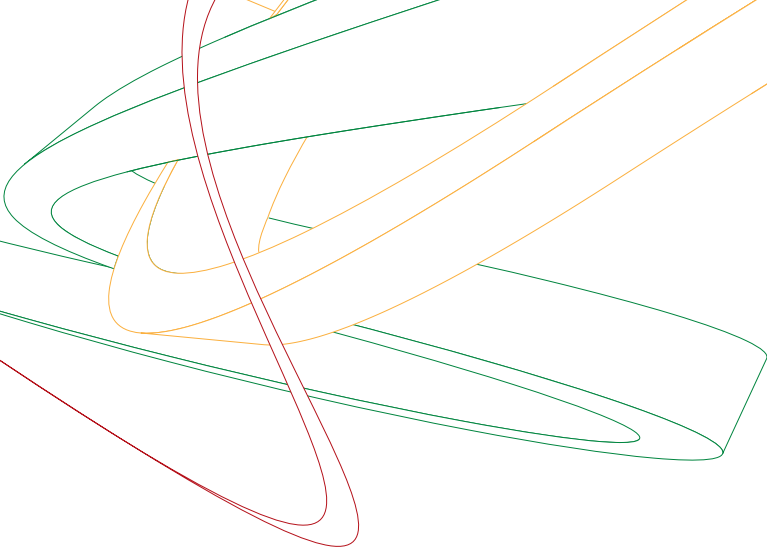# radware

Smart Network. **Smart** Business.

2006 Letter to Shareholders

To Our Valued Shareholders:

When we look back on 2006, it was a period in the company's history that is characterized by the market release of exciting new product innovations, preparation for the launch of its new "business-smart" network vision, the cultivation of key enterprise and carrier customers, the extension of leading technology alliances, and the deepening of analyst relationships – all of which occurred in tandem with a steady and renewed focus on the core operations of our business. We not only recast our company from the inside-out but we also honored our long-held commitment to making our customers' businesses better as we set in motion the precursors for an industry-shifting change for our market space. We would like to take this opportunity to recap the highlights of the past year as this year represents a seminal moment in the company's near decade of continual business growth.
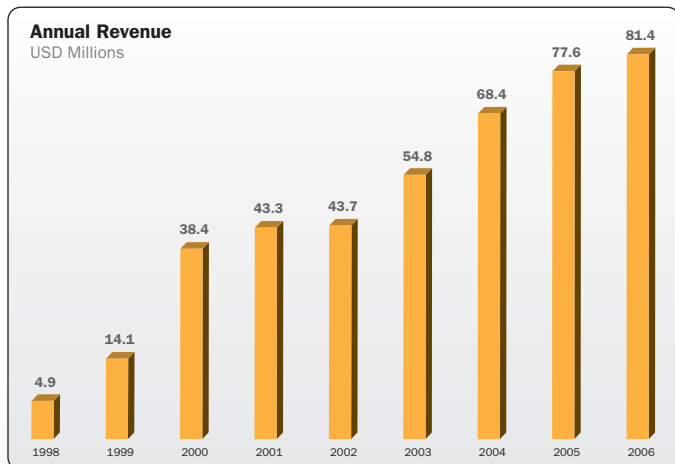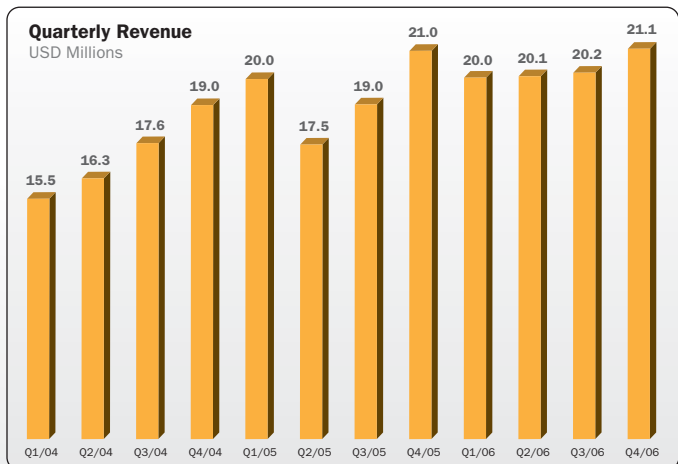
Financial Highlights: Investing in the Future

Our revenues for 2006 amounted to a record of $81.4 million, a total increase of 5% compared to revenues of $77.6 million for 2005. We maintained an industry-high gross profit margin of 81% in 2006, and continued our trend of quarter-over-quarter revenue increases from the second quarter throughout the remainder of the year, resulting in our highest quarterly revenues to-date with $21.1 million in the fourth quarter. Revenues across our three primary geographies (Americas, EMEA, and APAC) had a healthy and balanced distribution.

Net income excluding the effects of stock-based compensation expense for 2006 was $3.2 million or $0.16 per diluted share, compared with net income of $9.3 million or $0.47 per diluted share in 2005. Net loss on a GAAP basis for 2006 was $1.3 million or $0.07 per diluted share.

During 2006 we had an operating loss of $8.3 million, compared to an operating profit of $4.4 million in 2005. We incurred this loss as a result of increased expenses associated with our efforts to significantly increase our revenues, additional investments made in R&D resource allocations, and the first-time recording of stock-based compensation expenses, which was coupled with moderate revenue growth for the year as we restructured our Americas sales force in the latter half of the year. Despite the loss we benefited with the posting of financial income in the amount of $7.4 million and ended the year with a positive operational cash flow of $7.3 million, leading us to a total of $164.1 million invested in cash, bank deposits and marketable securities.

We feel it is important to continue to invest as we have done in the past in our R&D initiatives, sales and marketing efforts, and non-organic growth opportunities. From 2005 to 2006, we increased our R&D investments by 36% and our sales and marketing investments by 25% while we concurrently reactivated a stock repurchase program in September and successfully executed on our progressive acquisition strategy, culminating in the acquisition of Covelight Systems, Inc. in the first half of 2007. In combination, these investments will help fuel our future growth, increase market acceptance of our offerings, and competitively position us for market leadership in the years ahead.

Quarterly Revenue
USD Millions

Quarter	Revenue
Q1/04	15.5
Q2/04	16.3
Q3/04	17.6
Q4/04	19.0
Q1/05	20.0
Q2/05	17.5
Q3/05	19.0
Q4/05	21.0
Q1/06	20.0
Q2/06	20.1
Q3/06	20.2
Q4/06	21.1

Annual Revenue
USD Millions

Year	Revenue
1998	4.9
1999	14.1
2000	38.4
2001	43.3
2002	43.7
2003	54.8
2004	68.4
2005	77.6
2006	81.4

Market Highlights: Our Opportunity and Outlook for Growth

Estimations by IT industry analysts project a year-over-year worldwide CAGR of 7.4% for the application delivery market segment through 2010 and a commensurate growth in the market for network-based IPS solutions, which will result in a nearly equivalent $1.2 billion market opportunity by the same year. Radware, which uniquely straddles both segments through its broad product portfolio, is thus poised to sell into two growth segments that equally address worldwide enterprise and carrier customer bases.

In order to take advantage of the opportunity that lies before us, we have carefully put in place over the past three years, the needed foundation to support our business goals. Every aspect of the business and its value chain – from manufacturing all the way through customer service – has been assessed and subjected to rigorous improvement initiatives. We believe that these operational efficiencies in concert with our commitment to delivering innovations to the marketplace will help foster our objectives.

Some examples of this revitalized foundation include: the implementation of a company-wide Oracle ERP system; the hiring and infusion of new talent in a re-aligned R&D organization; the release of six new product innovations and four industry certifications; the institution of a formalized product realization process; restructuring of our Americas sales organization and rationalization of its reseller base; the roll-out of next generation branding and corporate positioning; and the opening of a new support center in India along with the deployment of an over-arching customer satisfaction initiative for the complete lifecycle management of customer interactions with our company. It is through focused and disciplined execution, and a company culture committed to driving change in the industry, that we will be able to best serve the ongoing needs of our customers, partners, and investors as we establish a sustainable structure for market growth.

Business Highlights: Paving the Way for a New Industry Era

As companies continue to pursue business-oriented IT strategies that shift the primary objectives of the IT organization from keeping their IT infrastructure up and running to advancing and contributing to the business, IT organizations are being pressured to meet SLAs, and enable fast development and deployment of new services for business agility, all at lower cost for improved ROI. To date, these key application networking trends have shaped Radware's approach to developing an integrated application delivery solution for "application-smart" networking that meets the evolving and complex needs of the data center.

At the core of this "application-smart" network approach is our innovative, service-layer APSolute OS architecture, which allowed us in 2005 to offer differentiated and compelling value to our customers in the areas of: global redirection for business continuity/disaster recovery; bandwidth management for data center consolidation; SIP application optimization to meet the growing trend towards VoIP, data, and video convergence; and acceleration and content transformation to support the rapid explosion of web-enabled applications in addition to the requirements of a remote, mobile workforce.

In 2006 we followed up the 2005 launch of our APSolute™ next-generation product family with several "first-to-market" product and feature introductions. We brought to market the industry's fastest Layer 7 performance with our high-end AS5 platform, which provides the power needed to support the demanding application requirements of new web services and XML applications, rich media content services and interactive services such as VoIP, video conferencing, information sharing and collaboration. We unveiled our AppDirector 6000 and DefensePro 6000 models to meet the high-transaction volumes and exacting security assurance needs of large enterprises and carriers. We introduced the first solution in the market (DefensePro 3.0) to provide self-learning, proactive protection against DoS, DDoS and zero-day attacks with an innovative combination of content based, behavioral-based and rate-based protection incorporated from our V-Secure acquisition. As a follow up to our advancements in the security arena, we also set a new price/performance standard in the industry with an expanded DefensePro line-up that offers scaleable throughput without additional hardware investment. And through a partnership with Forum Systems, a best-in-class leader in the XML security services space, announced our intention to deliver the industry's

first integrated application delivery solution for ensuring the fast and secure delivery of XML-based Web services running on service-oriented architectures (SOA).

Emerging data center trends that we believe will drive the requirements of the next approaching industry wave, center on: the migration to real-time data centers that can enable business process optimization; the implementation of service-oriented architectures (SOA) for reusable and flexible computing; the adoption of on-demand computing for efficient resource utilization and consumption-based pricing models; and the push for virtualization solutions that can create dynamic IT infrastructures. In essence, we are witnessing and helping guide the transition from an industry period reliant on technology-centric infrastructure solutions to one marked by the call for strategic, business-centric infrastructure solutions.

Once again, Radware is at the forefront of the next industry transition, leading the way for the "business-smart" era of application networking solutions. Each of the product introductions and feature enhancements released in 2006 led up to the official market launch of our business-smart networking vision in the first half of 2007, which was capped by the acquisition of Covelight Systems for its real-time, business event intelligence Inflight technology. Radware's mission has always been to make its' customers' networks more intelligent so they can extract greater business value from their data transactions, and therefore, their IT infrastructure investments. The addition of Inflight, which dovetails the enhancements to Radware's existing APSolute portfolio, accelerates this strategy and significantly differentiates it amongst other vendors in the application networking market. With the business-smart network, IT organizations are better equipped to align network behavior with business processes and policies as they aim to contribute to the business' revenue growth and regulatory compliance agendas.

Top-tier IT analysts have validated Radware's vision and applaud it as game-shifting in the marketplace, "Radware is taking a unique position and it's the first I've seen of this type of strategy…" and, "…you have what Cisco (SONA) promised" in addition to, "Radware's move will raise the stakes in the ADC market. It will get people thinking about the whole ADC value proposition…Businesses will benefit by enabling new capabilities such as transaction assurance, real time business intelligence and fraud detection." We will leverage this initial success heading into the second half of 2007 as we continue to carry out the various business elements of our strategy.

Summary: The Road Ahead

In summary, we have continued to invest heavily in the realization of our market vision for the "business-smart" network, which we believe will lead the industry going forward. Our customer-driven vision has been met with concrete validation from analyst constituencies and through careful, yet inspired and dedicated execution of our business strategy, we can create a winning formula for the mutual benefit of all of our stakeholders. The road ahead brings with it the prospects for growth, market leadership, and the attainment of our customer's business success. We hope that you will share in our enthusiasm for what lies ahead.

On behalf of the entire Radware organization and board of directors, we would like to thank you for your continued support and commitment to the company's achievement.

Roy Zisapel
President and Chief Executive Officer

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Christopher R. McCleary*, Chairman*

Ordinary Shares
Radware Ltd. Ordinary Shares (Common Stock) trade on the NASDAQ Stock Market (NASDAQ: RDWR) and Tel Aviv Stock Exchange.

Annual Report on Form 20-F
To review the company's Annual Report on Form 20-F, as filed with the U.S. Securities and Exchange Commission, please issue a request at ir@radware.com. The report is also available for download from the investor relations section of the company web site or from the Securities and Exchange Commission's web site at www.sec.gov.

About Radware
Radware (NASDAQ:RDWR), the global leader in integrated application delivery solutions, assures the full availability, maximum performance, and complete security of business-critical applications for more than 5,000 enterprises and carriers worldwide. With APSolute™, Radware's comprehensive and award-winning suite of intelligent front end, access, and security products, companies in every industry can drive business productivity, improve profitability, and reduce IT operating and infrastructure costs by making their networks "business smart". For more information, please visit www.radware.com.