



Company update

Conference call

Oct 9, 2018

Operator:

Ladies and gentlemen, welcome to the RADCOM Ltd. Company update Conference Call. Thank you for standing by. All participants are currently in a listen-only mode. Following the presentation, instructions will be given for the question-and-answer session. For operator assistance during the conference, please press star-zero. As a reminder, this conference is being recorded, and will be available for replay on the company's website, www.radcom.com, from October 10th, 2018.

On the call today is Yaron Ravkaie, RADCOM's CEO; and Amir Hai, RADCOM's CFO. Before we begin, I would like to review the Safe Harbor provision. Forward-looking statements in the conference call involve a number of risks and uncertainties, including but not limited to the company's statements about its third quarter and full year 2018 revenue and other performance guidance, potential future success, and the future of – and benefit from – NFV transformation, expected plans to transition to NFV and the pace of such transitions and the company's leadership in the industry, industry trends and their effect on the company, and projected sales cycles, orders, engagements, and relationships with customers, as well as the transition in the company's senior management team.

The company does not undertake to update the forward-looking statements. The full Safe Harbor provisions, including risks that could cause actual results to differ from those forward-looking statements are outlined in the company's SEC filings. Now, I would like to turn over the call to Yaron. Please go ahead.

Yaron Ravkaie:

Thank you, Operator, and thank you all for joining us today. We scheduled today's call in order to provide a detailed business update as promised during our last investors' call. Today, we will discuss two topics; the first is the status of our business, and the second is the recent change in the company's management. So, starting with the business update. I want to emphasize that we remain confident in our business strategy, the future of NFV, the superiority of our NFV offerings and the role RADCOM expects to play in the NFV transformation to come. As a result of our work over the last few years, we offer a portfolio of market-leading solutions that are well-known and appreciated in the industry.

We also have a strong and stable relationship – relationships with our customers. This includes AT&T, our other Tier 1 operator, Globe, and others. These relationships continue to carry us forward and we expect they will continue to play a big part in our leadership of the NFV transformation.

Now, I would like to talk about where the industry is at and the transformation to NFV. There is a consensus in the industry that NFV is the future. Today, many communication service providers are in some stage of evaluating and planning how to migrate to NFV.

RADCOM operates primarily in the mobile space. This is a complex space for the communication service providers, as they must keep up with never ending demand for data consumption and higher speeds while facing declining ARPUs. This pressure on the CSPs is fueling the desire to virtualize their networks, as virtualization is expected to result in CapEx and OpEx savings. While the motivation and desire to virtualize exists, reaching mature infrastructure for NFV in the industry is taking time, as CSPs are still trying to figure out the best approach. Some go with one vendor like an Ericsson, Nokia, Huawei, others, also known as the major NEPs (Network Equipment Providers) as a one stop shop for NFV.

Others use a best-of-breed approach, choosing various components from different providers and integrating those components on their own. And yet others are building NFV into future infrastructure investment plans, such as 5G rollouts. AT&T is implementing what can be considered the most aggressive transformation plan in the industry. They've put in place teams and budgets and made technology selections and have been in implementation and scaling to very high volumes mode since 2016. RADCOM has been with AT&T in this process, and as a result, we're able to mature and provide industry-leading NFV solutions. This has built up our portfolio and has given us invaluable knowledge and a significant competitive advantage.

As we look in the industry, almost all major carriers are interested in implementing NFV. However, there is a variability in the pace of implementation. Some carriers have launched small NFV implementations on portions of their network, while others are still in the design phase. A few other carriers have elected to wait and see how other transformations will go, before embarking on their own NFV transformation. In addition, there are operators who are building NFV into their future infrastructure plans, such as 5G.

We are engaged with all of the leading communication service providers in the market. With some, we have done NFV workshops, and some of these have matured to proof-of-concept installations. Throughout our engagements with customers, we see strong positive feedback on our technology, as well as on our knowledge and experience. During our last call, I mentioned that the pace of NFV adoption is slower than we expected.

We do not believe that this is a reflection of our product or our customers' experience with our product. It is simply that operator decision-making and technology implementation processes are taking longer than we expected. As these processes extend, our sales cycle lengthens, and certain opportunities that we expected would materialize by now, are being delayed.

We have experienced this with several key opportunities that we expected would drive revenue this year. We have seen this with our Tier 1 operator, where delays in the issuance of new POs have resulted in less revenue than we initially forecasted. We have seen something similar with our new Galaxy operator, where we have passed a significant purchasing milestone, yet they are

still in the process of formalizing a first purchase order. A similar trend occurred with a few other new logo opportunities that did not materialize as expected.

With the third quarter now concluded, we are now able to better estimate the impact of these delays on our business. We are reducing our guidance to a range of 33 to 35 million dollars in revenue for fiscal year 2018. This is based on revenues to date, including preliminary third quarter revenues in the range of 8 to 8 and a half million dollars, which includes meaningful license expansions with AT&T that we booked towards the end of the quarter. This guidance is also based on the current outlook with existing and potential new customers, and the delay of certain opportunities that were expected but did not materialize. This also reflects a reduction in revenues attributable to non-strategic legacy opportunities, which have brought in less revenue than we previously anticipated. We are not pleased with the slow pace of transition to NFV and its effect on our business. However, we remain confident in the transition to NFV, our leading solutions and our future.

RADCOM is ready and well-positioned to be a market leader for NFV solutions as the industry more actively pursues NFV transformation, and communication service providers take meaningful next steps.

Now, moving on, I also want to update that Keren Rubanenko, our Vice President of Professional Services will be leaving us later this month, to pursue a new opportunity. Tal Birenzweig will replace Keren. Tal has been our Director of Customer Success for two years and has been Keren's right-hand man in building a strong professional services team that is able and ready to answer our customers' need. We are confident in Tal's ability to lead the team to continued success, and wish Keren good luck in her new opportunity.

As we look at our leadership team today, and the changes that took place recently, we are pleased with what we see, and with our ability to continue to operate without interruption and to leverage changes in personnel. Amir Hai, our new CFO, has fully transitioned into the role. The position of Chief Business Officer has been eliminated, with marketing and sales now reporting to me in a regional structure. Sales and marketing continue to work aggressively on new opportunities and building the pipeline. Handover in our professional services team is under way and is progressing smoothly.

Before I turn the call over to questions, I think it's worth repeating that the industry is moving to NFV, and that although the pace may be slower than we expected, due to the complexity of transformation, we remain confident in RADCOM's future. Over the last few years, we've worked to make sure that RADCOM is the household name for NFV solutions. Today as we look at the market, we believe we are well-positioned for success, as there isn't a major operator out there who doesn't know RADCOM, our leading solutions, and the value we offer. Operator?

Operator:

Thank you. Ladies and gentlemen, at this time, we will begin the question and answer session. If you have a question, please press star-one. If you wish to cancel your request, please press star-two. If you are using speaker equipment, kindly lift the handset before pressing the numbers. Your questions will be polled in the order they are received. Please stand by we poll for your questions. *[pause]* I repeat, if you have a question, please press star-one. If you wish to cancel your request, please press star-two. Please stand by we poll for your questions. *[pause]* The first question is from Avner Sonnino, a private. Please go ahead.

Avner Sonnino:

Hi, Mr. Ravkaie. How are you? Thank you for the notes.

Yaron Ravkaie:

I'm doing good.

Avner Sonnino:

Great. Could you give us some indication of how do you believe it's going to affect the expected EPS for the quarter and for 2019?

Yaron Ravkaie:

We – first of all, we don't give profitability guidance. I can say that – a couple of things. One, for the quarter, we're still crunching the numbers. So, you know, it's only several days after quarter end, and we release results only next month, and the profitability is exactly what gets really impacted from the accounting, et cetera. So, revenue – we can – it's better earlier, but profitability takes more time.

The second piece is that on a higher level, we – we are continuing our investment plan, okay. So as people have modeled the company, or you look at the previous performance and we've disclosed the headcounts previously, we continue pretty much with the same run rate. We are not planning to slow down, we are planning to be heads down and capitalizing on this transformation. And we will give, of course, the results, soon, you know, on the next call.

Avner Sonnino:

Thank you.

Operator:

The next question is from Alex Henderson of Needham and Co. Please go ahead.

Alex Henderson:

Thanks. Yaron, I was hoping you could talk a little bit about, as you look at these individual companies that you've already, you know, worked with here – are they slowing it down because they're finding difficulty to integrate not so much your product, but other parts of the NFV process? Or is it slowing down because they're looking at how do they integrate NFV into 5G? Or is it because they want to move to a more of a cloud architecture? What – what are the root causes of the deceleration of the process that it's, you know undermining the growth rate?

Yaron Ravkaie:

Yeah, so – thanks, Alex. Hi. First of all, I want – I'm not sure I want to call it deceleration. And the reason is because I think it has – we – our expectation may have been higher than their plans, right? Something like that. So, saying that, I think, I would carefully say that you would probably see all of the things that you mentioned in the various operators. Some haven't – don't have 5G plans. The ones that have 5G plans do couple it with the NFV transformation. But they're – not in all cases they're 100% coupled. So, we do see operators that are doing some stuff in NFV pre-5G, we do see operators planning 5G, and 5G is going to be rolled out on a virtual technology. And we do see operators that are in the middle of – and have started a transformation plan. And we – we do see that they – because these are complicated plans, that they adjust the pace of the plans to – to their business plans. Some of it might be driven from some challenges that they have, typically from all the moving parts. So, remember, when you – let's say you are transforming a mobile network, so they will have, you know, a full mobile core with all of the components, an MME, a data gateway, all of these things need to be virtualized, and these are huge components. Scaling them to high volume, getting to work – getting them to work on an NFVI or an NFV infrastructure, it's not – not simple. So, each one has their own issues. And once in a while we also see some just straightforward issues, that some – seeing – some companies thought that they will make an X investment in 2018, and they're pushing some of the investment into 2019 for their P&L reasons. So, there's not one specific thing that I can put my finger on.

Alex Henderson:

So, given the slower pace in the back half of '18, are you also expecting a much slower pace to start '19? I mean, is this going to take six to nine, 12 months to reaccelerate, or should we be

thinking that this is just a back half of '18 phenomenon that is temporary, by the end of '19, we'll be back on track?

Yaron Ravkaie:

It's a tricky question. The real answer is, I don't know to fully forecast it, okay? What I expect in the near term is, I do expect some of the things that got pushed out to 2019, to materialize in 2019. So, they will drive, you know, numbers in 2019. But I don't know how to assess yet the pace of 2019 overall. I'm not sure, you know, I can give any accurate tempo now. I think what we need to do is continue to wait. We need to go through our planning stage, and also continue to follow on this. It can go – in my mind, at this stage it can go both ways. We can see some slowness, but we can see also some pent-up demand. I think that's because of the things that get pushed out.

Alex Henderson:

So, is it fair to say that you don't see any change in the competitive landscape, you're not losing customers, as a competitive basis, there's no price pressure per se as a result of, you know, somebody dropping their pants for – to win business? Or any of the network equipment providers that are larger, you know, 5G scale players winning business because of bundling or anything of that sort?

Yaron Ravkaie:

No, look, at the end, I don't think anything changed in the competitive landscape. The price pressure is there from day one. We have the disruptive technology which is 100% virtualized. So, we are able to cope better with the, you know, competitive pricing than the entire industry. And this is not new, this has been going on forever, and for sure for the last three years. Our, you know, our big competitor NetScout, we don't see them winning any new big logos and any virtual transformation project, and, you know, I'm closely getting input from the customers there because they're in – their legacies are installed in many – in many places. So, I don't think anything changed there. I'm sure they do their investment, will do their investment but we have, you know, AT&T is propelling us forward. I think the fact that AT&T is way ahead in their transformation plans compared to other transformation plan – on one hand, you know, it's not a great thing to have in the industry, because ideally, we would see more transformations coming and maturing. But from a competitive landscape, it's the holy grail of implementations.

Whoever is there under virtual stack, is gaining all this expertise, you know, all the innovation that needs to roll out, including all the real-world expertise of all the issues that you face when – primarily when you need to scale these mega implementations, and we're gaining it. And the

feedback that I'm getting from – from existing customers and potential customers is very strong, that they are eager for this expertise, because they're facing, you know, they're either sitting on the bench or facing all these challenges that I'm talking about. And we are taking a position and we've taken that, that our job is to help them in the transformation, because, you know, in our area, because we are participating in this very important AT&T transformation. This is how I think it's all – it all fits together.

Alex Henderson:

So, one more question if I could?

Yaron Ravkaie:

Sure.

Alex Henderson:

If we look at the pipeline of the customers that you're working with – the proof of concepts, you know, the testing in the labs, all of that type of stuff – has your pipeline increased? Is it more robust? Or has it also seen some slowing of the build around, you know, the pace of activity?

Yaron Ravkaie:

So, I'll be – I'll talk a little bit about it. I think overall, it's staying the same, okay? It's getting a little bit – it – and I don't want to use the word a little bit, but it's getting some weakness because the sales cycle is being – it's longer, okay? De facto, okay?

On the flip side, as some opportunities are experiencing a longer sales cycle, hence, you know, they're getting pushed out, et cetera, we're getting new opportunities in the pipeline. And areas where we dropped things in the pipeline are primarily legacy areas, which are less strategic.

We do have in our plan, and I think I've talked about it in the past, and I – in some of the quarters I do talk about it, there – we do have revenue from legacy, which is, customers are still buying it the old fashion way as an appliance. In that industry there is a – if it's like a competitive bid, there is a lot of price pressure in that area, we don't have a huge differentiator when they're only looking at equipment. We do have a big differentiator if they're future proofing their decisions, but not all of them are looking at it that way.

And once in a while we do lose an opportunity, because it's a mature market. So those of this – so, you know, one or two like us disappeared. But overall, I would say that – and want to be a little bit careful so the optics won't be misleading. But I would say that we have solid

opportunities in the pipeline, and we continue to strengthen it, and it's moving to a positive direction. But this is coupled with a longer sales cycle, which will affect, you know, the pace that we can turn these things into POs and revenue.

Alex Henderson:

So, if I were to paraphrase what you said, you've lost a little bit of the momentum in some of the legacy stuff which nobody really cares about, but does impact the numbers a bit?

Yaron Ravkaie:

Yeah.

Alex Henderson:

You've seen some acceleration in the number of proof of concepts or other trial activity, but the timeline for closing deals is stretched a little bit, so there's kind of three factors?

Yaron Ravkaie:

Yeah, yeah.

Alex Henderson:

All right. And I appreciate you answering my questions,

Yaron Ravkaie:

Again, Alex – and, Alex, maybe just to reemphasize, on the competitive landscape and on the situation with the engagement of customers, we continue to get very strong positive feedback from all the customers. This is why we're confident that the direction is okay, even though it's taking more time.

Alex Henderson:

The last piece of it, I don't think you addressed, was, have you seen any bundling impact?

Yaron Ravkaie:

Eh – *[pause]*

Alex Henderson:

5G wins that are bundled?

Yaron Ravkaie:

So, the only ones that can really – look – and the only ones that can really bundle some stuff of the mix, so they can come, so like a company like Ericsson or Nokia, or Huawei can come in and say, okay, I'm giving you 5G, I'll give you the assurance for it. Most of them don't have robust probe-based assurance. So, it might – they might bundle some stuff and might cause, you know, customers to evaluate what type of assurance they want to deploy, things like that. But it's not a direct competition with us.

Alex Henderson:

Yes. But have you seen it impact any of your business, is the question?

Yaron Ravkaie:

It's been impacting of our business always, okay? So, it's not something new. I would say, when they move to LTE, they bundle; when they move to VoLTE, they bundle, you know, the – it's – every time that the – some of these companies, they encounter purchasing – their own purchasing decision, so a communication service provider wants to buy something from them, they usually try to push something. And in some cases, they do bundle something, even though it's not 100% in our space, they do bundle something. And it does cause in our industry – not only for RADCOM, I think – in our industry in general, it does cause the communication service provider to evaluate. But I don't see a new trend, okay, there.

Alex Henderson:

So, the new trend would be that 5G bundling might have an impact on your business, and there's no change in that, is what you're saying?

Yaron Ravkaie:

Yeah, yeah. It's an expected impact, yeah.

Alex Henderson:

Okay, great. Thank you.

Yaron Ravkaie:

Thanks, Alex.

Operator:

If there are any additional questions, please press star-one. If you would like to cancel your request, please press star-two. Please stand by while we poll for more questions. *[pause]* The next question is from Josh Goldberg of G2 Investment Partners. Please go ahead. *[pause]* Josh, please go ahead. *[pause]* The next question is from Guy Ben-Simon of Globes. Please go ahead.

Guy Ben-Simon:

Hi, good afternoon. I want to ask, what about the – what is ... since last September in Philippine, is there news about that?

Yaron Ravkaie:

The – some blog talking about a typhoon?

Guy Ben-Simon:

Yes.

Yaron Ravkaie:

Yeah. So, there's no – I think it's now safe to say that we weren't impacted from any of that, you know. And I think I mentioned on the previous call that I was a little – that we weren't impacted, I was a little cautious, if somebody knows like in the Philippines something that I don't know, but there is zero impact.

Guy Ben-Simon:

So, the reduce in the revenues, just – like what is the main reason, again?

Yaron Ravkaie:

The reason for us why we're reducing the guidance?

Guy Ben-Simon:

Yes.

Yaron Ravkaie:

The pace of transition of customers to NFV is slower than we expected.

Guy Ben-Simon:

Mm-hmm. Okay, thank you.

[pause]

Operator:

As there are no further questions at this time, this concludes the RADCOM Ltd. Company update conference call. You may go ahead and disconnect.

[End of conference call]