



Casa Systems Q2'21 Earnings Call Transcript July 29, 2021 5pm EDT

[Operator Instructions]

Jackie Marcus, Investor Relations

Thank you, operator, and good afternoon, everyone. Casa Systems released results for the second quarter of 2021 ended June 30th, 2021, this afternoon after the market close. If you did not receive a copy of our earnings press release, you may obtain it from the Investor Relations section of our website at investors.casasystems.com.

With me on today's call are Jerry Guo, Chief Executive Officer, and Scott Bruckner, Chief Financial Officer. This call is being webcasted and will be archived on the Investor Relations section of our website. Before I turn the call over to Jerry, I'd like to note that today's discussion will contain forward-looking statements based on the business environment as we currently see it and as such, does include certain risks and uncertainties. Please refer to our press release and our SEC filings for more information on the specific risk factors that could cause our actual results to differ materially from the projections described in today's discussion.

Any forward-looking statements that we make on this call or in the earnings release are based upon information that we believe as of today, and we undertake no obligation to update these statements as a result of new information or future events. In addition to U.S. GAAP reporting, we report certain financial measures that do not conform to generally accepted accounting principles. During the call, we may use non-GAAP measures if we believe it is useful to investors or we believe it will help investors better understand our performance or business trends.

And with that, I'd like to turn the call over to Jerry. Jerry?



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Jerry Guo, Chief Executive Officer of Casa Systems

Good afternoon, everyone. Thank you for joining us today as we discuss our second-quarter results.

I'm pleased to report that Q2 was another growth quarter for Casa Systems.

Here are some of the highlights:

- 11% topline growth year-over-year;
- 111% year-over-year wireless revenue growth with continued strong momentum in all our wireless products;
- A 63% year-over-year increase in our wireless backlog, which now stands at over \$139 million;
- 56% of total revenue in the quarter from our wireless and fixed telco products...this makes four consecutive quarters of our new product offerings comprising over half of our revenue; and,
- Numerous customer advances with our strategic growth products that show growing demand for our products.
- Here are the numbers for quarter:
 - 11 new purchase orders for DAA and virtual CCAP;
 - 15 purchase orders for our wireless cores, radios, and FWA products... and an increase in our wireless customer count to 41 from 32 in the previous quarter; and,
 - 9 new purchase orders for our virtual router and fiber extension products.

Before I review our second quarter performance, I would like to comment on the ongoing supply chain situation. As you know, our business relies on sales of both software and hardware products. While our software products remain unaffected, we are seeing component shortages for our hardware products. During the first half of the year, we were



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able to take measures that minimized the impact of these shortages on our business. You can see this in our strong results for the two quarters. However, since the end of Q2 the situation has continued to worsen. As a result, we are seeing component lead times extending further, and order delivery schedules increasingly being pushed out into the first half of 2022. As of today, given the contribution of software to our business, I believe that we remain on track to meet our full-year guidance. And, as our large backlog demonstrates, we are continuing to benefit from strong demand that is driving our growth. However, while we view the supply chain issues as transitory, I would like to note that if the supply chain situation continues to deteriorate, our fiscal 2021 results could be adversely impacted.

With that said, let's turn to our Q2 performance.

Total revenue for the quarter came in at \$92.7 million...that's up 11% year-over-year. And if we look at our first half performance, revenue was up 18% year-over-year. To put these numbers in perspective, as of June 30th, we have delivered 45% of our fiscal 2021 revenue guidance...this is ahead of our initial expectations of 40%. And...we delivered this performance profitably... Q2 adjusted EBITDA was \$11.7 million...up 25% year-over-year...and the first half adjusted EBITDA was \$31.9 million...that's up 145% over the first half of 2020.

Turning now to our product areas and starting with wireless. We saw significant progress in our wireless business in the second quarter. Not only was wireless revenue up by 111% year-over-year, but we continued to receive meaningful industry and customer recognition for our differentiated cloud native 5G standalone core, and our industry leading 5G millimeter wave fixed wireless access products.

To name a few:



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- On 5G millimeter wave, using our AurusAI device, Optus in Australia set a world record with a single user reaching peak speeds of *over 5 gigabits per second* using a 5G fixed wireless connection. This is now the 4th world record for fixed wireless that demonstrates the power of fixed wireless as a broadband access technology...and I'm proud to say that each of these world records relied on Casa's 5G fixed wireless access devices.
- On our 5G core, we now have several deployments and multiple strong performances including:
 - Red Hat naming Casa as partner of the year after deploying our 5G converged core on its industry-leading Kubernetes platform, OpenShift
 - Orange announcing Europe's first 5G Standalone end-to-end cloud network, that featured Casa's cloud native 5G SA Core
 - And, working with Intel and Red Hat, we unveiled our private 5G multi-access network solution that will allow service providers and enterprises to deploy personalized and private networks with higher levels of security, application customization, and differentiated performance
 - These are in addition to the deployments of our 5G SA core by Google and Amazon Web Services that I noted last quarter.

Truly a great quarter for our wireless products!

Ok...moving on to Fixed Telco. Fixed telco revenue was \$17.2 million. This is down 29% year-over-year...but is up around 4% sequentially. As I mentioned last quarter, the lumpiness we are seeing in our fixed telco revenue has been due to product and customer concentration. I also noted that we are making progress in reducing this concentration. This segment is again gaining traction and is ramping well. For reference, we are seeing increased demand for fixed telco...and this is evident in the 9 purchase orders we received in the quarter for our virtual BNG router and fiber extension products.



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Finally, let's turn to cable. As expected, cable was steady in the quarter, with revenue of \$40.5 million. While this is within the \$40 to \$50 million range we have seen for the last nine quarters, in Q2 we had several qualitative advancements with our cable products. First, we expanded our footprint by taking share for some of our competitors. Second, we saw an acceleration in virtual CCAP license and node spend by some of our MSO customers. While we still believe that virtual CCAP and DAA spend will ramp up gradually, this is clearly a very positive sign that cable operators are more ready to make network infrastructure upgrade decisions.

Before I turn the call over to Scott to walk through our financials in detail, I would like to reiterate that I am very pleased with our progress year-to-date. We delivered growth. We did so profitably. And we made meaningful progress with our next-gen infrastructure products. For the remainder of the year, as we continue to grapple with supply shortages impacting our hardware products, I do see an important opportunity for us to continue to grow our software revenue. With that said, I'd like to turn the call over to Scott. Scott?

Scott Bruckner, Chief Financial Officer

Thank you, Jerry. Good afternoon, everyone.

Just to build on Jerry's remarks...I'm really very pleased with our second quarter results. In addition to the business achievements that Jerry noted in all our product areas, we delivered year-over-year growth in revenue, EBITDA and operating profit. And we ended the quarter with a strong balance sheet, enhanced liquidity, and lower leverage. These are great results.

Ok...let's look at these results in detail.

Revenue for the second quarter came in at \$92.7 million. Breaking this down across our product lines:



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- In the second quarter wireless revenue, including services, was \$35 million, or 38% of total revenue. And as Jerry mentioned, this was a significant increase of 111% over the second quarter of 2020.
- Cable revenue, including services, was \$40.5 million, or 44% of total revenue in the quarter.
- And our fixed telco revenue came in at \$17.2 million, or 18.5% of total revenue.

Moving down the income statement –

GAAP gross profit for the quarter came in at \$45.5 million...that's up 5.5% year-over-year. GAAP gross margin in Q2 was 49.1% ...but for the first half of 2021 it was 51.5%. Just a quick note on GAAP gross margin in the second quarter...the 49% margin was driven by product mix...we saw larger than expected shipments of wireless CPE from customers who were building up inventory to mitigate any impact from component shortages on their product rollout schedules.

Turning to GAAP operating expenses...OpEx for the quarter was relatively flat year-over-year at \$41.9 million, and this represented 45.2% of revenue, and this compares quite favorably to OpEx of 50.1% of revenue in the same quarter of 2020. And this quarter we did see higher headcount and higher stock-based compensation expenses as compared to second quarter of 2020...but these costs were offset by a payroll tax benefit of \$2.4 million. You may recall that we also saw this benefit in the first quarter of 2021. The benefit was from a CARES Act provision that unfortunately ceased when the federal government lifted COVID restrictions in the second quarter. So, I don't expect to see this benefit in the second half of the year. And as a result, quarterly GAAP OpEx from the remainder of the year will likely be between \$45 million and \$47 million.



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Adjusted EBITDA for the quarter was \$11.7 million, or 12.7% of revenue...and this is up 25% from the second quarter of 2020. If we look at our results for the first half of the year, adjusted EBITDA was \$31.9 million, or 16.2% of revenue...that's up 145% year-over-year. GAAP operating profit was \$3.6 million in Q2, which is up 173% from the prior year quarter. On a non-GAAP basis, operating profit was \$9.2 million, which increased 45% relative to the second quarter of 2020. After interest and other expenses, and a provision for tax in the quarter of \$3.2 million, we did have a GAAP net loss in the second quarter of \$3.2 million, or negative four cents per share on a fully diluted basis. Non-GAAP net income, however, came in at just under \$1 million, or one cent per fully diluted share.

Let me now turn to our balance sheet. We ended the quarter in a very strong liquidity position with a 20% year-over-year increase in our working capital. Looking at working capital, at quarter end, we had we had \$169.7 million in cash and that includes \$1 million of restricted cash...net receivables of \$65.6 million... inventory of \$95.8 million...and payables of \$26.3 million. Now our cash balance was up 16.2% sequentially and was driven primarily by AR collections in the quarter. Finally, as I've mentioned for several quarters in a row, our receivables agings remain very strong with less than 1% at greater than 90 days.

Let's look at our debt.

At the end of the quarter, gross debt was \$286.2 million...and that's down from \$293.8 million at the end of Q1 of this year. Our gross debt is comprised of \$279.7 million from our Term Loan B and \$6.5 million from our revolver. Gross leverage currently stands at 3.86x LTM EBITDA of \$74.2 million...and with net debt at \$116.5 million, net leverage is now just under 1.6x last twelve months' EBITDA. The reduction in total debt was mostly due to an excess cash flow payment we made in Q2 against our Term Loan B principal balance.

Before opening the call to questions I'd like to mention a couple of things. Despite the issues we've seen in our supply chain, we had a strong second quarter and strong first half



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of 2021. We've already delivered 45% of our revenue guidance for the full year, and as Jerry mentioned, this puts us ahead of our initial expectations for the year. However, as Jerry noted, for the next few quarters our focus will be on working through the supply chain situation, which as you know everyone in our industry is facing, in order to minimize the impact it may have on our business...As we do this...and this is the final thing that I want to leave you with... our company has never been stronger...in spite of the industry-wide disruption, we've seen growing demand for our products, as our large backlog demonstrates...and we have a very strong balance sheet that we have been leveraging (and will continue to leverage) as needed to procure inventory for the long-lead orders in our large backlog.

Ok...with that said, we will turn it back over to the operator for Q&A. Operator?

[Operator Instructions]

Question & Answer

Operator

Our first question comes from Meta Marshall with Morgan Stanley.

Dave Nwokonko, Morgan Stanley

This is Dave Nwokonko on for Meta Marshall. So, Crown Castle mentioned a slowdown in small cell deployments to make room for macro deployments. Are you seeing any pause in small cell deployments due to just the ability to allocate labor? Are there any changes to expectations on the cable side of the business?

Jerry Guo Founder, Chief Executive Officer of Casa Systems

Dave, let me answer that question. We continue to see demand for small cells. Of course, the deployment speed could be impacted by the component situation, and we're watching

it basically closely. As to cable, we continue to be cautious about the short term, but we do see positive signs, it may improve.

Scott Bruckner, Chief Financial Officer

I would just add one very quick thing to that on the small cell side, just to amplify Jerry's point. So, while we think the deployments could potentially be impacted by the supply chain situation. What we are not seeing is a slowdown in demand. And in fact, that's evident in the growth that we've seen in our wireless business and, in the quarterly growth in our bookings in wireless. So, our customers continue to order, our customers continue to plan for deployment, and everyone's just grappling with what the supply side is throwing at us.

Operator

Our next question comes from Tim Savageaux with Northland Capital Markets.

Tim Savageaux, Northland Capital Markets

A couple of questions on the wireless side as well. You mentioned strong kind of order dynamics. So that it looks like the backlog did come down a bit. I wonder if you could talk about the dynamics there. You also mentioned maybe some pull-ins of some wireless CPE products. Backing up to a higher level, with Ericsson and Nokia over the last couple of weeks, a pretty significantly increasing their estimate of radio access network growth this year, principally driven by 5G. What sort of impact do those or more optimistic views that the market have on Casa?

Jerry Guo, Chief Executive Officer of Casa Systems

Tim, we delivered \$92.7 million in products last quarter. And you see that significant part is wireless. We replenished the backlog with new orders. So, we still have a very strong backlog after the delivery of the wireless due to the new demand. And at the same time, we have 3 categories wireless products, the core, the CPE, and the small cells. And we don't

necessarily overlap with Nokia in all the categories. So, I wouldn't take that as a positive or negative from one vendor's view.

Tim Savageaux, Northland Capital Markets

Okay, great. If I could follow up on the cable side. You'd mentioned a pretty good number of POs in the virtualized CCAP and remote PHY space. I wonder if you could characterize those. You've got any significant deployments, are there a relatively kind of initial deployments that are small. How does that compare to what you've seen in the past in terms of activity? I know you had one big order a while back, but is it more broad-based at this point? Would you say in terms of the operator movement toward virtualized CCAP and remote PHY? Do you expect that to be an important factor in your second half?

Jerry Guo, Chief Executive Officer of Casa Systems

I would characterize that more broad-based. We have POs from both Tier 1 operators as well as smaller operators. So, it is more broad-based. The deployment pace is still relatively slow, both impacted by, of course, the gradual ramp of DAA architecture as well as partly by supply chain.

Operator

Our next question comes from Simon Leopold with Raymond James.

Simon Leopold, Raymond James & Associates, Inc.

I wanted to see if you could talk a little bit about your expectations for mix. I'm looking for insight in two dimensions. One, is just your sense of how mix will end up for the full year in your reported segments? The other one is, given what you've talked about in terms of supply chain constraints versus software, it feels like maybe you should see a little bit of a gross margin tailwind in the second half of the year, software is a bigger part of the mix than your original expectations? Then I've got a follow-up.



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Jerry Guo Chief Executive Officer of Casa Systems

Simon, on the mix, we continue to see wireless to be a big component to our second half. Our gross margins, as you actually noted, that's very much impacted by the product mix. We continue to try to ship both the software and hardware, we still cannot be certain what the mix is at this point yet.

Simon Leopold, Raymond James & Associates, Inc.

In terms of the supply chain constraints, in general, we hear a lot about semiconductor. So that feels sort of known. Just wondering whether there are other constraints that you think are worthy of highlighting or if that's really the primary issue for you?

Jerry Guo Chief Executive Officer of Casa Systems

Mostly the semiconductors.

Simon Leopold, Raymond James & Associates, Inc.

If you could give us an update on your thoughts regarding government stimulus programs, both add up here as well as other opportunities abroad. How are you thinking about that layering into the business, and at what point?

Jerry Guo Chief Executive Officer of Casa Systems

Yes, we continue to be encouraged by that government programs. We are engaged with quite a few customers which are in that program. We still cannot quantify that yet.

Operator

Our next question comes from John Marchetti with Stifel.

Jim Berents, Stifel

This is Jim Berents on for John. I wanted to go back to the wireless backlog comment where it fell a little bit sequentially. You guys had some pretty good customer adds net on the

quarter. Is that indicative that maybe some of these newer customers are still earlier, say, more trial size orders and haven't really ramped yet? Kind of along that, what these customer additions just if you could give us sort of a breakdown of by geography where you saw the most interest?

Jerry Guo Founder, Chief Executive Officer of Casa Systems

Yes, our wireless backlog consists of both volume products like production, ongoing production delivery as well as orders as well as early phases of new customers. So, because you saw the numbers, so it's a pretty large number of customers. So, there's a spectrum of those things. We do expect the order continues to grow.

Scott Bruckner, Chief Financial Officer

I would just add one more comment to that. As Jerry said, the size of the backlog moves around. The order volume fluctuates from quarter-to-quarter. I do want to point out that we saw a very significant jump from the fourth quarter to the first quarter of last year. If you remember, that's when the news about supply chain disruptions really started resonating through our industry. So, a lot of our customers jumped up to start ordering, and, on the CPE side of the business, products to ensure that they could meet their product rollout schedules. So, we saw that very first bump from Q4 to Q1. We also saw some very nice bookings between the first quarter and the second quarter, and we do expect that backlog to grow through the year.

Jim Berents Stifel

Great, and then could you talk to about the sort of the geographic mix of your new wireless customers in the quarter.



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Scott Bruckner, Chief Financial Officer

Yes, so it was global. What we see is North America moving more aggressively, but other regions also. We're also seeing traction in other regions as well. So North America was the largest in the quarter for wireless.

Operator

Thank you. There are no further questions at this time. I would like to turn the floor back over to Jerry Guo for any closing comments.

Jerry Guo, Chief Executive Officer of Casa Systems

Thank you everyone for joining us today. Before ending the call, I want to remind everyone that Casa Systems will be hosting an investor day later this fall. We have changed the timing of the event from September to November because of what is turning out to be a very busy period for investors in September with other scheduled events. Please look for a press release with more details on the event in the coming months. We appreciate you joining us today and look forward to sharing our progress next quarter. Thank you.

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