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TAKING STOCK: DragonWave gets fired up

By Krystle Chow, Ottawa Business Journal Staff
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Peter Allen, CEO of DragonWave Inc. (Etienne Ranger, OBJ)

A Nasdaq listing, new highs in stock price and an expected $150M in revenues for fiscal 2009 – and it's just the beginning for a company set to ride the bandwidth boom

Since going public in 2007, DragonWave Inc. – whose packet-based microwave radio backhaul equipment is one of the candidate technologies for supporting the appetite for fresh bandwidth – has seen a steady climb in its fortunes.

It's one of the country's fastest-growing companies, making Deloitte's Fast 50 rankings four years in a row, and its stellar sales are expected to triple in its fiscal 2010 to more than $150 million.

The markets have been paying attention to the company's recent customer wins and strong financials, sending DragonWave's share price soaring to an all-time high of $12.10 in October, a major recovery after the stock bottomed out at 80 cents at the end of 2008. It's also tripled in value since its $3.90 opening price when it made its debut on the Toronto Stock Exchange on April 19, 2007.

With a brand-new Nasdaq listing up and running, DragonWave is now seeking to replicate its success on the Canadian public markets in the United States, where investors have already noticed.

Still, analysts have expressed concern that a large portion of DragonWave's business is concentrated on one major customer, Clearwire. So what's the strategy going forward?

The company's view: DragonWave CEO Peter Allen doesn't deny that customer concentration is an issue, but said he would rather have that problem than the alternative of not having a strong anchor to get the company's business off at the races.

"We make no apologies for getting a very strong position with a first-mover (with Clearwire's business)," said Mr. Allen.

"For the first time ever, the battleground for 4G is taking place in North America, where normally there would be traction first in Europe ... There are some big prizes here."

Nevertheless, DragonWave is working on expanding its international reach. In addition to recent big wins such as its involvement in Australia's first-ever 4G network and a deal with Russian company Yota – as well as a large deployment with Canadian wireless upstart Globalive – the company is making its move into Southeast Asia, Northern Africa and Latin America, among other markets. In fact, Mr. Allen noted DragonWave is now hiring staff for its new offices in Singapore.

Some important markets remain, as yet, unreachable, but Mr. Allen said DragonWave is ready to pounce when the conditions are right. "We're on the sidelines watching India, which is yet to license spectrum for high-capacity systems," he said, pointing out that once DragonWave gets a toehold into that very large-volume market, it's likely to be a big step for its global success.

In the meanwhile, back in North America, the firm's new Nasdaq listing has provided a multi-pronged tool with which to continue pursuing its primary geographic market.

First off, the initial public offering attached to DragonWave's U.S. debut boosts the company's balance sheet so it can stand stronger against tier-one competitors, now that Clearwire's business has helped them move into that space, said Mr. Allen.

As well, it's an opportunity for U.S. investors and customers to get to know DragonWave a little better, allowing for some possible diversification from Clearwire. That's especially important as the company prepares to compete for the business generated by roughly $7 billion in stimulus funds President Obama's administration is handing out for broadband infrastructure.

"There's a ton of work to be done, and there's no sense that the job's done here; we're only just starting," said Mr. Allen.

The analyst says: There's a keen opportunity for DragonWave to participate in a market yielding more than $1 billion annually as cell towers shift to Ethernet backhaul, according to a note by National Bank Financial's Kris Thompson.

Mr. Thompson, who has a $14 target and an "outperform" rating on the stock, wrote that he expects Ethernet backhaul penetration to grow to more than 20 per cent in a few years from less than five per cent of global cell towers at present, and that the size of the market indicates there's plenty of room for DragonWave and others to play.

DragonWave's dependence on Clearwire business remains a concern, Mr. Thompson noted, especially with the latter's recent selection of competing firm Ceragon Networks as a second source for lower-capacity edge links.

However, in line with Mr. Allen's comments, Mr. Thompson agreed there's an upside to having an early lead with Clearwire, since the latter continues to aggressively build out its network.

At any rate, Mr. Thompson predicted Clearwire concentration would fall from an estimated 63 per cent of DragonWave's total revenues in fiscal 2010 to just 40 per cent in fiscal 2011.

Part of the reason for that, explained Mr. Thompson, is the company's recent $75 million equity financing. "The financing will bolster the company's balance sheet, making it more palatable for service providers like Verizon Wireless and AT&T Mobility to select DragonWave as a partner," he wrote.

Mr. Thompson added he's had indication that DragonWave has been shortlisted as a qualifying vendor for

Verizon's new long-term evolution network, which will cover 25 to 30 cities by the end of 2010.

Even without Verizon's business, there's good support for DragonWave to potentially reach $200 million in annual revenues and a $20 share price in fiscal 2011, ahead of expectations, Mr. Thompson wrote.

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