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Ceragon Networks Q2 FY 2023 Earnings Call Script

August 1, 2023

Operator

Welcome to Ceragon Networks Second Quarter 2023 Earnings Conference Call. At this time, all participants are in a listen-only mode. Following management’s prepared remarks, we will host a question-and-answer session.

If you wish to participate and ask a question on today’s call you will need to click on the “raise your hand” icon within the zoom application on your desktop or mobile device.

As a reminder, this call is being recorded. It is now my pleasure to introduce your host, Rob Fink of FNK IR.

Rob Fink

Thank you, operator, and good morning, everyone. Hosting today’s call is Doron Arazi, Ceragon’s Chief Executive Officer and Ronen Stein, Chief Financial Officer.

Before we start, I would like to note that certain statements made on this call, including projected financial information and other results and the company’s future initiatives, future events, business outlook, development efforts and their potential outcome, anticipated progress and plans, results and timelines and other financial and accounting-related matters, constitute “forward-looking statements” within the meaning of the Securities Act of 1933, as amended and the Securities Exchange Act of 1934, as amended, and the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995.

30

31 Ceragon uses forward-looking terminology, such as believes, expects, may, will, should,
32 anticipates, plans or similar expressions to identify forward-looking statements. Such
33 statements reflect only current beliefs, expectations, and assumptions of Ceragon's
34 management, but actual results, performance, or achievements of Ceragon may differ
35 materially, as they are subject to certain risks and uncertainties, which could cause Ceragon's
36 actual results to differ materially from those projected in such forward-looking statements.
37 Such risks and uncertainties include, but are not limited to, those that are described in
38 Ceragon's most recent Annual Report on Form 20-F and as may be supplemented from time to
39 time in Ceragon's other filings with the SEC, including today's earlier filing of the earnings PR, all
40 of which are expressly incorporated herein by reference. Forward-looking statements relate to
41 the date initially made, do not purport to be predictions of future events or results, and there
42 can be no assurance that they will prove to be accurate, and Ceragon undertakes no obligation
43 to update them.

44

45 Ceragon's public filings are available on the Securities and Exchange Commission's website at
46 www.sec.gov, and may also be obtained from Ceragon's website at www.ceragon.com.

47 Also, today's call will include certain non-GAAP numbers. For a reconciliation between GAAP
48 and non-GAAP results, please see the table attached to the press release that was issued earlier
49 today.

50

51 I will now turn the call over to Doron. Please go ahead.

52

53

54 **Doron Arazi**

55

56 Thank you, Rob, and good morning, everyone.

57

58 This was another strong quarter for Ceragon Networks. Demand for our solutions continues to
59 increase, and we have successfully grown our presence in key geographies. For the second
60 quarter in a row, revenues surpassed \$80 million and our book to bill ratio again exceeded one.
61 We were profitable, generated positive free cash flow and expanded our credit facility with
62 existing lenders, further solidifying our liquidity.

63

64 Importantly, the momentum we experienced in Q1 continued in Q2 and to date, we have NOT
65 seen any slowdown in customer spending, or any of the softness or pressures that some
66 technology providers in adjacent areas of our industry have spoken about. Our performance in
67 the first six months of 2023, combined with improving visibility into the third quarter, has given
68 us the confidence to increase our full-year outlook.

69

70 Revenue for the quarter was \$86.2 million, up 22% year over year. Our book to bill ratio was
71 again over 1. In fact, our bookings increased sequentially compared to Q1, with particular
72 strength in India and North America, bolstering our confidence in continued momentum.
73 Additionally, we were solidly profitable with 5 cents in non-GAAP earnings per share. Our sales
74 execution in key regions has improved. Under new leadership in Europe, we went through
75 significant organizational restructuring during the quarter. We see a significant opportunity to
76 expand in Europe and are optimistic that the new leadership and this business-focused new
77 structure will better position us to drive growth.

78

79 We are cognizant of the macro environment, and we have seen large players report soft results
80 and outlooks. However, those challenges have not impacted our business. We believe that the
81 demand for wireless transport solutions is driven primarily by the relatively faster time to
82 market and lower cost, yet satisfying the increased capacity needs. We are working hard on

83 leveraging our robust products and services offering to capitalize on this situation and are
84 pleased with the results.

85

86 For the second quarter in a row, the results also demonstrate the improving earnings power of
87 our organization, reflected in expanding gross margins, disciplined operating expense
88 investments and improved efficiency. We delivered \$2.1 million in GAAP net income in the
89 second quarter and \$4.4 million in non-GAAP net income. Ceragon has built a solidly profitable
90 business model, a robust backlog, and a diverse set of solutions that address key capex and
91 OPEX goals for customers around the world.

92

93 We have not encountered any significant impacts from supply chain disruption in the quarter,
94 and while we continue to carefully manage the supply chain, component availability continues
95 to improve.

96

97 Our geographic diversification continues to benefit our revenue. In the second quarter, we
98 generated sequential and year-over-year revenue growth in India, and year-over-year growth in
99 North America. In India, we generated our fifth-consecutive quarter of revenue over \$20
100 million, our highest quarterly revenues in recent years, and continued strong bookings. In North
101 America, we generated revenue of \$22.2 million, down from the record of \$26.4 million in the
102 first quarter but up from \$15.0 million in the second quarter last year.

103

104 We continue to advance the productization of our new system-on-chip technology. To date, our
105 efforts are advancing according to plan and while there is much work to be done, we believe we
106 remain on track to launch our new product line in 2024. In addition, in the coming months, we
107 expect to launch new products featuring a lower total cost of ownership. We believe these
108 new, additional products will help us expand our market presence and offer tangible benefits to
109 our customers. These products are also expected to help us with our long-term goal of
110 improving gross margins.

111

112 I'd now like to give an overview on our Q2 highlights by region, noting that on today's call we
113 will focus primarily on activities in North America and India, the two regions that have, and we
114 expect will continue to have, the greatest impact on our quarterly results.

115

116 **In North America** the 5G build continues to be strong, especially with Tier-one carriers. We
117 have continued to receive orders from major carriers, with one customer driving a significant
118 portion of our volume.

119

120 We have been engaging on new opportunities, where technology can be deployed in new ways.
121 For example, we recently signed an agreement to partner with one of the leading Open RAN
122 vendors to deliver a wireless high-capacity, low-latency, multigigabit transport solution for a
123 Caribbean customer's new 5G OPEN Radio Access Network. We utilized our existing IP-50FX
124 Disaggregated Open Router, providing the customer with an advanced switching and open
125 routing solution. The deployment of this project is ongoing and we have received very positive
126 feedback from the end customer. We are also expecting additional business to expand the
127 network and support network operations. This represents the first of its kind, Open RAN, Open
128 Routing and Open Transport project in North America.

129

130 We are also pursuing municipal and infrastructure-related contracts, including recent wins. A
131 great example is the multi-year contract worth up to \$4.2 million with the City of Cincinnati we
132 signed during the quarter, to upgrade the City's public safety network. Ceragon is deploying a
133 multi-technology, multi-service solution that provides a robust, modernized backhaul and
134 routing solution, followed by a long-term maintenance and support plan. This solution includes
135 turnkey services, including design and engineering, equipment, rollout, and integration of the
136 solution to enable the City to support mission critical applications such as artificial intelligence,
137 automation, and real-time video.

138

139 We continue to see many opportunities that introduce additional potential demand for our
140 solutions. The 5G higher frequencies availability as well as the evolving need for heterogeneous

141 services profiles with guaranteed level of service to different end-users, are driving up this
142 potential demand. This demand is also reflected in multiple RFP's in which we participate,
143 covering all segments of our addressable market namely Tier 1 operators, rural ISPs and small
144 carriers as well as Private networks.

145

146 Some of these opportunities, particularly in the rural broadband and critical infrastructure
147 segments, may take longer to mature, as they are also supported by Federal and State funding
148 plans. These initiatives remain a critical area of incremental opportunity and diversification for
149 our business.

150

151 We believe we are increasingly well-positioned to capitalize on all of these opportunities when
152 they mature.

153

154 I'd also note that we have been successful in increasing our services business in the region,
155 which often can double the value of an individual deal.

156

157 In **India**, telcos continue to aggressively invest in 4G technology network while beginning to
158 deploy 5G in certain regions. We are working with operators in the market for 4G rollout and
159 enhancement in selected regions. 4G continues to be the dominant subscription type in India,
160 with 4G subscriptions expected to peak in 2024. Simultaneously, the 5G rollout is accelerating,
161 especially in urban areas.

162

163 We continued to deliver our products for 4G networks as well as delivering our E-
164 band/multiband solution for 5G networks at an increased pace. We delivered another strong
165 booking quarter in India, giving us improved visibility for revenue for the second-half of the
166 year. Demand remains robust.

167

168 We are anticipating promising growth with 5G adoption, a trend that is accelerating as 5G
169 handsets become more and more affordable.

170

171 To summarize, we are delivering solid execution and conditions continue to improve, both on
172 the macro and micro levels. Demand for our solutions is strong and supply chain availability has
173 been getting better. Quarter-to-quarter variability in our financials is always a reality, but the
174 trailing twelve-month trends for our business, which we believe are a strong indicator to our
175 performance trajectory, are solid and improving, both from a revenue and a profitability
176 standpoint. We believe we can deliver similar revenue trajectory for the foreseeable future and
177 that we can be profitable, on a non-GAAP basis, for each quarter this year.

178

179 Before I turn the call over to Ronen to walk through the numbers, I wanted to mention that we
180 filed our proxy statement [with the SEC] for the 2023 Annual General Meeting, where we have
181 nominated Ilan Rosen, who has been serving on our Board since July 2021, as the new
182 Chairman of our Board of Directors. Ilan brings significant corporate governance expertise, as
183 well as a track record of successful M&A and value-creation. He also has significant experience
184 in the telco industry. He currently serves as Managing Director in HarbourVest Partners LLC, a
185 global private equity firm.

186

187 We have also nominated Ms. Yael Shaham, to be appointed by the Shareholders as a new,
188 independent director on our Board. Yael has more than 25 years of experience in management
189 and strategic leadership roles and a wealth of business and technology knowledge, particularly
190 in leading the development of robust software solutions for the Telecom space and selling them
191 under managed services models. We believe that Yael's vast experience can be a great
192 contributor to us in advancing and executing our strategy.

193

194 With that, I'll turn the call over to Ronen Stein, our CFO, to discuss the results in more detail.
195 Ronen, over to you.

196

197 **Ronen Stein**

198

199 Thank you Doron, and good morning, everyone.

200

201 As Doron outlined, this was another strong quarter for Ceragon. Though, it's important to keep
202 in mind that we are a project-driven business and as such there is inherent variability in results
203 from quarter to quarter. Because of this we analyze our bookings, revenue, and gross margin,
204 as well as other key performance indicators over a 12-month period, a duration which we
205 believe better reflects the underlying business trends.

206

207 In addition, to help you understand the results, I will be referring primarily to non-GAAP
208 financials. For more information regarding our use of non-GAAP financial measures, including
209 reconciliations of these measures, we refer you to today's press release.

210

211 Let me now review the actual results:

212

213 **Revenues** were \$86.2 million, an increase of 21.9% compared to \$70.7 million in Q2 2022 and
214 up 3.3% compared to \$83.4 million in Q1 2023. When we take the trailing twelve months' view,
215 our revenue was \$323.7 million, an increase compared to last quarter's trailing twelve months
216 revenue of \$308.3 million.

217

218 Our strongest regions in terms of revenues for the quarter were **India** and **North America** and
219 with \$26.9 and \$22.2 million, respectively, in line with the continuous strong demand we see in
220 these regions.

221

222 Our third strongest region in terms of revenues was **Latin America** with \$12.6 million.

223

224 We had two customers in the second quarter that contributed more than 10% of our revenues.

225

226 **Gross profit** for the second quarter on a non-GAAP basis was \$30.4 million, an increase of
227 41.2% compared to \$21.5 million in Q2 2022, and an increase of 7.2% compared to \$28.4

228 million in Q1 2023. Our non-GAAP gross margin was 35.3% compared to 30.5% in Q2 2022 and
229 34.0% in Q1 2023. We have achieved high gross margins even as revenue from India grew as a
230 percent of consolidated revenue mainly as a result of improved product mix, including more
231 software revenue, and further cost optimizations offset partially by higher inventory write-offs.
232 Our gross margins continue to fluctuate from quarter to quarter, due to changes in product and
233 regional mix.

234

235 When we take the trailing twelve months' view, our non-GAAP gross margin was 34.5%, an
236 increase compared to last quarter's trailing twelve months gross margin of 33.4%.

237

238 This upward trajectory of our gross margin trend reflects our ability to increase margins when
239 we execute on our strategy and operational efficiencies.

240

241 As for our **operating expenses**:

242

243 **Research & Development** expenses for the second quarter on a non-GAAP basis were \$7.6
244 million, up from \$7.5 million in Q2 2022, and slightly lower from the \$7.7 million in Q1 2023. As
245 a percentage of revenue, our R&D expenses were 8.8% in the second quarter compared to
246 10.6% in the second quarter last year.

247

248 **Sales & Marketing expenses** for the second quarter on a non-GAAP basis were \$9.4 million, up
249 from \$9.1 million in Q2 2022 and down from \$9.8 million in Q1 2023. As a percent of revenue,
250 sales and marketing expenses were 10.9% in the second quarter compared to 12.8% in the
251 second quarter last year.

252

253 **General and Administrative expenses** for the second quarter on a non-GAAP basis were \$6.1
254 million, up from \$4.6 million in Q2 2022 and up from \$5.0 million in Q1 2023. As a percent of
255 revenues, G&A expenses were 7.0% in the second quarter compared to 6.5% in the second
256 quarter last year.

257

258 We intend to continue being disciplined in our operating expenses while leveraging our strong
259 results to further invest in certain areas to support continuous profitable growth. Therefore, we
260 estimate average quarterly operating expenses in the second half of 2023 to range between
261 \$22 million to \$23 million.

262

263 **Operating profit** for the second quarter was \$7.4 million, up approximately \$7.0 million from
264 the operating profit of \$0.4 million in Q2 2022 and up \$1.5 million sequentially from the
265 operating profit of \$5.9 million in Q1 2023. Please note, this non-GAAP metric excludes a charge
266 related to restructuring and related charges in Europe, amounting to \$0.9 million.

267

268 **Financial and Other Expenses** for the second quarter on a non-GAAP basis were \$2.2 million, in
269 line with expectations.

270

271 **Our tax expenses** for the second quarter on a non-GAAP basis were \$0.8 million.

272

273 **Net income** on a non-GAAP basis for the quarter was \$4.4 million, or \$0.05 per diluted share,
274 compared to a net loss of \$(2.5) million or \$(0.03) per share in the second quarter last year. The
275 second quarter net income was up \$0.8 million from net income of \$3.6 million, or \$0.04 per
276 diluted share in Q1 2023.

277

278 As for our **balance sheet**:

279

280 Our **cash position** at the end of the second quarter was \$24.5 million, and our short-term loans
281 stands at \$39.6 million. During the second quarter we increased the bank loan facility to \$72
282 million and extended the maturity date for an additional year until June 30, 2024. We believe
283 we have cash and facilities that are sufficient for our operations and working capital needs.

284

285 Our **inventory** at the end of Q2 2023 was \$67.8 million, down from the \$72.0 million at the end
286 of December. We continue to monitor inventory levels, taking into consideration the
287 improvements in availability of components and expected changes in demand.

288

289 Our **trade receivables** are at \$107.6 million, as compared to \$100.0 million at the end of
290 December.

291

292 Our DSO now stands at 121 days.

293

294 As for our **cashflow**:

295

296 Net cash flow generated **by operations and investing activities** in Q2 2023 was \$0.4 million. We
297 expect to generate positive cash from operations for the full year.

298

299 As Doron indicated at the top of this call, demand in our business continues to be strong and
300 we are encouraged by our bookings, which give us good visibility into the third quarter. Based
301 on our results through the first half of this year we are raising our full year revenue outlook
302 from \$325 - \$345 million to \$334 - \$348 million and reaffirming expectations for full-year
303 profitability. The outlook we are providing today is based on our current visibility, and it leaves
304 us some room for adjustment as we progress further in to the back of the year.

305 With that, I now open the call for your questions. Operator?

306

307 **Doron's Closing Remarks**

308

309 To close, we are encouraged by our first half results. We delivered strong revenue, and
310 significantly improved profitability. Bookings have been strong, providing us with good visibility
311 into the 3rd quarter and we believe that we are well positioned to achieve self-sustaining cash
312 flows as we execute our growth strategy.

313 We expect that our product roadmap will give us a durable competitive advantage. We are
314 increasingly excited about Ceragon's opportunities.

315

316

317 I look forward to updating you further on our next call.

318

319 Have a good day everyone.