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Reason for Report:
Earnings Announcement

Changes	From (Previous)	To (Current)
Rating	--	Outperform
Price Tgt	--	\$18
FY01E EP-ADR	--	\$0.25
FY02E EP-ADR	--	\$1.20
FY01E Rev (mil)	--	\$160.0
FY02E Rev (mil)	--	\$195.0

Price: \$14.09
52-Wk Range: \$18.10-\$10.95
Price Target: \$18
(15x FY03E EP-ADR of \$1.20)
Shares Out (mil): 13.3
Market Cap (mil): \$187.4
Avg Daily Vol (000): 23
Book Value/Share: \$12.5
Cash Per Share: \$6.9
Debt to Total Capital: 0%
Div (ann) - Yield: Nil
Est LT EPS Growth: 20%-25%
P/E to LT Growth (2002): 2.3x
Est Next Rep Date: Aug. 2002
FY End: Dec. 2002

Rev (mil)	2001	2002E	2003E
Mar	\$25.1	\$36.1A	—
Jun	\$30.5	\$38.5	—
Sep	\$33.8	\$41.1	—
Dec	\$37.7	\$44.4	—
FY	\$127.1	\$160.0	\$195.0
CY	\$127.1	\$160.0	\$195.0

FY RM 1.5x 1.2x 1.0x
CY RM 1.5x 1.2x 1.0x

EP-ADR	2001	2002E	2003E
Mar	(\$1.04)	(\$0.09)A	—
Jun	(\$0.53)	(\$0.02)	—
Sep	(\$0.26)	\$0.10	—
Dec	(\$0.05)	\$0.22	—
FY	(\$1.87)	\$0.25	\$1.20
CY	(\$1.87)	\$0.25	\$1.20

FY P/E NMF 56.4x 11.7x
CY P/E NMF 56.4x 11.7x

Note: EP-ADR estimates ex. goodwill. EPS are fully diluted.

Disclosures (see last page for details):

- (#) Market Maker
- (^) Beneficial Interest
- (>) Beneficial Interest/Pre-IPO
- (@) Underwriter
- (-) Employee/Director

NICE Systems Ltd. (NICE- \$14.09)

Outperform

Volatility: High

NICE Log 1Q02: On Track Performance And Solid Outlook Bucking Industry Trend; Reiterate Outperform

KEY POINTS:

- **We are reiterating our Outperform rating on NICE shares** and our \$18 objective (15x CY03 EPS of \$1.20), as the Company logged a good March quarter and reiterated its 20%-30% top-line outlook. 1Q02 revenue of \$36 million met our estimates, while a loss per ADR of \$0.09 bested Street consensus of (\$0.12) and was a penny short of our Street-high projections.
- **Bucking recent trends, management reiterated its guidance for 20%-30% Y/Y revenue growth**, as the Company has the highest visibility since the late-2000 low, thanks to a number of multimillion deals signed in each of its business units and rising service revenue, backed by good overall momentum. Win rates have also improved and NICE believes it has displaced several competitors at customer sites.
- **NICE will integrate its security-related activities** in multimedia logging and monitoring for government, law-enforcement, aviation, enterprise, and other security activities to address market needs with combined solutions. The new group will account for 25% of revenue.
- **We are leaving our estimates unchanged, and expect consensus numbers to inch closer toward our Street-high estimates.** We expect NICE to return to profitability in 3Q02 and show \$0.25 EP-ADR in 2002 on revenue of \$160 million, in the mid-point of management guidance. For 2003, we continue to forecast revenue of \$195 million and EPS of \$1.20. Trading at 1.2x CY03E revenue, 2x cash, and 12x our CY03E EPS, we believe the stock is inexpensive and reiterate Outperform.

INVESTMENT RECOMMENDATION:

Despite the continued weakness in IT spending and lowered guidance by some competitors, NICE is bucking the trend with a solid outlook backed by the highest visibility in recent history. We believe that this is another testament to management's admirable restructuring job and strong execution combined with good demand for its solutions, and underscores our recently raised rating on these shares. **We expect the Company's continued solid performance and improving Street sentiment on the stock to enable these shares to outperform the market. Trading at 1.2x FY02 sales, 2x cash, and 12x our FY03E EPS, we believe that these shares are inexpensive.** Our conservative \$18 objective is based on 15x our FY03E EP-ADR, as we apply a 40% discount to its long-term growth rate due to time horizon and market conditions, and is well below the valuation afforded prior to its fall from grace in late-2000.

COMPANY DESCRIPTION: NICE Systems Ltd. (#) is a leading provider of multimedia recording and monitoring solutions. The CEM (Customer Experience Management) division (71% of CY01 rev.) allows enterprises to improve their call-center customer interaction. NICE's Security Group includes its digital video logging business (11% of rev.) and its multimedia logging for government, law-enforcement, and aviation bodies with logging, direction finding, and Communications Intelligence (15% of rev.).

NICE Log May 14, 2002: On-Track Performance

Yesterday, before market open, NICE reported on-track March quarter results, with revenue of \$36.1 million in line with our estimates, and down 4% sequentially, while loss per ADR of \$0.09 bested Street consensus of (\$0.12). However, actual results were a penny short of our Street-high projections, as gross margins fell 350 bps Q/Q to 45.1%, as loss-carrying service revenue rose 26% sequentially, while product sales slid 8%, bringing revenue to a 86%/ 14% product/ service mix. We note that the loss on services dropped from \$1.8 million to \$0.7 million thanks to more emphasis on expanding professional service and streamlining this organization. In addition to the high-service portion in the mix, gross margins were also negatively affected by lower overall volume, security solutions pricing, and the clearance of legacy video logging inventory. We believe that this is a temporary setback and expect margins to improve in the balance of the year on higher volume, an improved revenue mix, and the move to full outsourcing of manufacturing. The drop in gross margin was somewhat offset by a \$1.3 million reduction in operating expenses, mainly thanks to lower G&A, and to a lesser extent, a \$400,000 drop in expenses, thanks to the weakness in the Israeli Shekel versus the U.S. Dollar.

Despite seasonality, CEM revenue held up well, coming in at \$27.3 million and essentially flat over the previous quarter. We suspect that the strength in this business was accounted by the sharp rise in service revenue this quarter. The good performance in the CEM business offset the sequential decline in the video and the security and aviation solutions that dropped 18% sequentially. For the March quarter, CEM accounted for 76% of revenue, followed by security and aviation business under the ISS (Integrated Security Solutions) division of 13%, and video logging and monitoring accounting for 11%.

NICE managed to expand its business in the EMEA region by 10% Q/Q thanks to its bolstered presence and efforts; this geography contributed 36% of revenue. Due to seasonality, business in the Americas was down 13% sequentially and accounted for 50% of turnover, with the 14% balance coming from APAC that had a flat quarter. We note that many of the multimillion deals announced in recent months were driven from the North American market, including a \$2 million contract with a major U.S. Airport for video logging and an undisclosed contact center customer.

NICE's balance sheet continues to be strong with cash up \$2.7 million over 4Q01 to \$92 million, as the rise in payables and expenses, along with lower inventories, more than offset the rise in receivables. Management noted that the \$3.8 million rise in receivables was mainly due to the implementation of the ERP (Enterprise Resource Management) system, which delayed the invoicing process and expects to lower its DSO later in the year, especially in light of the large-scale deals and better linearity. For the March quarter, current DSO (based on same quarter numbers) rose to 98 days from 85 days in 4Q01. NICE's inventories dropped by \$1.9 million Q/Q to \$9.2 million as NICE continues to outsource its manufacturing, bringing current product inventory (based on same-quarter inventory levels and product COGS) turns to 6.2x from 5.2x in the previous quarter. The move to outsourcing, along with the successful implementation of its ERP system, will increase operating efficiencies and allow better controls over the business.

NICE Aligns Its Security Guns And Reshuffles Its Board

NICE will integrate its security-related activities in multimedia logging and monitoring for government, law-enforcement, aviation, enterprise, and others to better address market needs with combined solutions. The Company will continue to sell its products separately through its established channels, but will also pursue more integrated projects and expand its security alliances. While it will take some time until this integration process will bear fruit, we believe that this will allow the Company to cross-sell its systems, benefit from combined industry expertise, strengthen its solution offering, technology and market presence, and better streamline operations. As a result, NICE should **realize business and operational synergies and improve its overall competitive positioning**. The new group will account for roughly 25% of revenue and will be headed by Doron Eidelman, who formerly held executive positions at AudioCodes (#@) and Orbotech (ORBK-\$29.07-MP-#).

As NICE reestablishes its position at the top of the CEM market, the Company will increase its efforts in the security business to fully realize the potential in this market. Management estimates that the addressable market for this group is \$1-\$1.5 billion, out of the \$15 billion monitoring and identification segment of the total security industry, serving verticals like transportation and airport security, correctional facilities, gaming, corporate and residential security, local law enforcement and public safety, government programs, and intelligence agencies.

The \$2 million video monitoring deal with a U.S. airport and a multimillion deal for the NICE-Track system, with an undisclosed premier Western law-enforcement agency, along with management comments, and our own sources all point out that this division is enjoying strong momentum.

Separately, **Ron Gutler was appointed chairman of the board** after this position was vacant for more than a year. Mr. Gutler served who has been a director since May 2001, is chairman of Vitalgo, a real estate investment company, and also manages the Blue Border Horizon Fund, a \$200 million global macro fund, and was previously a director at Bankers Trust. Mr. Joseph Atsmon, a veteran in the technology industry and a Company director since September 2001, was appointed as vice chairman.

Solid Outlook Ahead

Management tone on the conference call was upbeat, as the Company has the highest visibility since the late-2000 low, thanks to a number of multimillion deals signed in each of its business units and rising service revenue. Backed by good overall momentum, improved win rates, and several displacements of competitors at customer sites, management guided for 2Q02 revenue to come at \$37-39 million and maintained its 20%-30% Y/Y top-line growth guidance. This clearly is bucking the general industry trend of lower-outlook revisions by some of its key competitors.

We are leaving our top- and bottom-line estimates unchanged, and expect consensus numbers to inch closer toward our Street-high estimates. We expect NICE to return to profitability in 3Q02 and show a \$0.25 EP-ADR in 2002 on revenue of \$160 million, in the midpoint of management guidance. For 2003, we expect revenue of \$195 million and EPS of \$1.20.

We believe that the good 1Q02 performance and momentum is another testimony of management's admirable restructuring job and strong execution, combined with good demand for its solutions. This underscores our recently raised rating on these shares, as **we expect the Company's continued solid performance and improving Street sentiment toward this story to push these shares to outperform the market.**

Trading at 1.2x FY02 sales, 2x cash, 1.1x book value, and 12x our FY03E EPS, we believe that these shares are inexpensive. Our conservative \$18 objective is based on 15x our FY03E EP-ADR, as we apply a 40% discount to its long-term growth rate due to time horizon and market conditions, and is below the valuation afforded prior to its fall from grace in late-2000.

NICE Systems Ltd.
Income Statements
(\$ in Thousands except per-ADR)

	1Q01	2Q01	3Q01	4Q01	2001	1Q02A	2Q02E	3Q02E	4Q02E	2002E	2003E
Total Revenue	\$ 25,124	\$ 30,477	\$ 33,808	\$ 37,699	\$ 127,108	\$ 36,065	\$ 38,500	\$ 41,100	\$ 44,400	\$ 160,065	\$ 195,000
Total Cost of Sales	\$ 17,875	\$ 18,263	\$ 18,264	\$ 19,365	\$ 73,767	\$ 19,790	\$ 20,600	\$ 20,960	\$ 21,530	\$ 82,880	\$ 91,650
Gross Profit	\$ 7,249	\$ 12,214	\$ 15,544	\$ 18,334	\$ 53,341	\$ 16,275	\$ 17,900	\$ 20,140	\$ 22,870	\$ 77,185	\$ 103,350
Research and Development, net	5,371	4,783	4,597	4,439	19,190	4,279	4,400	4,500	4,600	17,779	20,500
Sales and Marketing, net	8,808	8,343	8,596	9,299	35,046	8,988	9,300	9,600	10,000	37,888	41,500
General and Administrative	7,562	7,005	6,583	5,993	27,143	5,168	5,300	5,400	5,600	21,468	24,200
Goodwill	880	908	812	813	3,413	-	-	-	-	-	-
Merger and Reorg. Exp.	14,554	-	-	-	14,554	-	-	-	-	-	-
Total Operating Expense*	\$ 21,741	\$ 20,131	\$ 19,776	\$ 19,731	\$ 81,379	\$ 18,435	\$ 19,000	\$ 19,500	\$ 20,200	\$ 77,135	\$ 86,200
Operating Income*	\$ (14,492)	\$ (7,917)	\$ (4,232)	\$ (1,397)	\$ (28,038)	\$ (2,160)	\$ (1,100)	\$ 640	\$ 2,670	\$ 50	\$ 17,150
Financial Income	1,114	1,046	1,187	907	4,254	959	900	925	950	3,734	4,100
Other Income	(21)	(69)	(276)	(32)	(398)	31	-	-	-	-	-
Pretax Income*	\$ (13,399)	\$ (6,940)	\$ (3,321)	\$ (522)	\$ (24,182)	\$ (1,170)	\$ (200)	\$ 1,565	\$ 3,620	\$ 3,784	\$ 21,250
Taxes	33	10	9	146	198	20	30	50	100	200	1,500
Equity in loss of affiliate	-	-	-	-	-	-	-	-	-	-	-
Minority Interest	-	-	-	-	-	-	-	-	-	-	-
Net Income*	\$ (13,432)	\$ (6,950)	\$ (3,330)	\$ (668)	\$ (24,380)	\$ (1,190)	\$ (230)	\$ 1,515	\$ 3,520	\$ 3,584	\$ 19,750
Shares Outstanding	12,954	12,994	13,042	13,197	13,047	13,342	13,400	15,200	15,800	14,436	16,500
Fully Diluted Earnings per ADR	\$ (1.04)	\$ (0.53)	\$ (0.26)	\$ (0.05)	\$ (1.87)	\$ (0.09)	\$ (0.02)	\$ 0.10	\$ 0.22	\$ 0.25	\$ 1.20
<i>Margin Analysis:</i>						(3.5%)					
Gross Margin	28.9%	40.1%	46.0%	48.6%	42.0%	45.1%	46.5%	49.0%	51.5%	48.2%	53.0%
R&D, net	21.4%	15.7%	13.6%	11.8%	15.1%	11.9%	11.4%	10.9%	10.4%	11.1%	10.5%
S&M, net	35.1%	27.4%	25.4%	24.7%	27.6%	24.9%	24.2%	23.4%	22.5%	23.7%	21.3%
G&A	30.1%	23.0%	19.5%	15.9%	21.4%	14.3%	13.8%	13.1%	12.6%	13.4%	12.4%
Total Operating Expense*	86.5%	66.1%	58.5%	52.3%	64.0%	51.1%	49.4%	47.4%	45.5%	48.2%	44.2%
Operating Income*	(57.7%)	(26.0%)	(12.5%)	(3.7%)	(22.1%)	(6.0%)	(2.9%)	1.6%	6.0%	0.0%	8.8%
Financial Income	4.4%	3.4%	3.5%	2.4%	3.3%	2.7%	2.3%	2.3%	2.1%	2.3%	2.1%
Other Income	(0.1%)	(0.2%)	(0.8%)	(0.1%)	(0.3%)	0.1%	0.0%	0.0%	0.0%	0.0%	0.0%
Pretax Income*	(53.3%)	(22.8%)	(9.8%)	(1.4%)	(19.0%)	(3.2%)	(0.5%)	3.8%	8.2%	2.4%	10.9%
Tax Rate	(0.2%)	(0.1%)	(0.3%)	(28.0%)	(0.8%)	(1.7%)	(15.0%)	3.2%	2.8%	5.3%	7.1%
Net Income*	(53.5%)	(22.8%)	(9.8%)	(1.8%)	(19.2%)	(3.3%)	(0.6%)	3.7%	7.9%	2.2%	10.1%

Source: US Bancorp Piper Jaffray estimates and Company reports

Rating Definitions

Investment Opinion: investment opinions are based on each stock's return potential relative to the overall market*, not an absolute return.

- **Strong Buy:** Expected to significantly outperform the relevant broader market index over the next 6 to 12 months. An identifiable catalyst is present to drive appreciation.
- **Outperform:** Expected to outperform the relevant broader market index over the next 12 to 18 months.
- **Market Perform:** Expected to perform in line with the relevant broader market index over the next 6 to 12 months.
- **Underperform:** Expected to underperform the relevant broader market index over the next 6 to 12 months.

* Broader market indices = Russell 2000 and S&P 500

Volatility Rating: Our focus on growth companies implies that the stocks we recommend are typically more volatile than the overall stock market. We are not recommending the "suitability" of a particular stock for an individual investor. Rather, we are identifying the volatility of a particular stock.

- **Low:** The stock price has moved up or down by more than 10% in a month in fewer than 8 of the past 24 months.
- **Medium:** The stock price has moved up or down by more than 20% in a month in fewer than 8 of the past 24 months.
- **High:** The stock price has moved up or down by more than 20% in a month in at least 8 of the past 24 months. All IPO stocks automatically get this risk rating for the first 12 months of trading.

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