Q2-19 Financial results conference call

Management's prepared remarks and Q&A

Aug 12, 2019

Operator:

Ladies and gentlemen, thank you for standing by. Welcome to the RADCOM Ltd. Second Quarter 2019 Results Conference Call. All participants are at present in a listen-only mode. Following Management's formal 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 at www.radcom.com from August 12th, 2019. On the call today is Yaron Ravkaie, RADCOM's CEO, and Amir Hai, RADCOM's CFO.

By now, we assume you have seen the second quarter's results press release, which was issued earlier today. It is available on all the major financial news feeds. Please note that Management has prepared a presentation for your reference that will be used during the call. If you have not downloaded it yet, you may do so through a link on the Investor section of RADCOM's website at www.radcom.com/investor-relations. If you have any trouble, please send Mark Rolston an e-mail at markr@radcom.com, and he will send it to you right away.

Before we begin, I would like to review the Safe Harbor provision. Forward-looking statements in this conference call involve a number of risks and uncertainties, including but not limited to the company's statements about its 2019 revenue and other performance guidance, including statements about anticipated gross margins, statements about the Company's strategy, leadership position, potential sales, pipeline, opportunities, sales cycle or long-term prospects, statements about continued investment in research and development, and statements about the future of NFV, industry trends including 5G deployment, and future plans of industry participants and customers, such as AT&T and Rakuten Mobile and their success in penetrating and disrupting the market. The company does not undertake to update forward-looking statements. The full Safe Harbor provision, including risks that could cause actual results to differ from these forward-looking statements are outlined in the presentation and the company's SEC filings.

In this conference call, Management will be referring to certain non-GAAP financial measures, which are provided to enhance the user's overall understanding of the company's financial performance. By excluding certain non-cash stock-based compensation expenses, non-GAAP results provide information that is useful in assessing RADCOM's core operating performance, and in evaluating and comparing our results of operations consistently from period to period.

The presentation of this additional information is not meant to be considered a substitute for the corresponding financial measures prepared in accordance with Generally Accepted Accounting Principles. Investors are encouraged to review the reconciliations of GAAP to non-GAAP financial measures, which are included in the quarter's earnings release which is available on our website.

I would like to repeat information about the presentation. If you have not downloaded it yet, you may do so through a link on the Investor section of RADCOM's website at www.radcom.com/investor-relations. If you have any trouble, send Mark an e-mail at markr@radcom.com, and he will send it to you directly. 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 are very pleased to have signed a multiyear contract with Rakuten Mobile this quarter, presenting a unique and unparalleled opportunity to be part of the world's first end-to-end fully virtualized mobile network. Rakuten is a global leader with over 70 e-commerce, fintech and content services and more than 1 billion members worldwide. With Rakuten Mobile, they are launching a fourth mobile network in Japan in October.

Our second quarter results already reflect revenue from the Rakuten engagement. With this greenfield network, Rakuten aims to disrupt the mobile industry in Japan by building an innovative, highly automated network that has no legacy limitations or baggage. This cloud-native platform will enable Rakuten to deliver a customer-centric experience to their subscribers, making plans more affordable and allowing Rakuten to automate their operations. Rakuten is taking an end-to-end cloud-based approach that does not include specialized hardware and is 5G-ready from launch. This cloud approach produces dramatic savings in comparison to other operators, due to much lower investment cost. Also, from the outset, Rakuten can take full advantage of the newest and most innovative technology that is 5G-ready, without the need to migrate all the infrastructure.

Rakuten chose RADCOM because of our deep NFV expertise, our ongoing work in partnership with AT&T, and our advanced cloud-native, 5G-ready technology, which allows operators to assure the customer experience in a highly dynamic, virtualized environment from the network edge to the core. Our solution is tightly integrated into Rakuten's cloud to enhance the end-to-end user experience they deliver to their customers, while reducing operational costs. RADCOM is a crucial partner in Rakuten's move into disrupting the mobile market in Japan. Rakuten aims to revolutionize the way a mobile network is operated, by focusing on end-to-end customer-centric indicators rather than just network performance indicators, thus radically improving the overall customer experience. Our business model with Rakuten is recurring in nature, which allows RADCOM to provide on an ongoing basis innovative technology to support Rakuten's mobile launch and ongoing business needs.

Rakuten is a company that innovates rapidly and expects us to do the same. This rapid pace was demonstrated in the short sales cycle in which this contract was completed. As we continue to work with Rakuten, we'll be utilizing all the advantages of a cutting-edge virtual network with very high levels of automation, including machine learning and artificial intelligence capabilities. This agreement adds another anchor client to our roster, which includes AT&T, Globe and other top tier operators.

As we announced in the last quarter with our three-year contract with AT&T, we continue to integrate our solution into their cloud platform, to assure the customer experience for their current and future mobile services. AT&T continues to aggressively move forward with their transition to NFV and the transformation of its network into a software-centric platform. They are turning their network gear into software applications to provide a dynamic platform for the future innovation and the rollout of 5G to both business and consumers.

AT&T has been recognized as the fastest wireless network in recent months. They have accelerated their 5G and fiber build-out with the introduction of their first responder platform.

They now offer 5G service in part of 19 cities in the United States, expected to become the standard throughout the U.S. by 2020.

RADCOM continues to be a key partner to AT&T, providing them ongoing software releases into their cloud, to continually support their journey to virtualization and now 5G. Through our continued work with AT&T and the scale of their network and the amount of traffic they are putting on their virtual technology, coupled with Rakuten's very advanced architecture and fast-paced deployment, we are executing some of the most exciting projects in the industry and continue to gain unparalleled expertise and industry attention. We believe this will have a halo effect on the marketplace.

Operators have been very interested in what AT&T does. And now with Rakuten, there has been an intense level of interest around their strategy and their technology lineup for executing a very aggressive, fully virtualized approach. Rakuten chose the best vendors in each space, and this is another significant proof of our technology and expertise.

As Amir will discuss in detail, revenues for the second quarter were 8.5 million dollars. Considering the relationship with AT&T and the execution of this significant contract with Rakuten and market conditions, we are increasing our revenue guidance to be between 30 and 33 million dollars. With that, I will turn the call over to Amir Hai, our CFO, to discuss the financial results in detail. Amir, please go ahead.

Amir Hai:

Thank you, Yaron, and good morning, everyone. Please turn to Slide 6 for our financial highlights.

To help you understand the results, I will be referring mainly to non-GAAP numbers, which exclude share-based compensation. Revenues for the quarter were 8.5 million dollars, down by 20% year-over-year.

As a reminder, our quarterly revenue can become lumpy due to specific project milestones. Our gross margin for the quarter was 75.6% on a non-GAAP basis. Note that our gross margin can fluctuate depending upon the level of revenues and revenues mix. Our gross R&D for the quarter on a non-GAAP basis increased to 4.4 million dollars from 3.5 million dollars in the second quarter of 2018. This increase relates to headcount growth to support our continual investment in R&D to maintain and extend our technological leadership and capabilities.

Also, during the second quarter, we received 412 thousand dollars from the Israel Innovation Authority, compared to 754 thousand dollars in the second quarter of last 2018. As a result, our R&D for the quarter was 4 million dollars, an increase from 2.8 million dollars in the comparable period last year. Sales and Marketing expenses for the quarter were 2.4 million dollars on a non-GAAP basis, a decrease from 2.8 million – sorry, a decrease from 2.9 million dollars in the second quarter of 2018. G&A expenses for the quarter on a non-GAAP basis totaled 754 thousand dollars compared to 799 thousand dollars in the second quarter of 2018.

Operating loss on a non-GAAP basis for the quarter was 715 thousand dollars compared with an operating profit of 1.4 million dollars for the second quarter of 2018. Net loss for the quarter on a non-GAAP basis was 411 thousand dollars or a loss per share of 3 cents per diluted share, compared to a net income of 1.4 million dollars or 10 cents per diluted shares for the same period last year.

On a GAAP basis, as you can see on Slide 5, we reported a net loss for the quarter of 0.9 million dollars or a loss per share of 7 cents per diluted share, compared to a profit of 757 thousand dollars or 5 cents per diluted share last year.

At the end of the second quarter of 2019, our headcount was 245. We expect our headcount to remain around the current level in the near term. Turning to the balance sheet. As you can see on Slide 9, our cash and cash equivalents and short-term bank deposits at the end of the quarter were 58.6 million dollars. We believe that our healthy cash balance place us on a solid footing to execute on the opportunities in front of us.

That ends our prepared remarks. Yaron and I will turn it back to the Operator and take your questions.

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] The first question is from Alex Henderson of Needham and Company. Please go ahead.

Alexander Henderson:

Thanks, guys. Sorry, there seems to be some static on my line. I don't know if that's me or the conference call. But I was hoping you could give us a little bit of a commentary around 10% customers, and to what extent the Rakuten deal is driven by users, you know, post launch as opposed to initial spend to build the network, and how that contract is set up a little bit. So, can you start off with 10% customers, please?

Yaron Ravkaie:

10% customers, you mean the customers that are above 10% of our revenue mix?

Alexander Henderson:

Yup.

Yaron Ravkaie:

So, you know, we don't disclose specific customers. We're under NDAs with them. AT&T, which we have been updating, continue to be stable, active. We are continuing to give them comprehensive releases.

And we've signed in the beginning of the year a long-term agreement with them which we gave some color on. Others, we haven't disclosed, but, you know, the – basically, there's positive activity with all of them, and, you know, I don't think there is anything, like, problematic with any one of them.

Alexander Henderson:

Well, yeah, just asking how many 10% customers you had. It's not asking for the revenues per customer per se. Just generically, is it the vast majority of revenues coming two companies or is it coming from three or four, five companies? Could you give us a sense of –

Yaron Ravkaie:

The majority of the revenue is coming from AT&T. Rakuten now becomes a major revenue provider. There's a carrier in Asia Pacific which we've disclosed in the past that's another revenue provider. Then there's a couple of mid-size ones, and then there's a longer tail.

Alexander Henderson:

I see. And, relative to the Rakuten transaction, I assumed that there was some upfront investment there to build the network before they actually have revenues that they're kicking off the launch in October. Did you get some CapEx-related revenues, and then it flips to a subscription basis on the number of people who sign up? Or how does the contract work? Could you give us some clarity on it?

Yaron Ravkaie:

Yes. The contract is – can't disclose it accurately, but it's a double-digit multiyear contract. There is a component of a setup, but it's not huge. And the relationship, it's an ongoing quarterly relationship that is, again, meaningful. And it's not dependent on them acquiring subscribers. It's pretty stable, based on just the long-term relationship in the work and the technology work.

And all these contracts have also the potential of upside as two things might occur. One is some additional work that they'll ask us to do. And the second thing, if they launch outside of Japan then – which there are discussions and chatter about that, and then there will be, in that second scenario, significant upside.

Alexander Henderson:

Yaron, I thought I heard you say it was a subscription transaction on the prepared remarks. Am I incorrect in hearing that?

Yaron Ravkaie:

No. That's – I thought that's what I said. Did I say something different?

Alexander Henderson:

Well, if it's subscription, what is that subscription based on? Usually, that's –

Yaron Ravkaie:

Subscription to the software. They subscribe – they don't have, like, a perpetual license.

Alexander Henderson:

I see. So, it's a recurring fixed dollar amount

Yaron Ravkaie:

Yes.

Alexander Henderson:

I see. Okay. Thanks. Can you talk about your pipeline a little bit? I mean, Rakuten is a great deal, but, you know, what have you got going on in the rest of the pipeline?

Yaron Ravkaie:

So, we have an active pipeline. I'm – there are several things that are in the works that – with some ability to mature, you know, even this year. I can't disclose much more than that.

But, you know, there's several opportunities. Some – some of them are at a maturity level that there'll be – we expect something to happen this year.

Alexander Henderson:

Okay. If you were to look out into 2020, do you think that there is enough visibility in the pipeline to get back to a, you know, double-digit growth trajectory? Or do you think that, you know, the

AT&T is fairly flat, Rakuten is pretty well subscribed as is, therefore, it needs additional contracts to provide growth? Or how do we think about the longer term?

Yaron Ravkaie:

First of all, we haven't gone through the planning for next year yet, and it's only August. I would say, at this stage, we will have growth next year.

I think primarily because, you know, AT&T is stable, and Rakuten will only recognize in part of the year, so just inherent in that. That's going to generate growth, assuming the other parts of the business are stable. You know, you couple that with several wins.

I'm not sure we'll reach double digits, but I think we will be able to demonstrate growth next year. If this – if Rakuten halo effect that I'm talking about will pick up, we might see acceleration on that, but it's too early to say, and it's also a little bit too early to say at what pace can they launch beyond, beyond – and, you know, what type of upside can we get on Rakuten.

Alexander Henderson:

Okay. So, one more question, if I could. On the gross margin side, quite a bit of difference between the two quarters. Should we be using kind of the midpoint between the two quarters or the average for the half? Looking out into the back half, how do we think about GM shares?

Yaron Ravkaie:

So, I think, at the end of the day, you can average it.

We are going to have, I think – if you're looking at the – you're doing the math and you're looking at our guidance and looking what we did now, we are going to have a bit of a more loaded tail end for the second part of the year, though we do have some deliverables that are a part of, you know, former contracts that are not 100% software. We do deliver a – servers are part of them, so there will be fluctuations in the next two quarters.

You know, we haven't been measuring it quarter by quarter and updating it quarter by quarter. But on an annual basis, I think you can average them.

Alexander Henderson:

So, something around 73-ish, kind of, for the year then, is that, kind of, the way you're thinking of it?

Amir Hai:

It's between 70 to 75. This is the range...

Yaron Ravkaie:

So, you said 73, it's okay, 72 and a half.

Alexander Henderson:

All right. Okay, great. Thanks. I'll cede the floor.

Operator:

The next question is from Bhavan Suri of William Blair. Please go ahead.

Bhavan Suri:

Hey, gents, let me echo my congrats on a … job. I guess I just want to go back there for one second. You know, I have two questions there.

One, you know, your comment suggested, you know, there might be aggressive rebuilding up in your mobile network. I guess if you were to think about their growth plans, which you may or may not have insight to, but you've got some sense of where they need delivery. Do you think that that, sort of, low double-digit contract length is something that's a two- to three-year plan? Or is that more like a five to ten-year plan? Or do you think that that could be double, triple where it could be in, you know, long term, five, ten years?

Yaron Ravkaie:

The contract that we – so I'm not sure I understand the question. But the contract that we signed with Rakuten, it's for Japan.

Bhavan Suri:

Mm-hmm.

Yaron Ravkaie:

And we know to – for this specific contract, we know to predict for the next several years the revenues. You know, there is upside opportunities on that, like I said, in two dimensions. But what are you asking beyond that?

Bhavan Suri:

I guess, when you look at those dimensions, and you look at the level of contract, so that's to drill into the contract today, that's for Japan. But let's assume they expand. I'm assuming that's not for all the customers in, like, in Japan. I'm just trying to understand, sort of, the vectors of growth for them, and then how you're tied to those vectors of growth.

Yaron Ravkaie:

Ah. In Japan, we have – you know, they gave us a meaningful contract. In Japan, we have the – we are not dependent on their acquisition – our revenue is not dependent on their acquisition of customers.

So, they pay the – what's in the contract no matter how many they acquire. As they potentially launch in other countries, there will be significant upside to this contract, which, you know, will – the way that you need to think about it when you model it is, if they go into, like, a new country, there is an opportunity.

Their strategy will be to copy/paste the stack, okay? So, there will be an opportunity to basically do this type of deal for every country that they go to.

Bhavan Suri:

Got it. Got it, got it. Okay. That's helpful. And then, one more strategic one before we get into some of the more technical things.

You said other carriers, other operators are looking at Rakuten. I guess a little more specifically, have other carriers said that this software-based approach makes sense, or are you seeing new carriers, new potential operators who say, Hey, if Rakuten can do this in a software-based approach with their really small team, we can do this, too, on top of the existing infrastructure. Are those conversations happening? Is this still really early?

Are people still, sort of, watching and wait and see yet? Or is Rakuten at this point viewed somewhat as successful and other people are, sort of, thinking about, maybe in the next, you know, two, three, four years trying to copy it? How should we think about, sort of, what the conversations you're having with people who are sort of watching that model?

Yaron Ravkaie:

Look, it's – I'll give you the color, okay? You can make the – because it's at a cutting edge. So, the color is this. There is a train of visits all the time into Rakuten and all the industry is looking at what they are doing. And that visitation train is comprised of both established carriers that are learning in order to, you know, innovate themselves as well as, you know, companies that are not carriers that are – that as Rakuten, you know, might go into that business, Rakuten is going into that business. So, you see a combination.

It's still – in my opinion, it's still a little early to say, okay? Is this going, you know, is now Amazon going to be a carrier? Or Amazon-like companies, are they going to be a carrier? You know, there has been speculation on that. But, you know, your special – speculation is as good as mine. I think the major point here is that you see a company that hasn't been a carrier at a mega scale, okay? Rakuten is the Amazon of Japan, okay? It's as big, as innovative, and you can read their material.

There's a lot of articles that say that they are more innovative than Amazon. And I, you know, I want to make sure that I do them justice. And the moment that they've now gone into this, it means several things. One, is that they figured out probably an amazing business case. Two, they're utilizing technology. If you look at – if you just, like, do a Google search and you look at even YouTube publications that they put out, they're making a lot of their journey public. You see that they're going to leverage all of their assets in order to capitalize on this investment in mobile. And mobile will become another major asset here, so it's very, very interesting.

On the technology side, it's a proof point. It's a major proof point that, you know, – let's be accurate. They're launching in – they have a network that's up and running but their launch is in October, okay? So, as we follow that launch through, you know, the remainder of the year and as they scale up next year, I think there will be a lot of interest in the industry on how this is working, and how this is going. And I think we're going to see more and more and more innovation and things that will follow. We'll see them from Rakuten, and we'll see how, together, I guess, how it affects the industry. But this is definitely, I think, the most exciting thing that's happening in the industry, from a, you know, from a sea change, that we've seen for a while.

Bhavan Suri:

Got it, got it. It's really helpful. I guess sales cycle will be my next question. You know, Rakuten is an anomaly because, obviously, such a short sale cycle. But you've talked in the past about lengthening sales cycles. And given your commentary about some wins this year, it feels like those are improving. Just some color on what you're seeing in sale cycles, and have they started to improve? Are they stable? Are they still very mixed? Just to get some understanding there. Thank you.

Yaron Ravkaie:

Okay. So Rakuten was a short sale cycle, measured in months, somewhere around three months. I can't say – I can't predict what's going to be, like the telco sales cycle going forward, okay?

It's not a – what I'm seeing is, I'm seeing some increase in activity, I'm saying it carefully. I'm seeing some things that were in the pipeline that are maturing. But it's still early to see, will Rakuten or any other 5G or any other industry, will it create some shortening of the sales cycle.

As I mentioned before also, the fact that there were long sales cycles that we experienced, you know, through the second part of '18 and we've talked about it, at the end of the day, is creating some pinned up demand, okay? The older technology that these carriers are running is becoming obsolete. And whoever has, like, seven-year-old technology, and also five-year technology, starting to break. And this entire industry goes through a refresh cycle.

So, this should also give some – for the regular business, put some, you know, propellants into the mix. When you look at how can this affect us, you know, we are, you know, we hope that – and it, I think in my mind, it makes a lot of sense that these carriers will go to the most advanced software and network architecture that they can, that the mode that they refresh. So that should help us as well.

Bhavan Suri:

Got you, got you, got you. And then, if I go to, my last question, really, around renewals. You have two large renewals coming up in '19, in addition to AT&T, obviously, which is renewed. Just an update on how those renewals are progressing, and how we should – about what level we should expect those contracts to renew, relative to existing levels.

Yaron Ravkaie:

Oh, in '19, only AT&T was up. And we've done it.

Bhavan Suri:

Okay. My mistake. I thought you had two others. Okay. That's all for me, guys. Thanks for taking my questions. And, nice job on Rakuten.

Yaron Ravkaie:

Okay, thanks.

Operator:

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

Josh Goldberg:

Good morning, Yaron, how are you?

Yaron Ravkaie:

Doing good.

Josh Goldberg:

Good. I had a point, just one point to make, that I wanted you to comment on, and then two questions. I guess, the point I wanted to make was that, you know, the fact that you won AT&T, and now Rakuten, you know, I think analysts have a difficult time projecting quarterly numbers, and you're not a quarterly numbers business.

You're a project-driven business. And the fact that you won AT&T three and a half years ago, the biggest NFV rollout in the world, and then three and a half years later, your technology was validated by the most up and coming carrier in the world, with no connections, this is not – you're an Israeli company, you sold into an American telecom, and as well into a Japanese telecom.

One of our contacts to the industry said, any person that wins part of the network business at Rakuten has the best technology in the world in that space. And the fact that you've won that contract three and a half years after your first one, I think validates how strong your business is.

And looking at your company, with a 50-million-dollar valuation and 50 million dollars of cash, maybe people are worrying too much about the quarterly numbers, not looking at this bigger picture, that you've able to win these things. I mean, Yaron, in some ways, you guys are like the New York Yankees. No matter how much you win, you just want more.

Yaron Ravkaie:

So, you know, that's the feeling in the company.

I can tell you that – maybe the way that I'll add to the comment, okay, is that we've just started with Rakuten, okay? And the pace of innovation that we're going to – with AT&T, I touched on it a little bit in the remarks. With AT&T, AT&T chose our technology because it was the best out there. Then we went and started the journey with them and continue to journey with them. And we grew together in our domain. And we created, I think, an unparalleled system and architecture with maturity, with automation, with capabilities, that in our mind is second to none. And this has been continuously validated by AT&T, but also, you know, they're not – they all the time look at the industry.

And now, Rakuten, basically, like you mentioned, is – has chosen, you know, the best of every area in order to go for the most cutting-edge, best-of-breed approach, that is a combination of the technology and also the ability for a company to work with them and innovate. And that combination is, I think, a huge achievement for the company in a very short sale cycle. After – or doing where they looked at the entire industry, and by the way, because of the fact that they're very innovative, they'll not only look directly at, you know, the pro based assurances in the industry, they looked at even, you know, the one or two circles beyond. And when they saw our technology, it was downhill from there, okay? That we – both companies hit it off. We saw that our visions are aligned. We saw that our view of the future is aligned. And then we said, okay, now we can really get deep here and continue this journey. And this journey, when you look at the overall industry – and this is, I think, where investors are wanting to see, you know, what's next, the industry hasn't migrated to NFV yet.

So, it – the change hasn't happened. And we've captured, I think, two amazing assets partners, you know, they're not assets, they're our partners in this journey. And these are the ones that aggressively started. And in our mind, it definitely will have a halo effect. We're already starting to see it. And I think the fact that Rakuten is starting some greenfield and doing everything even in a way that's, I would say, it's more risky than AT&T, and testing out all the new technologies. They are even more relying on our technology because of making sure that everything works for them. But more than that, I think they're going to, very fast, have an impact as big as AT&T had on the industry in maturing the technology so more and more operators can follow. Now, it's – we'll see how the rest unveils. But in RADCOM, we are ultra-excited about how this is panning out, and, you know, that we get to work with the best of the best.

Josh Goldberg:

I guess what I was trying to point out more was that, you know, three and a half years ago, you fired the first shot and every other company in your space from Massachusetts to California, multibillion-dollar companies, had the ability to upgrade and develop products in the last three and a half years, and you've just been validated again that you are the best product.

Yaron Ravkaie:

Yeah.

Josh Goldberg:

That's a huge endorsement.

Yaron Ravkaie:

Yeah, yeah.

Josh Goldberg:

Can you talk a little bit about your cash balance? I know people have talked about passively buying another company, maybe adding on another feature. You're not burning that much cash. Maybe buying back the stock might be a good idea at these levels. Can you just talk a little bit what your mindset is, realistically in the next six months, if you're planning on using the cash for anything?

Yaron Ravkaie:

The cash would primarily be used to maintain a very healthy balance sheet as we continue to go after the top tier, you know, operators of this industry. The industry is, the industry is basically, looks like it – gravitated towards direct relationship with the technology partners. If in the past, you know, large companies would only do business, you know, with the Eric – with the Ness, with the Ericsson's, Huawei's, Nokia's of the world, Cisco's of the world.

Rakuten now is another great example like we talked, and others, I believe, will follow of doing business with companies our size. For that, they, you know, they do want to make sure that we have the long-term viability, which I think we've been demonstrating very nicely, and that's where we're going to make sure that the optics of the balance sheet help us.

Josh Goldberg:

Okay. Have you been building out a team in Japan on the ground like you did at AT&T to help them get through the upgrade cycle and implement your solution?

Yaron Ravkaie:

Yeah. We have a, we have, like, an A team on the ground there. Everything is happening very fast so some of it is being built as we speak. But the model is built on some, I would say, lean presence on the ground there.

Josh Goldberg:

Okay. Any update on anything going on in Europe with some of the tier 1 carriers and, you know, that thing that got delayed a little bit last year?

Yaron Ravkaie:

There's some activity in Europe. But, at this stage, I would say Western Europe is slow. We might see some activity in Eastern Europe, but there's nothing, like, super exciting there.

There is some activity so it might change, but it's not – there's nothing, like, earth shattering, like a, you know, a European Rakuten launching or something like that.

Josh Goldberg:

So, it sounds like you feel a lot more comfortable today than you were even six months ago.

Yaron Ravkaie:

The six months ago, we've basically seen – you know, we have – we've seen – didn't have enough pipeline and we've seen a slowness in the industry. Now Rakuten came in and shuffled all the cards, literally.

So short sales cycle, strong contract, recurring in nature, provides a very significant turf for the company, allows us to continue to, you know, run and innovate together with them, and with AT&T, and, hopefully, with others. They'll be a great reference.

They're very vocal, and I think they'll have a great impact.

Josh Goldberg:

As a long-term investor, thanks for all your hard work. Thank you so much.

Yaron Ravkaie:

Thanks, Josh.

Operator:

We have a follow-up question from Alex Henderson of Needham & Company. Please go ahead.

Alexander Henderson:

Yeah, just along the same lines of discussion. You had some discussion around a U.S. tier 1 service provider that was out last year. That seems to have stalled a little bit. Can you remind us where that is, and, you know, what's going on with that second customer in the U.S.?

Yaron Ravkaie:

They're stalled. Their spend, I would say, on NFV is under review, and the relationship is good, and our system is installed there. So we expect that as things start to pick up midterm, I would make the best estimate, then we can see them contributing, you know, more to revenues.

They're contributing a little bit to revenues now, but not so much. But it's primarily due to them rethinking their rollout plans in NFV, in 5G and a lot of change in the, you know, in the leadership of their company, et cetera.

Alexander Henderson:

So, can you address this one conundrum for me? So, as I understand it, you really can't roll out 5G without NFV virtualization, yet the market for NFV virtualization seems to have stalled, but the rollout of 5G seems to be getting plenty of press. So how do I reconcile those two data points?

Yaron Ravkaie:

So, you know, there's – it's more complicated than just a sentence.

So, I'll explain it in a way that a lot of these short-term 5G launches are done on a 4G architecture. So, when people say and you hear and you will read articles that 5G is dependent on NFV, it's more the midterm, longer-term 5G. Primarily, when they start to look at upgrading the core to a 5G core. That, you know, the chatter about it is 2020 and beyond. So, no one need to boost up 5G.

Alexander Henderson:

But what does it take to get to that point? Is it that they have to be doing network slicing, or they have to do, you know, high-broadband, high-bandwidth, you know, commitments to customers? What are the hurdles that require them to move off the 4G historical LTE backbone to a 5G architecture for their backbone as opposed to just simply putting 5G radios in the tower and leaving everything behind it as it had previously been?

Yaron Ravkaie:

No, it's a further – there are several things, okay? There are discussions around, like you mentioned, network slicing. There is a discussion around stand-alone 5G.

So, offerings that they're going to do, like, you know, a fixed broadband through mobile technology, so offer that to businesses. They might do some of its short term, but when they look at longer-term rolling this out in scale, they will want to upgrade their core. And at the end of the day, you know, the growth that they'll have on the 5G, they'll want to do on a modern core, not on – the LTE cores are, you know, are becoming old cores.

So, they won't want to do expansion on their core. So, as traffic grows on the mobile network, they'll do the growth on the next-gen core. But the industry needs to mature that next-gen core. There is a race that's happening. I don't think it's a long-term, you know, five years out race, but it's something that's going to impact more next year and the year after.

Alexander Henderson:

One last question, then I'll cede the floor. The shekel is hitting, I think, 18-month highs. So, can you remind me how you – whether you guys hedge, or whether that's, you know, something that's going to impact your OpEx over the next six months? How do we think about that?

Amir Hai:

Well, we are doing a short-term hedge. We're not one – we are doing hedge for one month, two months ahead. For longer term, we're not – we don't have the policy to hedge for this longer term. When you look historically, and we analyze if we hedge or not hedge, I think the effect was the same.

So, right now, I think, when you look at the shekel's rate compared to the dollar, that's 2% down from the average for the first half a year of '19 – sorry, for 2019. So, I think this will be at the same level. This was to … later.

Alexander Henderson:

Okay, thanks.

Operator:

There are no further questions at this time. This concludes the Radcom Ltd. second quarter 2019 results conference call. Thank you for your participation. You may go ahead and disconnect.

[End of conference call]