Tal: Thanks, guys, for coming. Perfect timing for our conversation. I've prepared a very long list of questions, but I'm going to ask you about the current events. Surprise, surprise. Ciena, great position. We spoke here, I'm going to give you the background a little bit, we spoke here at the conference a lot about data growth. We spoke about the applications that they're driving, and we just had a keynote from an internal Bank of America guy who basically spoke about what drives data, what drives growth.

And there is agreement that the networks that are needed are, or the networks need to support tremendous growth in data. With it, you're seeing pushout in spending of large customers or cloud customers. Can you give us the background to your recent statements on the quarter about some pushouts of contracts and also, something I asked you on the call I'll ask again, how do you distinguish between a pushout of a contract and a cancellation of a contract, or a pushout of deployment and cancellation of deployment.

Gary: Let me kind of start at the top and then the overall demand. Let's not sort of confuse quarterly commentary with the overall demand to it. Overall demand is super strong and has been very consistently for a long period of time. And we expect that to continue for all the dynamics that you guys sort of talked about, so sort of cover that.

We're dealing this year with the kind of whiplash as others are, too, around the whole supply chain, so supply/demand, etcetera. At the bottom end of our current range for the year, you're talking about 18% growth, which is pretty strong growth in any, by anybody's book. Part of the dynamics that we're seeing, and I'll answer the question in content players, cloud players, cloud players were up for Ciena 32% year-on-year, so clearly very strong segment.

We expect them to be greater than our corporate average for the year. So, midpoint of the range is 20% growth. The content players are not pausing. They're continuing to drive and build their network. No question about that. What we did see with the _____, it would have been even greater growth than that had they not said listen, we can't take all that equipment in one hit. We need to profile that out from our budgets and from our operational point of view.

And we're still seeing growth that will be in excess of 20% for the year for these guys in revenue. That's sort of a good news story and a positive piece. What we saw particularly in this quarter was tier one North American carriers where our supply chain is ameliorating. We're turning up at their front door with lots of trucks, and they're saying, whoa, this is all coming at once. Our sort of logistical aperture is only so wide. And by the way, our budget has not doubled this year and you're turning up with all of this. We need to profile it out a little bit and spread it out.

So, you've seen some of that, which really caused us to say, hey, we're taking the low end of the range down to 18% growth because that _____. So, the context of it is still, you're talking about not a lot of overall impact on the year. And then your last, the other part of your question, you've got about five in there, I think, Tal. Last part of your question, what's the difference between a cancellation and a pushout? One's a cancellation and one's a pushout.

This is rescheduling. We're not seeing the cancellations. This is, they want the kit, both the content players and the tier one carriers, they just can't take it all in one hit. Just because Ciena is ready to deliver everything now that they ordered in the last 18 months doesn't mean that the customer is prepared to take it.

Tal: Did something happen, did something change, though, for example, from the previous three months that suddenly they say not now?

Gary: I think what's happened, and I'm really being specific about North American tier one carriers. That phenomenon we're not seeing internationally and we're not seeing it amongst the content players. That's largely completely settled down and we're just delivering to profile. I think what happened with the North American tier one carriers in conversations with them is a number of their suppliers, not just Ciena, but just across their general ecosystem, have all kind of turned up at the same time.

So, servers and all the rest of the stuff, and all the other stuff that they ordered. I think that came to a head in the last sort of couple of months with them, which is sort of consistent with what we're hearing from other parts of different industries. I think it all sort of, all the trucks arrived at the same time.

Tal: Let's forget the ebbs and flows of deployment, one quarter better, one quarter weaker. Many of the investors here in the room are three-year investors, five-year investors. They're not just looking at the quarters. And the question is, how do you describe your position in the market? What drives your growth over the next three years, without thinking about when things are coming from a quarterly perspective?

Gary: A couple of things I'd say in context to that, there's this perception – you and I talked about this the other month – that the demand is cyclical. That's not true. If you look at the last two decades, demand as defined by bandwidth growth has grown 20 to 40% every year for about the last two decades. And that is continuing to go.

And then all the dynamics that we're familiar with, more people moving to the cloud, 5G buildouts, etcetera, dare I say the AI word, all of that's sort of in front. That's all pretty solid. One of the questions is around, if you look through the craziness of the last two to three years, what is Ciena's real size? What the real growth of the business, which I can totally understand given all the fluctuations going up.

The answer to the question is 7 to 8% growth. If you take sort of the midpoint of this year around what we think we'll finish at and you look back over the three to four years, you 7 to 8% growth. By the way, if you do the exercise for the last decade, the answer is 7 to 8%. In a market that's growing typically two to three, and I'm talking really optical now, and a demand characteristic for bandwidth of 20 to 30.

So, we're constantly taking cost out, and that's been the profile, and very consistent profile of the company. If you then get to answer your question around what do we think the next sort of one to three years is, I mean, clearly, if you take our core business, our optical business, we have a massive technology lead that's just about to be elongated with WaveLogic 6.

We were the first with 100 gig, we were the first with 400 gig, we were the first with 800 gig, we're the first with 1.6 terabytes, and it's not just the speed, it's the spectral efficiency and all the things that that will bring, and all the derivatives in that into the long haul, the metro, and pluggables, etcetera. We're going to do all the different variants of that with WaveLogic 6.

We've got tremendous technology, leadership, and relationships there, both with the cloud players and the major carriers around the world. And we're number one in data centric connectivity. We're number one in submarine connectivity. We're number one in the India market, which is the fastest growing market in the world right now. So, we're very well placed on the optical side for those dynamics that I talked about to continue.

The real question then is, okay, how do you grow faster than that 7 to 8% CAGR? And that really comes into question what we've been investing in for a long time now, which is the convergence of Packet Optical, which is an industry we've talked about for about two decades, but it's finally kind of happening I think now. And that's an upside opportunity for us. It really expands that TAM considerably. Basically, doubles that TAM over time to $20-odd billion.

That business right now, last year, was about $400 million. It's growing at a very healthy rate. This year will be in excess of half a billion. So, still a very small number, really, relative to the market opportunity, but we think we're very well placed now with the technologies to go expand in that space.

Tal: What drives the growth in this market?

Gary: It's really the shift in convergence to metro, so it's where people are converging their metro networks, which takes a lot of cost out for the carriers. Most of the tier one carriers around the world are at some stage of evolution of that, Verizon, etcetera, AT&T. And it's also the investment in broadband, so broadband _____.

You saw us make a number of acquisitions in the last 18 months really to strengthen our position on the optical side or the edge of the network, intercepting at 10 gig is where we're looking to do that. We're really filling out the whole converged optical packet portfolio.

Tal: On that, we are seeing trends from both ends, meaning wireless companies are, routing companies I meant to say, routing companies going down market and trying to have more, to consolidate the market to the router level with optical capabilities, and we're seeing Ciena going up market basically. Take us through the journey of the carrier, or the journey of the customer. What do you bring to the market that they don't have today, or they won't have from your competitors from other types of boxes? Not necessarily an optical box.

Gary: The religious war, if you will, is if you're coming from the IP layer, guess what you're going to lead with? You're going to lead with IP. If you're coming from optical, guess what we're going to lead with? There has been kind of an architectural battle going on in the last few years for it, and frankly, I'm biased to it, but I think what's winning is a more simplified architecture that's lower cost. And guess what? That bias is towards optical.

It's the old, the switch when you can route when you have to. The same thing could be applied to optical versus routing. And we've invested in enough capability around the routing space to be able to address the needs of the customers, but it's a much more simplified architecture and it's lower cost and incredibly simplified versus let's stick high end routers everywhere.

Listen, we're up against some very, very large and entrenched players that have got the large share of that market. But for us, it's all upside. We're the challenger and we can be disruptive, and we are being. We've won over 200 customers now in the IP packet space, and it's growing at 20, 30% a year.

Tal: You mentioned WaveLogic 6. Beyond just having another number on speed, what is driving the deployment of such a product and where do you see the demand?

Gary: I think it's multifaceted. It's, at the extreme, it's long haul, submarine type networks where you want to maximize the amount of capacity over long distance, and clearly 1.6 terabytes over single fiber. You've got that dimension to it. You've got the spectral efficiency that you can gain by putting multiple 800 gigs in the metro type space, which is the fastest growing space, whether it's converged IP or not.

And then you've got the whole interesting space of next generation of pluggables in their various forms. And also, potentially putting coherent technology into the datacenter. We've thought for a while that the datacenter at some point, pan forward, would run out of steam. And there'd be an intersect point where the economics and the technology of coherence would be qualified into the datacenter.

And the next version as we go through WaveLogic 6 will address that market. Now, we'll see about how quickly it takes up or whether that market is ready, but we're encouraged by what were the conversations we're having with some of the large hyperscalers.

Tal: Whenever I talk to you or I talk to executives at Ciena, I focus less about competition because I think that battle you won. Now, I'm more focusing about drivers. And I want you, if you don't mind, to take us through the three big pillars, there are more, but I want carriers, cloud, and cable, telecom carriers, cloud, and cable, and tell us what are the big drivers for growth? What are the big projects, the big things they're doing that drive your growth within these customers?

Gary: Let's start with at least a third of our business comes directly from cloud, directly from cloud, and a lot more of our business comes from cloud indirectly. When they go outside of North America in particular, they don't necessarily, and they don't want to necessarily own the fiber and all the rest of it. It's a massive segment for us.

What's driving the growth there is (a) more datacenters, more applications going up, more traffic, more eyeballs, etcetera. The other piece that I don't think is fully appreciated is machine-to-machine traffic growth, and that is a big factor in what's driving the network growth for the cloud players. And I don't think that is sort of fully appreciated.

And the diversity of the networks now are quite complicated, they're quite large in scale, as you'd expect, but these are the major players. The content players are the major owners of submarine cable architecture now. They're the number one players in the world. And it makes a lot of sense because they're linking up their datacenters and they're getting into growth in international markets.

I mean, the amount of activity in India right now from the cloud guys is pretty interesting. It's a multifaceted relationship. It's on long haul, it's on submarine, it's in different countries where they're growing national penetration. It's also into metro and connecting their short haul datacenters. Drivers for growth there are all of the things that I've just talked about, including machine-to-machine, and I also would speculate, of course it wouldn't be a presentation here without mentioning the AI acronym, of course.

Tal: You know it's my next question.

Gary: Trying to get out ahead of that. Listen, the answer to that is who knows to it. I mean, we're seeing a lot of machine-to-machine traffic anyway existing. The issue is a large part of our focus right now is intra datacenter and the fabric and how that plays out and what they've got to do. But you have to believe that that's going to come out of the datacenter at some point and it's going to drive and it's going to drive growth.

But all of the conversations we're having with these guys, notwithstanding all the AI conversation, is all super positive around the expansion of their network. All this stuff around their budgets, their reduction in force, and all the rest of it, we're not seeing any, they're continuing to invest strongly in their network, as you'd expect. And their business models, by the way, are still pretty solid.

I think most of us would be pretty envious around their business models. Tier one carriers, the big growth with them is really into, and I think to some extent into the cable, too, but it plays into there is really the growth in broadband. You've seen that in North America, this investment in rural(?) broadband. That's a major driver, both with tier ones, tier twos, and tier threes.

You're seeing very similar initiatives in broadband in different parts of the world, too. A lot of governments, for all reasons that you can understand, is propagating investment in broadband technology. So, that's, and then the second point with the carriers is really the whole automation and convergence of their metro. That's really where all their costs are, and they've got multiple networks.

People think about these carriers as having a network. They've got multiple networks really. And the classic in the metro side is their IP network and their optical network, and they're actually, most of them run them separately. Most of them are actually run separately. That's a massive opportunity with these guys.

The cable folks is more around the sort of broadband piece, and then moving away potentially from a DOCSIS type architecture to an optical architecture at the edge particularly. And I think some really strong opportunities with that, because I think increasingly over the next few years, you'll see optical at the edge with these guys and not just the DOCSIS piece.

Tal: None of the opportunities you mentioned are short-term in nature, meaning I can see us talking here another three years on the same things and it's going to be driving. On the other hand, we did talk about pushouts and deployments, etcetera because of timetable. How much visibility do you have to the new timetable that you've given us for deployment? What is the risk that another quarter and another quarter there's going to be another pushout or another pushout to deployment plans?

Gary: Listen, I think that generally if you look at the, all of the carriers, they want the equipment, they've got the demand, it's all about just a handover from the whole whipsawing of supply chain. That's purely it. Now, they will have to manage the budgets and the rest of it, but that's really all you're seeing. And even if you take the downside to that, you're still talking about 18% growth, so it's a pretty good absorption by the carriers and the cloud players really.

Then I think the other part of your question, when does normal service resume, my own view is I think as we go through '24, barring no other geopolitical disturbance. I think you begin to see a return to a more normalized piece. I mean, supply chain, lead times are getting back to, whether they've gotten exactly back there is a whole different question, but they're not the items anymore. I think you're dealing with a very short-term absorption issue from the carriers.

Tal: Backlog, we calculate, we published maybe two months ago, three months ago, we published a note where we looked at backlog as a percentage of revenues for all our companies and Ciena is high up, the highest ratio backlog to revenues. What's happening with backlog [overlapping sound] on the conference call, what's happening to backlog? And then if revenues are growing 18% but backlog is declining so much, it means that the orders are weaker. How should we interpret the declining orders?

Gary: First off, I'll take the accolade. It means more people want our stuff than anybody else. As we sort of go through this uncharted territory of demand and supply being out of balance and then getting back into balance, I think a natural piece to that, and I'll give you a sort of statistic, I think it was the end of our Q3 '22, our orders were up year-on-year 60%, which reaffirms your analytic. 6-0 in demand.

The other side of that mountain is how do you ship all of that out and the dynamics that you're seeing. Now, as you reduce lead times, customers do not need to place orders further out, and they've been used to placing, during this last environment, orders out for a year and beyond. They don't need to do that anymore. It's a natural part to that is that they don't need to order as much, and they've already got orders and they filter through.

Now, none of this is absolute because they're always ordering new stuff and all the rest of it. But what we expect to see is orders lower than revenue for a couple quarters. That's sort of to be expected, and that's sort of what I think we're seeing. But don't confuse that with demand because we're still having record shipments out there and the two will come into balance.

Now, precisely when will they come into balance? Tough to tell, but it's not the only datapoint that we get. We obviously have very sophisticated relationships with these guys around their projects, their pipeline, and all the rest of the stuff that you expect. We're seeing nothing but activity around planning and future pipeline stuff. So, we take great comfort in that.

But, yeah, we are going through this period where we've got less orders and revenue, but it's to be expected.

Tal: You had also elevated inventory levels. How do we interpret the elevated inventory levels and what's the outlook for that?

Gary: We built up inventory of parts that were waiting for the, I guess what's been termed the golden screw stuff, which we're all kind of familiar with. We're beginning to bleed that off. I think we had the first quarter, last quarter of a reduced inventory. It went down about $80 million, and we actually generated cash as well at $230 million.

So, we're beginning I think to see that come down. I would expect our inventories to continue to come down for the remainder of this year as we ship stuff out and we get rid of some of these other key components. It should come down.

Tal: By the way, if there's any questions from the audience, just raise your hand. We have a microphone. I want to touch on margins. Margin expectations, on one hand, you are talking about slightly lower revenue growth. On the other hand, margins are still 43% I think for the year, you guided. What's the link or what are the puts and takes of margins when it comes to growth and anything you can do on your end to improve the margins?

Gary: The function of margin right now to us is an overhang from increased costs on inventory and supply. That's going to be with us a little bit. And then right now is really mix. We're shipping out more line systems, which is great for the future, but they tend to be lower margins than the higher end fill. We're going through that dynamic.

But we're still, even with that, last quarter we were almost at 14% operating margin even though we know we're not firing on all cylinders, and you've still got an overhang on the margin. We expect margin to get back at some point into the mid-40s, which is where we quite comfortably prior to all of the COVID and supply chain craziness. Precisely when we get there has got a little bit of time for us to go figure out, but you can see we're making decent progress.

But I would expect the margins to be under pressure for the next couple of quarters because of mix.

Tal: Is there any change in the pricing environment from two things? Number one is sometimes when spending is down, competitors start acting crazy, and sometimes when spending is down, customers are just putting the finger on the brakes and saying you have to give me better pricing. Is there any change in the pricing environment?

Gary: Not really, and I would also say that spending's not down. And I think, I've heard this is quite a lot because they go, wow – listen, we're growing at 18% mature. It's bottom of the range. [overlapping comments]

Tal: I'll tell you what the concern is. First of all, when you look at 18%, it averages high growth…

Gary: When you get to the 7.5 for the three years.

Tal: So, number one. Number two, that the issue is we are hearing cloud companies saying that they're slowing to a certain degree. We are hearing telecom companies, telecom carriers saying they're slowing. The concern is not the 18% of 2023. That's not the issue. What we are looking at is 2024, is there a risk that customers will basically put the brake on and say, we are going to go to absorption phase and we're going to sweat out our assets and we're not going to buy more.

That's the risk. The risk is not really this year as much as it is, whether this slowdown slides into next year.

Gary: A couple of things I'd say to that. First of all, we're going to have an outsized backlog even going into next year, which gives us greater visibility. Second, well we're not seeing any of those dynamics with any of the customer base that we're talking to. We aren't. And on the pricing side, we're really not seeing anything particularly different than we've seen.

On the planning side for the customer base, generally we're not seeing any change in their approach to stuff. Their absorption actually, ironically is really this year. They should be in much better shape next year from a logistics and from a budget point of view. And again, our growth is not predicated on their increase in budgets. It's what they spend it on. They've been very consistent around the growth in their networks.

There's this notion in the investor community about things are going to fall off a cliff generally in the industry _____. It really hasn't because you've got 20 to

30% growth in the bandwidth demand. Now, can you get ebbs and flows of it between particular customers? And I say, yes, absolutely. Of course. And customers will go through areas of investment and not and different areas.

But frankly, we've had that for years, and Ciena has been able to navigate through that because we've got a very diversified set of customers, we have a diversified set of applications. To think about, if we're right about our TAM growth, that should accelerate our growth.

Tal: Last question, as time permits, is about when we talk a lot about slowdown and pushouts, etcetera, we talked about the US. You said it before. Can you give us kind of the rest of the world? What's happening in Europe? What's happening in India? What's happening in other parts?

Gary: I touched on India, and that's kind of the fastest growing place right now. We're up about 88% year-on-year from a very small base in there. But that market clearly is in – it is one of the places that is cyclical, and it is investing in it. And the whole 5G rollout there is, you've got one to three years of good growth.

Europe, the opportunity continues to be solid. There's a lot of talk about the replacement of Huawei there, which is a multiyear tailwind that's continuing. And then you've got good growth in other markets, particularly Japan, particularly ANZ is very strong, different part of Latin America. Same kind of dynamics. People are investing in the network, and so we see some good opportunities internationally.

Tal: We ran out of time. Thank you so much.

Gary: Thank you, Tal. Thanks, folks.

END