Transcription

ADVA Optical Networking Full Year 2021 IFRS Financial Results

{EV00132336} - {57 Min}

24 February 2022

PRESENTATION

00:00 Operator

Dear Ladies and Gentlemen, welcome to the conference call of ADVA Optical Networking for the full year 2021 IFRS financial results. This call is being recorded. As a reminder, all participants will be in a listen-only mode. After the presentation, there will be an opportunity to ask questions. If any participant has difficulty seeing the conference, please press the * key on your telephone for operator assistance. I now hand over to Mr. Steven Williams, ADVA Optical Networking's Director of Finance and Investor relations. Please go ahead, sir.

00:37 Steven Williams

Thank you, Judith. And welcome to ADVA's Q4 and full year 2021 financial results conference call. In addition to this call and the press release, we have posted a presentation, which is available for download from our home page adva.com, on the Conference Call page in the Financial Results section, of the About Us/Investor section. Before turning the call over to Brian, please be reminded that this presentation contains forward-looking statements with words such as "believes", "anticipates", and "expects" to describe expected revenues and earnings, anticipated demand for networking solutions, internal estimates, and liquidity. These factors are discussed in greater detail in the "Risk and opportunity report" section of our annual report 2021.

Please also be reminded that ADVA provides consolidated pro forma financial results in this presentation solely as supplemental financial information to help the financial community make meaningful comparisons of our operating results from one financial period to another. This pro forma information is not prepared in accordance with IFRS and should not be considered a substitute for historical information presented in accordance with IFRS. Pro forma operating EBIT is calculated prior to non-cash charges related to the stock compensation programs, and amortization and impairment of goodwill and acquisition-related intangible assets. Additionally, expenses related to M&A and restructuring measures are not included. Unless stated otherwise, all numbers are presented in euros. We will target to limit this conference call to 60 minutes. As usual, Brian will start this call, providing a business update. Then Uli will guide us through our Q4 and full year 2021 financials and Outlook. And finally, we will have sufficient time for your questions, which we will be happy to answer. And at that, I'll turn the call over to Brian. Go ahead.

02:40 Brian Protiva

Thank you, Steven. Starting with our standard procedure, we move to page number 4: "Q4 and full year 2021 highlights."

It is with pride that we look back on a successful Q4 and fiscal 2021. Despite ongoing challenges due to the Covid pandemic, the semiconductor crisis, and supply chain bottlenecks, we delivered excellent results. We met all our targets and even exceeded them in many areas. Thanks to the continued, strong customer demand, and great efforts in purchasing, manufacturing, and logistics, we were able to further increase our revenues and achieve the most profitable fiscal year in our 27-year history.

Q4 revenues were up 12.2 percent compared to the year-ago quarter and reached EUR 157.7 million. Annual revenues were up 6.8 percent year-over-year reaching, an all-time high of EUR 603.3 million. Our pro forma operating income reached 9.1 percent of revenues in Q4 2021 and was up 61.5 percent for the full year 2021. Our net promoter score, the performance indicator which we use to measure customer satisfaction was at a very positive 48 percent. Net cash increased by EUR 61.7 million year-over-year. Thus, we've further expanded our liquidity cushion and, excitingly, we are starting the 2022 fiscal year with a record order backlog.

Page number five, "Business transformation update". For several quarters, the macroeconomic environment has brought us encouraging growth in customer demand, while at the same time presenting us with major supply chain challenges. This tension will continue in 2022.

Against this backdrop, we've continued to work diligently to execute our business transformation strategy. And things are going well.

At the beginning of the fiscal year 2021, we presented our strategy for sustainability, sustainably increasing the margins of our business model, to the financial community at our Digital Capital Markets Day.

The plan is essentially based on three pillars. First, disproportionate growth private and security-relevant networks outside the traditional network operator infrastructure. We have been winning new customers outside the telco community in verticals such as transportation, medical, and research and education. The slide shows several of the wins announced since our last earnings call in October 2021.

Second, we focus on increasing revenue contributions from software and services. In 2020, we went from 20 percent to 23 percent. Last year, we increased the contribution further to 25 percent. We keep expanding our capabilities in this space and recently launched a new software product. Our Ensemble Simulator enables customers to perform full, end-to-end network testing in a virtual environment, saving time and money for capex-intense hardware test beds.

And third, we are driving the development of new markets, while simultaneously achieving cost optimizations through verticalization activities. Our Micromux family of pluggable transceivers is selling well and we will announce new members of this product family later this quarter. And, in fact, within the next few weeks at the OFC. Overall, the results we've achieved in the past year clearly demonstrate the strength of these strategic cornerstones and show the success we had implementing them.

Page number six, "Unprecedented market opportunity at the edge." While we were – or while we are – executing very well on our vision and strategy, we also see an unprecedented set of positive macro trends that are supporting our business. Digitization continues to move center stage in politics and business. High-performance network infrastructure is now regarded as the backbone of an increasingly digitized society and has greatly increased in importance and value over the last few years. The resulting high demand for communication technology is currently being further reinforced by numerous government stimulus and funding programs in many countries around the world. In the USA, many billions of US dollars will be made available over the next few years for network expansion, especially underserved and rural areas, as part of the Infrastructure Build, Rural Digital Opportunity Fund, and American Rescue Plan Act programs. The UK has announced more than 25 billion pounds of private and government funding for accelerated network expansion, and across the EU, government support programs totaling EUR 30 million have been launched. Many programs in Western countries will predominantly benefit Western suppliers. And the focus of investment will be in the network access vector through to metro networks, due to the universal right for information access within every home. Technology capabilities, stemming from 5G, packet optical integration, miniaturization, and next-gen PON fiber access, creates an opportunity where ADVA's extremely well-positioned within the network edge. We will further strengthen our market position to the merger with ADTRAN. With almost USD 250 million of combined R&D spending focused on the converged edge, you will see market-impacting innovation driving our growth.

Page seven – more specifically, "Our vision for the converged edge." In order to break down our mutual vision a bit more, we grouped a number of the areas accordingly.

We will:

Empower service providers to benefit from seamless service creation, regardless of customer type and application. This includes residential, work-from-home and business services, as well as assured wholesale, X-haul for mobile operators, and edge cloud services.

Former homogeneous, single-purpose parallel network architectures will evolve into a more unified access infrastructure, including various first-mile technologies and on-premise solutions, such as multi-generation PON with meshed WiFi6 capabilities, combined with second-mile technologies, including packet, OTN, and edge compute solutions with outdoor-hardened optical products covering industrial temperature ranges.

Our programmable, open optical line systems, in combination with packet optical terminals and pluggable optics provide a wonderful set of building blocks to create a lean and cost-efficient edge transport solution that provides operators with the scale they need to handle the soaring bandwidth demand. All this is wrapped in an end-to-end security envelope with low-latency, multi-layer networking encryption solutions.

And last but not least, we all know that the world needs better timing. With our Oscilloquartz technology, we provide assured precision timing for communication networks and critical infrastructure-enabling 5G, open and disaggregated networks, assured PNT, and many critical technologies which are changing our world.

When you take all these modules and modular building blocks, built on a philosophy that embraces, open, disaggregated, and cloud-native concepts, and put them under an end-to-end orchestration umbrella with software-as-a-service, you have the most comprehensive solution set for the industry's most interesting market space. We are convinced that this strategic business combination will permanently change the competitive landscape in our industry.

And moving to my last slide, page number eight: "ADTRAN+ADVA is strongly positioned to capitalize on momentum in the converged edge." Per my comments on the previous slide, ADTRAN and ADVA share a common vision about what it takes to win at the edge. Jointly, we can further accelerate our momentum and capitalize on the following three aspects.

First of all, we expect significant cross-selling opportunities. A complementary geographic focus with ADVA's strong EMEA presence and ADTRAN's strong US presence will help. We will also gain strategic vendor status with certain carrier relationships due to the size and strength of our balance sheet, which will create new opportunities. And our comprehensive solution portfolio will increase win rates. The potential annual revenue synergies are in the range of USD 60 to 120 million.

Secondly, we will have increased scale to accelerate R&D innovation. The merger enhances scale and improves ability to compete against other fiber networking vendors. We will also be able to achieve real optimization, which is to be expected with the combination of R&D processes. And we will have a greater ability to focus on software, virtualization, and monetization. Not to be repetitive, but a combined R&D spend of nearly a quarter of a billion USD for the converged edge gives us a significant innovation power even when compared with some of the other larger players like Nokia.

Thirdly, there will be some operational efficiencies from well-defined cost synergies. These include significant supply chain efficiencies and optimization of our new operating model with improved profitability. We have quantified approximately USD 52 million of annual cost synergies with should be reached within two years after the closing.

And finally, almost two-thirds of the existing voting shares for ADVA have agreed to the exchange offer and we look forward to a common future with much optimism and enthusiasm. Currently, we are still working with the government authorities on open questions regarding the foreign direct investment approvals and are confident of receiving the necessary response support.

With that, I hand it over to Uli.

15:00 Uli Dopfer

Thank you, Brian. Welcome everybody and thank you for joining us on our full year 2021 conference call.

I will start by reviewing our results for Q4 in the financial year 2021 followed by our outlook for 2022. Then I will provide a brief update on the ongoing merger process with ADTRAN. As always, all numbers are presented in euros. Now, let's move to my first slide, "Financial year 2021 at a glance."

2021 was a record year for revenues, profitability, and cash generation. Despite the ongoing challenges caused by the pandemic as well as global supply bottlenecks and semiconductor shortages, we managed to grow our top line in the mid-single-digit percentage range. We closed the year with revenues of EUR 603.3 million, up 6.8 percent from EUR 565 million a year ago. Revenues were at the upper end of our guidance corridor of between EUR 580 and 610 million. Demand continued to be strong throughout 2021 and resulted in a record-level order backlog at the end of the year. Our pro forma EBIT was 9.1 percent of revenues or EUR 54.6 million and increased by 3.1 percentage points compared to the 6 percent, or EUR 33.8 million, we had seen in 2020. This result was at the upper end of our guidance corridor of between seven and ten percent of revenues. Despite increased purchasing costs that started to impact our gross margins particularly in the second half of the year, we achieved the highest full year profitability in our history. These results were strongly supported by the continued execution of our business transformation strategy and strict cost control.

New applications outside the CSP segment set the stage for a more favorable customer and product mix, and we were also able to increase our software and service revenue contribution from 23 to 25 percent.

Cash generation in 2021 was very strong. We were able to turn a net debt position of EUR 25.5 million into a net cash position of EUR 36.2 million. We repaid EUR 15 million of our outstanding debt while we were still able to increase our gross cash position from EUR 65 million in 2020 to EUR 109 million in 2021.

Now let's take a deeper look into Q4, slide 11. Revenues in Q4 2021 reached EUR 157.7 million, up by 12.2 percent from EUR 140.6 million in the year-ago quarter. Similar to Q2 and Q3, our Q4 revenues were heavily impacted by supply challenges.

Once again, we had to defer shipments with a volume of more than EUR 20 million into a following quarter. However, we still managed to grow both quarter-over-quarter and year-over-year. Growth in Q4 was predominantly driven by an uptick in demand from CSPs, particularly in the cloud access solution area.

Higher purchasing costs due to the silicon shortage had a significant impact on our gross margins and increased our costs by a substantial amount in Q4 2021. Consequently, gross margins were down by 3.3 percentage points. However, we were still able to increase gross profit slightly by 2.6 percent compared to the year-ago quarter. We also continued our strict opex discipline and were able to achieve a pro forma EBIT of 9.1 percent of revenues. This is a decrease of 1.1 percentage points when compared to the record Q4 we had seen in 2020. However, an impressive result considering all of the macroeconomic circumstances we are currently facing.

Net income reached EUR 17.5 million, significantly up from EUR 13.2 million in the year-ago quarter. Apart from the strong EBIT contribution, this is mainly attributable to a tax benefit of EUR 5.2 million. The standalone profitability of

ADVA SE enables us to use past losses for activation of a deferred tax asset under IFRS. We saw a similar effect already in Q3 2021.

Diluted earnings per share increased from 26 cents in Q4 2020 to 34 cents in Q4 2021.

As mentioned earlier, cash generation and deleveraging was once again outstanding, and we improved our net debt by over EUR 60 million compared to Q4 2020 and now report a net cash position of EUR 36.2 million.

Next slide, please, slide 12. As explained in the past, we added this slide for the purpose of transparency, and to provide our analysts and investors an enhanced comparison, since most of our peers report their numbers in US GAAP. Please note, the US GAAP numbers here have not been audited.

The main differences between the two standards are due to the capitalization and amortization of R&D under IFRS. The R&D amortization leads to higher costs and for Q4, the resulting difference in gross margin is 7.1 percentage points. The R&D capitalization, on the other hand, leads to lower R&D opex. Positive impact from R&D capitalization was 0.2 percentage points and thus, pro forma EBIT margin under IFRS was 9.1 percent compared to 8.9 percent under US GAAP.

Slide 13, “Regional revenue development Q4 and FY 2021.” EMEA Q4 revenues increased by 15.8 percent year-over-year, now representing 63.8 percent of revenues and 63.2 percent respectively for the full year. 2021 growth of 23.5 percent was mainly driven by CSP and enterprise customers.

In the Americas, Q4 revenues increased slightly by 1.2 percent year-over-year, now representing 25 percent of revenues. However, full year revenues were down by 17.6 percent compared to 2020, mainly due to delays of shipments based on the difficult supply situation.

Compared to the year-ago quarter, Asia-Pacific increased significantly by 20.1 percent, and now represents 11.2 percent of Q4 revenues or 9.3 percent of full year 2021 revenues. Growth in Q4 was predominantly driven by strong demand from customers in Japan and Australia.

Moving to the next slide, slide 14, “Cash flow and balance sheet.” Cash flow generation was outstanding. Operating cash flow for the full year increased by EUR 26 million and free cash flow improved by EUR 20.1 million. This is mainly explained by high profitability when compared to the previous year. Our strong cash flow generation resulted in record cash levels of EUR 109 million, up by around EUR 44 million year-over-year.

With a debt leverage ratio of 0.4 x EBITDA and an equity ratio of 56.5 percent, we have a very solid capital structure and further improved our investment-grade credit metrics. 2021 ROCE was 11.7 percent and reflects our commitment to deliver shareholder value.

Slide 15, “Outlook.” Our business transformation strategy will remain one of our key focus areas also in 2022. From a demand perspective, the macro environment is expected to stay very positive for ADVA. Communications infrastructure is a valuable asset with this growing focus on security aspects.

In many industrialized nations of the Western world, the dependence on large Chinese network equipment suppliers is perceived as a serious threat. After the US, the affected network operators in Europe are now also working on concepts for reducing this dependency, which leads to significant opportunities for us.

Our technological setup is well-prepared for the transformation of networks with respect to cloud, mobility, 5G, automation, and security, in addition to the high-quality performance features of optical data transmission, precise network synchronization technology, and programmable cloud access solutions. And our broad service portfolio also provides increasing value for our customers.

The global semiconductor crisis, however, will continue to keep us extremely busy also in 2022, and supply and financial risks will remain. And with respect to the Covid-19 pandemic, it remains to be seen whether the impact of the crisis will lessen over the course of the year.

In our 20-year history, we have never seen stronger demand for all of our products and services, and the before-mentioned macroeconomic environment creates unprecedented opportunities for us.

Despite this positive outlook, but in light of the ongoing supply challenges, we remain cautious and guide for 2022 annual revenues of between EUR 650 and 700 million, and a pro forma EBIT margin of between 6 and 10 percent.

Now to my last slide, “Road to business combination with ADTRAN.” Last but not least, I want to provide a brief update on the ongoing merger process with ADTRAN. At the end of the additional acceptance period, which expired on February 14, we ended up with a total acceptance rate of 66 percent. The last outstanding closing condition is the FDI approval from the German government. We are confident of receiving the necessary support and anticipate a closing within Q2 or Q3 2022.

And with that, I would like to open the Q&A.

Q&A

26:16 Operator

Thank you very much. Ladies and Gentlemen, we are now starting the question and answer session. If you like to ask a question, please press 0 and 1 on your telephone keypad. Your questions will be answered in the order they are received. If you are using speaker equipment today, please lift the answer before making your selection. One moment, please, for the first question.

And the first question is from about Robert-Jan van der Horst, Warburg Research. Your line is now open.

26:48 Robert-Jan van der Horst (Warburg Research)

Hi, thanks for taking my question.

I have a couple of those, actually. So ,first of all, congratulations on especially the strong cash flow and the margin you achieved. Considering that you will probably continue to succeed with your transformation strategy, I must ask why the target range for the [27:20 adjust???] pro forma EBIT margin is so low at the lower end.

Do you expect significant worsening of the procurement costs over the year? And also maybe a little bit more information on why that is, that would be very helpful.

The second question is actually an update also on the transformation strategy. You already mentioned that software and service revenues increased to, I think, 24.9 percent. Could you give us maybe a little bit of an update, how the revenue shares of the CSPs versus verticals developed? That would also be very helpful. And the last question is on your US, on the Americas business, which saw decline you mentioned because of some softness with major customers. Any indications how that will develop this year. That should be all for now. Thanks.

28:23 Uli Dopfer

Okay, I think I start, Brian? Unless you want to start.

28:31 Brian Protiva

No, go for it.

28:32 Uli Dopfer

Alright. So, regarding the outlook for next year. You know, if you look into, if you look at slide 12, the US GAAP versus IFRS comparison, you see the massive drop in gross margin that hit, that started hitting us, you know, in Q3, and then you can see it also in Q4.

This supply shortage cost us millions, right? And we had our teams scrambling day and night to secure components, expedite shipments, and it's just, you know, we don't see that this is getting any better as of now.

So that's why we have to have to anticipate, we will continue to, you know, have delayed shipments, we need to anticipate with a higher volume that maybe risks, supply risks even increase, you know, there are many critical components. We have to work alternative components into our products, and so on and so forth.

So it's simply a huge, I would say, burden for all of our teams and that's why we are very cautious with this one. We don't want to promise anything, but it's still, you know, it's still early days. And we see a huge pile of open issues and open items, critical items that need to be resolved, and that's why we remain cautious.

But on the positive side, as you see also on the huge bandwidth that we provided for our top line guidance, I think you can imagine the opportunities that we have. And if things turn to the better, I guess you can quickly see better results or maybe the range narrowing, but I think it's just too early right now to be more aggressive when it comes to our guidance. There's too many moving parts.

30:04 Brian Protiva

So, adding to that comment, Uli, can I also add the comment that it's fully, I mean, as each quarter goes through, it becomes more fully loaded: the costs, the semiconductor piece … it takes some time to average-in costs, etc.

So, you know, all to what Uli said, plus the fact that probably, you know, Q1 or Q2 we see the peak of all those, that impact, and therefore we're cautious. We have, through our transformation strategy, as you pointed out, been able to help counteract that some, we do plan on increasing again in 2022, software and services – that's mostly in the software side, but adding a couple percentage points so that helps to offset some of those pieces.

But the cost basis, it's really aggressive. And some of, even this latest semiconductor cost increase, has come end of the year/beginning of this year, so they've just continued to hit not just us but the industry as a whole.

And therefore I think people have to understand that probably the highest cost impact is still yet to come and then hopefully it will, like a cliff, come back and in the second half we'll start to recover a lot of those extra costs that we have and that we're managing very well with those costs, but clearly they're going to have impact on us in the first half of this year.

So, further to the transformation strategy.

The enterprise business did increase by, I think, four percentage points, almost. Around four percentage points of our revenue came more from the Enterprise space – that also clearly helps our average margins. So that's a nice supportive step for us as well.

And we do believe that our verticalization will yield more revenues this year than last year –we have very good products, very good quality feedback, we're just not able to produce enough yet.

We've said that a couple of times over the last quarters, it's getting better, but it's getting better linearly and we would like a hockey stick effect here over the next few quarters.

We hope that we can achieve that.

And then we have some nice offsets to some of the supply chain risks that we've had. So we're working feverishly to get to the higher end of our guidance, but step by step, we need to still do some homework to make that happen.

And then, finally, the US business I think you mentioned and the US business, you know, we haven't lost customers and in fact, we've done well to win some new footprint recently with some of our products.

We do see a lot of upside once the deal's complete with ADTRAN, just because of their strength there. So if you look at it as a whole, I think the US is steady as it goes from a customer game. And if you look at it, it's more product mix/customer mix of ordering that has led to some weakness there. And I do believe, though, that combined with ADTRAN we're going to get a lot more, let's say, political heft and breadth to be able to win more new footprint going forward.

33:29 Uli Dopfer

Thank you, Brian. I guess it's fair to say that, also, you know, some of our larger US customers were over-proportionally impacted by the supply shortage. So from a demand perspective, you know, a huge portion of the record-level order backlog we have is actually from North America. So without a supply shortage we would have seen stronger numbers for the region of North America.

33:52 Robert-Jan van der Horst

Okay. Got it. Thank you.

33:59 Operator

The next question is from Simon Scholes, First Berlin Equity Research. Your line is now open.

34:06 Simon Scholes (First Berlin Equity Research)

Yes, hello, thanks for taking my questions. I've got three.

I'm just back on the subject of the pro forma gross margin. I mean, you just had a slight pickup in Q4, but it sounds from what you're saying that the situation is still pretty tight. So should we interpret the pickup in Q4 as just being down to a more favorable customer mix or, I mean, do you have any additional comments there?

And then, second question is: I was wondering if you could give us some idea of how much higher the backlog is or was at the end of December last year compared with December 2020. And then, just a last question on sales and marketing. I mean, the last couple of years, because of the pandemic, sales and marketing has been between 10 and 11 percent of sales. And would you expect it to go back over 11 percent this year as the pandemic possibly eases. I mean, what are you seeing there? That's it from me.

35:12 Brian Protiva

Uli, you start?

35:15 Uli Dopfer

Go ahead, Brian.

35:17 Brian Protiva

I was just going to add to the pro forma gross margin and say, yes, Q4, you know, good customer and product mix helped us clearly, and as, you know, referencing, you know, some of the costs they continue to hit us with, cost increases, the semiconductor players have not come back once but two, sometimes even three times with cost increases.

So there's a mix, there's a bunch of moving pieces in that question, mark. It's not easy to answer, but I you know in general I do feel, yes, the cost side of things continues to be very challenging and, you know, we're trying to offset those with our business transformation strategy, and some of that helped in Q4, but it is product mix and customer mix, and it's not something we can guarantee is a smooth transformational change and add for quarter-for-quarter. It's a, you know, it's a long term … as we pointed out with our business transformation strategy. That's a three-year, actually even five-year strategy shift as an organization. So lots of moving parts there.

Um, Uli: I don't know if you want to add there or if you want to address the higher backlog or the sales and marketing question?

36:35 Uli Dopfer

I'll let you address the backlog. I will just talk real quick about the sales and marketing.

We had about ten percent last year in sales and marketing costs in terms of, relative to revenues. I think, you know, with the growing revenues or expected growing revenues in 2022, we should see a similar percentage of revenues, so the absolute number will go up, Simon. But I think the relative number will pretty much be the 10 percent or just short of 10 percent of revenues

37:06 Simon Scholes

OK. Any comment on the backlog?

37:11 Brian Protiva

Yeah, the high backlog. I notice that Uli didn't want to answer that one, so he's pushed it to me. That was sophisticated…

My view is… We haven't given backlogs, but it's a massive increase and we're not talking here a few percentage points. We're talking a massive double-digit percentage point increase in the backlog.

But since we haven't gone out there and labeled that exactly, we haven't, I don't think we plan to start that this time around and that ,actually, that would be, you know, something that we have to take to our Board and have a discussion on. So I'm sorry that I can't answer more than that, but it is a huge shift.

37:52 Simon Scholes

OK, I get the idea. Thanks very much.

38:00 Operator

The next question is from Paul R. Essi, William K. Woodruff. Your line is now open.

38:10 Paul R. Essi (William K. Woodruff)

Yeah, thank you for taking my question. I had a question on the cross-selling in North America after the merger.

ADTRAN and some of their competitors are saying that the market there, the stimulus of a USD 100 billion, is less than half of the future, you know, less than half of demand going forward. And if you were to assume that that's basically half of the demand, you're looking at a USD 200 billion number there. If you divide that by five because a lot of the stimulus has to be, you know, spent over that five-year period, you're looking at a USD 40 billion market, roughly 10 percent of that would be for access and I think your ratio you gave me was 1:4 for the middle mile. So if you were to take that, you got a USD 1 billion annual market, roughly, you know, give or take, and you're looking at USD 120 million in cross-selling opportunities.

To me, it looks as though you don't have a lot of direct competition there, and a company like Ciena would, you know, they're not as nimble as you. So, how much, I guess the question would be how much of that market do you expect to be able to take? Because it looks like it's going to be more than USD 120 million. How quickly can you gear up for that as well, especially with the chips that ADTRAN has, you ought to be able to make a big dent in that market?

39:38 Brian Protiva

So I'll dance around this a little now … clearly, the bigger picture … I mean, you know, ADTRAN has given you guys models of what the combined organization looks like, you know, and on some slides it's a USD 5 billion increase in total available market, but yet, very conservative on revenue planning. So if you were to, you know, answer that question from a revenue planning view then that, you know, remember that USD 60 to 120 million is not even in our numbers and the numbers look outstanding as a combined organization.

So now comes the, you know, well, OK, our conservative view on the amount of cross-selling opportunities and that's that USD 60 to 120 million. As you pointed out, there's a billion upside in just our technologies and a much bigger upside in ADTRAN's technologies.

Why can't we get a much bigger part of that equation? Because we're one of the few companies that actually have both technologies.

It's us and Nokia, really. Calix doesn't have the optical piece and Ciena doesn't have the access piece. And so the combination makes us really strong with a spend USD 250 million of R&D. The only one that can match us from an innovation firepower is Nokia – and of course Huawei, but they're not a competitor in any of this opportunity.

So, you know, I look at it, you know, similarly, and to say, why not a much bigger piece? Well, I guess it's always, you have to understand how the market's going to decide, how many of them are already buying products from a Ciena, or a Cisco or Infinera or somebody else already? How quickly can the combined organization, you know, go after that market opportunity and share?

So there's a lot of question marks around there.

But, bottom line is, is that ADTRAN's a well-liked supplier by many of the companies that are going to benefit strongly from the funding and they want, most of these small carriers want fewer suppliers. And why do they want fewer suppliers? Because they don't have big teams. So they want one management platform with fewer suppliers, end-to-end architecture and we're one of the very few that can do that. And as you point out, we are also nimble: also the combined organization, ADTRAN and ADVA, are very nimble organizations compared to most others.

And therefore, I personally feel really, really good about that opportunity and leveraging that ADVA infrastructure into a lot more sales, but I really you know, it's not my place to say, hey, we're gonna drive this amount of percentage of that spend that you indicated.

So, thank you for pointing it out with a very pointed question.

Again, I tried to dance around that a little bit and give you a full perspective and, fingers crossed, that the combined organization does a hell of a lot better than what is being anticipated by any of the numbers at this point.

42:35 Paul R. Essi

OK, thank you. And one follow-up: how quickly do you think you can gear up? Because I'm hearing that people are already going to ADTRAN, asking, you know, how to, you know, get connected with you guys.

42:48 Brian Protiva

I think that goes very quickly once the deal is consummated.

And we've got, as we mentioned, two thirds of the ADVA shareholders have voted, so we're through all the hurdles except for one, and that's the FDI here in Germany. And that to me, you know, that's something that we can't control, but that's anywhere from probably, you know, 2-4, 3-6 months, somewhere in that range. And that's something that we are pushing and we have said we feel very positive, but there's a lot of work behind that. A lot of modeling, a lot of commitments, a lot of discussions. So once we get that, I believe the next day we'll be able to leverage most of these opportunities.

You have the advantages right then, we can kind of co-sell once that deal is, you know – and "co-sell" meaning we can … we can be more transparent.

What we still need, to be one company, one management system, one offer, is a DPLTA – our domination profit and loss pooling. And that could take some period of time or maybe not even – not at all for that matter, depending on the next steps. So, the answer, the day that it closes, we can get a lot more transparent and faster at accessing those accounts, but full integration and, you know, reducing software architecture concepts, that takes some period of time still.

So, I think we're in, the first step is, even today, we can just give a hey, a notice, there is a lead or interest in connecting to people, but nothing can be shared, nothing can be done together, nothing, no feedback, nothing at all. After closing, a little bit more transparency. After the domination and pooling agreement, full, combined approach into those companies.

So my view would be, we win a few accounts now. We start winning handfuls of accounts once the deal is closed, and we're going after all the accounts when that domination agreement – if and when the domination agreement – is actually signed.

45:06 Paul R. Essi

Thank you very much.

45:12 Operator

And the next question is from Tim Savageaux, Northland Capital Markets. Your line is now open.

45:21 Tim Savageaux (Northland Capital Markets)

Hi, good morning from me and congratulations on the results. And especially the outlook, which is kind of what I wanted to ask a couple questions about.

So you're calling for a pretty significant acceleration in your growth rate at the high end, a good doubling or more of your growth rate in calendar 22, and I want to try to understand that along a couple of lines.

First, you know, is there an element of supply catch-up implied in there? And, just as an aside, is that an impact, you know, seasonality in Q1, given the push-outs, it sounds like you expect it to continue? But is there an element of supply catch-up there or are you, to what degree are you seeing, you know, acceleration and inorganic growth in the end market?

That's one. And then two, from a geographic perspective. Obviously EMEA led the way in 21, with declines in Americas, I wonder how you'd expect that to just sort out at this point, given, you know, the backlog commentary sounds like you expect Americas to bounce back pretty strongly – and I'll follow up from there.

46:32 Brian Protiva

OK. So, first of all, I mean, I think, you know, in my presentation … can I try to focus, you know, focus on separate issues? And there is more demand out there. There is more demand. Even if you have the existing, same customer base, there's more demand out there, it looks like.

And part of this is because funding is already starting to play a role and the strategic nature of, you know, work from home, high-quality services needed, you know, in a distributed fashion, changing network needs, are all things that are leading to, I think, a good environment for most players out there.

So that's the one piece. The second piece is, yes, there will be some supply catch-up. I think, you know, at this point we feel, you know, strong enough early in the year that we are going to grow and that, you know, at least as fast as this year, even faster in the bottom part of our growth rate, and much more clearly in the high end.

So, you know that that's a pretty strong statement to the market that we feel good, that demand is strong, yes, we do have some supply catch-up out there because of our really high backlog, and that's inferred and, having a really high backlog, I think it's that we have much more kind of a good solid view to the year. Meaning also that, you know, we feel good to start the year. So all good indications of where we're at as an organization.

We have, you know, some areas for growth. Where we're taking some market share as well, you know, if we're able to drive our software and services growth. Some of our encryption and other markets, new market areas, we continue to be able to grow those spaces, like we said, you know, 4 percent growth – and that in 2021.

Those are all leading to, you know, underlying themes that are helping us position ADVA as a company. And then, finally the US. Yeah, I mean, we feel again, we haven't lost anything. We've won some things, we haven't won as much as we had wanted to, good strong competition there as well, but we're doing well and we think it will, you know, recover. As Uli also said, is that it was maybe a little artificially lower because just, it happened that some of the logistics issues hit the customers there. That's just a pure product-mix issue, you know, certain products where you had more leverage in a region that then hurt a little bit more, but we feel that, you know, United States will hold its own but EMEA, EMEA's growth rates could even continue.

We continue to see very good opportunity across the board and ADVA's really well-positioned as a player that's been committed to this market for the last 27 years, to not only win footprint, but to build out and get mindshare. And by the way, the ADTRAN deal helps us even further because we become strategically important to many tier-1s in Europe because they need both product ranges from us going forward. So, I hope that answers your question. Anything else?

49:48 Tim Savageaux

It does. And if, certainly if EMEA growth rates continue over 20 percent as they were in 21, your guidance looks fairly conservative.

And, just as an aside, you mentioned record backlog in Q3 as well, you know, the fact that that's increased to a new record, you know, I will assume that book-to-bill was pretty positive in Q4. But, you know, do you see customers ordering with, I think we saw this with Ciena, customers ordering, you know, farther out to get supply chain visibility as a driver of bookings? Or to what extent was that just more indicative of the strong demand, the accelerating demand that you referenced?

50:44 Brian Protiva

So I'd like to address two issues. First of all your comment about Europe at 20 percent. I think that's a little bit, I wasn't trying to make that statement Tim.

50:53 Tim Savageaux

You said it, not me, Brian.

50:56 Brian Protiva

What I said, it's Europe, it's strong and moving forward, remains strong. I don't say that it stays at the same growth rate necessarily. I think, you know, we spent a lot of time with our forecast. So let's stick with our, you know, EUR 650–700 million. I think that's showing almost 16 percent growth as a combined organization.

So, again, and Europe is strong in that model. I don't want to, you know, boil down to that 20 percent and leave that hanging because it could be, you know, somewhere less than that, US catch up a little bit. But as a company, we're well-positioned for the growth.

Record backlog, yes, backlog. I think, you know, ADVA was very conservative. We had big customers coming to us, saying, listen I want to place some big orders with you. But would it help us? If those big orders are placed, and they're standardized orders, and you come back around then and start adjusting those orders as it gets closer to delivery, it doesn't even help us plan.

You know, we're working with you, we trust you, we have very, very close relationships with our customer base. We're helping forecasting and stuff like that.

So we actually pushed back, other people just took those orders, a number of companies in the industry took those orders. So I think we were actually very smooth, even though we're building these record backlogs. It wasn't all just based on these companies coming out there placing 12 months in advance. And we'll continue to be well-positioned in, we believe in orders, and building backlog through the beginning of the year.

And so my statement would be that, I guess, you know, we are working closely with our customers. We are having to take some extra orders in there. We've tried to actually educate you guys on that in prior calls where we said, you know, some percentage of that … and we still were over, you know, well over a one-to-one book-to-bill, even when we x that out. And so I guess the question really is about demand and ordering going through this year. And I'd say that we could have continued to have a good period of ordering and backlog building in fact as an organization, because we've kind of pushed off and not asked for those big ones, but have asked for better transparency closer, even closer relationships, forecasting together, etc. Now, here comes a caveat: and that is, you know, prices in the industry are being adapted out there by players, suppliers, etc. And, clearly, we're part of an industry that is getting extra costs. And if you go into a model where you start to, you know, have price increases to customers, clearly they're going to be incentivized if you give them a period of time to take even bigger orders up front and longer term.

So there's many complex issues right now in our industry and we're trying to do the very, very best for our customers in that environment, and manage order rates and consistency, and in building the model. And so, I guess, in a nutshell, we will continue to do well in the ordering at some point, yes, could there be some kind of a turndown? I'm not sure because demand is strong enough today, and the funding off into the future is so big that it could actually very well lead to a situation where we have a smooth transition, as a company and hopefully even as an industry going forward.

54:29 Uli Dopfer

Let me add one more comment, Brian. Tim, about 75 percent of our order backlog, of our record order backlog has a customer wish date of the first half of 2022. So it's not that customers are ordering, you know, far into the next year or so. So the majority really has a solid wish date – if you can deliver is a different question – but they want it as quickly as possible.

54:55 Tim Savageaux

That's great color, thanks very much.

55:01 Operator

We have no further questions, so I would like to hand back to you, Mr. Steven Williams, for some closing remarks.

55:08 Brian Protiva

So I'll jump in for Steven, you guys, thank you for the nice questions.

As you saw in the presentation, clearly, you know, ADVA as a company's doing quite well, we believe it will continue to do, you know, well, going forward. We do have a lot of challenges that we are addressing and I think we continue to address. It is costing us a lot of energy and money and therefore, you know, the model is consistency right now: it's not, you know, growth and take-off, it's growth and consistency. I believe that that's probably the case for most of the industry, moving through the first half of this year. And I see that, you know, ADVA's well-positioned to enter the marriage with ADTRAN and together we're going to get a lot stronger.

Thank you for your support, fingers crossed that we get the last approvals from the government going forward. And if we do, I believe in a really strong, highly innovative, well-differentiated company going forward. So thank you for your time and interest and questions. I'm sure we will have another chance next quarter, but in the future, we might not be able to spend this intimate time with each other step-by-step, but you should be hearing from us next quarter. Thank you very much.

56:30 Uli Dopfer

Thank you.

56:32 Operator

Thank you, Ladies and Gentlemen, thank you for your attendance. This conference has been concluded. You may disconnect.