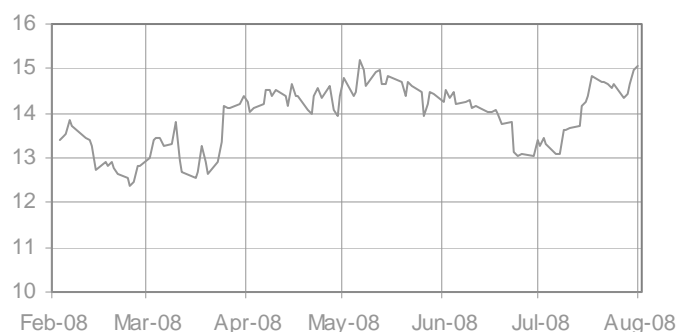
In addition to licensing their technology to chip manufacturers and designers, Transmeta is currently testing its LongRun2 power saving technology with a major fab in Asia. We expect an a licensing deal to be announced sometime during the second half of the year.

Transmeta has developed unique technologies that improve chip yields and address the critical problem of power leakage. We reiterate our buy recommendation and raise our price target from \$18.75 to \$23.40 based on valuation methodologies highlighted below.

EPS		2007A	2008E (old)	2008E (new)
Q1	Mar	\$(1.88)A	\$0.00A	\$0.00A
Q2	June	(1.15)A	0.01E	0.02A
Q3	Sept	(1.24)A	0.01E	1.79E
Q4	Dec	(1.99)A	0.18E	0.17E
Year (Dec)		\$(6.33)A	\$0.20E	\$1.98E

Revenue (MM)		2007A	2008E (old)	2008E (new)
Q1	Mar	\$2.07A	\$0.66A	0.66A
Q2	June	0.17A	1.00E	0.37A
Q3	Sept	0.04A	1.42E	26.10E
Q4	Dec	0.13A	3.60E	2.75E
Year (Dec)		\$2.41A	\$6.68E	\$29.88E

TMTA



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INVESTMENT OVERVIEW

Transmeta has ceased manufacturing microprocessors. The company is now focused on licensing its LongRun2 power and yield management technologies to chip makers, designers, and fabs as well as developing intellectual property.

2Q OVERVIEW

Revenue for the second quarter of 2008 was \$366,000 compared to \$171,000 during the second quarter of 2007 and \$661,000 for the first quarter of 2008. All of 2Q 2008 revenues were all from licensing. This compares to none in 2Q 2007 and \$240,000 in 1Q 2008. Net income was \$214,000, or \$0.02 per share, compared with a net loss of \$41,000, or \$0.00 per share, in the first quarter of 2008 and a loss of \$11.45 million or \$-1.15 in 2Q07.

Total operating expenses for the second quarter of 2008 were \$1.9 million, compared with \$3.1 million in the first quarter of 2008 and included net restructuring charges of \$455,000, non-cash charges of \$908,000 for amortization of intangible assets, and non-cash stock compensation charges of \$1.3 million. This was partially offset by the \$5.9 million of income from the settlement and licensing agreement with Intel. Interest income was \$1.8 million, including \$1.1 million of imputed interest income from the settlement and licensing agreement with Intel.

Cash and short term investments at June 30, 2008 were \$141.8 million vs. \$158.8 million on March 31st. \$12.5 million of the \$17.0 million decline was attributable to accrued compensation related to the cash bonus that the company paid to its general counsel for negotiating the \$250 million litigation settlement and licensing deal with Intel.

INVESTMENT OUTLOOK

With the licensing deal with NVIDIA, Transmeta took another step forward in its transition to an established licensor of IP. While we expected a microprocessor maker like AMD to be the next chip maker to license LR2, NVIDIA was in a difficult position after several of its graphics processors recently failed due to thermal stress. The damage to NVIDIA's reputation, balance sheet, and share price could encourage other chip makers to adopt power saving technologies like LongRun2.

With the exception of the one time \$25 million from NVIDIA, the majority of Transmeta's income in 2008 will come from the patent litigation settlement with Intel. TMTA received the initial \$150 million payment in January. It will receive annual payments of \$20 million each January from 2009 through 2013, for total payments of \$250 million. Transmeta will recognize \$234.6 million as an operating gain from the litigation settlement by using a subscription model over the ten year capture period through 2017, and \$15.4 million of interest income over the payment period from 2008 to 2013.

Transmeta will recognize \$5.87 million as an operating gain from the Intel settlement for each of the four quarters of 2008 for a total of \$23.46 million. The Company expects to recognize \$1.2 million in imputed interest income from the settlement in each of the remaining two quarters of 2008.

NEC's M2 chipset for low power applications, the primary royalty paying product for Transmeta, continues to gain traction with wireless applications. Several of Transmeta's licensees are currently sampling products that utilize LongRun2 technologies. We expect production royalties from at least one of these products sometime in the second half of the year.

Transmeta is currently testing and modifying its LongRun2 technologies at a major chip foundry in Asia. We expect the companies to sign a license agreement sometime in the second half of the year.

With the NVIDIA deal, our 2008 revenue estimate has been increased to \$29.88 million from \$6.68 million. Our 2008 EPS estimate has been increased from \$0.20 to \$1.98.

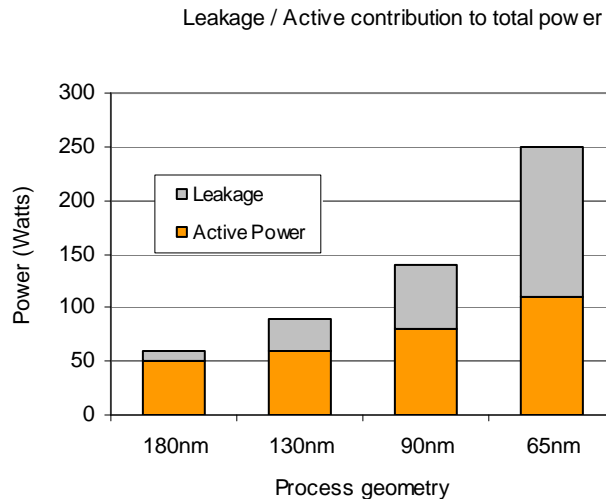
PRICE TARGET

Our price target has been raised from \$18.75 to \$23.40 based on a blended valuation of the discounted cash flow model and P/E of 15 X 2008 EPS of \$1.98. The DCF model used a discount rate of 14.00%.

THE POWER LEAKAGE PROBLEM IN CHIPS

Power usage is one of the biggest issues facing chip designers and manufacturers today. The problems of excessive chip heat and transistor leakage get progressively worse as fabrication process technologies scale down from 90 nm (nanometer) to 45 nm dimensions. Leakage, also known as standby power consumption, is power that is dissipated when a device is powered-up, but idle.

The newest chips are extremely dense with over 500 million transistors squeezed onto them. The closer the transistors are to each other the higher the temperature and leakage gets. The higher the leakage is the more power the chip requires completing a vicious cycle.



Transmeta's LongRun2 Technologies provide semiconductor manufacturers and chip designers with innovative ways to reduce power consumption and leakage as well as reduce variations between chips, which improves yields. LongRun2 Technologies include algorithms, modular circuits, unique structures, software, and manufacturing optimization techniques. In addition to their use during chip design, the technologies can also be utilized post manufacturing to correct process variation.

Other approaches to reduce power leakage include using strained silicon and tri-gate (3-D) transistors. LongRun2 technologies are complementary to these solutions.

TECHNOLOGY PORTFOLIO

Transmeta's patent portfolio continues to grow. It added 26 patents in 2007 and has added another 19 in 2008, bringing its total U.S. patent portfolio to 135. In addition to its portfolio of intellectual property for power and yield management, the company has developed the IP for microprocessor cores.

RECOMMENDATION HISTORY

Date	Closing Price	Rating	Price Target
5/15/2008	\$ 14.95	Buy	\$ 18.75
3/20/2008	\$ 12.68	Buy	\$ 18.75
11/28/2007	\$ 12.96	Buy	\$ 18.75

GENERAL DISCLOSURES

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I, Philip Zera, hereby certify that the views expressed in this research report accurately reflect my personal views and opinions about the subject company and its securities. I also certify that I have not and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation in this report.

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