

Orckit Communications

(ORCT^{5,8} \$7.16 - Intraday) Market Perform

No Carrier Wins; Reducing Estimates

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- Revenue was \$1.9 million in 2Q07 compared to our estimate of \$1.7 million and the Street of \$1.8 million. Loss per share was (\$0.40) versus our/Street estimate of (\$0.50). The loss per share was aided by financial income of \$1.6 mm from adjustments due to the conversion terms of convertible notes issued in March 2007.
- Management guided 3Q07 to \$1.5 million in revenue and a loss of \$0.53. Revenue is coming from the recognition of previously deferred income.
- Management expects little follow-on revenue from KDDI until the carrier enters its FY2008.
- The Japanese tier-1 carrier that Orckit was expecting a decision from by June has no plans to proceed with ORCT, but will re-evaluate its plans in 2008.
- The CM-4000 platform is expected to begin trials in late 2007 or early 2008. We caution that sales cycles tend to be very long for carrier decisions.
- We are lowering our 2007 revenue estimate to \$10.4 million from \$18.2 million. Our loss per share estimate goes to (\$1.66) from (\$1.62) on the lower revenue and higher operating expenses.
- The company's cash balance at the end of June was \$74 million (net of debt) and \$123 million gross. On a per-share basis, net cash was \$4.51 and gross about \$7.51. The company was also recently awarded \$12 million in damages in an arbitration ruling against Conexant Systems (CNXT, \$1.27-Intraday, NR), although the ruling is subject to appeal.
- In our view, the stock will likely trade at or below its cash level, as there is little prospect of any business in the near-to-medium term and the company will continue to burn significant cash to complete development of its next-gen platform.

Key Data

52-Week Range	\$12.42 - 7.21
Shares Outstanding (MM)	15.8
Float (MM)	14.0
% Held Institutionally	22.6%
Market Capitalization (MM)	\$128
Average Daily Volume (000)	110
Revenues - LTM (MM)	\$30.4
Total Debt (MM)	\$23.7
Cash per Share (excludes convert)	\$4.51
Long-Term Growth Rate	0%

Fiscal Year Ends: Dec.	2005A	2006A	2007E	
Revenue (MM)	\$101.2	\$63.6	\$10.4	
Previous Revs (MM)	NE	NE	\$18.2	
Earnings per Share				
	Q1	\$0.20	\$0.34	(\$0.36)
	Q2	\$0.21	\$0.02	(\$0.40)A
	Q3	\$0.30	\$0.06	(\$0.45)
	Q4	\$0.45	(\$0.12)	(\$0.45)
Year	\$1.16	\$0.32	(\$1.66)	
Previous EPS	NA	NA	(\$1.62)	
P/E	6x	22x	NA	
Diluted Shares (MM)	16.8	16.4	15.8	

Orckit Communications Ltd. was founded in 1990 and is headquartered in Tel-Aviv, Israel. Orckit is the parent company of wholly-owned Corrigent Systems, which today comprises all of Orckit's business. The subsidiary provides next generation metro transport systems for carriers to migrate to converged networks.

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Table 1
Orckit Communications
Annual Earnings Model, 2001-2007E

(in thousands)	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006A</u>	<u>2007E</u>
Revenue	\$141,647	\$53,420	\$1,683	\$11,276	\$101,247	\$63,648	\$10,426
Cost of sales	112,007	32,963	748	5,901	51,872	30,219	5,022
Gross profit	29,640	20,457	935	5,375	49,375	33,429	5,404
Research and development, net	19,085	19,291	15,003	15,043	16,147	15,554	20,721
SG&A	16,993	14,699	12,656	11,993	16,086	16,017	16,505
Total operating expense	36,078	33,990	27,659	27,036	32,233	31,571	37,226
Operating income	(6,438)	(13,533)	(26,724)	(21,661)	17,142	1,858	(31,822)
Financial Income, net	-	-	5,108	1,529	2,636	3,346	5,596
Income before taxes	(6,438)	(13,533)	(21,616)	(20,132)	19,778	5,204	(26,226)
Income tax (pro forma)	-	-	-	-	-	-	-
Net income	(\$6,438)	(\$13,533)	(\$21,616)	(20,132)	\$19,778	\$5,204	(\$26,226)
EPS	(\$0.44)	(\$0.87)	(\$1.55)	(\$1.54)	\$1.16	\$0.32	(\$1.66)
Avg. shares out. (diluted):	14,625	15,489	13,931	13,074	17,003	16,408	15,797
Yr/Yr % change:							
Revenues	NA	(62%)	-97%	570%	798%	-37%	-84%
Gross profit	NA	(31)	(95)	475	819	(32)	(84)
Operating income	NM	NM	NM	NM	NM	(89)	NM
Pretax income	NA	NM	NM	NM	NM	(74)	NM
Net income	NA	NM	NM	NM	NM	(74)	NM
EPS	NA	NM	NM	NM	NM	(73)	NM
Avg. shares outstanding	NA	6	(10)	(6)	30	(3)	(4)
Gross margin	20.9%	38.3%	55.6%	47.7%	48.8%	52.5%	51.8%
Research and development	13.5	36.1	891.4	133.4	15.9	24.4	198.7
SG&A	12.0	27.5	752.0	106.4	15.9	25.2	158.3
Total Operating Expense	25.5	63.6	1,643.4	239.8	31.8	49.6	357.0
Operating margin	(4.5)	(25.3)	(1,587.9)	(192.1)	16.9	2.9	(305.2)
Pretax margin	(4.5)	(25.3)	(1,284.4)	(178.5)	19.5	8.2	(251.5)
Net margin	(4.5)	(25.3)	(1,284.4)	(178.5)	19.5	8.2	(251.5)
Tax rate	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: Company data and C.E. Unterberg, Towbin estimates

Table 2
Orckit Communications
Quarterly Earnings Model, 2005-2007E

(in thousands)	<u>1Q05</u>	<u>2Q05</u>	<u>3Q05</u>	<u>4Q05</u>	<u>1Q06</u>	<u>2Q06</u>	<u>3Q06</u>	<u>4Q06</u>	<u>1Q07</u>	<u>2Q07A</u>	<u>3Q07E</u>	<u>4Q07E</u>
Revenue	\$20,647	\$21,754	\$25,443	\$33,403	\$24,959	\$14,706	\$14,961	\$9,022	\$4,526	\$1,900	\$2,000	\$2,000
Cost of sales	10,547	11,115	13,060	17,150	12,028	7,357	6,933	3,901	2,044	978	1,000	1,000
Gross profit	10,100	10,639	12,383	16,253	12,931	7,349	8,028	5,121	2,482	922	1,000	1,000
Research and development, net	3,966	3,941	3,983	4,257	4,240	3,982	3,640	3,692	4,974	4,897	5,450	5,400
SG&A	3,686	3,709	3,825	4,866	3,903	3,662	4,236	4,216	4,011	4,094	4,200	4,200
Total operating expense	7,652	7,650	7,808	9,123	8,143	7,644	7,876	7,908	8,985	8,991	9,650	9,600
Operating income	2,448	2,989	4,575	7,130	4,788	(295)	152	(2,787)	(6,503)	(8,069)	(8,650)	(8,600)
Financial Income	693	865	583	495	1,032	589	833	892	890	1,706	1,500	1,500
Income before taxes	3,141	3,854	5,158	7,625	5,820	294	985	(1,895)	(5,613)	(6,363)	(7,150)	(7,100)
Income tax (pro forma)	-	-	-	-	-	-	-	-	-	-	-	-
Net income	3,141	3,854	5,158	7,625	5,820	294	985	(1,895)	(5,613)	(6,363)	(7,150)	(7,100)
EPS	\$0.20	\$0.21	\$0.30	\$0.45	\$0.34	\$0.02	\$0.06	(\$0.12)	(\$0.36)	(\$0.40)	(\$0.45)	(\$0.45)
Avg. shares out. (diluted):	15,999	18,167	17,014	16,831	17,022	16,685	16,282	15,644	15,709	15,776	15,826	15,876
Yr/Yr % change:												
Revenue	6352%	6115%	1154%	289%	21%	-32%	-41%	-73%	-82%	-87%	-87%	-78%
Gross profit	4,900	4,803	1,387	294	28	(31)	(35)	(68)	(81)	(87)	(88)	(80)
Operating income	NM	NM	NM	NM	96	NM	(97)	NM	NM	NM	NM	NM
Pretax income	NM	NM	NM	NM	85	(92)	(81)	NM	NM	NM	NM	NM
Net income	NM	NM	NM	NM	85	(92)	(81)	NM	NM	NM	NM	NM
EPS	NM	NM	NM	NM	74	(92)	(80)	NM	NM	NM	NM	NM
Avg. shares outstanding	23	39	30	28	6	(8)	(4)	(7)	(8)	(5)	(3)	1
Gross margin	48.9%	48.9%	48.7%	48.7%	51.8%	50.0%	53.7%	56.8%	55.0%	48.5%	50.0%	50.0%
Research and development	19.2	18.1	15.7	12.7	17.0	27.1	24.3	40.9	109.9	257.7	272.5	270.0
SG&A	17.9	17.0	15.0	14.6	15.6	24.9	28.3	46.7	88.6	215.5	210.0	210.0
Operating Expense	37.1	35.2	30.7	27.3	32.6	52.0	52.6	87.7	198.5	473.2	482.5	480.0
Operating margin	11.9%	13.7%	18.0%	21.3%	19.2%	-2.0%	1.0%	-30.9%	-143.7%	-424.7%	-432.5%	-430.0%
Pretax margin	15.2	17.7	20.3	22.8	23.3	2.0	6.6	(21.0)	(124.0)	(334.9)	(357.5)	(355.0)
Net margin	15.2	17.7	20.3	22.8	23.3	2.0	6.6	(21.0)	(124.0)	(334.9)	(357.5)	(355.0)
Tax rate	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Qtr/Qtr % change:												
Revenue	141%	5%	17%	31%	(25%)	-41%	2%	-40%	(50%)	(58%)	5%	0%

Source: Company data and C.E. Unterberg, Towbin estimates

Table 3
Orckit Communications
Quarterly Balance Sheet, 2005-2007E

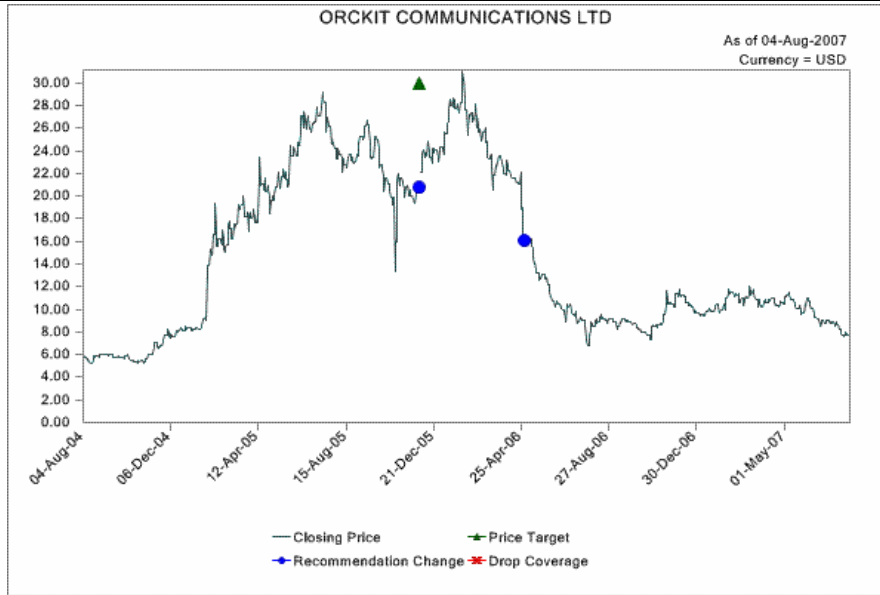
(in thousands)

	<u>4Q05</u>	<u>4Q06</u>	<u>1Q07</u>	<u>2Q07A</u>
Cash and short term investments	\$45,379	\$46,011	\$42,946	\$60,808
Restricted cash			\$25,761	\$25,885
Trade receivables	702	1,581	23	344
Other receivables	1,520	2,077	2,624	1,915
Inventories	3,330	3,464	3,669	1,996
<u>Total current assets</u>	<u>50,931</u>	<u>53,133</u>	<u>75,023</u>	<u>90,948</u>
Long-term investments	72,381	40,561	39,389	33,166
Other Investments	0	0	0	0
Severance pay fund	2,894	3,173	3,397	3,147
Property and Equipment, net	3,740	2,490	2,164	1,839
Deferred insurance costs, net	0	0	799	858
<u>Total assets</u>	<u>\$129,946</u>	<u>\$99,357</u>	<u>\$120,772</u>	<u>\$129,958</u>
Bank loan	\$0	\$0	\$469	\$20,796
Trade payable	9,282	4,907	5,524	4,687
Accrued expenses and other payables	19,173	10,134	10,739	8,559
Deferred Income	28,736	3,196	1,796	1,830
<u>Total current liabilities</u>	<u>57,191</u>	<u>18,237</u>	<u>18,528</u>	<u>35,872</u>
Accrued Severance pay	3,689	4,257	4,926	4,559
Long-term bank loan	0	0	0	0
Convertible subordinated note	0	0	25,752	23,719
<u>Total liabilities</u>	<u>60,880</u>	<u>22,494</u>	<u>49,206</u>	<u>64,150</u>
<u>Stockholders' equity</u>	<u>69,066</u>	<u>76,863</u>	<u>71,566</u>	<u>65,808</u>
<u>Total liabilities and stockholders' equity</u>	<u>\$129,946</u>	<u>\$99,357</u>	<u>\$120,772</u>	<u>\$129,958</u>

Balance Sheet Metrics

Net cash	116,965	85,488	80,346	73,932
Net cash per share	6.95	5.26	4.93	4.51
LT debt to capital (%)	0%	0%	46%	43%
Working capital	(6,260)	34,896	56,495	55,076
DSO	56	56	0	16
Turns	20.6	4.5	2.2	2.0

Source: Company data and C.E. Unterberg, Towbin estimates



ORCKIT COMMUNICATIONS LTD

Currency = USD

Date	Closing Price	Recommendation Change	Date	Closing Price	Price Target
28-Apr-2006	16.12	MARKET PERFORM	01-Dec-2005	20.77	30.00
01-Dec-2005	20.77	BUY			

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- Market Perform: Performance in line with the market averages anticipated.
- Under Perform: 12 months, estimated underperformance of 20% or more

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	% of CEUT Universe with this rating	% of rating tier for which CEUT provided IB services
Buy	60%	88%
Market Perform	38%	12%
Under Perform	2%	0%

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