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**ISRAEL  
Technology**

## Radware (USD 11.22) 1 - Overweight

Operating Results

**Momentum Continues at Radware**

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### Investment Conclusion

Radware's momentum continues. The company posted another solid quarter with a clean balance sheet, and guided for continued sequential growth in Q203. However, the 45% year-to-date share price increase makes us reassess our view on the potential upside from current levels.

### Summary

- Radware reported revs of \$12.6m, up 5% q/q and 25% y/y, slightly exceeding our \$12.5m est. EPS at \$0.05 came in a cent above our est and two cents above the Street consensus.
- Remarkably, the operating loss was reduced to just \$180k and we now expect Radware to turn profitable from operations in the second quarter.
- The combination of Radware's technological and execution strengths with its selling and marketing relative weaknesses make the name attractive to a potential strategic investor.

	FY Jan Currency USD	2002A		2003E		2004E		Change %	
		Actual	Old	New	Old	New	2003	2004	
Revenue (m)		43.7	52.6	52.7	65.6	65.8	21%	25%	
Net Income (m)		-2.1	3.5	3.5	9.1	9.1	NM	157%	
EPS		-0.13	0.20	0.20	0.50	0.50	NM	150%	
Consensus			0.23		0.48				
EV/Revenues		1.58		1.31		1.05			
P/Sales		4.36		3.62		2.90			
P/E		NM		56.1		22.4			

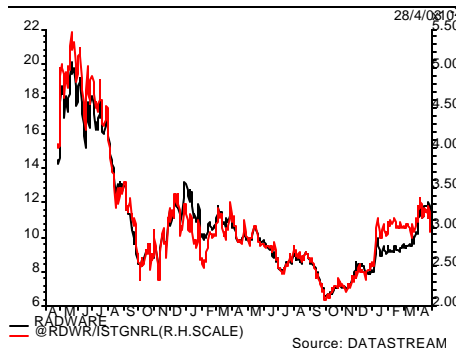
### Market Data

Market Cap (\$m)	196.1
Shares Outstanding (m)	17.5
Float (%)	58.3
Net Div Yield (%)	-
Convertible	No
Share per ADR	-

### Financial Summary

Five – Year EPS CAGR (%)	NM
Return on Equity FY01 (%)	NM
Current BVPS (\$)	7.33
Net Cash Per Share (\$)	7.26

### Stock Overview



Reuters	RDWR
Bloomberg	RDWR US
ADR	-
<b>Performance</b>	<b>1M</b> <b>3M</b> <b>12M</b>
Absolute %	14 19 7
Rel. Market %	11 14 30
Rel. Sector %	2 0 -15
52 Week Range	11.99 - 6.5

### Company Rating

New: 1 - Overweight  
Old: 1 - Overweight

### Target (USD)

New: 12.00  
Old: 12.00

**Sector View: 2 - Neutral**

### Investment Conclusion

Radware's momentum continues. The company posted another solid quarter with a clean balance sheet, and guided for continued sequential growth in Q203. However, the 45% year-to-date share price increase makes us reassess our view on the potential upside from current levels.

On one hand there seems to be a broad consensus in the marketplace about Radware's technological edge; on the other hand, Radware continues to lack major strategic partners that would enable it to tap a decent share of the ITM market opportunity, as it expands in the coming years. The combination of Radware's technological and execution strengths with its selling and marketing relative weaknesses make the name attractive to a potential strategic investor.

Under an M&A scenario, Radware benefits from a solid – and growing – cash position, and would be able to demand a substantial premium to its market value. Although we are not suggesting that Radware is about to get acquired anytime soon, we would not be surprised to see renewed interest in the company (as has been the case in the past). In such an event, and assuming Radware maintains its current business momentum, an acquisition price of \$14-17

**PLEASE SEE ANALYST(S) CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 3**

does not seem implausible to us. This price range suggests a P/E of 31x our FY04 EPS of \$0.50. The largest the marketing infrastructure of an acquiror the higher the price it would be ready to offer.

In the absence of such an M&A event, we doubt RDWR shares can rise towards the high-teens unless the company achieves a long-awaited, strategic marketing, selling or distribution agreement.

### 1Q03 Results

Radware reported revenues of \$12.6m, up 5% q/q and 25% y/y, slightly exceeding our \$12.5m estimate. EPS, at \$0.05, came in a cent above our estimate and two cents above the Street consensus. Remarkably, the operating loss was reduced to just \$180k and we now expect Radware to turn profitable from operations in the second quarter.

Continuing a positive trend initiated in early 2002, Radware generated record cash from operations of \$1.9m, and free cash flow of \$1.6m. This resulted in an increase in the cash balance to \$127m, or \$7.26 per share, no debt. DSO declined to 60 from 65 days in Q402. Inventories also declined 18% to \$2.5m.

The geographical sales break-down remained stable, with 48% of sales being generated in the US, 26% in Europe and 26% in Asia.

### Outlook and Guidance

Management guided for Q2 sales of \$12.8-13.0, in line with our current \$13.0 estimate, and actually better than close competitor F5 Networks; early last week F5 provided a guidance range which includes the possibility of a sequential decline in a seasonally strong Q2. Radware mentioned its current pipeline gives it confidence in the continuation of the current growth trend the company has been experiencing since Q3 2001.

The company expects to make \$0.06 in EPS in Q2, a cent better than our current estimate, primarily on slightly higher gross margins. Radware added that it can grow revenues as much as 30% without expanding its current operating structure. We expect RDWR to grow 21% and 25% in 2003, and 2004, respectively.

### Valuation

Despite the strength demonstrated by Radware, and as a result of the ongoing weakness in technology spending globally, we continue to value RDWR conservatively using a 1.5x EV/Revenues multiple, leading to a valuation of roughly \$206M, or \$12 per share. We acknowledge this target price is not significantly above the market price. The reason we are currently maintaining our 1-Overweight rating is that we deem Radware's technological edge and recent success in the marketplace make it increasingly attractive to potential strategic investors, primarily for companies in the networking equipment area. We estimate that a potential acquisition would not take place at a valuation of less than \$250-300, or \$14-17 per share – roughly 31x FY04 EPS.

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### Company description

Radware develops and markets Internet Traffic Management (ITM) solutions that provide intelligent IP load balancing between global and local network resources. Radware's product suite enables network performance optimisation at corporate enterprises, e-commerce, businesses and major ISPs worldwide.

Company Name	Disclosure(s)*	Reuters Ticker	Price(28-04-2003)	Rating
Radware	-	RDWR	(USD 11.22)	1 - Overweight

\* PLEASE SEE DISCLOSURE LEGEND ON THE LAST PAGE

**Analyst Certification:**

I, Tobias Fischbein, hereby certify (1) that the views expressed in this research report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this report and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views contained in this report.

**Important Disclosures:**

The analysts responsible for preparing this report have received compensation based upon various factors including the Firm's total revenues, a portion of which is generated by investment banking activities.

**Risk Disclosure:** Radware's ability to continue penetrating new markets depends on its liking up with a major distributor or OEM partner. Failure to establish such a relationship may result in Radware becoming a marginal entity within the Internet traffic management industry.

**Other Material Conflicts:** None.

**Key to Investment Opinions:****Stock Rating**

**1 - Overweight** - The stock is expected to outperform the unweighted expected total return of the industry sector over a 12-month investment horizon.

**2 - Equal weight** - The stock is expected to perform in line with the unweighted expected total return of the industry sector over a 12-month investment horizon.

**3 - Underweight** - The stock is expected to underperform the unweighted expected total return of the industry sector over a 12-month investment horizon.

**RS - Rating Suspended** - The rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Lehman Brothers is acting in an advisory capacity in a merger or strategic transaction involving the company.

**Sector View**

**1 - Positive** - sector fundamentals/valuations are improving

**2 - Neutral** - sector fundamentals/valuations are steady, neither improving nor deteriorating

**3 - Negative** - sector fundamentals/valuations are deteriorating

**Stock Ratings From February 2001 to August 5, 2002 (sector view did not exist):**

This is a guide to expected total return (price performance plus dividend) relative to the total return of the stock's local market over the next 12 months.

**1=Strong Buy** - expected to outperform the market by 15 or more percentage point.

**2=Buy** - expected to outperform the market by 5-15 percentage points

**3=Market Perform** - expected to perform in line with the market, plus or minus 5 percentage points

**4=Market Underperform** - expected to underperform the market by 5-15 percentage points

**5=Sell** - expected to underperform the market by 15 or more percentage points.

**Stock Ratings Prior to February 2001 (sector view did not exist):**

**1=Buy** - expected to outperform the market by 15 or more percentage point

**2=Outperform** - expected to outperform the market by 5-15 percentage points

**3=Neutral** - expected to perform in line with the market, plus or minus 5 percentage points

**4=Underperform** - expected to underperform the market by 5-15 percentage points

**5=Sell** - expected to underperform the market by 15 or more percentage points

**V=Venture** - return over multiyear timeframe consistent with venture capital; should only be held in a well diversified portfolio

**Distribution of Ratings:**

Lehman Brothers Equity Research has 1529 companies under coverage.

34% have been assigned a 1-Overweight rating which, for purposes of mandatory regulatory disclosures, is classified as a Buy rating. 37% of companies with this rating are investment banking clients of the Firm.

42% have been assigned a 2-Equal weight rating which, for purposes of mandatory regulatory disclosures, is classified as a Hold rating, 14% of companies with this rating are investment banking clients of the Firm.

24% have been assigned a 3-Underweight rating which, for purposes of mandatory regulatory disclosures, is classified as a Sell rating, 53% of companies with this rating are investment banking clients of the Firm.

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