

## Radware Ltd.

(NASDAQ: RDWR)

Price Target  
Downgrade  
EPS Revision

## Outperform

Speculative Risk

### Mark Sue, Analyst

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Price: 15.51      Price Target: 20.00 ↓ 24.00  
 52-Wk High: 27.95      52-Wk Low: 15.51  
 Float (MM): 15.3      Debt to Cap: 0.0%  
 Shares Out (MM): 20.3      Market Cap (MM): 315  
 Dividend: NA      Yield: NM  
 Tr. 12 ROE: 9.20%      Est 3-Yr EPS Gr: 15.00%  
 Trading Vol. (MM): 0.269  
 Institutional Own.: 52%

(FY Dec)	2003A	2004A	2005E	2006E
EPS	0.35	0.70	0.45	0.85
Prev.			0.96	1.13
P/E	44.31x	22.16x	34.47x	18.25x
Revenue Net (MM)	54.78	68.44	76.52	90.00
Prev.			85.27	95.30
MktCap/Rev	5.75x	4.60x	4.12x	3.50x

EPS	Q1	Q2	Q3	Q4
2003	0.05A	0.07A	0.10A	0.13A
2004	0.14A	0.16A	0.19A	0.22A
2005	0.22A	0.04E	0.06E	0.13E
Prev.		0.24E	0.26E	0.29E
Revenue Net (MM)				
2003	12.59A	13.17A	14.01A	15.00A
2004	15.52A	16.30A	17.57A	19.05A
2005	20.02A	17.50E	18.50E	20.50E
Prev.		21.00E	21.50E	22.75E

EPS estimates are non-GAAP, which exclude the effects of charges from acquisitions, deferred stock based compensation and certain non recurring items

All values in USD unless otherwise noted.

Priced as of prior trading day's market close, EST (unless otherwise stated).

## Dude, Not So Rad

### Event

Preannounces Weak June Quarter Results

### Investment Opinion

- This morning the company pre-announced weak preliminary results of \$17.5 million in revenues and \$0.03-\$0.05 in earnings, which were far below our expectations and consensus of \$21 million and \$0.23.
- We believe the disappointing results are due to rising competitive pressures following recent merger and acquisition activity in the layer 4-7 market (i.e., Cisco's acquisition of Fineground as well as its announcement of AON and Juniper's acquisition of Redline as well as Citrix acquiring Netscaler). We believe the dramatic change in the competitive environment continues to create purchasing delays. These issues may take more than a quarter or two to be rectified, in our opinion. Weakness in sales was seen throughout the geographic regions.
- The balance sheet continues to remain strong however, with Radware generating approximately \$3-4 million in cash during the June quarter, ending the quarter with roughly \$8-9/share in cash. We believe a share buyback may be forthcoming in the near future.
- We are lowering our June quarter results from \$21 million and \$0.23 to \$17.5 million and \$0.04. For the full year C2005, our estimates move from \$85.3M and \$0.96 EPS to \$76.5M and \$0.45 respectively. Our C2006 estimates move from \$95.3M and \$1.13 to \$90M and \$0.85 respectively.
- We are reducing our price target on Radware from \$24 to \$20, which represents 18x times our CY06 earnings estimate, a slight discount to its peer group average due to the uncertainties around rising competitive pressures.

**Valuation**

Radware's shares currently trade at 34x our C2005 earnings estimate of \$0.45, of which \$8.06 remains in cash. Our price target now stands at \$20 or 18x our C2006 earnings estimate, slightly below peer group average.

**Price Target Impediment**

Impediments to reaching our price target include competitive pressures, a prolonged IT spending recovery period and geo-political risks.

**Company Description**

Radware develops Internet traffic solutions that enable service providers, enterprises, and e-commerce businesses to manage and optimize the performance of servers, security devices and ISP links. By distributing IP traffic within a network, Radware's products can improve productivity and business operations. Applications provided by Radware solutions include traffic redirection (i.e., load balancing), health monitoring, bandwidth management and security.

## Required Disclosures

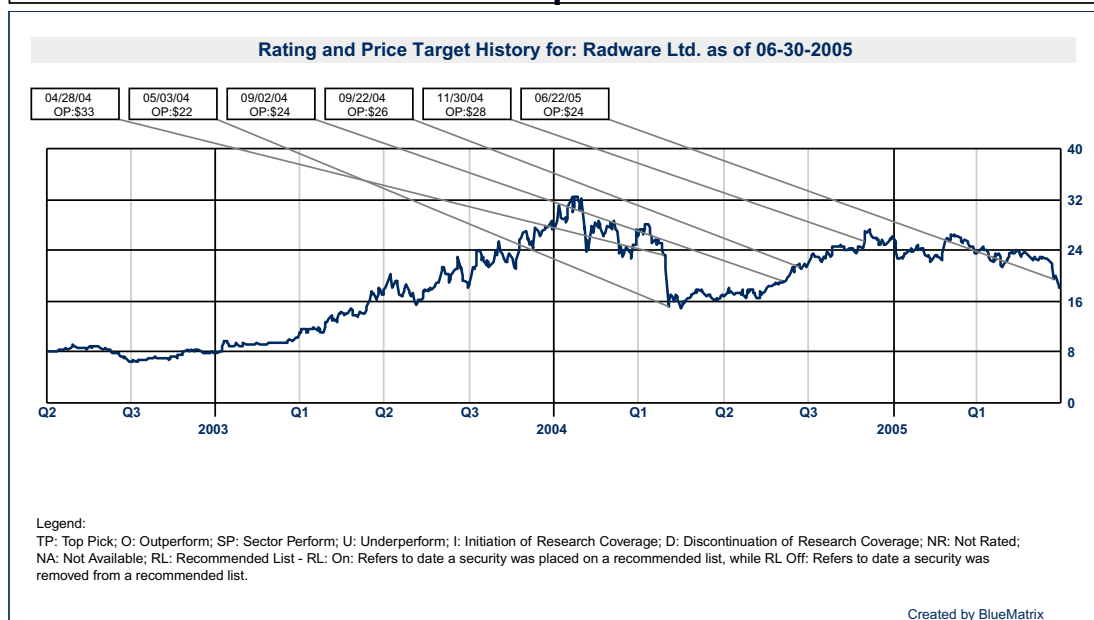
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Period Ending (\$000 Except EPS and Ratios)	Mar-04 1Q	Jun-04 2Q	Sep-04 3Q	Dec-04 4Q	Mar-05 1Q	Jun-05 2QE	Sep-05 3QE	Dec-05 4QE	Mar-06 1QE	Jun-06 2QE	Sep-06 3QE	Dec-06 4QE	Dec-04 FY	Dec-05 FYE	Dec-06 FYE
<b>Income Statement</b>															
<b>Total Revenue</b>	<b>15,522</b>	<b>16,298</b>	<b>17,572</b>	<b>19,047</b>	<b>20,021</b>	<b>17,500</b>	<b>18,500</b>	<b>20,500</b>	<b>21,000</b>	<b>22,000</b>	<b>22,500</b>	<b>24,500</b>	<b>68,439</b>	<b>76,521</b>	<b>90,000</b>
YoY Growth	23.3%	23.7%	25.4%	26.9%	29.0%	7.4%	5.3%	7.6%	4.9%	25.7%	21.6%	19.5%	25%	12%	18%
QoQ Growth	3.4%	5.0%	7.8%	8.4%	5.1%	-12.6%	5.7%	10.8%	2.4%	4.8%	2.3%	8.9%	-	-	-
Cost of Sales	2,760	2,899	3,130	3,395	3,555	4,200	3,700	4,100	4,200	4,400	4,500	4,900	12,184	15,555	18,000
<b>Gross Margin</b>	<b>12,762</b>	<b>13,399</b>	<b>14,442</b>	<b>15,652</b>	<b>16,466</b>	<b>13,300</b>	<b>14,800</b>	<b>16,400</b>	<b>16,800</b>	<b>17,600</b>	<b>18,000</b>	<b>19,600</b>	<b>56,255</b>	<b>60,966</b>	<b>72,000</b>
R&D	2,337	2,467	2,660	2,878	3,026	3,250	3,200	3,250	3,000	3,000	3,100	3,100	10,342	12,726	12,200
Sales & Marketing	7,702	7,805	7,989	8,402	8,996	9,200	10,200	10,400	9,600	9,500	9,500	9,800	31,898	38,796	38,400
G&A	1,020	1,038	1,192	1,243	1,214	1,250	1,250	1,300	1,600	1,600	1,700	1,800	4,493	5,014	6,700
Total Operating Exp.	11,059	11,310	11,841	12,523	13,236	13,700	14,650	14,950	14,200	14,100	14,300	14,700	46,733	56,536	57,300
<b>Operating Income</b>	<b>1,703</b>	<b>2,089</b>	<b>2,601</b>	<b>3,129</b>	<b>3,230</b>	<b>(400)</b>	<b>150</b>	<b>1,450</b>	<b>2,600</b>	<b>3,500</b>	<b>3,700</b>	<b>4,900</b>	<b>9,522</b>	<b>4,430</b>	<b>14,700</b>
Financial Income	1,052	1,023	1,137	1,353	1,226	1,150	1,175	1,225	1,125	1,131	1,136	1,142	4,565	4,776	4,534
<b>Income before inc. taxes</b>	<b>2,755</b>	<b>3,112</b>	<b>3,738</b>	<b>4,482</b>	<b>4,456</b>	<b>750</b>	<b>1,325</b>	<b>2,675</b>	<b>3,725</b>	<b>4,631</b>	<b>4,836</b>	<b>6,042</b>	<b>14,087</b>	<b>9,206</b>	<b>19,234</b>
Taxes on income	0	93	113	135	55	15	27	54	335	417	435	544	341	150	1,731
Minority Interest	11	23	0	0	0	11	11	11	11	11	11	11	34	33	44
<b>Net Earnings</b>	<b>2,766</b>	<b>3,042</b>	<b>3,625</b>	<b>4,347</b>	<b>4,401</b>	<b>746</b>	<b>1,310</b>	<b>2,633</b>	<b>3,401</b>	<b>4,225</b>	<b>4,412</b>	<b>5,509</b>	<b>13,780</b>	<b>9,089</b>	<b>17,547</b>
<b>Earnings per Share</b>	<b>\$0.14</b>	<b>\$0.16</b>	<b>\$0.19</b>	<b>\$0.22</b>	<b>\$0.22</b>	<b>\$0.04</b>	<b>\$0.06</b>	<b>\$0.13</b>	<b>\$0.17</b>	<b>\$0.21</b>	<b>\$0.22</b>	<b>\$0.27</b>	<b>\$0.70</b>	<b>\$0.45</b>	<b>\$0.85</b>
EPS YoY Growth	193%	121%	93%	71%	57%	-76%	-66%	-40%	-24%	461%	237%	107%	100%	-36%	91%
Shares O/S	20,072	19,580	19,400	20,167	20,289	20,289	20,500	20,500	20,500	20,500	20,500	20,750	19,805	20,395	20,563
<b>Percent of Sales:</b>															
Gross Profit	82.2%	82.2%	82.2%	82.2%	82.2%	76.0%	80.0%	80.0%	80.0%	80.0%	80.0%	80.0%	82.2%	79.7%	80.0%
Operating Income	11.0%	12.8%	14.8%	16.4%	16.1%	-2.3%	0.8%	7.1%	12.4%	15.9%	16.4%	20.0%	13.9%	5.8%	16.3%
Pre-Tax Income	17.7%	19.1%	21.3%	23.5%	22.3%	4.3%	7.2%	13.0%	17.7%	21.0%	21.5%	24.7%	20.6%	12.0%	21.4%
Net Income	17.8%	18.7%	20.6%	22.8%	22.0%	4.3%	7.1%	12.8%	16.2%	19.2%	19.6%	22.5%	20.1%	11.9%	19.5%
R&D	15.1%	15.1%	15.1%	15.1%	15.1%	18.6%	17.3%	15.9%	14.3%	13.6%	13.8%	12.7%	15.1%	16.6%	13.6%
Sales & Marketing	49.6%	47.9%	45.5%	44.1%	44.9%	52.6%	55.1%	50.7%	45.7%	43.2%	42.2%	40.0%	46.6%	50.7%	42.7%
G&A	6.6%	6.4%	6.8%	6.5%	6.1%	7.1%	6.8%	6.3%	7.6%	7.3%	7.6%	7.3%	6.6%	6.6%	7.4%
Tax Rate, Net	0.0%	3.0%	3.0%	3.0%	0.0%	2.0%	2.0%	2.0%	9.0%	9.0%	9.0%	9.0%	2.4%	1.6%	9.0%

Source: Company Data, RBC Capital Markets Estimates

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Source: Company Reports, RBC Capital Markets