

# Mossberg's Investor Digest

## Best Idea Profile:

## Sycamore Networks, Inc. (NASDAQ:SCMR)

### DESCRIPTION:

Headquartered in Chelmsford, Massachusetts, Sycamore Networks provides solutions that help telecom carriers manage bandwidth in their wireless and wire line networks. Customers include Sprint, Verizon, Telstra, China Unicom, and the U.S. Department of Defense. Founded in 1998, SCMR provides 1) Intelligent Bandwidth Management solutions and 2) Mobile Broadband Optimization solution (under the brand name IQstream®). The company is no longer investing in its intelligent bandwidth management business, as this market is in secular decline largely due to the fact that most of the large networks requiring the technology have already been built. Instead, the Company is focusing its efforts on its IQstream® Mobile Broadband Optimization solution. This is an emerging market opportunity that leverages Sycamore's current business. This technology adapts to changing traffic and content patterns to reduce congestion at critical mobile broadband flashpoints and improves the user experience.

### KEY INVESTMENT CONSIDERATIONS:

**Accelerating worldwide demand for mobile broadband** – There is increasing growth and concentration of video that is driving much of the demand for mobile broadband. This is a challenge to the operator as it tries to harness its expenses yet preserve the customer's experience.

#### Sycamore Networks, Inc. (NASDAQ:SCMR)

Investment Data (as of 10/11/12)

<b>Recent Price</b>	<b>\$14.47</b>
52-Week Range	\$13.02 - \$20.16
Fiscal Year End	July
Dividend	NA
Yield	NA
Shares Outstanding	28.9 M
Average Trading Volume (3 mos)	180k
Market Capitalization	\$421 M
Cash	\$351 M
Long-term Debt	N/A
Enterprise Value (EV)	\$72 M
Book Value	\$15.37
TTM Revenue	\$53.4 M
P/ Revenue	7.93x
TTM EPS	\$(0.49)
P/ EPS	NA
TTM EBITDA	\$(12.6) M
EV/ EBITDA	(5.75)

**Positive revenue trends** – Fourth-quarter revenue that was reported in September was \$16.8 million, well above street estimates and 29% above the prior-year's final quarter.

**IQstream potential is huge** – IQstream is a unique and dynamic solution to help carriers manage bandwidth during peak periods of usage. IQstream is still undergoing trials with no real customer acceptance as of yet, but the trials are moving from lab to field trials. Testing continues to validate IQstream's core system functionality and reliability during increased traffic volumes and higher levels of congestion. Sycamore's complex and unique solutions are powerful, and will be significant contributors to the company's success upon customer acceptance.

**Cash Distribution and disciplined expense management** – Sycamore announced in September that it would distribute \$10 in cash to shareholders (ex-dividend date is October 12). The Company's ongoing operations and disciplined expense management have yielded a strong cash balance \$439.4 million, compared with \$441.4 million at July 31, 2011. On a per share basis the company has \$15.22 in cash prior to the \$10 special dividend and \$5 per share in cash, post dividend.

**Risk** – Obviously, the greatest risk to investors is that there is no assurance that Sycamore's IQstream will get out of trials and be broadly accepted by customers. Non-acceptance risk is mitigated by Sycamore's current cash position, even after the special distribution of \$10 per share.

### VALUATION:

This is a speculative stock, but one with significant downside protection. And, if the IQstream product catches on with customers, the impact to revenue, margins and earnings will reward patient investors. Citrix (Nasdaq: CTX) recently bought Bytemobile (comparable to IQstream) for \$435 million. Post acquisition, Citrix said it expects to recognize \$15 million in Bytemobile related revenue during the fourth quarter. This would imply a \$60 million revenue run rate and approximately 7x multiple of revenue for the purchase price. Should IQstream generate significant revenue, it could garner a similar multiple and significant upside from current levels.

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