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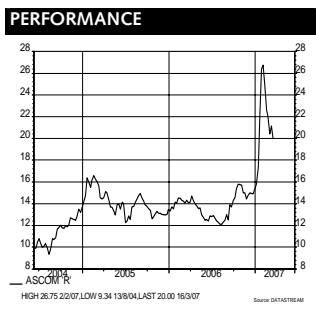
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**FY 06 results – the calm before the storm?**

Ascom's FY 06 results held no surprises. Although both core divisions displayed good order backlogs at the beginning of 2007, Ascom's FY 07 outlook is not very encouraging and remains uninspiring in terms of EBIT margin, especially for the Security Solutions division. While we do not exclude corporate action in the months to come, we fear that the transition phase management is in could negatively impact Ascom's operating businesses, especially its core Security Solutions division. The stock is fully valued at its current level when excluding any takeover premium. We therefore reduce our PT to CHF 20 (17x 08E EPS excluding CHF 4.6 in cash) from CHF 21 and confirm our Market Perform rating. While Chairman Anttila has publicly stated that he enjoys the support of major shareholder Victory (25% stake) for his proposed re-election at the AGM, we are still somewhat sceptical that a lasting truce has been reached. From our perspective, the probability of corporate action is still high. While the stock is now fully valued, we still believe that the final chapter in the Ascom/Victory story has not yet been written. Corporate M&A action or shareholder activism could still drive the stock materially higher than our current price target.

**Uninspiring FY 07 outlook:** Our FY 07 estimates are near the upper end of the company's guidance as it is hard to reconcile the uninspiring outlook, especially for Security Solutions, with the good order backlog and the healthy market environment unless we anticipate a very negative impact from the management transition.

**Acquisitions looming:** Net cash of CHF 166 mn and the clear intention to accelerate sales growth in both divisions in our view increases the probability of acquisitions or strategic alliances in the near future. Both divisions could benefit from stronger distribution capabilities in order to accelerate regional expansion.



PER SHARE DATA	
Price target CHF	20.00
Price ASCN.S on 16-03-07 CHF	20.00
No. of shares ASCN.S in '000	35,835
Market cap. ASCN.S (CHF mns)	717
Other market cap. (CHF mns)	0
Total market capitalization (CHF mns)	717
Free float %	75
Victory (voting 25%)	25
Average daily trading volume (12 months)	
	294,580

SHARE VALUATION				
CHF	2005	2006	2007E	2008E
EPS	4.04	0.48	0.74	0.91
EPS growth %	210	-88	55	23
P/E	5.0	41.7	27.0	21.9
CEPS	4.04	0.48	0.74	0.91
P/CE	5.0	41.7	27.0	21.9
Dividend	0.28	0.00	0.00	0.00
Dividend yield %	1.4	0.0	0.0	0.0
Book value	10.8	6.17	6.91	7.82
Price/Book	1.9	3.2	2.9	2.6
EV/EBITDA	7.6	11.4	10.9	9.0

HIGH	12-month	LOW
27.50		11.90

BREAKDOWN		
	CHF mns	Share in %
Net sales 2006		
- by sector		
Wireless Solutions	286	51
Security Solutions	195	35
Special Products	69	12
Group Functions	22	4
Consolidation	-8	-1
Total	565	100

KEY DATA			
CHF mns	2006	2007E	2008E
Sales	565	582	562
EBIT	33.0	33.5	41.0
EBIT margin %	5.8	5.8	7.3
Shareholders' net profit	17.1	26.5	32.6
Return on equity %	7.8	10.7	11.7
Total assets	493	524	534
Equity	220	247	279
Equity ratio %	44.7	47.1	52.3
Interest-bearing debt	0.10	0.10	0.10
Cash	166	187	211
Operating cash flow	45.0	38.9	47.1
Capex	-13.5	-13.5	-13.5

EXCESS PERFORMANCE		
	SPIX <sup>1</sup>	SMLCPSW <sup>2</sup>
3M	33.5%	23.2%
6M	35.9%	21.4%
12M	27.9%	10.7%

<sup>1</sup>SPI ex Div.  
<sup>2</sup>Vontobel Small Caps Index

## Muted outlook for Security Solutions – showdown at AGM or some time thereafter?

### **FY 06 results held no surprises**

Ascom's FY 06 results held no surprises as the company had already pre announced key figures (orders, sales, net income) on 1 February 2007. Group orders increased by 9.1% to CHF 614.8 mn, driven by large contract wins at its core division, Security Solutions (SeSo). Net sales rose 2.1% to CHF 564.9 mn, not yet displaying the effect of the strong order intake. EBIT was up 5.1% to CHF 33 mn and group net income reached CHF 17.1 mn including a CHF 16.1 mn loss from discontinued operations. Net cash at the end of FY 06 amounted to CHF 166 mn, in-line with expectations. Cash flow from operations reached CHF 45 mn with working capital intensity declining further (net working capital as a % of net sales: 15%).

### **Chairman Anttila to stand for re-election – omission of dividend payment**

The board has proposed that current Chairman Juhani Anttila be re-elected, that there be no dividend payment this year and that the number of board members be reduced to six. Ascom plans to use its cash hoard for value-enhancing investments and acquisitions. The proposals not to pay a dividend this year and to reduce the number of board members to six did not come as a surprise as both were requested previously by major shareholder Victory.

### **Wireless Solutions: good order intake in direct business – OEM still hurting**

Both of Ascom's core divisions demonstrated strength in terms of order intake. Wireless Solutions (WS) recorded order intake of CHF 297.2 mn (+6.2%), but revenue growth of 2.5% was negatively impacted by a further decline of 17% in the OEM business. Direct sales grew by 5%. WS reached a good EBIT margin of 9.7%, in-line with the company's guidance of 8-10%. We believe that Ascom is not close to signing any new OEM customers at present which is dampening prospects for revenue growth. While entry into the US has been successful, Ascom needs to strengthen its distribution capabilities in this market. We note that US competitor Spectralink is in the process of being acquired by Polycom (expiry for tender offer on 20 March). The outlook for WS is not very encouraging. Growth for WS is expected to be 5% (vs. 5-10% mid-term guidance) and the EBIT margin 8-10% (vs. 9-11% mid-term guidance), implying no y-o-y improvement. With the backlog up by 21.2% to CHF 70.6 mn at the end of FY 06, strong growth momentum in several countries (US, CH, NL), 20 distributors signed up in the US and a large installed base (over 70'000 customers to sell service contracts), we are somewhat disappointed by the outlook for sales growth of only 5% even when anticipating a further high single-digit decline in the growth rate of the OEM business and no OEM customer wins.

**Security Solutions: reasons for muted outlook remain unclear**

SeSo had strong order intake of CHF 243.1 mn (+13.8%), mainly as a result of a large (>CHF 60 mn) order from the Swiss Army which was awarded in December. FY 06 revenues of CHF 195 mn represented a decline of 5% y-o-y with an EBIT margin of 1.1%. As the majority of the legacy projects have been concluded and the division has a strong order backlog of CHF 161.5 mn (+44.5%), we are again somewhat disappointed with the FY 07 guidance for revenue growth of >5% and an EBIT margin of only 1-3%. We see a number of potential reasons for this muted outlook:

- Overly conservative management guidance
- Intrinsic profitability at SeSo below earlier management expectations
- Transformation of the divisions will take longer than expected, thereby negatively affecting margins
- Lower profitability due to lower capacity utilisation if expected contract wins fail to materialize
- Lower probability of successful implementation of international expansion strategy due to loss of the former head of division Rudolf Hadorn.

We note that the overall tone regarding the prospects for SeSo was unusually downbeat and cautious.

**Security Solutions: important role of former CEO Hadorn**

Security Solutions garnered several major contract wins (Swiss Army, Russia, Finnish Army) after Rudolf Hadorn became head of the division at the end of October 2006. We believe his strong relationships with large government or near-government clients together with his deep understanding of Eastern Europe and extensive experience in that market were instrumental in securing these contract wins. We therefore fear that the management changes could damage Ascom's reputation and make the company unable to compete for similar contracts. In addition, as Security Solutions actually comprises four different business units (Defence, Traffic Security, Public Safety, Telecom) with a low level of synergy and diverse customer bases, the next division head of the SeSo would need substantial time before being able to make qualified decisions.

**Wireless Solutions: growth acceleration is the main challenge**

We fear that Fritz Mumenthaler as ad-interim CEO could be distracted from his duties as head of Wireless Solution, a division where he spearheaded the launch of new products as well as growth initiatives and EBIT margin improvements. As WS faces some challenges (i.e. finding new OEM clients, expanding in the US, achieving higher growth), we fear that the temporary lack of appropriate management resources could also negatively impact this business.

**FY 07 and FY 08 estimates revised downwards by 10.8% to CHF 0.74 and CHF 0.91, respectively**

Following the publication of Ascom's FY 06 results, we have reduced both our FY07 and FY08 estimates by 10.8% to CHF 0.74 and CHF 0.91, respectively (see Table 1). Our estimate cut reflects the following assumptions: 1) slower-than-expected growth at WS; 2) no margin expansion at WS 3); ongoing transition phase at SeSo 4); divestment of what is left of the Special Products division only by end 2007. The group EBIT margin now stands at 5.8% for 2007E (previously: 6.8%) and at 7.3% for 2008E (previously: 7.8%).

**TAB. 1: ESTIMATE REVISIONS FOR 2007E AND 2008E**

(in USD mn)	2007E old	2007E new	Change	2008E old	2008E new	Change
Sales	543	582	7.2%	581	562	-3.3%
- change y-o-y	-8.1%	3.0%	NA	7.0%	-3.4%	NA
- thereof Wireless Solutions	319	303.0	-5.0%	347	325.7	-6.1%
- thereof Security Solutions	213	210.6	-1.1%	224	221.5	-1.1%
Gross margin	38.0%	36.0%	NA	38.3%	38.0%	NA
EBITDA	50.3	48.8	-3.0%	59.0	56.3	-4.6%
- margin	9.3%	8.4%	NA	10.2%	10.0%	NA
Depreciation	-12.0	-13.5	-12.5%	-12.0	-13.5	-12.5%
Operating result	36.3	34.3	-5.5%	45.0	41.8	-7.1%
- margin	6.7%	5.9%	NA	7.7%	7.4%	NA
Amortization	-1.5	-1.8	-20%	-1.5	-1.8	-20%
Other income/expenses	2.0	1.0	-50%	2.0	1.0	-50%
EBIT	36.8	33.5	-9.0%	45.5	41.0	-9.9%
- change y-o-y	82%	1%	NA	24%	22%	NA
- margin	6.8%	5.8%	NA	7.8%	7.3%	NA
Financial result	3.0	2.0	-33%	3.5	2.5	-28.6%
Taxes	-10.0	-9.0	10.0%	-12.5	-10.9	12.8%
- tax rate	25.1%	25.4%	NA	25.5%	25.1%	NA
Profit from cont. operations	29.8	26.5	-11.1%	36.5	32.6	-10.7%
Profit from discont. operations	0.0	0.0	0%	0.0	0.0	0%
Shareholder's net profit	29.8	26.5	-11.1%	36.5	32.6	-10.7%
EPS in CHF	0.83	0.74	-10.8%	1.02	0.91	-10.8%
- y-o-y	605%	55%	NA	22%	23%	NA

Source: Vontobel Equity Research

**FY 07 guidance seems overly conservative**

Our FY 07 estimates are near the upper end of the company's guidance (Table 2) as we fail to align the uninspiring outlook with the good order backlog and the healthy market environment unless we take a very negative view on the potential impact of the management transition. While there is anecdotal evidence for the latter, we have not built in a worst case scenario into our model.

**TAB. 2: ASCOM GUIDANCE VS. VONTOBEL ESTIMATES**

FY07-Guidance vs. Vont 2007E	Sales Growth	Sales Growth	EBIT-Margin	EBIT-Margin
	Ascom	VontE	Ascom	VontE
Wireless Solutions	around 5%	6.0%	8-10%	9.8%
Security Solutions	>5%	8.0%	1-3%	2.8%
mid-term* guidance vs. Vont 2008E	Sales Growth	Sales Growth	EBIT-Margin	EBIT-Margin
	Ascom	VontE	Ascom	VontE
Wireless Solutions	5-10%	7.5%	9-11%	10.5%
Security Solutions	around 5%	5.0%	5-7%	3.8%

\* = 2-3 yrs

Source: Vontobel Equity Research, Ascom

Ascom has made some progress towards becoming a growth company with orders in both core divisions Wireless Solutions and Security Solutions rising y-o-y by 6.2% and 44.5%, respectively. We are therefore slightly disappointed that the strong backlog in both divisions did not lead to a more encouraging outlook as we believe strong orders should eventually convert into higher sales and stronger margins. We wonder if the outlook for the operating business is already deteriorating or if the company includes one-off costs in the guidance as we could envisage a further simplification of the organisational structure (divestments of business units?).

**Full valuation – stock looks expensive based on outlook for operating business**

Ascom trades at a 08E P/E of 17x ex-cash, which is in-line with its peer group. Based on 08E EV/EBIT of 13.5 and 08E P/S of 1.3, the stock does not look particularly attractive, either. However, we believe the share price is poised to find good support near current levels as long as the strategic plans of major investor Victory (24.8% stake) remain unclear.

**PT down to CHF 21 (old: CHF 20) – Market Perform**

While we do not exclude corporate action in the months to come, we fear that the current management transition phase could negatively impact Ascom's operating businesses especially in Security Solutions core division. The stock is now fully valued at current levels excl. any takeover premium. We therefore reduce our PT to CHF 20 (17x EPS 08E excl. CHF 4.6 in cash) from CHF 21 and confirm our Market Perform rating.

**Still high probability for corporate action could drive stock materially above our PT**

While chairman Anttila has publicly stated that he enjoys the support of major shareholder Victory for his proposed re-election at the AGM, we are still somewhat hesitant to call the truce. From our perspective, the probability for corporate action is still high. However, we fear that the current management transition phase could negatively impact Ascom's operating business especially in Security Solutions. While the stock is now fully valued, we still believe that the final chapter in the Ascom/Victory story has not been written. Corporate M&A action or shareholder activism could still drive the stock materially higher than our current price target.

CONSOLIDATED FINANCIAL DATA (CHF MNS)								SPS/7182
	2001	2002	2003	1) 2004	2) 3) 2005	4) 5) 2006	6) 2007E	2008E
<b>SALES</b>	<b>3143</b>	<b>2066</b>	<b>1515</b>	<b>838</b>	<b>689</b>	<b>565</b>	<b>582</b>	<b>562</b>
- change (%)	0.0	-34.3	-26.7	-44.7	-17.8	-18.0	3.0	-3.4
<b>EBITDA</b>	<b>-110.0</b>	<b>-43.1</b>	<b>32.8</b>	<b>85.8</b>	<b>57.6</b>	<b>48.5</b>	<b>48.8</b>	<b>56.3</b>
- as % of sales	-3.5	-2.1	2.2	10.2	8.4	8.6	8.4	10.0
DEPRECIATION	-141.0	-107.1	-59.0	-31.1	-17.6	-13.8	-13.5	-13.5
- as % of sales	-4.5	-5.2	-3.9	-3.7	-2.6	-2.4	-2.3	-2.4
<b>OPERATING RESULT ("EBITA")</b>	<b>-251.0</b>	<b>-107.4</b>	<b>-27.2</b>	<b>45.1</b>	<b>22.8</b>	<b>33.0</b>	<b>34.3</b>	<b>41.8</b>
- as % of sales	-8.0	-5.2	-1.8	5.4	3.3	5.8	5.9	7.4
AMORTIZATION	-87.3	-80.5	-19.0	-12.7	0.0	0.0	0.0	0.0
OTHER AMORTIZATION	0.0	0.0	0.0	0.0	-5.3	-1.7	-1.8	-1.8
OTHER INCOME/EXPENSES	0.0	-42.8	1.0	9.6	17.2	1.7	1.0	1.0
<b>EBIT</b>	<b>-338.3</b>	<b>-230.7</b>	<b>-45.2</b>	<b>42.0</b>	<b>34.7</b>	<b>33.0</b>	<b>33.5</b>	<b>41.0</b>
- change (%)	-549	-32	-80	-193	-17	-5	1	22
- as % of sales	-10.8	-11.2	-3.0	5.0	5.0	5.8	5.8	7.3
FINANCIAL RESULT	-45.5	-30.7	-12.5	-12.1	-6.4	0.0	2.0	2.5
PRETAX PROFIT	-383.6	-261.4	-57.6	29.9	28.3	33.0	35.5	43.5
- change (%)	-501	-32	-78	-152	-5	17	7	23
- as % of sales	-12.2	-12.7	-3.8	3.6	4.1	5.8	6.1	7.7
TAXES	-15.7	-23.1	-10.2	6.5	1.2	0.2	-9.0	-10.9
- tax rate (%)	-4.1	-8.8	-17.7	-21.7	-4.2	-0.6	25.4	25.1
<b>PROFIT FROM CONT. OPERATIONS</b>				<b>36.4</b>	<b>29.5</b>	<b>33.2</b>	<b>26.5</b>	<b>32.6</b>
- change (%)				0	0	13	-20	23
- as % of sales				4.3	4.3	5.9	4.6	5.8
<b>PROFIT FROM DISCONT. OPERATIONS</b>				<b>10.5</b>	<b>115.3</b>	<b>-16.1</b>	<b>0.0</b>	<b>0.0</b>
MINORITY INTERESTS	3.8	3.2	-0.1	0.0	0.0	0.0	0.0	0.0
<b>SHAREHOLDERS' NET PROFIT</b>	<b>-395.5</b>	<b>-281.3</b>	<b>-67.9</b>	<b>46.9</b>	<b>144.8</b>	<b>17.1</b>	<b>26.5</b>	<b>32.6</b>
- change (%)	-689	-29	-76	-169	209	-88	55	23
- as % of sales	-12.6	-13.6	-4.5	5.6	21.0	3.0	4.6	5.8
- as % of equity shareholder	-76.9	-143.8	-33.4	19.1	37.6	7.8	10.7	11.7
CASH FLOW FROM OPERATIONS	12.2	105.4	54.2	44.3	41.0	45.0	38.9	47.1
- change (%)	-11	764	-49	-18	-7	10	-14	21
- as % of sales	0.4	5.1	3.6	5.3	6.0	8.0	6.7	8.4
CAPITAL EXPENDITURE	-64.3	-51.9	-22.9	-14.0	-17.1	-13.5	-13.5	-13.5
- 5-year average	NA	-105.3	-75.5	-53.9	-34.0	-23.9	-16.2	-14.3
R & D	-203.1	-109.3	-54.5	-28.4	-36.3	-30.8	-32.0	-33.0
- as % of sales	6.5	5.3	3.6	3.4	5.3	5.5	5.5	5.9
<b>DATA PER REG. (CHF ADJ.)</b>								
<b>EARNINGS</b>	<b>-17.58</b>	<b>-12.56</b>	<b>-2.50</b>	<b>1.30</b>	<b>4.04</b>	<b>0.48</b>	<b>0.74</b>	<b>0.91</b>
- change (%)	-689	29	80	152	210	-88	55	23
CASH EPS CHF	22.86	8.73	-1.80	1.66	4.04	0.48	0.74	0.91
- change (%)	-45	-62	-121	-192	144	-88	55	23
DIVIDEND IN CHF	0.00	0.00	0.00	0.28	0.28	0.00	0.00	0.00
- payout ratio (%)	N.M.	N.M.	N.M.	21	7	0	0	0
CASH FLOW	0.54	-0.26	1.77	2.77	1.70	1.20	1.17	1.32
BOOK VALUE	22.9	8.7	7.5	6.8	10.8	6.2	6.9	7.8
TOTAL ASSETS	2,482	1,504	1,108	955	762	493	524	534
CASH & SECURITIES	152	230	321	344	279	166	187	211
INTEREST-BEARING DEBT	783	494	266	218	2	0	0	0
<b>NET DEBT</b>	<b>631</b>	<b>264</b>	<b>-55</b>	<b>-127</b>	<b>-277</b>	<b>-166</b>	<b>-187</b>	<b>-211</b>
- as % of group equity	122.0	135.2	-27.0	-51.5	-71.9	-75.2	-75.9	-75.5
<b>EQUITY SHAREHOLDER</b>	<b>514</b>	<b>196</b>	<b>203</b>	<b>246</b>	<b>385</b>	<b>220</b>	<b>247</b>	<b>279</b>
GROUP EQUITY	517	196	204	246	385	220	247	279
- as % of total assets	20.8	13.0	18.4	25.7	50.6	44.7	47.1	52.3
NO. OF EQUIV. REG. (MNS)	22.500	22.399	27.174	35.995	35.834	35.684	35.684	35.684

1) 2004 restated for new IFRS 5 reporting in 2005

2) IFRS 5 reporting (accounting for cont. and discount. Operations)

3) Network Integration CH, B, Transport Revenue divested by end 2005

4) Network Int D, Powerline Communication, Ascodi, real estate divested by end 2006, 180 mn returned to shareholders

5) Network Integration I divested by 1.12.2006, book loss CHF 10 mn in profit from discount. Operations

6) Toll France/HK, Payphones divested by end of 2007; assumed book losses and gains compensate each other

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- Key business figures and ratios (valuation and profitability, e.g. NAV, embedded value and franchise value) compared to the sector (peer group comparison) and in relation to the company's history
- "Sum-of-the-parts" model

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<i>Perform</i>	Performance of between +5% and -5% expected to the benchmark
<i>Underperform</i>	Underperformance of more than -5% expected to the benchmark

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