

TeleCommunication Systems (TSYS)

TCS Reports Solid EPS Upside on Lower Revenue and Increases Guidance; Reiterate BUY and Increasing Target to \$6 from \$5.50

- **We remain positive and are buyers of TCS given the company's attractive valuation, upside EPS, and increased guidance.** While revenue was moderately below our expectations, better margins for each segment and a material revenue mix shift to higher margin Commercial Systems (messaging software) revenue, EBITDA and GAAP EPS easily exceeded expectations.
- **Despite lower revenue, Q1 GAAP EPS and EBITDA were better than expected due to higher segment margins and a revenue mix shift to higher margin messaging revenue.** Revenue was \$40.4 million. This compares to our estimate of \$42.6 million and consensus estimate of \$43.1 million. GAAP EPS was \$0.11, which was better than our estimate of \$0.09 and consensus estimate of \$0.08. EBITDA per share was \$0.19, which was also above our estimate of \$0.16.
- **Backlog levels remain solid and provide good visibility into growth.** While total backlog decreased sequentially to \$225 million from \$232 million in Q4, it is up materially YoY from \$90 million in 1Q07. We believe these backlog levels provide solid visibility into long-term growth. We would note that backlog can be lumpy given the nature of renewing large long-term 911 service contracts.
- **Momentum in high-margin messaging revenue set to have a profound impact on profitability.** While messaging revenue is not as key to revenue growth as low-margin government systems revenue, it is very material to profitability given that the revenue carries very high profit margins. Given YoY text messaging growth of 137% in the U.S. and 160% at TCS' largest customer Verizon Wireless, and the desire for carriers to drive additional messaging growth, we believe this segment will be a good revenue and key EPS growth driver for the company.
- **We are increasing our EPS and EBITDA estimates given the solid Q1 and that management increased EBITDA guidance.** We are modestly lowering our 2008 and 2009 revenue estimates to take a more conservative view on the low margin Government Systems segment. However, given solid contribution from high-margin messaging software we are increasing our EPS and EBITDA per share estimates. Management still expects 2008 revenue of \$165-175 million, but increased its EBITDA per share guidance to \$0.45-\$0.52 from \$0.38-0.45.

Maintain our BUY rating and increasing our price target to \$6 from \$5.50. Our price target is derived from our DCF analysis (Figure 1) and represents a 12x multiple on our 2009 pro forma EPS estimate of \$0.45. This represents a substantial discount to the company's projected long-term EPS growth rate of 22%.

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Price (as of close 5/01/08)

\$3.62

Rating

BUY

12- Month Price Target

\$6 (from \$5.50)

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Company Information

52-Week Range	\$2.71 - \$5.77
Shares Outstand.	43.8 million
Insider/Institutional	34% / 35%
Public Float	41.8 million
Market Cap.	\$158.5 million
Long-Term Debt	\$12.8 million
Debt/Capital	20.4%
ROE	36.9%
Cash & Inv/Share	\$0.17
Book Value/Share	\$1.09

Company Description

TeleCommunication Systems, Inc., based Annapolis, Maryland, engages in the development & application of wireless data communications technology. The Commercial Applications segment offers software & services that enable 911, text messages, location information, & Internet content. The Government segment provides the government communication systems & services.



Source: Thomson

FYE DEC	2007A	2008E			2009E		
REV. (\$m)	ACTUAL	CURR.	PREV.	CONS.	CURR.	PREV.	CONS.
Q1 Mar	\$34.1A	\$40.4A	\$42.6E	\$43.1	\$44.8E	\$45.7E	\$45.7
Q2 Jun	35.3A	40.1E	39.0E	38.3	46.1E	47.5E	47.5
Q3 Sep	37.6A	41.9E	43.3E	43.2	47.5E	49.3E	49.4
Q4 Dec	37.1A	43.5E	46.2E	46.1	49.0E	51.4E	51.4
Year**	\$144.2A	\$165.9E	\$171.1E	\$170.6	\$187.4E	\$193.9E	\$192.6
Change	15.4%	15.1%		18.3%	13.0%		12.9%
	2007A	2008E			2009E		
EPS*	ACTUAL	CURR.	PREV.	CONS.	CURR.	PREV.	CONS.
Q1 Mar	\$0.11A	\$0.19A	\$0.16E	\$0.15	\$0.13E	\$0.13E	\$0.10
Q2 Jun	0.01A	0.08E	0.03E	0.01	0.14E	0.14E	0.11
Q3 Sep	0.11A	0.10E	0.13E	0.10	0.14E	0.15E	0.12
Q4 Dec	0.13A	0.12E	0.14E	0.11	0.15E	0.16E	0.16
Year**	\$0.35A	\$0.48E	\$0.45E	\$0.37	\$0.56E	\$0.56E	\$0.45
P/E	10.3x	7.5x		9.8x	6.5x		8.0x
Change	-20.6%	37.2%		5.7%	14.7%		21.6%

Consensus estimates are from Thomson First Call.

* EPS calculated as EBITDA EPS

** Numbers may not add up due to rounding.

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Financial Analysis

Revenue: Revenue was \$40.4 million, which was below our estimate of \$42.6 million and the consensus estimate of \$43.1 million. Revenue was up 9% sequentially and up 18% YoY. The revenue increase was primarily due to better-than-expected Commercial Services and much better than expected Commercial Systems revenue, while Government Services revenue was in line with expectations while Government Systems revenue was well below expectations. Commercial Systems revenue benefited from solid demand for text messaging software. Although the Government Systems segment had poor showings, this segment tends to be choppy and the pipeline of business appears robust and thus we expect this segment to rebound in upcoming quarters.

GAAP EPS & EBITDA: For Q1, TCS reported GAAP EPS of \$0.11, which was \$0.02 above our estimate and \$0.03 above consensus expectations. EBITDA per share was \$0.19, which was \$0.03 ahead of our estimate of \$0.16. Despite lower revenue, Q1 GAAP EPS and EBITDA were better than expected due to higher segment margins and a revenue mix shift to higher margin messaging revenue.

Gross Margin: Overall gross margin was 48.4% versus our estimate of 40.4% and 40.4% last quarter. The improvement in gross margin was due to better gross margins across all segments and a revenue mix shift away from lower margin Government Systems and towards higher margin Commercial Systems.

Operating & EBITDA Margin: TCS' GAAP operating margin was 13.7% versus our estimate of 9.9% and 7.3% last quarter. The sequential increase was primarily due to better gross margin, which was partially offset by higher OPEX. Higher-than-expected R&D and G&A expenses essentially drove higher OPEX. Higher R&D was attributed to investments on VoIP public safety technology, wireless location based service technology, and continuing improvement of the company's messaging and secure Satcom deliverables. Higher G&A expenses resulted from nonrecurring charges associated with vacating its Tampa facility prior to the end of its lease to relocate into a larger facility to accommodate the sharp increase in government system design and assembly business. Expenses were also impacted by higher non-exec variable comp. EBITDA margin was 20.9% versus our estimate of 17.1% and 15.8% last quarter. EBITDA margins benefited from higher gross margin.

Balance Sheet and Cash Flow: Total cash, investments, and notes came in at \$19.1 million or \$0.43 per share. This represents a \$2.5 million increase from 16.8 million or \$0.38 per share in Q4, after reducing (without penalty) \$4.6 million of term debt and capital lease balances. Cash and investments benefited from \$8.4 million in EBITDA and \$0.1 million from exercising of stock options. This was used for capex of \$0.6 million, about \$0.5 million in working capital, and \$0.3 million of interest expense.

Backlog: While total backlog decreased 3% sequentially from \$232 million to \$225 million, Q1 marks the third highest level in the company's history and is up 151% YoY from \$84 million. 12-month backlog was generally lower at \$78 million compared to \$85 million last quarter. We expect backlog to modestly trend up in the near term as management indicated that the pipeline remains strong with several new government, messaging and LBS deals expected to contribute. We believe these backlog levels provide solid visibility into long-term growth. We would note that backlog can be lumpy given the nature of renewing large long-term 911 service contracts.

Business Analysis

Government Systems – Growth Visibility Remains Solid Despite Soft Q1 Revenue

Government Systems generated \$6.9 million of revenue in Q1, which was down 35% sequentially, but up 8 % YoY. This was well below our estimate of \$11.5 million. Segment gross margin was 26%, which is up from 23% in Q4 and 15% in 1Q07. This was well above our estimate of 15%.

While the lower revenue was disappointing, the higher gross margin enabled TCS to exceed our gross profit estimate of \$1.7 million by \$100K. Management indicated that some Government Systems revenue was pushed into Q2 due to the company's facility relocation in Tampa and some slowdown from the government side. We are not overly concerned given that revenue from this segment tends to be choppy. Furthermore, given the low gross margin on this segment, it has a modest impact on the bottom line. Lastly, with strong backlog growth in this segment over the last year and the multiple master contracts that TCS is involved in, which total in the billion, we believe visibility into growth for the next couple of years are good. On the gross margin side, management indicated that it is seeing higher margin follow-on orders and other new contracts at higher margins. Management highlighted several products and contract wins in the quarter including the recently won \$15.8 million contract that should be mostly recognized in 2008. We were most encouraged by the company's win with the Department of Homeland Security (DHS). The company has built a relationship with the CIO of DHS and indicated it has already done deals with other related agencies such as FEMA, the Coast Guard, and Secret Services. The company also highlighted wins with the U.S. Army, the Marine Corp., and a subcontract with competitor Datapath.

Going forward, management expects YoY growth for the remainder of the year to be better than the 8% in Q1. While we are still modeling YoY growth, we are keeping our growth assumptions more moderate given the choppiness of revenue from this segment. Management also indicated that margin should remain in the low 20% range, which we find encouraging.

Government Services – Revenue and Margins Both Improve

Government Services generated \$7.3 million of revenue in Q1, which was up 4% sequentially and 1% YoY. This was in line with our estimate of \$7.4 million. Segment gross margin was ~21%, which is essentially flat from the Q4 level, but down from 22% in 1Q07. This was slightly above our estimate of 20%.

Government Services includes logistics work to support government SwiftLink systems, professional services, satellite bandwidth services, and maintenance revenue. Thus, as Government Systems revenue grows, we expect Government Services revenue to rise in the following quarters. In addition, as revenue grows in this segment, management indicated that it can generate some scale and thus improve margins. In addition, management indicated it is getting involved with more consulting services, which is part of its Homeland Security contract.

Going forward, we expect this segment to delivery steady growth and believe margins have the potential to improve ahead of our expectations.

Commercial Systems –Text Messaging Drives a Robust Quarter

Commercial Systems generated \$10.7 million of revenue in Q1, which is up an impressive 167% sequentially and 57% YoY. This was well above our estimate of \$9.0 million. Segment gross margin was 81%, which is up from 69% in Q4, and 79% in 1Q07. This was above our estimate of 77%.

Commercial Systems is typically the smallest segment (though larger than Government Services in this quarter), but has the most profound impact on profitability given the high margins. Thus, given the strong revenue and margins, it is not surprising to see TCS' solid profitability overall. We believe the company continues to benefit from robust SMS growth in North America with customers such as Verizon Wireless, Alltel, and 30 other carriers. While CTIA indicated that text messaging grew 137% from 158 billion messages in 2006 to 363 billion messages in 2007, TCS' largest customer (Verizon Wireless) recently indicated 160% YoY growth. Management indicated the company delivered 25% of the 363 billion messages in 2007 and expects this market share to improve with two competitive displacement wins. We also believe this segment will benefit from the recent move by Verizon to raise its pay-per-use text messaging rate while introducing all-you-can eat messaging plans. More precisely, the increase of the pay-per-use text messaging rate should help Verizon to migrate casual SMS users towards messaging bundles, which should translate into higher messaging usage and spending. Ultimately this expected higher messaging volume could benefit TCS' Commercial Systems segment. In the past 12 months, an increasing number of U.S. carriers have migrated towards a flat-rate messaging pricing strategy, and we expect this to continue, which should play in favor of TCS. On the location front, we believe the uptake of LBS such as navigation is driving market awareness. Management announced several deals worldwide ranging from its infrastructure software to applications. Management also highlighted traction of 112 safety services in Europe, which has spurred infrastructure wins for the company in UK, Sweden, and Denmark.

Going forward, management indicated it sees a floor of \$7.5 million in messaging revenue under existing contracts for Q2 and Q3. In addition, management believes a recent carrier win and revenue from LBS should layer on top of this. Given the magnitude of visibility. We are increasing our estimates for Commercial Systems revenue. We also expect margins to remain high in the 60-80% range. With text messaging growth following similar trends as Europe, we agree with management that there is several years of robust growth left.

Commercial Services – Steady, Profitable, and Undervalued 911 Business

Commercial Services generated \$15.5 million of revenue in Q1, which was flat sequentially and up 14% YoY. This was above our estimate of \$14.7 million. Segment gross margin was 49%, which is down from 54% in Q4, but up from 46% in 1Q07. This was slightly better than our estimate of 48%.

Commercial Services is primarily driven by hosted E911 services, but also benefits from hosted LBS applications. For E911 services, management indicated that it has worked to improve margins on the wireless front and is seeing additional traction with MSOs and VoIP providers, which is allowing the company to penetrate the wireline market. Management also highlighted traction in Europe for 112. Management also highlighted newer services such as RAVE911 (Real Time Address Validation Engine 911), which automates some of the complexities of 911 by leveraging TCS's Master Street Address Guide (MSAG) with digital maps. Management indicated it won a Tier 1 MSO for this product. We are also intrigued with the FCC push for an emergency notification system, though it is still too early to talk of revenue. On the hosted application front, we were surprised to hear that in conjunction with Rand McNally and offered through a managed service powered by Qualcomm, it has been selected by 23 regional operators. Typically, this type of service runs \$10 per month and vendors (split between TCS, Rand McNally, and Qualcomm) garner roughly 30-50%. Lastly, we continue to point out the hidden value of this segment. Given that Intrado was sold to West Corp for 3x revenue and that we estimate TCS' wireless 911 annual revenue run rate at \$50 million, we believe this service alone could be valued between \$100-150 million.

Going forward, we expect steady revenue growth and margin expansion from this highly recurring revenue stream from hosted E911, which is unlikely to see any market share shifts between TCS and Intrado.

Management Guidance

Management maintained revenue guidance, but raised EPS and EBITDA guidance to reflect better margins. For 2008, management maintained revenue guidance of \$165-175 million. Our previous revenue estimate of \$171 million is at the mid range of guidance, which matches the previous consensus estimate. Government and Commercial Services margins are expected to improve in 2008, which should benefit EPS. In addition, a larger contribution from high-margin Commercial Systems revenue will also help margins. Thus, management increased its EBITDA guidance to \$20-23 million or \$0.45-0.52 per share from \$17-20 million or \$0.38-0.45 per share. Thus our previous estimate of \$20.4 million or \$0.45 per share, which was at the high end of previous guidance, is now at the low end of new guidance. Consensus estimate for EBITDA is \$0.37, thus we expect consensus estimates to materially rise. GAAP EPS is expected to be \$0.13-0.20. This is inline with our previous estimate of \$0.18.

WMS Estimate Revisions

We are lowering our revenue estimate for 2008 and 2009 to take a more conservative view on the low margin Government Systems segment. However, given solid contribution from high-margin messaging software we are increasing our EPS and EBITDA per share estimates. Lastly, with significant demand in text messaging software, we believe there can be some positive surprises to the bottom line in 2008. We are conservatively leaving our 2009 EBITDA estimate unchanged until we have more clarity on 2009 growth opportunities.

For Q1, we are increasing our EBITDA per share estimate to \$0.08 from \$0.03 and increasing our revenue estimate to \$40.1 million from \$39.0 million. We are decreasing our GAAP EPS estimate to \$0.00 from \$0.09.

For 2008, we are increasing our EBITDA per share estimate to \$0.48 from \$0.45, but we are decreasing our revenue estimate to \$166 million from \$171 million. We are maintaining our GAAP EPS estimate of \$0.18.

For 2009, we are maintaining our EBITDA per share estimate of \$0.56, but we are decreasing our revenue estimate to \$187 million from \$194 million. We are decreasing our GAAP EPS estimate slightly to \$0.30 from \$0.31.

Valuation

We are maintaining our BUY rating and increasing our price target to \$6 from \$5.50. Our price target is derived from our DCF analysis (Figure 1) and represents a 12x multiple on our 2009 pro forma EPS estimate of \$0.45. This represents a substantial discount to the company's projected long-term EPS growth rate of 22%. We believe there is upside to our target if management can demonstrate execution on a consistent basis.

Figure 1: DCF Analysis Summary

	Terminal Growth				
	1%	2%	3%	4%	5%
10.0%	\$8.88	\$9.60	\$10.54	\$11.79	\$13.53
12.5%	\$6.94	\$7.32	\$7.79	\$8.37	\$9.10
15.0%	\$5.70	\$5.93	\$6.20	\$6.51	\$6.89
17.5%	\$4.85	\$5.00	\$5.16	\$5.35	\$5.57
20.0%	\$4.23	\$4.33	\$4.44	\$4.56	\$4.70

Source: Company Reports, Wedbush Morgan Securities

Risks

Risks to attainment of our share price target include timing of systems sales, more significant competition in new growth markets, management execution, customer concentration, and limited balance sheet flexibility.

TeleCommunications Systems Revenue Model
(in 000's, except per share data and ratios)

	2007A				2008E				2009E			
	Mar-07 Q1:07A	Jun-07 Q2:07A	Sep-07 Q3:07E	Dec-07 Q4:07A	Mar-08 Q1:08A	Jun-08 Q2:08E	Sep-08 Q3:08E	Dec-08 Q4:08E	Mar-09 Q1:09E	Jun-09 Q2:09E	Sep-09 Q3:09E	Dec-09 Q4:09E
Revenue Analysis												
Services - Commercial Apps	13,641	14,665	15,014	15,472	15,500	15,810	16,126	16,449	16,778	17,113	17,456	17,805
Services - Government	7,244	7,953	7,035	7,037	7,300	7,665	8,048	8,451	8,620	8,792	8,968	9,147
Services Total	20,885	22,618	22,049	22,509	22,800	23,475	24,174	24,899	25,397	25,905	26,423	26,952
Systems - Commercial Apps	6,810	1,291	4,418	4,001	10,700	4,548	5,002	5,252	5,384	5,518	5,656	5,798
Systems - Government	6,424	11,427	11,168	10,568	6,913	12,098	12,703	13,338	14,005	14,705	15,440	16,212
Systems Total	13,234	12,718	15,586	14,569	17,613	16,645	17,705	18,590	19,388	20,223	21,096	22,010
Total Revenues	34,119	35,336	37,635	37,078	40,413	40,120	41,879	43,490	44,786	46,128	47,520	48,962
Cost of Revenue												
Services - Commercial Apps	7,323	7,517	7,434	7,073	7,900	8,063	8,063	8,060	8,221	8,385	8,553	8,724
Services - Government	5,625	6,133	5,455	5,601	5,800	6,132	6,358	6,592	6,723	6,858	6,995	7,135
Services Total	12,948	13,650	12,889	12,674	13,700	14,195	14,421	14,651	14,944	15,243	15,548	15,859
Systems - Commercial Apps	1,442	1,207	1,141	1,233	2,036	1,774	1,751	1,576	1,561	1,545	1,527	1,507
Systems - Government	5,434	9,798	9,467	8,184	5,113	9,920	10,353	10,804	11,204	11,690	12,198	12,727
Systems Total	6,876	11,005	10,608	9,417	7,149	11,694	12,103	12,379	12,765	13,236	13,725	14,234
Total Cost of Revenues	19,824	24,655	23,497	22,091	20,849	25,889	26,525	27,031	27,709	28,479	29,273	30,093
Segment Gross Profit												
Services - Commercial Apps	6,318	7,148	7,580	8,399	7,600	7,747	8,063	8,389	8,557	8,728	8,902	9,080
Services - Government	1,619	1,820	1,580	1,436	1,500	1,533	1,690	1,859	1,896	1,934	1,973	2,012
Services Total	7,937	8,968	9,160	9,835	9,100	9,280	10,660	11,018	10,453	10,662	10,660	11,018
Systems - Commercial Apps	5,368	84	3,277	2,768	8,664	2,774	3,251	3,677	3,822	3,973	4,129	4,290
Systems - Government	990	1,629	1,701	2,384	1,800	2,178	2,350	2,534	2,801	3,015	3,242	3,486
Systems Total	6,358	1,713	4,978	5,152	10,464	4,952	6,849	4,770	6,623	6,988	6,849	4,770
Total Gross Profit	14,295	10,681	14,138	14,987	19,564	14,231	17,509	15,788	17,076	17,650	17,509	15,788
Segment Gross Margins												
Services - Commercial Apps	46.3%	48.7%	50.5%	54.3%	49.0%	49.0%	50.0%	51.0%	51.0%	51.0%	51.0%	51.0%
Services - Government	22.3%	22.9%	22.5%	20.4%	20.5%	20.0%	21.0%	22.0%	22.0%	22.0%	22.0%	22.0%
Services Total	38.0%	39.6%	41.5%	43.7%	39.9%	39.5%	40.3%	41.2%	41.2%	41.2%	41.2%	41.2%
Systems - Commercial Apps	78.8%	6.5%	74.2%	69.2%	81.0%	61.0%	65.0%	70.0%	71.0%	72.0%	73.0%	74.0%
Systems - Government	15.4%	14.3%	15.2%	22.6%	26.0%	18.0%	18.5%	19.0%	20.0%	20.5%	21.0%	21.5%
Systems Total	48.0%	13.5%	31.9%	35.4%	59.4%	29.7%	31.6%	33.4%	34.2%	34.6%	34.9%	35.3%
Total Gross Margin	41.9%	30.2%	37.6%	40.4%	48.4%	35.5%	36.7%	37.8%	38.1%	38.3%	38.4%	38.5%
Segment Mix												
Services - Commercial Apps	40.0%	41.5%	39.9%	41.7%	38.4%	39.4%	38.5%	37.8%	37.5%	37.1%	36.7%	36.4%
Services - Government	21.2%	22.5%	18.7%	19.0%	18.1%	19.1%	19.2%	19.4%	19.2%	19.1%	18.9%	18.7%
Services Total	61.2%	64.0%	58.6%	60.7%	56.4%	58.5%	57.7%	57.3%	56.7%	56.2%	55.6%	55.0%
Systems - Commercial Apps	20.0%	3.7%	11.7%	10.8%	26.5%	11.3%	11.9%	12.1%	12.0%	12.0%	11.9%	11.8%
Systems - Government	18.8%	32.3%	29.7%	28.5%	17.1%	30.2%	30.3%	30.7%	31.3%	31.9%	32.5%	33.1%
Systems Total	38.8%	36.0%	41.4%	39.3%	43.6%	41.5%	42.3%	42.7%	43.3%	43.8%	44.4%	45.0%
Total Revenue	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
QoQ Revenue Growth												
Services - Commercial Apps	-8.5%	7.5%	2.4%	3.1%	0.2%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
Services - Government	-2.3%	9.8%	-11.5%	0.0%	3.7%	5.0%	5.0%	5.0%	2.0%	2.0%	2.0%	2.0%
Services Total	-6.4%	8.3%	-2.5%	2.1%	1.3%	3.0%	3.0%	3.0%	2.0%	2.0%	2.0%	2.0%
Systems - Commercial Apps	50.7%	-81.0%	242.2%	-9.4%	167.4%	-57.5%	10.0%	5.0%	2.5%	2.5%	2.5%	2.5%
Systems - Government	75.6%	77.9%	-2.3%	-5.4%	-34.6%	75.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Systems Total	61.9%	-3.9%	22.6%	-6.5%	20.9%	-5.5%	6.4%	5.0%	4.3%	4.3%	4.3%	4.3%
Total Revenue	11.9%	3.6%	6.5%	-1.5%	9.0%	-0.7%	4.4%	3.8%	3.0%	3.0%	3.0%	3.0%
YoY Revenue Growth												
Services - Commercial Apps	-10.0%	-5.6%	6.1%	3.8%	13.6%	7.8%	7.4%	6.3%	8.2%	8.2%	8.2%	8.2%
Services - Government	6.6%	11.9%	-3.9%	-5.1%	0.8%	-3.6%	14.4%	20.1%	18.1%	14.7%	11.4%	8.2%
Services Total	-4.8%	-0.1%	2.7%	0.8%	9.2%	3.8%	9.6%	10.6%	11.4%	10.4%	9.3%	8.2%
Systems - Commercial Apps	96.5%	-65.7%	-19.2%	-11.4%	57.1%	252.2%	13.2%	31.3%	-49.7%	21.3%	13.1%	10.4%
Systems - Government	2.4%	106.4%	188.9%	188.9%	7.6%	5.9%	13.7%	26.2%	102.6%	21.6%	21.6%	21.6%
Systems Total	35.8%	36.7%	66.9%	78.2%	33.1%	30.9%	13.6%	27.6%	10.1%	21.5%	19.2%	18.4%
Total Revenue	7.7%	10.6%	22.2%	21.6%	18.4%	13.5%	11.3%	17.3%	10.8%	15.0%	13.5%	12.6%
Backlog Metrics												
Total Backlog	89,600	159,000	253,000	232,100	225,000							
QoQ Total Backlog Growth	7.0%	77.5%	59.1%	-8.3%	-3.1%							
YoY Total Backlog Growth	-22.3%	53.2%	167.4%	177.3%	151.1%							
Commercial	39,200	96,800	93,900	130,500	124,800							
Government (Total)	50,400	62,200	159,100	101,600	100,200							
12-Month Backlog	57,800	71,300	88,000	84,600	78,000							
QoQ 12-Month Backlog Growth	12.7%	23.4%	23.4%	-3.9%	-7.8%							
YoY 12-Month Backlog Growth	-5.9%	24.2%	46.1%	64.9%	34.9%							
12-Month Revenue	150,462	155,246	159,491	165,902	170,275							
Revenue Coverage	38.4%	45.9%	55.2%	51.0%	45.8%							
Bookings	40,019	104,736	131,635	16,178	33,313							
QoQ Booking Growth	104.4%	161.7%	25.7%	-87.7%	105.9%							
YoY Booking Growth	59.0%	414.3%	507.3%	-17.3%	-16.8%							
Book/Bill	1.2x	3.0x	3.5x	0.4x	0.8x							

Source: TCS and Wedbush Morgan Securities

TeleCommunications Systems Quarterly Income Statement

(in 000's, except per share data and ratios)

	2007A				2008E				2009E			
	Mar-07	Jun-07	Sep-07	Dec-07	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09
	Q1:07A	Q2:07A	Q3:07A	Q4:07A	Q1:08A	Q2:08E	Q3:08E	Q4:08E	Q1:09E	Q2:09E	Q3:09E	Q4:09E
Total Revenues	34,119	35,336	37,635	37,078	40,413	40,120	41,879	43,490	44,786	46,128	47,520	48,962
Cost of Revenue	19,824	24,655	23,497	22,091	20,849	25,889	26,525	27,031	27,709	28,479	29,273	30,093
Gross Profit	14,295	10,681	14,138	14,987	19,564	14,231	15,355	16,459	17,076	17,650	18,247	18,869
Research and development	3,105	3,266	3,329	3,372	4,088	4,012	3,979	4,023	4,101	4,182	4,265	4,350
Sales and marketing	3,163	3,157	2,729	2,868	3,099	3,210	3,317	3,410	3,476	3,545	3,615	3,688
General and administrative	4,652	5,499	4,656	4,526	5,318	5,115	5,130	5,219	5,240	5,262	5,285	5,310
Total Operating Expenses	10,920	11,922	10,714	10,766	12,505	12,337	12,426	12,651	12,818	12,989	13,166	13,348
Add backs included in COS and OPEX												
Noncash stock compensation expense	988	1,133	1,000	1,212	975	1,100	1,100	1,100	1,100	1,100	1,100	1,100
Amortization of software development costs	344	372	396	409	409	380	354	333	308	288	271	256
EBITDA	4,707	264	4,820	5,842	8,443	3,374	4,383	5,240	5,667	6,049	6,452	6,877
Depreciation/amortization of fixed assets	1,668	1,556	1,497	1,479	1,490	1,718	1,581	1,469	1,380	1,408	1,439	1,472
Noncash stock compensation expense	988	1,133	1,000	1,212	975	1,100	1,100	1,100	1,100	1,100	1,100	1,100
Amortization of software development costs	344	372	396	409	409	380	354	333	308	288	271	256
Amortization of other intangibles	37	37	37	37	37	37	37	37	37	37	37	37
Operating Profit (EBIT)	1,670	(2,834)	1,890	2,705	5,532	139	1,311	2,301	2,842	3,216	3,605	4,011
Cash interest and other, net	(507)	(444)	(128)	(165)	(742)	3	(1)	36	57	83	103	125
Noncash financing cost	(396)	(257)	(23)	(42)	(124)	(124)	(124)	(124)	(124)	(124)	(124)	(124)
Income before income taxes	767	(3,535)	1,739	2,498	4,666	19	1,186	2,213	2,776	3,175	3,584	4,013
Income taxes	-	-	-	-	48	-	-	-	-	-	-	-
GAAP Net Income	767	(5,993)	1,716	2,498	4,618	19	1,186	2,213	2,776	3,175	3,584	4,013
Pro forma Net Income	3,286	(1,163)	3,760	4,551	7,259	2,113	3,122	3,979	4,406	4,788	5,191	5,616
Earnings per share												
Continuing Ops GAAP EPS	\$ 0.02	\$ (0.15)	\$ 0.04	\$ 0.06	\$ 0.11	\$ 0.00	\$ 0.03	\$ 0.05	\$ 0.06	\$ 0.07	\$ 0.08	\$ 0.09
Pro forma EPS	\$ 0.08	\$ (0.03)	\$ 0.08	\$ 0.10	\$ 0.17	\$ 0.05	\$ 0.07	\$ 0.09	\$ 0.10	\$ 0.11	\$ 0.12	\$ 0.12
EBITDA EPS	\$ 0.11	\$ 0.01	\$ 0.11	\$ 0.13	\$ 0.19	\$ 0.08	\$ 0.10	\$ 0.12	\$ 0.13	\$ 0.14	\$ 0.14	\$ 0.15
Diluted Shares Outstanding	42,471	45,220	44,792	44,305	43,778	43,953	44,128	44,303	44,503	44,703	44,903	45,103
EBITDA												
Depreciation & Amortization	3,037	3,098	2,930	3,137	2,911	3,235	3,072	2,939	2,825	2,833	2,846	2,866
EBITDA	4,707	264	4,820	5,842	8,443	3,374	4,383	5,240	5,667	6,049	6,452	6,877
EBITDA Margin	13.8%	0.7%	12.8%	15.8%	20.9%	8.4%	10.5%	12.0%	12.7%	13.1%	13.6%	14.0%
Margin Analysis												
Gross Margin	41.9%	30.2%	37.6%	40.4%	48.4%	35.5%	36.7%	37.8%	38.1%	38.3%	38.4%	38.5%
Research and development	9.1%	9.2%	8.8%	9.1%	10.1%	10.0%	9.5%	9.3%	9.2%	9.1%	9.0%	8.9%
Sales and marketing	9.3%	8.9%	7.3%	7.7%	7.7%	8.0%	7.9%	7.8%	7.8%	7.7%	7.6%	7.5%
General and administrative	13.6%	15.6%	12.4%	12.2%	13.2%	12.8%	12.3%	12.0%	11.7%	11.4%	11.1%	10.8%
Operating Margin	4.9%	-8.0%	5.0%	7.3%	13.7%	0.3%	3.1%	5.3%	6.3%	7.0%	7.6%	8.2%
Pre Tax Margin	2.2%	-10.0%	4.6%	6.7%	11.5%	0.0%	2.8%	5.1%	6.2%	6.9%	7.5%	8.2%
Tax Rate	0.0%	0.0%	0.0%	0.0%	1.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net Margin	1.9%	-17.4%	4.7%	6.6%	11.4%	0.0%	2.8%	5.1%	6.2%	6.9%	7.5%	8.2%
Year/Year Growth												
Revenues	7.7%	10.6%	22.2%	21.6%	18.4%	13.5%	11.3%	17.3%	10.8%	15.0%	13.5%	12.6%
Gross Profit	5.4%	-25.0%	4.2%	14.1%	36.9%	33.2%	8.6%	9.8%	-12.7%	24.0%	18.8%	14.6%
Research and development	5.9%	-6.1%	11.2%	5.9%	31.7%	22.8%	19.5%	19.3%	0.3%	4.2%	7.2%	8.1%
Sales and marketing	3.8%	0.5%	-2.1%	4.7%	-2.0%	1.7%	21.5%	18.9%	12.2%	10.4%	9.0%	8.1%
General and administrative	10.1%	32.5%	8.9%	5.1%	14.3%	-7.0%	10.2%	15.3%	-1.5%	2.9%	3.0%	1.7%
Depreciation and amortization	-15.0%	0.2%	-2.4%	11.1%	-4.1%	4.4%	4.8%	-6.3%	-3.0%	-12.4%	-7.3%	-2.5%
Operating Income	91.3%	-279.3%	19.2%	143.4%	231.3%	-104.9%	-30.6%	-14.9%	-48.6%	2212.1%	175.0%	74.3%
Pre Tax Profit	124.3%	-565.6%	128.5%	2146.4%	508.3%	-100.5%	-31.8%	-11.4%	-40.5%	17031.1%	202.1%	81.3%
Net Profit	-137.6%	294.8%	-112.9%	-152.1%	618.2%	-100.3%	-33.0%	-9.2%	-39.9%	17031.1%	202.1%	81.3%
Quarter/Quarter Growth												
Revenues	11.9%	3.6%	6.5%	-1.5%	9.0%	-0.7%	4.4%	3.8%	3.0%	3.0%	3.0%	3.0%
Gross profit	8.8%	-25.3%	32.4%	6.0%	30.5%	-27.3%	7.9%	7.2%	3.8%	3.4%	3.4%	3.4%
Research and development	-2.5%	5.2%	1.9%	1.3%	21.2%	-1.9%	-0.8%	1.1%	2.0%	2.0%	2.0%	2.0%
Sales and marketing	15.5%	-0.2%	-13.6%	5.1%	8.1%	3.6%	3.3%	2.8%	2.0%	2.0%	2.0%	2.0%
General and administrative	8.0%	18.2%	-15.3%	-2.8%	17.5%	-3.8%	0.3%	1.7%	0.4%	0.4%	0.4%	0.5%
Depreciation and Amortization	7.5%	2.0%	-5.4%	7.1%	-7.2%	11.1%	-5.0%	-4.3%	-3.9%	0.3%	0.5%	0.7%
Operating Income	50.3%	-269.7%	-166.7%	43.1%	104.5%	-97.5%	842.6%	75.5%	23.5%	13.2%	12.1%	11.3%
Pre Tax Profit	589.7%	-560.9%	-149.2%	43.6%	86.8%	-99.6%	6301.5%	86.6%	25.4%	14.4%	12.9%	12.0%
Net Profit	-113.7%	-1054.6%	-128.8%	37.7%	89.5%	-99.6%	6301.5%	86.6%	25.4%	14.4%	12.9%	12.0%

Source: Company reports and Wedbush Morgan Securities estimates.

TeleCommunications Systems Annual Income Statement

(in 000's, except per share data and ratios)

	2005A	2006A	2007A	2008E	2009E
Total Revenues	102,153	124,935	144,168	165,902	187,396
Cost of Revenue	56,949	70,423	90,067	100,293	115,554
Gross Profit	45,204	54,512	54,101	65,609	71,841
Research and development	13,863	12,586	13,072	16,101	16,899
Sales and marketing	10,535	11,714	11,917	13,035	14,324
General and administrative	15,044	16,959	19,333	20,782	21,097
Total Operating Expenses	39,442	41,259	44,322	49,919	52,320
Add backs included in COS and OPEX				47,483	50,851
Noncash stock compensation expense	720	3,117	4,333	4,275	4,400
Amortization of software development costs	786	1,272	1,521	1,475	1,123
Pro Forma Operating Income	7,268	17,643	15,633	21,440	25,044
Depreciation/amortization of fixed assets	8,625	7,956	6,200	6,259	5,698
Noncash stock compensation expense	720	3,117	4,333	4,275	4,400
Amortization of software development costs	786	1,272	1,521	1,475	1,123
Amortization of other intangibles	177	147	148	148	148
Operating Profit (EBIT)	(3,040)	5,151	3,431	9,283	13,675
Interest expense	(532)	(3,321)	(1,776)	(1,174)	(961)
Other income (loss), net	(244)	143	508	(25)	833
Income before income taxes	(4,316)	1,974	1,469	8,084	13,547
Income taxes	-	-	-	48	-
Loss from Enterprise assets held for sale	(7,151)	(23,670)	(276)	-	-
W/O unamortized debt discount and issuance			(2,481)		
Continuing Operations Net Income	(4,316)	1,974	1,469	8,036	13,547
Pro forma Net Income	5,901	12,933	10,434	16,473	20,000
Net Income	(11,467)	(21,696)	(1,288)	8,036	13,547
Earnings per share					
Continuing Ops GAAP EPS	(\$0.11)	\$0.05	\$0.03	\$0.18	\$0.30
Pro Forma EPS	\$0.15	\$0.32	\$0.24	\$0.37	\$0.45
EBITDA EPS	\$0.19	\$0.44	\$0.35	\$0.48	\$0.56
Enterprise segment	(\$0.18)	(\$0.60)	(\$0.01)	\$0.00	\$0.00
Basic Shares Outstanding	39,060	39,688	41,366	42,873	43,673
Diluted Shares Outstanding	39,060	39,688	44,305	44,303	45,103
EBITDA					
Depreciation & Amortization	10,308	12,492	12,202	12,157	11,369
EBITDA	7,268	17,643	15,633	21,440	25,044
EBITDA Margin	7.1%	14.1%	10.8%	12.9%	13.4%
Margin Analysis					
Gross Margin	44.3%	43.6%	37.5%	39.5%	38.3%
Research and development	13.6%	10.1%	9.1%	9.7%	9.0%
Sales and marketing	10.3%	9.4%	8.3%	7.9%	7.6%
General and administrative	14.7%	13.6%	13.4%	12.5%	11.3%
Operating Margin	-3.0%	4.1%	2.4%	5.6%	7.3%
Pre Tax Margin	-4.2%	1.6%	1.0%	4.9%	7.2%
Tax Rate	0.0%	0.0%	0.0%	0.0%	0.0%
Net Margin	-11.2%	-17.4%	-0.9%	4.8%	7.2%
Year/Year Growth					
Revenues		22.3%	15.4%	15.1%	13.0%
Gross Profit		20.6%	-0.8%	21.3%	9.5%
Research and development		-9.2%	3.9%	23.2%	5.0%
Sales and marketing		11.2%	1.7%	9.4%	9.9%
General and administrative		12.7%	14.0%	7.5%	1.5%
Depreciation and amortization		21.2%	-2.3%	-0.4%	-6.5%
Operating Income		-269.4%	-33.4%	170.6%	47.3%
Pre Tax Profit		-145.7%	-25.6%	450.3%	67.6%
Net Profit		89.2%	-94.1%	-723.9%	68.6%

Source: Company reports and Wedbush Morgan Securities estimates.

TeleCommunications Systems Annual Balance Sheet

(in 000's, except per share data and ratios)

	2005A	2006A	2007A	2008E	2009E
Assets:					
Cash and cash equivalents	9,320	10,358	15,955	31,798	46,834
Accounts receivable, net	20,886	21,544	20,424	26,577	29,921
Unbilled receivables	6,361	7,636	15,229	14,497	16,321
Inventory	3,197	5,293	5,373	6,487	7,222
Other current assets	2,970	2,818	4,688	5,781	5,781
Current assets of discontinued operations	22,891	13,596	-	-	-
Total Current Assets	65,625	61,245	62,542	85,788	106,727
Property and equipment, net	16,323	12,853	11,209	9,197	10,057
Software development costs, net	3,825	4,402	4,406	3,830	3,722
Intangible assets, net	1,004	856	709	561	413
Goodwill	1,813	1,813	1,813	1,813	1,813
Other assets	1,982	2,526	1,445	1,740	1,958
Total Assets	90,572	83,695	82,124	102,928	124,691
Liabilities:					
Accts payable and accrued exp.	14,146	16,084	17,374	21,024	23,406
Deferred revenue	4,123	3,485	4,685	7,835	8,821
Cur. portion of debt, cap leases and LT debt	13,181	4,900	5,444	3,836	3,836
Current liabilities of discontinued operations	6,719	11,400	-	-	-
Total Current Liabilities	38,169	35,869	27,503	32,695	36,063
Capital leases and LT debt, less current	3,341	12,721	10,657	8,976	8,976
Total Liabilities	41,510	48,590	38,160	41,671	45,039
Common stock & addl paid-in capital	210,398	218,137	227,987	235,904	240,752
Accumulated deficit	(161,336)	(183,032)	(184,023)	(174,647)	(161,100)
Total Stockholders' Equity (deficit)	49,062	35,105	43,964	61,257	79,652
Total Liabilities and SE (deficit)	90,572	83,695	82,124	102,928	124,691

Return Ratios

Return on Sales	-11.2%	-17.4%	-0.9%	4.8%	7.2%
Total Asset Turnover	1.13	1.49	1.76	1.61	1.50
Financial Leverage	1.85	2.38	1.87	1.68	1.57
Retention Ratio	100%	100%	100%	100%	100%
Return on Equity	-23.4%	-61.8%	-2.9%	13.1%	17.0%
Return on Assets	-12.7%	-25.9%	-1.6%	7.8%	10.9%
Sustainable Growth	-23.4%	-61.8%	-2.9%	13.1%	17.0%

Activity Ratios

Receivables Turnover	4.9	5.8	7.1	6.2	6.3
Days Receivable	73.6	62.1	51.0	57.7	57.5
Unbilled Receivables Turnover	16.1	16.4	9.5	11.4	11.5
Unbilled Days Receivable	22.4	22.0	38.0	31.5	31.4
Payables Turnover	4.0	4.4	5.2	4.8	4.9
Days Payable	89.4	82.2	69.4	75.5	72.9

Liquidity/Leverage

Current Ratio	1.7	1.7	2.3	2.6	3.0
Quick Ratio	0.2	0.3	0.6	1.0	1.3
Debt to Equity	0.3	0.5	0.4	0.2	0.2
Debt to Capital	0.3	0.3	0.3	0.2	0.1
Net Working Capital	27,456	25,376	35,039	53,093	70,664
ST Debt	13,181	4,900	5,444	3,836	3,836
LT Debt	3,341	12,721	10,657	8,976	8,976
Book Value per Share	\$1.26	\$0.88	\$0.99	\$1.38	\$1.77
Tangible Book Value per Share	\$1.18	\$0.82	\$0.94	\$1.33	\$1.72
Cash & Investments per Share, Net	\$0.24	\$0.26	\$0.36	\$0.72	\$1.04

Source: Company reports, Wedbush Morgan Securities estimates.

Public companies mentioned in this report (as of close 5/1/08)

Company	Ticker	Rating	Current Price	Price Target
QUALCOMM	QCOM	N/R	\$44.36	N/A
VERIZON COMMUNICATIONS	VZ	N/R	\$37.04	N/A

ANALYST CERTIFICATION

I, Scott P. Sutherland, CFA, certify that the views expressed in this report accurately reflect my personal opinion and that I have not and will not, directly or indirectly, receive compensation or other payments in connection with my specific recommendations or views contained in this report.

IMPORTANT DISCLOSURES

INVESTMENT RATINGS

STRONG BUY – The stock is expected to return at least 20% over the next 6-12 months.

BUY – The stock is expected to return at least 15% over the next 6-12 months.

HOLD – The stock is expected to return between -15% and +15% over the next 6-12 months.

SELL – The stock is expected to decline by at least 15% over the next 6-12 months.

DISTRIBUTION OF RATINGS (as of March 31, 2008)

BUY – 48% (2% of this rating category were investment banking clients within the last 12 months).

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