

Mossberg's Investor Digest

Best Idea Profile:

Ikanos Communications, Inc. (NASDAQ:IKAN)

DESCRIPTION:

Ikanos Communications provides advanced broadband semiconductor and software products. The Company's broadband DSL, communications processors and other offerings are used in both access infrastructure and customer premises equipment. Its customers include Alcatel-Lucent, DASAN Networks, Gemtek, ZTE, etc. Second quarter revenue breakdown was 59% broadband DSL, 31% communications processing and 10% from other technologies. The Company was formerly known as Velocity Communications and changed its name in December 2000. Ikanos was incorporated in 1999 and is headquartered in Fremont, California.

KEY INVESTMENT CONSIDERATIONS:

Leader in developing low-cost technology that enables carriers to deliver triple play voice, Internet and video – Traditional voice carriers have a difficult choice as they look to add video to their voice and Internet service offerings. In order to meet the higher bandwidth and other requirements for video, carriers are faced with deploying fiber to the curb, which can cost as much as 2x to 6x that of deploying DSL technology. Ikanos has been an early developer and holds foundational patents surrounding a new technology they call node-scale vectoring, which can deliver 50 to 100 Mbps at a fraction of the cost of fiber and offers an attractive solution for carriers.

Foundational patents may provide competitive moat – As of January 1, 2012, Ikanos has a total of 289 issued patents and a larger number of provisional patents and applications pending. The expiration dates range from 2015 through 2030. Despite recent announcements by competitors, management has chosen not to enforce its patents, but clearly could pursue this strategy to get strategic advantage.

Chairman and CEO interests aligned with shareholders – A new CEO was hired in June 2012. Omid Tahernia has over 28 years of experience in leading global high technology organizations and businesses providing systems and semiconductor solutions. He was granted non-qualified stock options to purchase up to 2.1 million shares. The Chairman of Ikanos, Dado Banatao, is a 32% owner through his venture capital firm, and is well connected in the industry. Both their interests are aligned with shareholders.

Risk – Fundamentals have deteriorated since August 2010 with disappointing losses, declining market share, restructuring charges, engineering delays, and management chaos just to name a few. Others have entered the market for VDSL and may make it more difficult for IKAN to ramp revenue from its new technologies.

VALUATION:

The Company has \$33 million in cash, and a market cap of \$60 million, leaving an enterprise value of just \$26 million. This kind of liquid value provides a support base for the stock. As the company gains traction in the VDSL market, incremental revenue should provide a disproportionately larger contribution to earnings. Also, with a market capitalization of \$60 million, significant cash and patents, the stock could be a likely target for acquisition at a value significantly above the stock's current price.

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Investment Data (as of 8/30/12)

Recent Price	\$0.92
52-Week Range	\$0.64 - \$1.12
Fiscal Year End	Dec
Dividend	NA
Yield	NA
Shares Outstanding	70 M
Average Trading Volume (3 mos)	66 K
Market Capitalization	\$64 M
Cash	\$33 M
Long Term Debt	0
Enterprise Value (EV)	\$30 M
Book Value	\$0.80
TTM Revenue	\$134 M
P/ Revenue	0.44
TTM EPS	\$(0.12)
P/ EPS	NA
TTM EBITDA	\$2.7 M
EV/ EBITDA	9.5

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