Ceragon Networks Q4 FY 2023 Earnings Call Script

February 20, 2024

Operator

Welcome to Ceragon Networks Fourth 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.

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

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

Also, today's call will include certain non-GAAP numbers. For a reconciliation between GAAP and non-GAAP results, please see the table attached to the press release that was issued earlier today which is posted on the Investor Relations section of Ceragon's website.

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

Doron Arazi

Thank you, Rob, and good morning, everyone.

This was a significant quarter in the evolution of Ceragon. We closed a strategic acquisition that we believe will accelerate our growth, especially in key markets. We exceeded our guidance for revenue and delivered record full-year non-GAAP operating income, giving us great momentum and confidence as evidenced by our guidance for significant growth and margin expansion in 2024. Major parts of our strategy are steadily coming together, while we increase our footprint in North America and grow our business with private networks around the world.

This might be the right moment to discuss some of the KPIs that are giving us confidence that we are making progress in the execution of our strategy. For example, our bookings from private networks this year were nearly $40M. This is a very substantial number for us. But even more importantly, while this consists of slightly above 10% of our total booking, the total booking from new private networks customers was above 30% of the company's total booking from new customers – 3 times higher. In terms of the number of new customers, the progress is even more impressive. Approximately 50% of our total new customers this year were private networks customers. As part of our plans, we aspire to double the amount of private network bookings in 2024. In parallel we continued to increase our business in tier 1 and tier 2 customers. This has been our bread and butter for many years, in existing as well as new customers, such as the most recently noted, new customer in India. With a few of our longstanding customers we are in advanced discussions on selling software-led managed services and we hope for more business with them in 2024.

According to analyst reports, the mmW market segment had the highest growth rate within Wireless Transport market, with a compound annual growth rate of 35% for the last four quarters ended September 30, 2023. This particular market segment is expected to continue out pacing the total wireless transport market growth in the coming years. I believe that some of the actions we took in 2023 are positioning Ceragon to monetize on this expected continued high growth. We continued deploying our IP-50E in different regions. We developed our optimized TCO driven IP50-EX that is expected to be launched in the coming weeks, and we have started the design of the next generation millimeter wave product that will be based on our new SoC enabling up to 100Gbs wireless transport link. Last, but not least, we acquired Siklu further expanding our mmW offering to additional market segments and enhancing our end-to-end solution. With all these actions taken, we believe we will maintain the broadest and strongest millimeter wave products in our market, with the richest price/performance range.

In early December, we completed the acquisition of Siklu. The integration is well underway. Siklu contributed only a modest amount of revenue in the nearly one month they were part of Ceragon, and the majority of our growth was organic. However, after closing the acquisition, we received a significant purchase order from one of Siklu's larger customers, an important vote of confidence for us. The financial key indicators of the acquisition have come in as expected.
During 2023, Ceragon generated more than $30 million in cash from operations, on a full-year basis, and $10 million in free cash flow for the full year, even including the cash impact related to the acquisition of Siklu.

In the fourth quarter, Ceragon grew revenue nearly 20% to $90.4 million, our highest quarterly revenue level of the year. Again, since the acquisition of Siklu closed only in early December, Siklu's contribution to this revenue was essentially insignificant. We delivered non-GAAP operating income of $7.8 million, the third consecutive quarter above $7 million. On a GAAP basis, our operating income was $4.2 million. Our non-GAAP net income was $3.7 million, the fourth consecutive quarter of non-GAAP net income exceeding $3 million. This strong end to the year enabled us to grow revenue more than 18% for the full year to $347 million, exceeding our full-year guidance of $338 million to $346 million. Even excluding the nearly one month of Siklu, we would have achieved our full-year revenue guidance, with revenue at the high end of the provided range. For the full year, we delivered operating income of $29.0 million on a non-GAAP basis – an all-time record for Ceragon. On a GAAP basis, operating income was $21.2 million. Net income on a non-GAAP basis was $16.7 million, and $6.2 million on a GAAP basis.

Clearly, Ceragon has successfully navigated macroeconomic challenges impacting our industry. Continued strong demand for our solutions, especially in North America and India, has enabled us to continue robust growth, as we take market share, and deliver consistent profitability. In fact, we grew revenue in North America by 43%, in 2023 compared to 2022. We continue to believe that our growth strategy of expanding our addressable market beyond Tier-1 and Tier 2 customers is coming into clear focus. The acquisition of Siklu is expected to accelerate this initiative.

Our performance in 2023, combined with improving visibility and the expected synergies with Siklu, has given us the confidence to guide to continued double-digit revenue growth. We are also targeting significant margin expansion in 2024. Ronen will speak to our guidance in more detail during his comments.

In the next few weeks, two new products are expected to be introduced, providing our customers with a lower total cost of ownership and excellent performance attributes. We believe these new, additional products will help us further expand our market presence and offer tangible benefits to our customers. In addition, they are expected to also help us with our long-term goal of improving gross margins. We continue with the testing of our new system on a chip, named Neptune, and expecting to launch the first product using this chip by the end of 2024. As we already announced, it is our intention to demonstrate some of the Neptune capabilities at MWC exhibition in Barcelona next week. In particular, we will have a live demonstration of our upcoming Neptune-based millimeter wave technology which we believe far surpasses competitors’ capabilities. We will also display our

IP-50CX microwave radio, and IP-50EX millimeter wave radios. Both radios demonstrate a dedication to delivering high performance in compact packages for an optimized total cost of ownership (TCO).

As we have said, this SoC platform represents a meaningful competitive advantage which should help us further take market share in the future.

I’d now like to provide an overview of our Q4 highlights by region. Noting that on today’s call we will focus primarily on activities in North America and India, the two regions that have, and we expect will continue to have, the greatest impact on our results in the near term.

In North America, we have continued to expand our business in the private network market. We pursue additional opportunities in the Enterprise domain, large campuses (including universities), as well as municipalities. Importantly, these contracts typically have a greater component of services, and specifically managed services, which is expected to improve the visibility of our backlog and reduce the lumpiness of our business.

North America revenue was $24.5 million. Our solutions are in demand, even as service providers move cautiously in their capital expenditures.

Bookings in North America were in-line with expectations in this Q, adding to our backlog and reflecting several private network wins, and strong demand from our largest service provider customer. Siklu North America benefitted from a strong finish to the year, reflecting solid demand for Siklu's mmW solutions.

In **India,** we have continued to see strong demand for our solutions, even as others report softness. Revenue from India was $30.5 million. Bookings were strong, increasing our backlog. We signed a deal in India valued at approximately $150 million, with the potential for additional revenue over time. Ceragon collaborated with a large global integrator on this project, which will support a network modernization project for a Tier 1 Operator in India. This is a brand-new customer for Ceragon, and this customer will be the first to deploy our newest solutions. The agreement involves planning, product delivery and deployment services, as well as a multi-year contract for Ceragon's Managed Services that covers day-to-day monitoring, management, and maintenance oversite of the microwave and millimeter wave network. We expect to begin delivery and deployment of the new sites in the second quarter, and deployment is expected to complete within approximately two years. Approximately 75% of the project value expected to be recognized during this timeframe. The remaining approximately 25% of the contract value is for Managed Services & Maintenance and is expected to start being recognized over the time of the agreement, beginning a year post deployment.

This project will certainly benefit our presence in India, and while this win includes margins typical to India, we do not expect this win to be a drag on plans to continue improving our consolidated gross margins.

Clearly, we continue to be successful in India and North America and we anticipate this trend to continue in 2024.

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

Ronen Stein

Thank you Doron, and good morning, everyone.

As Doron outlined, the fourth quarter represented a solid end to a strong year for Ceragon. For the year, we grew revenue by 18% to $347.2 million, expanded our gross and operating profit margins, and delivered positive GAAP and non-GAAP net income along with positive free cash flow. This demonstrates the progress we have made in unlocking the earnings power of Ceragon. 2023 was a very strong year for Ceragon, and we enter 2024 with accelerating momentum.

We remain a project-driven business, with inherent variability in results from quarter to quarter, but we delivered four strong quarters, each with revenue over $80 million, and each with a non-GAAP net income of above $3 million. On an annual basis, we were profitable on a GAAP basis for 2023, the first time since 2018.

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

Let me now review the actual results:

Revenues were $90.4 million, up 20% from $75.5 million in the fourth quarter of 2022. Sequentially, revenue increased approximately 3.6% from $87.3 million in the third quarter of 2023.

Our strongest regions in terms of revenues for the quarter were **India** and **North America** with $30.5 million and $24.5 million, respectively, in line with the continuous strong demand we see in these regions.

Our third strongest region in terms of revenues was **Latin America** with $11.8 million.

We had 2 customers in the fourth quarter that contributed more than 10% of our revenues.

Gross profit for the fourth quarter on a non-GAAP basis was $31.8 million, an increase of 27.1% compared to $25.0 million in Q4 2022, and up 4.4% compared to $30.4 million in Q4 2023. Our non-GAAP gross margin was 35.1% compared to a gross margin of 33.1% in Q4 2022 and 34.9% in Q3 2023. We continued to achieve high gross margins mainly as revenues from North America continued to maintain its high level and product mix continued to be favorable, while we keep costs under control. Our gross margins continue to fluctuate from quarter to quarter, due to changes in product and regional mix as well as other operational factors. However, we continue to see a positive trajectory.

As for our **operating expenses**:

Research & Development expenses for the fourth quarter on a non-GAAP basis were $7.7 million, down from $7.9 million in Q4 2022 and up from $7.3 million in Q3 2023. As a percentage of revenue, our R&D expenses were 8.5% in the fourth quarter compared to 10.4% in the fourth quarter last year.

Sales & Marketing expenses for the fourth quarter on a non-GAAP basis were $10.2 million, up from $8.6 million in Q4 2022 and from $9.7 million in Q3 2023. As a percent of revenue, sales and marketing expenses were 11.3% in the fourth quarter compared to 11.4% in the fourth quarter last year.

General and Administrative expenses for the fourth quarter on a non-GAAP basis were $6.1 million, down from $17.6 million in Q4 2022, which included a $12.3 million credit loss provision for a specific customer, and up from $5.5 million in Q3 2023. As a percent of revenues, G&A expenses were 6.7% in the fourth quarter compared to 23.4% in the fourth quarter last year.

Our non-GAAP operating expenses are expected to increase in 2024, due to the full consolidation of Siklu. However, as we have already said, with our growth plan and the added business from Siklu, we are targeting operating margin expansion. We will continue to be disciplined in regards to our operating expenses to drive increased operating leverage. Our goal is to achieve at least 10% non-GAAP operating margin for 2024 at the mid-point of our revenue guidance. We expect to utilize our strong cash flow to invest in our strategic initiatives to expand our addressable market and target private network customers. We continue to believe that such investments can better position us to see further growth in these segments in 2024.

Operating profit for the fourth quarter on a non-GAAP basis was $7.8 million compared with operating loss of $(9.1) million for Q4 2022 and a profit of $8.0 million for Q3 2023.

Financial and Other Expenses for the fourth quarter on a non-GAAP basis were $2.5 million, slightly higher than we expected due to currency losses from our operations in Africa.

Our tax expenses for the fourth quarter on a non-GAAP basis increased to $1.5 million mainly due to an update in our Fin-48 provisions following tax assessments in one of the territories in which we operate.

Net income on a non-GAAP basis for the quarter was $3.7 million, or $0.04 per diluted share, compared to a net loss of $(12.5) million, or $(0.15) per diluted share for Q4 2022 and net income of $5.0 million, or $0.06 per diluted share for Q3 2023.

GAAP Net loss for the fourth quarter was $(1.2) million, negatively impacted mainly by $1.6 million charges related with the acquisition of Siklu and a $1.2 million one-time charge related to a termination of a long-term agreement with a third party for a joint development of 5G technologies. In accordance with the terms of this termination, we remained the sole owner of the developed technologies in return for waiving $1.2 million future payments by the third party. This agreement termination also had a significant balance sheet effect on our non-current assets and deferred revenue. It is important noting that it does not have any impact on our future revenue projections.

Turning to the full-year results …

Revenues were $347.2 million, up 17.6% from $295.2 million in 2022. The growth is mainly attributable to a substantial growth in North America and India.

Gross profit on a non-GAAP basis was $120.9 million, up $27.0 million from $93.9 million in 2022, giving us a gross margin of 34.8%, compared with a gross margin of 31.8% in 2022. This substantial improvement in gross profits as compared with 2022 is mainly attributable to the substantial increase in revenues, while maintaining same or higher margins in most regions, keeping general operational costs under tight control, improved supply chain costs, partially offset by higher inventory write-offs.

Operating income on a non-GAAP basis was an all-time record at $29.0 million compared with operating loss of $(3.0) million for 2022. Once again, this demonstrates the progress we have made in unlocking the earnings power of Ceragon and our ability to increase operating leverage.

Net income on a non-GAAP basis was $16.7 million, or $0.20 per diluted share, compared with a net loss of $(12.7) million, or $(0.15) per diluted share for 2022.

As for our **balance sheet**:

Our **cash position** at the end of the fourth quarter was $28.2 million, compared to $22.9 million at the end of 2022. Short-term loans were $32.6 million compared to $37.5 million as of December 31, 2022. We believe we have cash and facilities that are sufficient for our operations and working capital needs.

Our **inventory** at the end of Q4 2023 was $68.8 million, down from the $72.0 million at the end of December 2022. We continue to monitor inventory levels, taking into consideration the improvements in availability of components and expected changes in demand.

Our **trade receivables** are at $104.3 million, as compared to $100.0 million at the end of December 2022.

Our DSO now stands at 110 days.

The main impacts of consolidating Siklu into our balance sheet include the increase of intangible assets and goodwill, the increase of other long-term payables, the impact on our cash position and additional inventory.

As for our **cashflow**:

Net cash flow generated **by operations and investing activities** excluding the $8.0 million impact of Siklu business combination, net of cash acquired in Q4 2023 was $7.8 million. We generated nearly $11 million in cash from operations in the fourth quarter, and nearly $31 million for the full year.

As Doron indicated at the top of this call, we believe that the demand in our business will continue to be strong. For 2024, with the caveat of lumpiness between quarters, we expect revenue of $385 million to $405 million, representing growth of 11% to 17% compared to 2023. This guidance includes the contribution from Siklu. Non-GAAP operating margins are targeted to be at least 10% at the mid-point of the revenue guidance. As a result, we expect increased non-GAAP profit and positive free cash flow for the full year of 2024.

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

Doron’s Closing Remarks

This was an encouraging year for Ceragon. We are increasing our footprint in multiple domains and expect to continue delivering significant revenue growth. The overall wireless transport market continues to grow, based on projections from independent industry analysts, and the expectation is that growth will continue in coming years. We believe we can grow much faster than the market growth, by focusing on the parts of the market that are expected to grow faster and expanding to new domains. Beyond delivering strong radio products to this market and primarily focusing on mmW that is expected to outpace the market growth, we are expanding our business in other focused domains, which are Private Networks as well as the software led Managed Services. This growth profile serves as the basis for our expectation of double-digit growth going forward.

We are solidly profitable and expect to further expand our margins in 2024. We believe that we are well positioned to continue to achieve self-sustaining cash flows as we execute our growth strategy.

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

Have a good day everyone.