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# Intrinsyc Software Inc.[1,7]

BUY

ICS C$0.75

Target: C$1.50

| What's Changed | | New | Old |
|---|---|---|---|
| | | New | Old |
| Recommendation | | n/c | BUY |
| Target | | n/c | C$1.50 |
| Revenue 2007A (mm) | | n/c | C$19.7 |
| Revenue 2008E (mm) | | n/c | $22.3 |
| Revenue 2009E (mm) | | n/c | $43.4 |
| EPS 2007A | | n/c | C($0.18) |
| EPS 2008E | | n/c | ($0.11) |
| EPS 2009E | | n/c | ($0.01) |
| **Share Data** | | | |
| Shares – mm (basic/f.d.)* | | | 152.3/152.3 |
| 52-week high/low | | | C$1.30/C$0.39 |
| Market capitalization (mm) | | | C$114 |
| Enterprise value (mm) | | | C$70 |
| Net cash (mm)* | | | C$44.5 |
| Total projected return | | | 100% |
| **Financial Data** | | | |
| YE Dec. 31 | 07A | 08E | 09E |
| Revenue (mm) | C$19.7 | $22.3 | $43.4 |
| EV/Revenue | 3.5x | 3.1x | 1.6x |
| EPS | (C$0.18) | ($0.11) | ($0.01) |
| P/E | nm | nm | nm |
| EBITDA (mm) | (C$14.2) | ($15.9) | ($0.9) |

All figures in US$, unless otherwise stated
Note: F07 in C$ with Aug YE; all others reflect Dec YE
*reflects impact of recent equity financing

## *Transition period results in line; Soleus on track for royalty revenues in 2H08*

- Rev $5.2 mm (as expected), and net loss $7.3 mm (vs. our $6.8 mm loss estimate)
- Investors should focus on Soleus, which should start to make an impact on revenues and gross margins in 2H/08 and beyond as royalty revenues start to ramp
- All Soleus customers are progressing well and tracking to plan, in our view
- We continue to expect at least one new design win per quarter to maintain the positive momentum
- No changes to our forecast; reiterate BUY rating

## NO MAJOR SURPRISES TO STUB PERIOD RESULTS

For the four-month period, revenues of $5.2 million matched our estimate. On the bottom line, net losses amounted to $7.2, compared to our $6.8 million loss estimate. Net losses include a $0.7 million charge related to a previously announced restructuring to close the UK operations. The variance relative to our net loss estimate is primarily attributed to lower-than-expected gross margins of 36.4% (vs. our 40.7% estimate). We had already factored in a decline in gross margins to reflect lower-margin services business for three Soleus customers. However, the company had a further impact due to the weaker US$ relative to the C$, and a delay in signing an Engineering Services contract during the transition period (which has since been signed).

## SOLEUS IS PROGRESSING WELL AND TRACKING TO PLAN, IN OUR VIEW

Recall, the key to our investment thesis is Soleus, and the company's successful transition from an Engineering Services business to a more attractive royalty-based software business model with Soleus. During the transition period, Soleus revenue was still immaterial at only $140K reflecting upfront licensing and maintenance fees from announced design wins. Based on the comments during the call, we remain confident that Soleus is tracking to plan. Management indicated that MSI's 5608 device is currently in field trials, and initial shipments of Soleus-based devices are expected to start late in Q2/08. This is exactly in line with our forecast model.

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In addition to existing design wins, Intrinsyc continues to have active discussions with potential customers for future Soleus wins. We continue to expect multiple design wins with existing customers, similar to Mitac, and intentions from MSI to launch additional devices based on the Soleus platform. In addition, we believe Intrinsyc has made a positive impact on its initial Soleus customers as evidenced by their willingness to introduce Intrinsyc to other departments and deepen the business relationships (increasing the potential for additional design wins). Future versions of the platform (i.e., 3G, enhanced user interface) will continue to add value to customers.

## NO CHANGES TO OUR FORECAST, REITERATE BUY RATING AND C$1.50 TARGET

### *Our outlook*

Q1/08E: We expect revenue of $5.0 million and net loss of $4.4 million, or ($0.03) per share. In Q1/08, we expect Soleus revenue to be immaterial again as Soleus-based devices will not start shipping until late Q2/08.

F2008E: We expect revenue of $22.3 million and net loss of $16.3 million, or ($0.11) per share. In F2008, we expect Soleus to contribute $3.0 million.

F2009E: We expect revenue of $43.4 million and net loss of $1.5 million, or ($0.01) per share. Soleus revenue is expected to contribute $23 million in F2009. We expect the company to be profitable by Q4/09.

F2010E: We expect revenue of $60.0 million and net income of $6.7 million, or $0.04 per share. Soleus revenue is expected to contribute $38 million to overall sales in F2010.

## RECOMMENDATION

We continue to believe Intrinsyc is an exciting story with significant upside potential for growth-oriented investors. The company is led by a strong management team that has proven its ability to execute. Intrinsyc is at the cusp of finally reaping the rewards of transitioning from an engineering services business to a more attractive royalty-based software business model, which comes with more scalability, higher margins and greater predictability of revenue streams. The success of Soleus is key to the story. Intrinsyc has an impressive pace of design wins to date, which speaks to Soleus' ability to address the critical needs of a large and growing market for consumer-oriented feature phones and converged mobile devices.

We reiterate our BUY rating and C$1.50 target price on Intrinsyc. Our target price implies a C2009 EV/S multiple of 4.2x and is supported by a sum-of-the-parts analysis (valuing Soleus and the Engineering Services business separately) and a DCF valuation. At current levels, the shares are attractively valued, trading at a C2009 EV/S of 1.6x, a discount to the group average of 2.7x. We believe a premium multiple for Intrinsyc is justified given the strong expected growth as Soleus revenues ramp up. We are projecting Intrinsyc's 2009/2008 sales to grow 95%, compared to the group average of 23%.

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