



Operator

Greetings, and welcome to Casa Systems third-quarter 2022 earnings call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press *0 on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host Dennis Daly, Director of Corporate Development and Investor Relations. Please go ahead.

Dennis Daly, Director of Corporate Development & Investor Relations

Thank you, operator, and good afternoon, everyone. Casa Systems released results for the third-quarter fiscal year 2022 ended September 30, 2022, this afternoon after the market closed. 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.casa-systems.com.

With me on today's call are Jerry Guo, our Chief Executive Officer, and Ed Durkin, our Chief Financial Officer. This call is being webcast 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 it 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 on information we believe as of today and 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 believe it will be helpful to investors to better understand our performance or business trends.

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

Jerry Guo, Chief Executive Officer of Casa Systems

Thank you, Dennis. Good afternoon and thank you all for joining Casa's third-quarter fiscal 2022 earnings call. The first nine months of 2022 have been critical in customer validation of Casa as the leading provider of cloud-native core software for wireless and the wireline networks, and in laying the foundation for growth in our physical broadband technology solutions.

Our recent customer engagements continue to highlight our progress, and there are some examples I would offer. Within our cloud software product group, we continue to make tremendous progress with our cloud-native 5G core since the announcement of the \$140 million TCV multiyear license and contract of our cloud-native 5G core for consumer networks, and the \$40 million strategic equity investment from Verizon in April.

We announced a partnership with the Google Cloud in August and have been jointly working on multiple customer projects which I will discuss in greater detail shortly. There are many other customer and partner projects being actively worked, and the Verizon and Google Cloud public news is great validation of our differentiated and our truly cloud-native software. We expect to be able to announce additional customer and partner successes for our cloud-native software offerings in the coming months.



Within our cable product group, progress here is evidenced by our increased cable revenues in Q3 2022, despite continuous supply chain challenges. And we expect continued sequential improvement in revenue in Q4 from the shipment of backlog cable orders and the new cable deals. We continue to expand our virtual CCAP core and remote PHY node deployments with the leading MSOs both in North America and in internationally. But overall, 2022 has continued to be a low spent year for most of our cable MSO customer base.

However, we expect significant changes in cable broadband spend in the coming year, and we are laying the foundation for growth in 2023, by working with MSOs worldwide with our leading next-generation technologies in all distributed product categories, including virtual CCAP core and remote PHY, FMA manager and in remote MACPHY. I will discuss our pipelines in more detail later.

Within our CAD product group as discussed on our August earnings call, we have worked hard to cultivate new major customer relationships with the major telco operators in North America, as well as the new customers and distributors in Europe, and have closed large orders in Q2 and Q3 with these new customers and partners. This now provides us good line of sight to improve CAD results in 2023, given the backlog orders we have from these new customers which are now slated for delivery in 2023.

Within our small cell RAN product group, as we also discussed on our own August earnings call, we announced new RAN contracts with a major North American mobile network operator in August. We expect to close more radio deals with a major mobile network operator soon, and we expect radio access network revenue to grow significantly and contribute nicely in 2023, based on the progress we have made during 2022.

In summary, while the progress is not reflected in our topline GAAP revenue results yet, our strategy of investing heavily in R&D and delivering market-leading innovative products for our customers across all of our product groups in order to help our



customers expand their networks and maximize their capabilities positions us well for renewed growth in 2023 and beyond.

Despite this progress and increasing demand for our products, our financial performance in the quarter does not reflect our potential or our expectations for Casa going forward, and we continue to work hard to overcome the issues impacting our financial performance. In particular, we experience continued challenges from our supply chain partners in Asia and sub chip availability issues, which limited our ability to ship products to customers.

As a result of these supply chain issues and a few other factors, revenue for the quarter was \$66.9 million, which is down 6% from the prior quarter. While we experienced a decline in revenue from our wireless and the fixed telco segments, we did see a 20% improvement in our cable revenue compared to Q2 2022, due to an uptick in demand from our existing customers. And we expect this positive momentum for cable to continue in Q4 and into 2023.

Ed will cover the Q3 financials in more detail in his section, including gross margins, operating expenses, and balance sheet metrics. And we are pleased to take questions on these actual retrospective financial results. As I look forward, I do believe growth in both top lines and bottom lines is ahead across all product groups, as we execute on our strategy and complete our transformation, with my belief rooted in the following: Cloud software product group. Our cloud software product group includes our cloud-native 5G core software and our virtual BNG routing software. As I mentioned, we have the great Verizon \$140 million TCV license and deal for our 5G core software for consumer networks. We are on track with our development deliverables under this agreement. Verizon paid us \$20 million in licensing fees in Q3 2022, and we have another \$120 million to bill in increments of \$24 million per year, and that is a great foundation to build on.

As communication service providers continue to transform their wireless and wireline networks using cloud-native technologies, we are providing them with options to build



their 5G core functions and BNG functions over private clouds or public clouds. Our new Google Cloud partnership announced in late August is a public cloud or hybrid cloud option that is progressing well, and we are actively working with the Google Cloud on joined customer engagements. And we expect to be able to announce a few wins in the coming months.

We have great interest from our other cloud providers and system integrators to work with us on both consumer public networks and mobile private networks. After evaluating and integrating our software, our partners have determined that it is indeed truly cloud-native and able to seamlessly integrate it with their cloud platforms. This seamless integration of Casa's cloud-native 5G core functions with the cloud platforms will enable communication service providers to realize the value of 5G: fast and flexible deployment of new services, fast reconfiguration and slicing of networks, automated operations, and secure, reliable, and resilient networks. Finally, we are seeing strong demand for our virtual BNG router product line on both private cloud and the public cloud as well, which should contribute to 2023 results.

On cable product group, as I mentioned earlier, there was continued pause in cable spend in 2022, as cable MSOs evaluated future product technical directions, remote PHY or remote MAXPHY, as you may have seen in recent press articles. Several of the largest MSOs made their technology direction decisions and are moving forward with RFPs and spending plans for 2023 and beyond. We believe that there are only two virtual CCAP cores deployed in live networks today, and Casa has one of them. Virtual CCAP core is the key to next-generation cable broadband upgrade, and Casa has the leading technology in virtual CCAP core, as well as in remote PHY nodes.

In this regard and with the exception of Comcast, we are working closely with every other cable operator now. Based on our extensive customer engagement, we believe we are well-positioned to compete for what we believe is a coming wave of renewed cable network upgrade and capital spend and have a complete product portfolio ready today to meet whatever product, technical direction, that cable MSOs would like to proceed with. Based on the engagement that we have with the leading MSOs, including



live evaluation -- live evaluation and a few trials of our virtual CCAP core and our remote PHY nodes, we have built a very strong sales pipeline of large cable deals we expect to close in the near future.

The recent decisions of several large MSOs to go with the virtual CCAP core and the remote PHY position us very well to capitalize on upcoming increasing capital in cable MSO Capex spend. Just like the virtual CCAP core and the remote PHY, Casa is also leading in remote MACPHY node technology and FMA manager. This gives us a complete cable product portfolio ready today to meet any direction that cable MSOs want to go.

Access devices product group. As mentioned in our earlier calls, our 2022 CAD results were impacted by a product end-of-life decision in 2021, with one large CSP, where that CSP did some final sizable product buys in 2021. This was a significant component of 2021 CAD revenues that did not repeat in 2022. This did impact CAD results in the first nine months of 2022, as well as for the three months ended September 30, 2022, as compared to Q3 2021.

This 2021 end-of-life matter also masked the great progress we made cultivating new customer and partner relationships in North America and Europe for our fiber extension and fixed wireless access products. I believe we have made good progress backfilling this 2021 CSP end-of-life matter, and this will be evident in the expected renewed growth in our CAD product groups in 2023.

Radio access network product group. Finally, as to radio. We've invested in our small cell radio R&D over the last few years and have proven products that have been deployed today. We now have 5G small cell supply contract with a Tier 1 CSP for product delivery in 2023. We expect to close additional RAN contracts with other Tier 1 mobile network operators soon. Given the strong interest we have seen in 5G small cells in the last few months, we expect our small cell radio to have significant revenue growth in 2023.



In summary, I expect we'll see topline growth across all product groups in 2023, based on the visibility I have today. While we are not prepared to provide 2023 guidance at this time, we will provide 2023 annual guidance after we complete our 2023 operating and financial plan.

Finally, as mentioned in our press release, our board authorized us to buy back \$50 million of our existing debt as part of our plan to delever. We are pleased to report that we purchased and retired approximately \$40 million of debt this week. Implicit in this debt retirement is our confidence in renewed topline growth and improved financial results coming in 2023. Ed will provide more details in his commentary on this transaction, as well as progress and plans to refinance our remaining term loan B debt which matures in December 2023.

Before I turn the call over to Ed, I want to spend a few moments addressing the supply chain headwinds that continue to hinder our ability to ship completed products to customers briefly. We continue to work closely with our key chip suppliers, and we are seeing an improvement in supply from these partners. We are hopeful there will be fewer COVID-related disruptions and closures within our Southeast Asia partners in the coming months, and we are aggressively working on our contingency plans to ensure we can meet demand.

We have seen the lead times for certain components slowly get better over the past couple quarters, and we are optimistic that this trend will continue over the next couple quarters. As I noted in our Q2 call, which I believe still is correct today, these issues will begin to abate in 2023. Finally, we are working closely with our vendors, partners, and customers to manage inflationary pressures and control costs.

In conclusion, Casa is at a critical inflection point in our transformation. We are partnering with the right partners across all product groups, accessing new markets around the world, and strategically investing in our R&D capabilities. I strongly believe we are setting the stage for improved performance and long-term sustainable growth moving forward.



I'd now like to turn the call over to Ed to review the financials. Ed?

Ed Durkin, Chief Financial Officer

Okay. Great CEO overview and thanks, Jerry; and good afternoon, everyone, and thanks for joining us today. I'll keep my prefacing comments short, as Jerry covered things very well in his opening remarks. I'd first like to reiterate the Verizon license deal for our cloud-native 5G standalone MAC software is continuing to progress as planned, and that's evidenced by the \$20 million in licensing fees they paid us in Q3 2022.

And I do think it's very safe to say the whole Casa team is excited about the further progress we've made with our multiyear transformation towards software and cloud, as evidenced first by the strategic Verizon deal we announced in April, and then further validated by the late August 2022 announcement of our strategic partnership with Google Cloud, which is also going really well. And I think it's safe to say we are really excited about really the considerable opportunities that lie ahead for Casa across all of our product groups -- that's cable, CAD, cloud and RAN -- and as Jerry said, do look forward to improved results in 2023.

So, with those prefacing comments done, I'd like to get into the details for the quarter ending 9-30-2022. Revenues for the quarter came in at \$66.9 million, with Q3 revenues impacted by ongoing supply chain issues as well as some delays, not losses, in cable deals which we expect to close in Q4 or early 2023.

Breaking down the revenue results across product lines, third-quarter wireless revenue was \$21.4 million, down 25% from Q2 2022. This decline is due to continued supply chain matters as backlog remains strong for our wireless access device hardware products.

On the cable side, cable revenues came in at \$30.2 million, a 20% increase over the prior quarter. The increase in cable revenue was driven by renewed demand from our



cable customers. We actually believe this positive cable momentum is going to continue into Q4 and further into 2023, for the reasons Jerry cited, including some recent decisions by some major cable MSOs on their technical direction, which should serve us really well. And growth in our sales pipeline for cable deals, you know, the vast majority of which are with our large global cable customer install base, which are inherently lower risk deals than new logo pipeline opportunities.

Moving to fixed telco revenues which includes our virtual BNG router and our fixed wireless access device hybrid products, revenues here came in at \$15.3 million, an 11% decline from Q2 2022; again, as a result of supply chain matters. And finally, during Q3 2022, we had approximately \$7 million in backlog orders that we were unable to ship for revenue recognition due to supply chain delays. And as we exit the quarter, our total backlog deferred revenue on the balance sheet and remaining \$120 million of future billings under the Verizon contract, you know, approximately \$330 million.

And then regarding backlog and to put a finer point on this, if you exclude the \$120 million of future Verizon billings which are scheduled to be billed in increments of about \$24 million per year over the next five years as we deliver and acceptance occurs, we believe a significant majority of the remaining backlog will ship for revenue in 2023; again, obviously assuming no unanticipated deterioration in supply-chain commitments that occur in the future.

So moving off of revenue and on to gross profit, GAAP gross profit for the quarter came in at \$14.4 million. It's important to note that that includes a warranty settlement accrual of \$12.9 million recorded within cost of revenue, given it's related to a warranty matter. And that's related to the customer matter disclosed in our second-quarter 10-Q; and we also had modestly increased inventory surcharges of \$1.7 million that go into cost of revenue. And on a pro forma basis when you exclude those two charges in Q3, gross margins would have been \$29.1 million or approximately 43% of revenue.



And finally on gross margins, I would say we do expect that we'll see improved gross margins alongside a better mix of higher-margin cable, RAN and software revenue going forward, which is good.

Turning to operating expenses, Q3 GAAP operating expenses were \$44.5 million and in line with prior quarters. I think it's important to recognize we continue to invest in product offerings across all product groups, and that's important to note as it positions us well for this renewed growth in 2023. And to this point and as Jerry mentioned, within our cable product group, we are really only one of two providers globally that offers a ready for prime time virtual CCAP core solution, and demand for this is growing fast, as Jerry mentioned. And we are engaged with every major cable MSO globally, other than Comcast, on opportunities for our cable product suite.

And within cloud, we know we have a differentiated truly cloud-native offering, as validated by Verizon and GCP, and we have many other ecosystem partners: cloud providers, SIs, large-cap tech companies, very interested in working with Casa on our cloud offerings.

Within our access device group, our technical excellence there has allowed us to close those new telco customers Jerry mentioned. And we actually have ongoing discussions with other telcos for our CAD products, including select new products which are also technically differentiated.

And finally, in our RAN group, the R&D investments we have made and continue to make are bearing what I'll call bookings fruit, as evidenced by the RAN contracts that Jerry mentioned which should contribute to revenues in 2023, as deliveries on these new RAN supply contracts occur.

The operating loss for the quarter did increase to \$30.1 million over \$18.1 million in Q2. This was influenced by many factors, but when you adjust for the rare accrued warranty provision recording cost of revenue and the \$1.7 million increase in inventory reserves, I think the quarterly context improves.



And finally, related to P&L comments, our net loss for the quarter was \$31.2 million versus a net loss of \$18.8 million in Q2 2022. That increase in the net loss is primarily the result of the \$12.9 million accrual related to the warranty matter, as well as the other items I just covered. And before moving off of the P&L and specifically related to this warrant provision of \$12.9 million, I'm guessing there will be many questions on this. And we have to be limited and judicious in our comments, given the discussions to formally and finally resolve are still ongoing. But what we can say is this: This customer dispute was related to one product delivered to one customer back in the 2019 timeframe, and further limited to one faulty component in one lot of products. It doesn't extend to a full product line.

The root cause of the issue appears to be a third-party subcontract manufacturer substituted a resistor component in this product without anyone's knowledge or approval, that did not formally comply with technical specs. And so now we're working with this truly great customer who we've had a long-standing relationship over many years on an amicable business settlement to really this unfortunate and complex matter, and we will provide more details once finalized. But that's the nature and totality of that Q3 \$12.9 million charge.

Moving off the P&L and to the balance sheet, we continue to have a great liquidity position with a working capital balance of \$234 million at quarter end, and with \$196.6 million in cash, including approximately \$3 million in restricted cash. And that strong cash balance at September 30 was down only very slightly, approximately \$2 million, from cash at June 30, 2022.

And further, notwithstanding the Q3 and year-to-date accrual losses, I think you should take note that cash is currently up \$39 million compared to 12-31-21, and also up over 9-30-21. And our year-to-date operating cash flow was positive at \$11.7 million. And the increase in cash and positive operating cash flow for the nine months ended 9-30 is a function of many things, including, number one, limited Capex spend. It's a Capex-light business. We also have strong AR payments from our excellent high pedigree customer base.



It reflects the \$40 million Verizon equity investment in April we announced. It reflects about \$14 million of tax cash refunds in Q1. Also reflects like a high level of non-cash charges in our net loss. Between depreciation, amortization, and non-cash-based comp, that approximates \$20 million. It's a function of an increase in deferred revenue overall. And for Verizon specifically, we received \$20 million in cash from Verizon for license payments in Q3, but we've only recognized \$6 million of GAAP revenue through 9-30. Also a function of the accrual for the warranty settlement provision of \$13 million in Q3. Inventory reserve increases of about \$6 million in 2022. And hopefully, this cash context is helpful as this strong cash position provides us a great foundation as we go forward into Q4 of '22, and then further into 2023.

So moving off of cash, at quarter end we had net receivables about \$49 million and an inventory balance about \$82 million. And to wrap up the balance sheet, our gross debt was approximately \$275 million. And on this debt matter and it's highlighted in the earnings release, we are pleased to report we did reduce our debt since the quarter closed by about \$41.7 million face value debt, using cash on our balance sheet to repurchase this debt at a modest discount to par and retire it. And we will consider additional repurchases as part of our delevering plan.

And at the risk of stating the obvious, implicit in the use of cash to retire the approximately \$42 million face value of debt is the strong confidence we have for renewed topline growth and return to profitability in 2023, for all the reasons Jerry covered in his remarks.

Beyond this good debt repurchase and retirement, we are also pleased to say we are actively evaluating options for the refinance of the remainder of the term loan B that matures at the end of December 2023. In this regard, we've formally engaged in an investment bank that specializes in these matters to work with us. We're making good progress on this refinancing front, and we and they are optimistic we'll have this resolved in the coming few months.



And as we execute through 2022 and turn the page to Q4 and 2023, we are disappointed with the GAAP accrual results, but we are confident we will improve in Q4 and rebound considerably in 2023, as all our product groups continue -- contribute to 2023 topline results. And just as additional context on this, the optimism and confidence in the future, it is rooted in the fact that we have two mature product groups, you know, cable and CAD; and two new product suites which we've internally funded over the past five years, really as a result of Jerry's prescient vision to invest ahead of the curve, anticipating where the market was headed.

So now, as we stand here and look forward, there is a lot to be optimistic about across all these product groups. Specifically for our cloud software product group, we've got the great Verizon \$140 million TCV licensing deal, which we are on track with our development deliverables, as reflected in the payments in Q3. We've got another \$120 million to bill in increments of \$24 million per year to Verizon, as delivery and acceptance occurs. And that's a great foundation to build on. And beyond Verizon, this new Google Cloud partnership which is progressing well. And as Jerry mentioned, we expect to be able to announce a few customer wins with GCP in the coming months.

We further have strong inbound interest from other cloud providers and SIs who have evaluated our cloud-native software, you know, determined that it is indeed truly cloud-native and who also want to engage with us in go-to-market activities. And finally, we are seeing strong demand for our virtual BNG routing software as well, and that will help 2023, too.

Turning to cable, as Jerry mentioned, there was a bit of a pause in cable spend in early 2022, as the cable MSOs evaluated future product technical direction such as virtual CCAP cores. And as is now public and as Jerry mentioned, several of the largest MSOs have made this technology decision and are moving forward with RFPs and spending plans for 2023. And they are also dealing with subscriber losses to alternative technologies, which is generally when cable Capex spending typically ramps.



And again, in this regard and with the exception of Comcast, we are working with every other major cable MSO globally now. And again, we are only one of two providers that have a ready for prime time virtual CCAP core, which is of high interest to them. And based on our extensive cable customer engagements, we believe we are really well-positioned to compete for what we believe is a coming wave of renewed cable MSO Capex spend, and this will inure to our benefit in 2023.

And moving over to access devices, our 2022 CAD access device results were impacted by that product end-of-life decision that Jerry mentioned that occurred in 2021. But the good news is while it's not showing up in our GAAP revenue line yet, as we have to build and ship new orders, we have made great progress cultivating those new customer and partner relationships in North America and Europe and getting sizable bookings for our fixed wireless access and higher extension products, much of which remains in backlog today. And these new orders will flow into revenue in 2023, as we deliver on the orders in 2023.

And finally, as to our RAN product group, we've invested again heavily in our small cell radio R&D over the past few years, and we have proven products ready for market today. We now have new RAN supply contracts with a Tier 1 North America telco, and we expect to close another RAN contract with an international operator soon. And RAN should contribute to 2023 revenues and gross margins as well.

So it's for these primary reasons, as well as a host of other reasons, we do believe 2023 should be a year of renewed growth and return to profitability for Casa. You know, this confidence was reflected in the debt paydown we announced today, and we appreciate everyone's patience as we complete what I believe is really an amazing transition and transformation of Casa over the coming few months.

Finally, as Jerry mentioned, we will provide annual guidance in Q1 of 2023, upon completion of our financial plan for that year. So we do thank you for your continued support and interest in Casa, and look forward to sharing our progress as we complete this transformation.



And with that, I'd like to turn the call back over to the operator to open the line for questions. Operator?

Operator

Thank you. Ladies and gentlemen, we will now be conducting a question-and-answer session. If you would like to ask a question, please press *1 on your telephone keypad and a confirmation tone will indicate your line is in the queue. You may press *2 if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment, please, while we poll for questions.

Ladies and gentlemen, there are no questions at this time. I like to turn the call over to Mr. Jerry Guo for any closing remarks.

Jerry Guo, Chief Executive Officer of Casa Systems

Thank you for joining us today. We are continuing to make progress in our strategic partnerships to bring our innovative technology to new markets. We are well on our way to achieving our multiyear transformation to become a leading provider of cloud-native software and the physical infrastructure technology solutions for mobile, cable, and fixed networks. I'm encouraged by the team we have assembled and look forward to sharing our achievements with you next quarter. Thank you.

Operator

Thank you. This concludes today's conference. Thank you for your participation. You may now disconnect.



casa systems

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