

# Radware

RDWR.OQ

## Solid Q2 - Upgrade to Buy

- **Upgrading to a Buy with a price target of US\$11:** We upgrade Radware from a Hold and a price target of US\$9, to a Buy with a price target of US\$11, based on a compelling valuation and signs of stabilisation in the end market as evidenced by 2Q results from peers such as F5 and Packeteer..
- **2Q 02 Highlights:** Radware posted a solid set of Q202 results, with revenue at \$10.6m, up 5% sequentially. EPS of \$-0.05 was better than our expected \$-0.06 EPS loss. The balance sheet remains healthy: DSOs were at 76 days, and the company finished the quarter with \$124m in cash.
- **Short term catalysts:** We believe there should be a number of H2 catalysts that should help the stock:
  1. Radware is on track to break-even in Q4 2002E;
  2. An expanded product portfolio (Configware);
  3. Better distribution reach (Westcon), particularly the US;
- **Best-of-breed positioning paying off:** Based on our conversations with distributors, we believe that Radware's best-of-breed approach in the load-balancing market seems to be paying off, especially as the larger competitors (Cisco and Nortel) increasingly focus their resources in other core areas.
- **Maintain estimates:** We maintain our FY02 and FY03 EPS estimates at \$-0.16 and \$0.09 respectively. We marginally adjust revenue estimates expecting \$43.3m for FY02 and \$52.6m for FY03 (from \$44.1m and \$51.4 respectively).
- **Valuation:** Radware trades at EV/sales for 02E and 03E at 0.4 and 0.3 respectively. Our price target of US\$11, implies EV/sales for 02E and 03E at 1.3x and 1.1x, respectively, which we believe is in-line with peers.

Radware develops intelligent load-balancing solutions for network service providers, ISPs, ASPs, content distributors, and telcos.

### research team

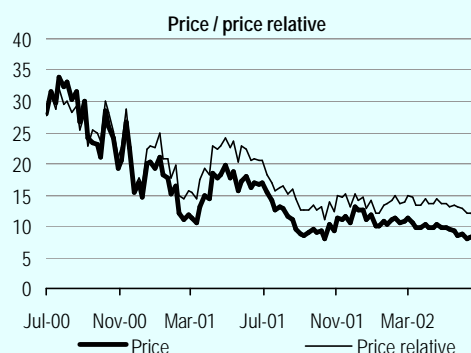
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Recommendation	(formerly HOLD) BUY
Price (26 Jul 02)	8.41 (US\$)
Target price (12 months)	11.00 (US\$)
Market cap. (US\$ m)	138.93
Enterprise value (US\$ m)	17.33
Region/country	European/Israel
Sector	Networking Equipment
Date	29 July 2002



The price relative chart measures performance against the isr\_ta10 index. On 26/07/02 the isr\_ta10 index closed at 351.94. On 26/07/02 the spot exchange rate was US\$0.99/eu 1. - eu0.99/US\$1.

Performance over	1mth	3mths	12mths
Absolute (%)	-2.8	-18.3	-48.6
Relative (%)	-5.0	-13.9	-36.4

Year	12/00A	12/01A	12/02E	12/03E
Revenues (US\$ m)	38.4	43.3	43.3	52.6
EBITDA (US\$ m)	1.05	-5.91	-5.0	-0.3
Net income (US\$ m)	6.4	-1.3	-2.6	1.7
CSFB adj. EPS (US\$)	0.37	-0.08	-0.16	0.09
ROIC (%)	-16.6	-92.1	-69.3	-16.0
P/E (x)	22.7	NM	NM	93.4
P/E rel (%)	—	—	—	—
EV/EBITDA (x)	7.7	-23.5	-3.5	-57.8

Dividend 2001 (US\$)	Book value/share (12/01, US\$)
—	—
Dividend yield (%)	Free float (%)
—	85.0
IC (12/02E, US\$ m)	Number of shares (m)
9.12	16.52
Net debt (12/02E, US\$ m)	EV/IC (12/02E, x)
-121.6	1.9
Net debt/equity (12/02E, %)	Current WACC (12/02E, %)
-97.5	—

Source: FTI, Company data, Datastream, CSFB (EUROPE) LTD. Estimates.

## Relative valuation

**Figure 1: Relative valuation chart for Radware**

US\$ in millions, unless otherwise stated

Company Name	Reuters ticker	CSFB rating	Closing price 26/07/02	Market cap. (US\$M)	52 week		Price below 52W Hi	EPS			Sales growth		Net debt (US\$M) 02E	EV / Sales	
					Lo	Hi		01A	02E	03E	02E	03E		02E	03E
<b>RADWARE (USD)*</b>	<b>RDWR.O</b>	<b>Hold</b>	<b>8.4</b>	<b>139</b>	<b>6.6</b>	<b>18.3</b>	<b>54%</b>	<b>-0.44</b>	<b>-0.16</b>	<b>0.09</b>	<b>1%</b>	<b>16%</b>	<b>-121.60</b>	<b>0.40</b>	<b>0.34</b>
AKAMAI (USD)*	AKAM.O	Hold	1.1	128	0.8	8.2	87%	-1.71	-1.07	-0.70	65%	58%	-179.00	n.a.	n.a.
EXTREME NETWORKS (USD)*	EXTR.O	Buy	9.6	1103	5.8	32.1	70%	0.13	0.07	0.24	-10%	10%	-93.96	2.29	2.07
F5 NETWORKS (USD)	FFIV.O	n.a.	11.1	286	7.0	28.7	61%	-1.36	-0.23	0.17	2%	15%	-78.90	1.89	1.64
FOUNDRY NETWORKS (USD)*	FDRY.O	Hold	7.0	840	4.7	22.5	69%	0.13	0.12	0.22	-10%	19%	-228.08	2.18	1.84
INFOSPACE (USD)*	INSP.O	Hold	0.5	139	0.4	2.8	84%	-0.06	-0.10	n.a.	46%	n.a.	-116.18	0.07	n.a.
PACKETEER (USD)	PKTR.O	n.a.	3.9	117	2.7	9.6	60%	-2.40	0.07	0.23	15%	28%	-62.50	1.02	0.80
<b>Average</b>							<b>69%</b>				<b>15%</b>	<b>24%</b>		<b>1.31</b>	<b>1.34</b>

Source: Company data, \*CSFB estimates, I/B/E/S estimates.

## Financials

**Figure 2: Radware quarterly results**

*US\$ in millions, unless otherwise stated*

	Q1/02	Q2/02	Q3/02	Q4 02E	2002E
<b>Sales</b>	<b>10.1</b>	<b>10.6</b>	<b>11.0</b>	<b>11.6</b>	<b>43.3</b>
growth %	7.4%	4.5%	4.5%	5.0%	-0.1%
Total COGS	1.9	1.9	2.1	2.2	8.1
% sales	18.4%	18.4%	18.9%	19.4%	18.8%
<b>Gross profit</b>	<b>8.2</b>	<b>8.6</b>	<b>8.9</b>	<b>9.3</b>	<b>35.1</b>
	81.6%	81.6%	81.1%	80.6%	81.2%
Research & Development expenses, net	2.0	1.9	2.1	2.1	8.1
% sales	19.9%	18.1%	18.7%	18.1%	18.7%
Selling expenses, net	7.4	7.6	7.3	7.0	29.3
% sales	73.5%	71.5%	66.2%	60.8%	67.8%
General and administrative expenses	1.0	1.0	1.0	1.0	4.1
% sales	10.2%	9.7%	9.1%	9.0%	9.5%
<b>Operating income (loss)</b>	<b>(2.2)</b>	<b>(1.9)</b>	<b>(1.4)</b>	<b>(0.8)</b>	<b>(6.4)</b>
% sales	-22.0%	-17.8%	-12.9%	-7.3%	-14.7%
4.0%					
Financial income net	0.9	1.1	0.9	0.9	3.8
% sales	8.5%	10.3%	8.0%	8.0%	8.7%
Other income net	0.0	0.0	0.0	0.0	0.0
% sales	0.0%	0.0%	0.0%	0.0%	0.0%
Income before tax	(1.4)	(0.8)	(0.5)	0.1	(2.6)
% sales	-13.6%	-7.5%	-4.9%	0.7%	-6.0%
Taxes on income	0.0	0.0	0.0	(0.0)	0.0
% pre-tax income	0.0%	0.0%	5.0%	5.0%	0.9%
<b>Net income for the period</b>	<b>(1.4)</b>	<b>(0.8)</b>	<b>(0.5)</b>	<b>0.1</b>	<b>(2.6)</b>
% sales	-13.6%	-7.5%	-4.7%	0.7%	-6.0%
# shares	16.54	16.57	16.65	16.73	16.62
# shares fully diluted	16.54	16.57	16.65	16.73	16.62
Including financial Income					
EPS	-0.08	-0.05	-0.03	0.00	-0.16
<b>EPS (fully diluted)</b>	<b>-0.08</b>	<b>-0.05</b>	<b>-0.03</b>	<b>0.00</b>	<b>-0.16</b>

Source: Company data, CSFB estimates.

**Figure 3: Yearly income statement for Radware***US\$ in millions, unless otherwise stated*

Income Statement	1999	2000	2001	2002E	2003E
<b>Revenues</b>	<b>14.1</b>	<b>38.4</b>	<b>43.3</b>	<b>43.3</b>	<b>52.6</b>
COGS	2.3	6.1	7.7	8.1	10.8
<b>Gross Profit</b>	<b>11.9</b>	<b>32.2</b>	<b>35.6</b>	<b>35.1</b>	<b>41.8</b>
R&D	1.6	5.5	8.2	8.1	9.2
Sales and marketing	9.7	24.6	30.0	29.3	30.3
General and administrative	1.1	3.1	4.5	4.1	4.2
Operating Income	-0.6	-1.0	-7.2	-6.4	-1.9
Depreciation and Amort.	0.7	2.0	1.3	1.4	1.6
<b>EBITDA</b>	<b>0.1</b>	<b>1.0</b>	<b>-5.9</b>	<b>-5.0</b>	<b>-0.3</b>
Financial Income (net)	0.9	7.4	6.3	3.8	3.6
Other Income (Expenses)	0.0	0.0	0.0	0.0	0.0
Income before Taxes	0.3	6.4	-0.9	-2.6	1.6
Taxes on Income	0.0	0.0	0.4	0.0	-0.1
Net Income before minorities	0.3	6.4	-1.3	-2.6	1.7
Minorities	0.0	0.0	0.0	0.0	0.0
Extraordinary items	0.0	0.0	0.0	0.0	0.0
<b>Net Income (inc. financial inc)</b>	<b>0.3</b>	<b>6.4</b>	<b>-1.3</b>	<b>-2.6</b>	<b>1.7</b>
# shares					
simple	11.18	15.87	16.43	16.62	16.94
diluted	12.72	17.60	17.29	16.62	16.94
EPS (incl. financial inc)					
simple	0.03	0.41	-0.08	-0.16	0.09
<b>diluted</b>	<b>0.03</b>	<b>0.37</b>	<b>-0.08</b>	<b>-0.16</b>	<b>0.09</b>
EBITDA/per share					
simple	0.01	0.07	-0.36	-0.30	-0.02
<b>diluted</b>	<b>0.01</b>	<b>0.06</b>	<b>-0.34</b>	<b>-0.30</b>	<b>-0.02</b>

Source: Company data, CSFB estimates.

**Figure 4: Radware balance sheet***US\$ in millions, unless otherwise stated*

Balance Sheet	1999	2000	2001	2002E	2003E
<b>Assets</b>					
<b>Current Assets</b>					
Cash and cash equivalents	68.7	130.8	125.7	121.6	123.7
Accounts receivable	2.9	9.3	7.9	10.6	12.4
Other Rec and Prepaid Exp	0.9	1.6	1.2	1.9	2.4
Inventories	0.8	4.2	4.8	5.6	6.8
<b>Total Current Assets</b>	<b>73.4</b>	<b>145.9</b>	<b>139.5</b>	<b>139.8</b>	<b>145.3</b>
<b>Non-current Assets</b>					
Long Term Loan	0.0	0.7	0.0	0.0	0.0
P, P & E	1.0	2.8	4.0	4.8	5.8
Deposit with Insurance companies	0.3	0.7	0.9	0.9	1.1
Security deposit	0.0	0.0	0.0	0.0	0.0
<b>Total non-current assets</b>	<b>1.3</b>	<b>4.2</b>	<b>5.0</b>	<b>5.6</b>	<b>6.8</b>
<b>Total Assets</b>	<b>74.7</b>	<b>150.1</b>	<b>144.5</b>	<b>145.4</b>	<b>152.2</b>
<b>Liabilities and Shareholders' Equity</b>					
<b>Current liabilities</b>					
Accounts Payable	1.8	6.7	2.5	2.6	3.2
Other payables and accr. expenses	3.2	6.8	12.1	12.6	14.2
<b>Total current liabilities</b>	<b>5.1</b>	<b>13.4</b>	<b>14.6</b>	<b>15.1</b>	<b>17.4</b>
<b>Non-current Liabilities</b>					
Convertibles	0.0	0.0	0.0	0.0	0.0
Accrued severance pay	0.3	0.7	0.9	0.9	1.1
<b>Total non-current liabilities</b>	<b>0.3</b>	<b>0.7</b>	<b>0.9</b>	<b>0.9</b>	<b>1.1</b>
Minority interest	0.0	0.0	0.0	0.0	0.0
Share capital	0.4	0.4	0.4	0.4	0.4
Paid-in Capital	71.8	131.5	131.6	131.6	131.6
Adj. Retained Earnings	-2.8	4.0	-3.1	-2.6	1.7
<b>Total Equity</b>	<b>69.4</b>	<b>135.9</b>	<b>128.9</b>	<b>129.4</b>	<b>133.7</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>74.7</b>	<b>150.1</b>	<b>144.5</b>	<b>145.4</b>	<b>152.2</b>

*Source: Company data, CSFB estimates.*

AMSTERDAM..... 31 20 5754 890  
 ATLANTA..... 1 404 897 2800  
 AUCKLAND..... 64 9 302 5500  
 BALTIMORE..... 1 410 659 8800  
 BANGKOK..... 62 614 6000  
 BEIJING ..... 86 10 6410 6611  
 BOSTON..... 1 617 556 5500  
 BUDAPEST ..... 36 1 202 2188  
 BUENOS AIRES..... 54 11 4394 3100  
 CHICAGO..... 1 312 750 3000  
 FRANKFURT ..... 49 69 75 38 0  
 HOUSTON..... 1 713 890 6700  
 HONG KONG..... 852 2101 6000

JOHANNESBURG..... 27 11 343 2200  
 KUALA LUMPUR ..... 603 2143 0366  
 LONDON..... 44 20 7888 8888  
 MADRID..... 34 91 423 16 00  
 MELBOURNE..... 61 3 9280 1888  
 MEXICO CITY..... 52 5 283 89 00  
 MILAN..... 39 02 7702 1  
 MOSCOW..... 7 501 967 8200  
 MUMBAI..... 91 22 230 6333  
 NEW YORK..... 1 212 325 2000  
 PALO ALTO..... 1 650 614 5000  
 PARIS ..... 33 1 53 75 85 00  
 PHILADELPHIA..... 1 215 851 1000

SAN FRANCISCO ..... 1 415 836 7600  
 SÃO PAULO..... 55 11 3841 6000  
 SEOUL ..... 82 2 3707 3700  
 SHANGHAI..... 86 21 6881 8418  
 SINGAPORE ..... 65 6212 2000  
 SYDNEY..... 61 2 8205 4433  
 TAIPEI..... 886 2 2715 6388  
 TOKYO..... 81 3 5404 9000  
 TORONTO..... 1 416 352 4500  
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