

Rating	Buy 1 <i>Unchanged</i>
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Price target	US\$38.00 <i>Prior: US\$32.00</i>
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Price	US\$29.26
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RIC: NICE.O BBG: NICE US

29 December 2004

UBS Investment Research
Nice Systems Limited

Expecting Strong Q4 - Raising Price Target to \$38

■ Comfortable with our Q4 high-end EPS estimate

We forecast NICE will meet our Q4 EPS estimate of 47c (guidance is 44c-49c) when they report Q4 results expected during the first week of February. We note that our estimate is the highest among published forecasts in IBES and is 2c higher than consensus.

■ NICE Perform should start contributing in 2005E

We do not expect any significant revenues this quarter from NICE Perform and estimate NICE added less customers this quarter compared to the 8 new ones signed on in Q3, who were testing the product beforehand. We believe that our \$5m estimated revenue contribution from this product in 2005 is below management's internal targets.

■ Adjusting estimates and introducing 2006E

We are shaving 1c off our Q4 EPS estimate and 5c of our 2005 forecast, driven primarily by a higher share count of fully diluted shares used in calculating EPS, a result of the recent appreciation in the share price. We are also introducing 2006 estimates for revenues of \$305m (+9%) and EPS of \$1.90 (+23%).

■ Valuation: Raising target to \$38 from \$32

We continue to rate NICE shares a Buy-1 and our revised price target is still derived by using what we consider to be an undemanding PE of 20x; however, we are shifting to our '06 forecast from '05. We note that NICE trades at a meaningful discount to some of its competitors.

Trading data

52-wk. range	US\$29.63-17.85
Market cap.	US\$0.54bn
Shares o/s	18.5m
Free float	80%
Avg. daily volume ('000)	104
Avg. daily value (US\$m)	2.7

Balance sheet data 12/04E

Shareholders' equity	US\$0.23bn
P/BV (UBS)	2.5x
Net cash (debt)	US\$0.15bn

Forecast returns

Forecast price appreciation	+29.9%
Forecast dividend yield	0.0%
Forecast stock return	+29.9%
Market return assumption	8.1%
Forecast excess return	+21.8%

EPS (UBS, US\$)

	12/04E			12/03
	From	To	Cons.	Actual
Q1	0.14	0.14	0.14	0.03
Q2	0.24	0.24	0.24	0.13
Q3	0.28	0.28	0.28	0.19
Q4E	0.48	0.47	0.45	0.39
12/04E	1.14	1.14	1.11	
12/05E	1.55	1.55	1.49	

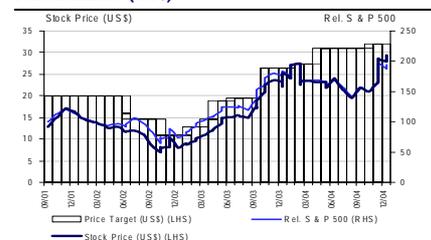
Highlights (US\$m)	12/02	12/03	12/04E	12/05E	12/06E
Revenues	155	224	252	279	305
EBIT	(6)	12	20	30	40
Net income (UBS)	(3)	13	21	30	39
EPS (UBS, US\$)	(0.20)	0.73	1.14	1.55	1.90
Net DPS (UBS, US\$)	0.00	0.00	0.00	0.00	0.00

Profitability & Valuation	5-yr hist. av.	12/03	12/04E	12/05E	12/06E
EBIT margin %	3.2	5.2	7.9	10.8	13.1
ROIC (EBIT) %	6.0	12.5	25.9	41.5	54.6
EV/EBITDA x	22.4	4.7	12.3	8.5	-
PE (UBS) x	74.3	20.9	25.7	18.9	15.4
Net dividend yield %	0.0	0.0	0.0	0.0	0.0

Source: Company accounts, Thomson Financial, UBS estimates. UBS EPS is stated before goodwill, exceptionals and other special items. Valuations: based on an average share price that year, (E): based on a share price of US\$29.26 on 28 Dec 2004

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Performance (US\$)


Source: UBS

www.ubs.com/investmentresearch
ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 3

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We estimate that NICE will meet our high-end Q4 EPS estimate of 47c, which is 2c higher than consensus, when they report results during the first week of February. We are shaving 1c off our Q4 estimate due to the share price appreciation this quarter, which we estimated impacted the share count. During its Q3 conference call held on November 3, 2004 management reiterated its full year '04 EPS guidance of \$1.10 and \$1.15 yielding Q4 guidance of 44c-49c. We believe the strength in the quarter was spread across business segments though we estimate the enterprise business was particularly strong driven by year-end spending patterns.

We are comfortable being the high-end of Q4 estimates

We have also slightly adjusted our EPS estimates for 2005, and while we have not changed our 2005 revenue estimate of c\$280m (guidance is \$275-280m) we shaved 5c off our EPS estimate, which is now \$1.55 (guidance \$1.40-1.50). We estimate that the 35% increase in the share price since the end of Q3 will impact the share count used to calculate EPS and we have adjusted our model accordingly.

Shaving 5c off 2005E EPS due to expected higher share count

We are also at this time introducing 2006 estimates for revenues of \$305m (+9% y/y) and EPS of \$1.90 (y/y +23%). We believe that the success of NICE-Perform will be a key growth driver and we believe our \$15m revenue estimate for that product in 2006 is conservative (up from an estimated \$5m in 2005). It is important to note that NICE-Perform is sold as part of a suite of products unless the customer is already using NICE's solutions used to capture the data/interaction. Accordingly, forecasting NICE-Perform revenues on a standalone basis is not necessarily relevant. We estimate that in Q4 NICE recognized a minimal amount of revenues (if at all) from NICE Perform and we do not believe the company was able to match the number of customers it added for the product in Q3 (8) as those were mainly customers that were testing the product beforehand.

Introducing '06E EPS estimates of \$1.90 +23% above our '05E

We believe NICE is entering 2005 with a product portfolio that should enable it to at least achieve their current guidance. However, it is prudent, in our opinion, to highlight the fact that historically Q1 is seasonally weak and we believe that pattern will continue in 2005 as well. We are currently modelling for a q/q decline of -6% roughly the same as in Q1-04.

Q1-05 expected to be seasonally lower than Q4

We continue to view NICE as an attractive investment. We are increasing our price target to \$38 from \$32 still based on what we consider to be an undemanding PE of 20x. However, we are shifting our target PE to 2006E from 2005E. We note that even after the recent appreciation in the share price NICE is still trading at a meaningful discount to competitors such as Verint which currently commands a 2005E PE of 35x and Witness Systems (WITS, \$17.76) which trades at 31x consensus 2005 estimates. In comparison, NICE is currently trading at 19x our '05E EPS estimate. We continue to rate NICE shares a Buy-1.

Upping price target to \$38 from \$32, shares trade at meaningful discount to competitors

■ Nice Systems Limited

NICE Systems offers multimedia digital recording solutions, applications and related professional services for business interaction management. Products are sold primarily to contact centres, financial institutions, public safety sites, ATC (air traffic control) sites, CCTV (closed circuit television) security installations and government institutions. Corporate headquarters are based in Israel, with subsidiary companies and local offices in the United States, Canada, Germany, United Kingdom, France and Hong Kong.

■ Statement of Risk

We forecast that NICE's growth will be driven by the success of its new product NICE Perform. A failure of that product will most likely have a negative impact on financial results.

■ Analyst Certification

Each research analyst primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.

Required Disclosures

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UBS Investment Research: Global Equity Ratings Definitions and Allocations

UBS rating	Definition	UBS rating	Definition	Rating category	Coverage ¹	IB services ²
Buy 1	FSR is > 10% above the MRA, higher degree of predictability	Buy 2	FSR is > 10% above the MRA, lower degree of predictability	Buy	41%	33%
Neutral 1	FSR is between -10% and 10% of the MRA, higher degree of predictability	Neutral 2	FSR is between -10% and 10% of the MRA, lower degree of predictability	Hold/Neutral	50%	33%
Reduce 1	FSR is > 10% below the MRA, higher degree of predictability	Reduce 2	FSR is > 10% below the MRA, lower degree of predictability	Sell	9%	27%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS; as of 30 September 2004.

KEY DEFINITIONS

Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

Market Return Assumption (MRA) is defined as the one-year local market interest rate plus 5% (an approximation of the equity risk premium).

Predictability Level The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

Under Review (UR) Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

Rating/Return Divergence (RRD) This qualifier is automatically appended to the rating when stock price movement has caused the prevailing rating to differ from that which would be assigned according to the rating system and will be removed when there is no longer a divergence, either through market movement or analyst intervention.

EXCEPTIONS AND SPECIAL CASES

US Closed-End Fund ratings and definitions are: Buy: Higher stability of principal and higher stability of dividends; Neutral: Potential loss of principal, stability of dividend; Reduce: High potential for loss of principal and dividend risk.

UK and European Investment Fund ratings and definitions are: Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Reduce: Negative on factors such as structure, management, performance record, discount.

Core Banding Exceptions (CBE): Exceptions to the standard +/-10% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Companies Mentioned table in the relevant research piece.

Companies mentioned

Company Name	Reuters	Rating	Price
Nice Systems Limited ¹⁶	NICE.O	Buy 1	US\$29.26
Verint Systems Inc. ^{4,16}	VRNT.O	Reduce 1	US\$36.58

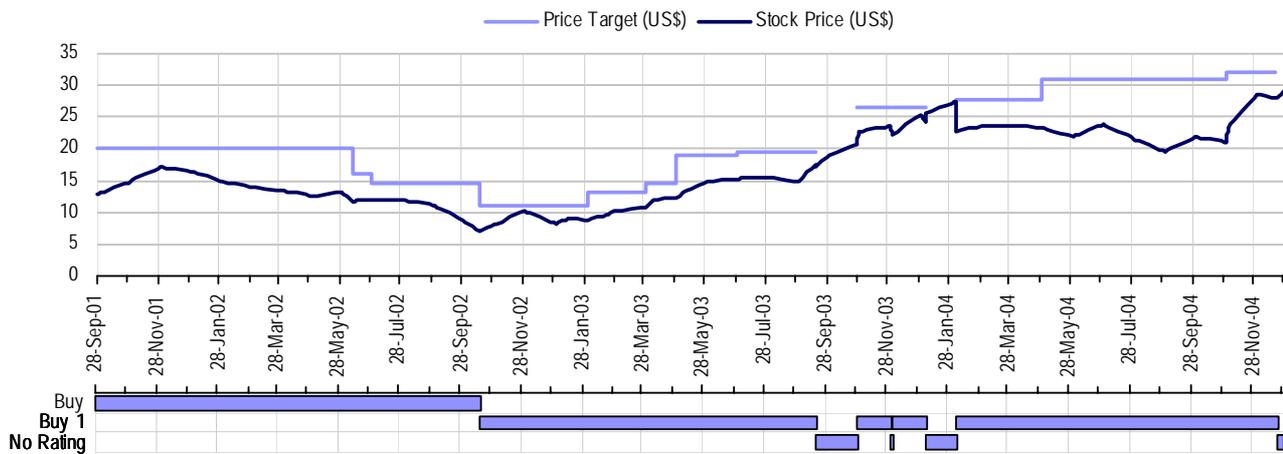
Price(s) as of 28 December 2004. Source: UBS.

4. Within the past three years, UBS AG, its affiliates or subsidiaries has received compensation for investment banking services from this company.

16. UBS Securities LLC and/or UBS Capital Markets LP makes a market in the securities and/or ADRs of this company.

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

Nice Systems Limited (US\$)



Source: UBS; as of 28 December 2004.

Note: On October 13, 2003, UBS adopted new definition criteria for its rating system. (See 'UBS Investment Research: Global Equity Ratings Definitions and Allocations' table for details.) Between January 11 and October 12, 2003, the UBS ratings and their definitions were: Buy 1: Excess return potential > 15%, smaller range around price target; Buy 2: Excess return potential > 15%, larger range around price target; Neutral 1: Excess return potential between -15% and 15%, smaller range around price target; Neutral 2: Excess return potential between -15% and 15%, larger range around price target; Reduce 1: Excess return potential < -15%, smaller range around price target; Reduce 2: Excess return potential < -15%, larger range around price target. Prior to January 11, 2003, the UBS ratings and definitions were: Strong Buy: Greater than 20% excess return potential, high degree of confidence; Buy: Positive excess return potential; Hold: Low excess return potential, low degree of confidence; Reduce: Negative excess return potential; Sell: Greater than 20% negative excess return potential, high degree of confidence. Under both ratings systems, excess return is defined as the difference between the FSR and the one-year local market interest rate.

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