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PRESENTATION

Operator

Welcome to the Ciena Corporation first quarter 2017 earnings conference call.

(Operator Instructions)

As a reminder, today's conference is being recorded. I'd now like to introduce your host for today's conference, Mr. Gregg Lampf, Vice President, Investor Relations. Sir, please go ahead.

Gregg Lampf - *Ciena Corporation - VP, IR*

Thanks, Liz. Good morning and welcome to Ciena's 2017 first-quarter review. With me today is Gary Smith, President and CEO, Jim Moylan, CFO, and Steve Alexander, CTO. This morning's press release is available on National Business Wire and Ciena.com. We also will post to the Investors section of Ciena.com an accompanying investor presentation, including certain highlighted items for the quarter being discussed today.

In our prepared remarks, Gary will discuss Management's view on the market and our overall progress, and Jim will provide details on our results as well as guidance. We will then open the call to questions from the sell-side analysts, taking one question per person with follow ups as time allows.

Before turning the call over to Gary, I will remind you that during this call, we will be making certain forward-looking statements. Such statements are based on current expectations, forecasts and assumptions regarding the Company that include risks and uncertainties that could cause actual results to differ materially from those statements discussed today.

These statements should be viewed in context of the risk factors detailed in our most recent 10-K filing. Our 10-Q is required to be filed with the SEC by March 9, and we expect to file by that date. Ciena assumes no obligation to update the information discussed in this conference call, whether as a result of new information, future events or otherwise.

Today's discussion includes certain adjusted or non-GAAP measures of Ciena's results of operations. A detailed reconciliation of these non-GAAP measures to our GAAP results is included in today's press release available on Ciena.com. This call is being recorded and will be available for replay in the Investors section of our website. Gary?

Gary Smith - *Ciena Corporation - President and CEO*

Thanks, Gregg, and good morning, everyone. And thanks for joining us today. With the first-quarter results we announced this morning, we're off to a very good start to FY17.

Revenue grew approximately 8.5% over Q1 of last year. The fundamental demand drivers as well as our market momentum continued to strengthen.

In the quarter, we won significant customers in the US, India, Japan, and the Middle East. And we continued to gain share in key segments of the market, including DCI and submarine applications. As a result of all this, we saw our highest ever product order inflows in Q1. We shipped more product in Q1 than in any previous fiscal quarter, and we ended the quarter with the largest product backlog in Ciena's history.

All of this clearly demonstrates that we are winning in today's market. And that's largely due to our strategy to diversify the business with targeted investments aimed at key geographies, market segments, new product lines, and a broad range of high-growth applications.

And as we discussed in December, we are also positioning ourselves to win the next race as the IT and telecom worlds converge. And we're helping network operators transform their networks and their business with an approach that leverages openness, co-development, and agility in how technologies are consumed.

In Q1, we continued to make progress in delivering these capabilities, especially with platforms like Waveserver and Blue Planet. Both of which bring IT tools essentially to the telecom environment. For Waveserver, it was a record quarter in which we added 11 new customers. Waveserver sales were up more than 10 times over Q1 of 2016, albeit from a relatively small number.

And since closing the quarter, we've won another piece of significant business with a top-five web-scale provider, which we expect to result in volume shipments as early as Q2. Obviously, we're very pleased with the market's response to this platform, including the recently announced Waveserver AI that leverages our next-generation chipset to achieve unprecedented capacity and service densities. And while it's still early days, based on the customer adoption we've seen to date as well as our forecast for the second half, we now believe that Waveserver revenue will likely be at the high end of our expected range of $50 million to $100 million for the full fiscal year.

We also added two more orchestration customers for Blue Planet, both tier 1 operators in North America and the Middle East. Blue Planet is allowing us to transform the conversations we're having with our customers, from just the strategic value of hardware as part of their infrastructure to the strategic value of applications and services related to transformation across all facets of their business.

In fact, the relationship between software and overall customer engagement has become so interrelated for us that we've recently combined our Software and Services organizations into a global unified team. We've learned essentially that while customers are embracing the new environment, they want and need more guidance in implementing software-enabled orchestration. And we believe that this unique model will benefit both Ciena and our customers as they continue to evolve towards openness.

This seamless integration of Software Services and programmable hardware really underscores our ability to elevate and differentiate the value we're bringing to market. It is essentially this combination of technologies and services.

As an IT mentality increasingly influences network decisions, we're providing customers with much greater choice and agility in how they manage their networks and their business. This further separates us from our competitors, and it is increasingly apparent in our differentiated performance.

Before turning the call over to Jim, I'd like to take a moment to thank Francois Locoh-Donou for his many contributions to the growth and success of the business over the last 20 years. As you know, Francois has accepted the position of CEO at F5 networks and is stepping down from Ciena later this month. We will certainly miss him, but we wish him continued success in his next assignment and in his career.

In the meantime, we've activated our succession plan, which takes advantage of the depth we've built on our global leadership team. In addition to uniting Software and Services, we've also brought together global sales and marketing under a single leader.

All hardware development will continue to reside in our Networking Platforms group, and the reporting segments remain unchanged. We're confident that we've got the right structure, and more importantly, the right leaders in place to continue to drive our business forward as we aim to become the industry's leading enabler of choice. Jim?

Jim Moylan - *Ciena Corporation - CFO*

Thank you, Gary, and good morning, everyone. Our Q1 results clearly demonstrates Ciena's differentiated performance against the competition, and they highlight the importance of the investments we've made to build a broad-based, diversified business. I'd like to take a moment to highlight a few of the areas of diversification that are contributing to our continued faster-than-market growth.

Waveserver now has 36 total customers. Frankly, we're thrilled with the market's adoption of this relatively new product and its open approach. The success of Waveserver has helped us claim number one market share in DCI applications. And in fact, Dell'Oro recently named Ciena the market leader across every quarterly DCI category that they track.

Our two new customers from Blue Planet bring us to 20 total customers. Use cases for Blue Planet are varied, and we believe strategic to our customer's business. For example, our new North American Tier 1 Blue Planet customer is using the platform to orchestrate bandwidth on demand between data centers, while our new Middle Eastern customer is using Blue Planet to automate optical services across the wide area network.

These use cases are representative of the kinds of engagements we're seeing for the platform. And we expect the recent announcements of Blue Planet Analytics and Blue Planet MCT to drive additional use cases.

We also added three new customers for our 8700 Packetwave Platform for a total of 43. The 8700 Platform is part of our Packet Networking portfolio, which had another excellent quarter in Q1 with revenue up 50% over the year-ago period.

Taking a look at customer segments, approximately 30% of revenue came from non-telco sales. This included direct sales to web-scale customers in our expected range of 5% to 10% of total revenue. Notably, a major web-scale player was a top-five customer in the quarter.

And our momentum continued in the submarine upgrade market as well. In fact, in the first industry analyst report to measure the SLTE upgrade market, Ovum recently reported that Ciena now holds nearly 55% of this market.

Turning now to our financial performance in fiscal Q1. Revenue in Q1 came in at $622 million, slightly lower than expected, partially due to an ERP upgrade that affected our shipping process longer than we anticipated, limiting our flexibility at the end of the quarter. Notwithstanding, we had an excellent quarter that was driven by continued growth across key geographies.

APAC revenue grew nearly 60% over Q1 of last year. India, in particular, continues to be a fast-growing market for us. Submarine applications remain a significant driver in India, but we're also now engaged with every major Indian carrier.

Beyond India, we're seeing opportunities emerge with web-scale players across APAC, Both local ICPs as well as US-based players expanding in the region. We believe APAC will continue to be a growth driver over time.

Our performance in EMEA continues to improve, with revenue up 13% year over year. We're seeing traction in Europe, particularly with the web-scale community, including ICPs and exchanges and also in submarine applications. And Tier 1 service providers in both Europe and the Middle East continue to drive revenue growth in the region. Overall, international sales made up 39% of total revenue in Q1.

And in North America, revenue grew 14% year over year, exclusive of AT&T, driven by a strong quarter with web-scale customers and Tier 1 service providers. AT&T and Verizon were both 10% customers in Q1. Our overall North American business continues to be very well-balanced, with solid contributions from MSOs, enterprise, government, and R&E customers as well.

Q1's adjusted gross margin was 44.9%. Operating expense in Q1 was $226 million. We achieved $53 million in adjusted operating profit in Q1, or 8.5% adjusted operating margin.

We continue to take steps to improve our balance sheet, having repurchased an additional $46 million of our convertible debt. We also refinanced our existing term loans shortly following quarter end, further reducing our debt by approximately $93 million and reducing our go-forward interest expense on the remaining term loan borrowings. And as a result of our continued balance sheet improvement, we recently received two upgrades from the debt rating agencies.

Going forward, we expect our adjusted interest expense to be reduced by approximately $2 million per quarter due to our debt reduction and refinancing efforts. In Q1, we used $26 million in cash from operations, largely due to a very back-end loaded quarter. We ended the quarter with $1.05 billion in cash and investments. And finally, adjusted earnings per share in Q1 was $0.26.

I will now turn to guidance for our fiscal second quarter. We expect revenue in Q2 to be in the range of $680 million to $710 million. We expect Q2's adjusted gross margin to be in our mid-40%s percentage target range, and we expect adjusted operating expense to be approximately $240 million.

I'd also like to provide some commentary on our annual guidance. Based on our first-quarter performance and our expectations for the remainder of the year, we continue to expect to achieve the results for the full fiscal year that we indicated in December.

You'll recall that in addition to expecting to continue to grow revenue faster than the overall market growth rate of mid-single digits. We said that for FY17, we expected adjusted gross margin in the mid-40%s percentage range, adjusted OpEx to average approximately $235 million per quarter, and adjusted operating margin in the range of 11% to 13%.

In closing, we believe Ciena is in an excellent competitive and financial position. We have built our portfolio and our business in alignment with the direction of the market. And we are expanding the kinds of conversations we are having with customers, as they increasingly embrace IT capabilities to transform their networks and their business.

We remain confident that over time, we will continue to drive greater value for both our customers and our shareholders as we position Ciena as the leading enabler of choice in the marketplace. Liz, we will now open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Rod Hall, JPMorgan.

Rod Hall - *JPMorgan - Analyst*

I guess I wanted to just ask you, Gary, if you could talk a little bit more about India? India seems like a large opportunity this year and I wonder if you could juxtapose the size of it with something like Verizon. It sounds like it's probably significantly larger, maybe your largest growth opportunities.

So is there anything you can do to quantify that opportunity for us? And then Jim, could you just talk about this ERP impact? Do you expect that to carry over into fiscal Q2 and are you pretty much catching up in fiscal Q2 for the negative impact in Q1? Thanks.

Gary Smith - *Ciena Corporation - President and CEO*

Thanks, Rod. Let me take the first part of that. I would say and I think most of you have read what's going on in the India market right now. It's a confluence of things that have come together to stimulate the growth in that marketplace. There are some very large builds underway, essentially to underpin bringing 4G basically out to the marketplace there with the number of carriers investing significantly.

We've been there for a number of years. I mean this is an investment that we've made dating back 12 years, both in terms of software development teams and market development teams there. It is our fastest growing country. And we are basically with every single major carrier in India and we are very well-positioned for it.

So I think it's a multi-year opportunity; it's not just one quick buildout that's getting all the attention. It's across a very broad base of technologies for Ciena and really, it's a market that I think will be very, very high growth for us over multiple, multiple years.

Jim Moylan - *Ciena Corporation - CFO*

And on the ERP upgrade, we have been engaged in this upgrade, really, for going on two years. It's a huge project for us ; we spent a lot of money. We've upgraded to Oracle Release 12 and we cut over during the quarter. We -- it ended up being that bringing up shipping capacity to full capacity took a bit longer than we thought.

And that did affect our revenue in the quarter. We believe that, that's behind us now. We should be able to operate at full capacity for the quarters going forward. There is a bit of a pick-up in Q2. We -- if we hit the midpoint of the guidance for Q2, we'll be, frankly, ahead of plan on both revenue and bottom-line.

Gary Smith - *Ciena Corporation - President and CEO*

Rob, the other point I would make is there's never a good time to implement these ERP systems but we felt that given the scaling of the business, it was very important that we built a bigger engine for the business that had global reach. So this should really underpin now a much greater velocity capability for the business going forward.

Rod Hall - *JPMorgan - Analyst*

Great. Thanks, guys.

Operator

Doug Clark, Goldman Sachs.

Doug Clark - *Goldman Sachs - Analyst*

My first one is on Verizon popping up as a 10% customer. Is this due, in part, to kind of early Metro deployments? And then secondarily, looking at OpEx jumping kind of above the expected midpoint or average OpEx range for the full year, can you talk about why it's jumping in the second quarter and then is it, I guess implicitly expected to come back down in the second half slightly?

Gary Smith - *Ciena Corporation - President and CEO*

Let me take the first part of that one, Doug; I'll take the Verizon. We are seeing initial stages of the Metro rollout that did contribute to them becoming a 10% customer in the quarter. I would also point that the other aspects of our business with them are also doing well, including the long-haul packet, ethernet switching, and their global-based switching network as well. So we're seeing good adoption across the broad range with Verizon.

Jim Moylan - *Ciena Corporation - CFO*

And on the OpEx point, yes, we are on plan; in fact, we're slightly ahead of plan on OpEx and below the expect OpEx for the first half if we hit $240 million in the second quarter. OpEx is -- there are going to be projects, particularly in R&D, sometimes in real estate and even IT that are going to cause OpEx to move from the mean for the year up and down.

And you saw that in Q1, we were below the average of $235 million for the quarter that we talked about and in Q2, we're going to be slightly above the average for the quarters but we still expect OpEx to average roughly $235 million per quarter as we move through this year. So by definition, it will come down some.

Doug Clark - *Goldman Sachs - Analyst*

Thanks, guys.

Operator

Vijay Bhagavath, Deutsche Bank.

Vijay Bhagavath - *Deutsche Bank - Analyst*

I think my question is on the cloud optical business. Help us understand if you anticipate any volatility or higher volatility in the DCI optical build-outs and the reason I ask is some of your peers have been seeing more volatility than they can handle in this cloud DCI optical rollout so I'd like to get your viewpoint. Thanks.

Gary Smith - *Ciena Corporation - President and CEO*

Yes, I mean given what we're doing with Waveserver and the other platforms that address that space, I think the difference between us and the competition is where many of them are many niche-based in terms of engagement. We've got a very broad global engagement with the ICPs. I mean we help them not just in North America but outside of North America, including all the submarine stuff, including places like India.

And I think that allows us a much more diverse and broader-based engagement, frankly, with a broader set of customers in the DCI connectivity market. So while we're still seeing fluctuations customer to customer, overall, we're seeing a very positive growth in that space but we expect to continue and those fluctuations, because we've got such a broad base of customers, has really just led to nice solid growth performance for us overall. And we continue to take market share in that space.

Jim Moylan - *Ciena Corporation - CFO*

And as Gary pointed out, we have a pretty significant win at the end of at the beginning of this current quarter Q2, which will show itself up in revenue this year. Shipments in Q2, potentially revenue in Q2.

Vijay Bhagavath - *Deutsche Bank - Analyst*

Perfect. Jim, a quick follow-on for you would be timing of maintenance service contracts. Did you see any pronounced delays in maintenance service renewals? Thanks.

Jim Moylan - *Ciena Corporation - CFO*

I wouldn't say delays. We do often try to get multi-year maintenance agreements with our customers and sometimes it takes a bit longer to negotiate those because there are multiple years under consideration. So I wouldn't say that we've seen any slowdown there.

Vijay Bhagavath - *Deutsche Bank - Analyst*

Thank you.

Operator

Tal Liani, Bank of America Merrill Lynch.

Tal Liani - *BofA Merrill Lynch - Analyst*

I have a few questions; maybe I'll start with the Blue Planet software. How is it trending this quarter and how is it versus your previous expectations of up $20 million to $25 million for the year? And if I can squeeze in one more, I want to -- I had a broader question about North America overall. What are the puts and takes in North America for 2017? You highlighted a few things; if you could summarize it for the region versus the rest of the world kind of?

Gary Smith - *Ciena Corporation - President and CEO*

Why don't I take the first part of that, Tal. The Blue Planet is tracking well. We had two new Tier 1 customers in the quarter and looking at the pipeline, we expect to add more, obviously, as we go through the year. The engagement is still nascent in this space but I do think it will be on track to be in that $25 million-type range for the year.

We seem to be tracking well to that and I think we're adding additional capability through it. The analytics suite that we announced and the MCP capabilities as well will continue to drive it as we come out of the year. And I think the point about it is it's a different set of engagements with customers as well, which is we're seeing a great deal of richness around that.

And I think that's opening up additional opportunities for us on the services side, which is why we've combined those elements as well. So I think the quick takeaway is we're on track and we've seen very good traction with it.

Jim Moylan - *Ciena Corporation - CFO*

On North America, when you include AT&T, the growth rate comes down because as we've said, AT&T, we expect to be flat to down for this year; that's as expected. By the way, their CapEx for the year are down a little bit from last year. That's not always just positive of our results but they are focusing on moving to next gen as quickly as they can.

And I'm happy to report that we are actively involved in many strategic projects with them, including software services and hardware ; expect that to be a strong customer for us for the long term, although flat to down for this year. As we said, absent AT&T, North America grew by 14%. I -- that is indicative of what we're doing across the board in North America.

We are number one market share provider in North America. I believe we can continue to grow market share with the success we're having with the ICPs, with the success we're having on the Metro deployments that are taking place. And the other thing I'd say is that as you heard from Mobile World Congress, people are beginning to think about 5G.

And although deployments are pretty scattered now; it's early stages and we don't expect it to be a huge driver for us right now, we are extremely well-positioned to take advantage of the growth and demand for capacity that will come out of 5G implementation. The other thing that's happening is that MSOs are talking about this -- taking denser networks closer to the customer.

The initiatives are called the Fiber Deep. We're extremely well-positioned to win in that section as well so I'd say this year we're going to do well in North America. We'll grow even though AT&T will be flat to down and we expect to continue growing in America ; it's a great place for us to deploy our technology.

Tal Liani - *BofA Merrill Lynch - Analyst*

Got it. Thank you.

Operator

Simon Leopold, Raymond James.

Victor Chiu - *Raymond James & Associates, Inc. - Analyst*

This is Victor Chiu in for Simon Leopold. Can you provide us an update around your progress with web-scale customers and the percentage of sales? And also just kind of where your expectations are around FY17 for this vertical?

Gary Smith - *Ciena Corporation - President and CEO*

Let me take the first part of that; I think we've covered it in some of the commentary here. We've -- as Jim said, we added a significant piece of business from a top five web-scale player which, really, was a competitive takeaway on a pretty large scale. And I think it's testament to that Waveserver technology that we're deploying now.

So I feel very good about the overall space, not just in North America as well. I mean we're seeing, as I said, global capabilities that we're able to bring to bear. Because we've got global scale, we have all of the major carriers pretty much around the world, we're able to be a fabulous partner for these ICPs in terms of finding them the right kinds of capacity and connectivity, not just in North America, but in international markets as well.

And the submarine space where they are now number one, two, and three in terms of the Atlantic cable capacities as well. And Ciena's got well over 50% of that marketplace, as Jim said. So I'd encourage folks not to just think this as connecting data centers and within North America; that's a large part of it.

But this is a much more global phenomenon across much -- many different facets of our technologies that we're able to deploy. So that's why we're sort of uniquely positioned to be able to address this marketplace and why we don't see as many fluctuations as other niche players do as well. Jim, any --

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Jim Moylan - *Ciena Corporation - CFO*

The other thing I'd say is that the 55% market share that we quoted was in the SLTE upgrade market. There is coming a new build market and we are extremely well-positioned to be a player there with our new engagement with TE SubCom, so I feel really good about that submarine market and how the ICPs are applying there.

Victor Chiu - *Raymond James & Associates, Inc. - Analyst*

Did you say the percentage of sales from web-scale customers?

Jim Moylan - *Ciena Corporation - CFO*

We said between 5% and 10%. And that's the direct sales. Remember that we sell indirectly, including in the submarine business, tons of capacity to the web-scale players.

Victor Chiu - *Raymond James & Associates, Inc. - Analyst*

Great and just a quick follow-up. We pay a lot of attention to Verizon as a reference project but where are the other carriers in terms of implementation similar architectures and opportunities for 100G Metro?

Gary Smith - *Ciena Corporation - President and CEO*

I think you're seeing this across a broad sway; in the North American environment, we pretty much had a clean sweep of all of those Metro deployments and their begetting places like CenturyLink, et cetera, AT&T, Verizon, Comcast. All of the major players are deploying and we're pretty much -- we had a clean sweep of wins there with our 6500 Converged Packet Platform.

So North America, incredibly strong and across a broad sway of customers, and you're also seeing the same phenomenon internationally as well -- you saw EMEA up year over year, which is pleasing for us. You've seen great growth in APAC as well and also I would say, the other phenomenon of you've seen is really the move to 200G, which we've got the leading market share.

We're the first to market with that and that also is a great technology being deployed into the Metro space, and particularly with people like ICPs as well. So very broad sway of adoption across the carrier marketplace globally.

Victor Chiu - *Raymond James & Associates, Inc. - Analyst*

Great. Thank you.

Operator

Paul Silverstein, Cowen and Company.

Paul Silverstein - *Cowen and Company - Analyst*

If you already answered these questions, my apologies to you ; I was on another call. But first off, I think I heard you say orders were at a record level again but in general, how would you characterize linearity for the quarter and visibility today versus 90 days ago and a year ago? And the other question is relative to the previous question, Jim and Gary, can you all actually quantify how many Metro deployment wins you have and how many of those have now advanced the revenue rollout stage?

Gary Smith - *Ciena Corporation - President and CEO*

Let me take the first part of that, Paul. I think the first one was linearity in the quarter. It was more back-end loaded in this quarter, principally because we upgraded the ERP system when we closed down shipping for awhile. As I said, there's never a good time to do that ; we've been in the planning for it for two years.

We felt very strongly that it's not just an ERP reimplementation; we basically reengineered a lot of our global processes, because we felt strongly we needed to build a bigger engine, basically given the scale of the business globally. So that caused us to have a very tail-end loaded quarter more than normal; took away a little flexibility at the end there. But I think that was driven, really, principally by the reengineering project that we did.

Overall, though, I would say given the commentary about the order flows overall and the strength of the backlog right now is the largest that we've had from a product point of view, I think our visibility has improved. Your direct question was in the last 90 days, did it improve ; I think it's improved. And these are the -- the best -- the key element of it is visibility to orders but it's also the softer elements around engagements with the customers and understanding their plans and overall, I think we've got we've got better visibility into the year than we had a few weeks ago.

Jim Moylan - *Ciena Corporation - CFO*

One of the reasons that we did use cash in the quarter is we built inventory in the quarter and you can see that, that happened both in deferred cost of sales which is material which is out at customer sites awaiting either deployment or acceptance and we built finished goods inventory in anticipation of the increase in demand which is coming.

So Paul, I'd say we have very good visibility. We're not seeing any sort of slow down from any of the things that other people had mentioned. We're not seeing a M&A-based slow down. We're seeing wins across the board and so we feel really good about what's going to happen for the rest of the year.

On the Metro and regional piece of the business, the best I can give you is this. What we have said is that and this goes back a couple of years, we've said that Metro was roughly 40% of our business and long-haul was roughly 60%. We are now seeing that it's about 50%. 50/50 Metro and long-haul so the change that we projected at that time to sort of reverse those percentages is occurring.

And we expect that it will continue to occur. To sort of draw the line and by the way, those are estimates because drawing the line between Metro and long-haul deployments is not always perfectly clear. So that's what we can tell you about it.

Operator

Michael Genovese, MKM Partners.

Michael Genovese - *MKM Partners - Analyst*

I just wanted to ask about (Technical Difficulties) questions. Number one, can you just kind of comment on market share trends at Verizon and the Metro project versus your competitor there? And then secondly, given your clean sweep in the US, could you talk about your market share targets in Europe and the competitive environment over there versus in North America? Thank you.

Jim Moylan - *Ciena Corporation - CFO*

On Verizon. We have said repeatedly that we expect that we will get at least our fair share, half, if not more and we base that on information that Verizon has given us about the cities that we would build out to. As far as whether we get a lot more than our share or a bit more than our share it's really hard to tell.

We're in the really early days of deployment. Things are going well. They're happy with our gear; we're working with them well. We think and we feel good about where that project is going.

Gary Smith - *Ciena Corporation - President and CEO*

On Europe, we had some challenges last year, as I think we shared with everybody, some of which were self-inflicted ; some of which were market dynamics. We're seeing a much better execution in Europe since we've made some changes there and realigned some of our priorities and we're actually, frankly, seeing good traction and pipeline build there.

We're up 13% year on year in the quarter and we think we'll have reasonable growth in Europe this year and again, it's the same kind of mix of customers. We're seeing web-scale folks moving into Europe, trying to grow their business there and we're well-positioned with that because of our relationships with most of the European carriers and their various flavors, and also the submarine business, particularly Transatlantic.

So we see the dynamics there as being way more positive for us than this time last year. We're pleased with our progress and I think we're at the point where we're beginning to actually take market share back from where it was.

Michael Genovese - *MKM Partners - Analyst*

Thanks again.

Operator

Meta Marshall, Morgan Stanley.

Meta Marshall - *Morgan Stanley - Analyst*

I wanted to ask two quick questions. The first was just the step-down in the consulting and network design revenues for the quarter, I just wanted to see that kind of normal seasonality where there are certain projects that were finishing up? And then the second was just touching base on LatAm ; other vendors have notice softness in that region, but is that something you were picking up on as well or were there some projects wrapping up that contributed to the downturn? Thank you.

Jim Moylan - *Ciena Corporation - CFO*

Yes, on the services side, Meta, there's always timing involved when projects get recognized when they get completed. And so we're not seeing really any change, fundamental change in that services business.

Gary Smith - *Ciena Corporation - President and CEO*

On the LatAm side, as you alluded, I think we've seen some downtick in there that we kind of predicted. We've had two or three years of fabulous growth there and penetration of the market. I think specifically in Brazil, you've seen a quieting down of the investment, really, based on big build-outs in infrastructure around the Olympics and the World Cup, the World Soccer Cup and I think you've seen a bit of a tail-end of that.

Overall, I think in terms of market share, I think we're doing well there, particularly in places like Mexico, but I do think after the extraordinary growth, frankly, over the last two to three years; it's going to be a quieter year this year. It is kind of what we expected.

Meta Marshall - *Morgan Stanley - Analyst*

Great. Thank you.

Operator

Jeff Kvaal, Nomura.

Jeff Kvaal - *Nomura Securities International - Analyst*

I was wondering if you could help us parse through the web-scale bit a little bit. It sounds as though you had a pretty impressive customer roster in the past quarter and yet web-scale was still in the 5% to 10% of sales range and where it did end, with the exception of one quarter, a few quarters ago. And then secondly, it sounds like there's another new customer that you were adding for the April quarter.

Should we be thinking that, that is in your guidance for the upcoming quarter? Will that help us get out of that 5% to 10% range that you've been stuck in for a long time? Thanks.

Gary Smith - *Ciena Corporation - President and CEO*

Let me try and add a little more color to it. And I caution folks around this sort of 5% to 10%. As Jim said, we try and break that out just for transparency and to give you some indication around it. Increasingly, our engagements with these web folks go through other channels. That's really the point.

They're both carriers and to some extent, some of the integrators and the folks that own the dark fiber. And so and it's more difficult for us to pull that out but I will tell you it is a very strong growth driver across our business. The direct relationships that we have has continued to grow as the business does; I would expect some quarters where you're going to see greater than 10%, direct engagement with them, depending on their particular model.

But overall, the expansion comes through -- increasingly, as they go -- another way of thinking about this, increasingly as they get more and more international outside of North America, they have to go through other entities. That's really the point. Because as you hit other regulatory environments, India being a great example; they can't really go direct in India.

They have to go through a carrier that has the capacity. And so therefore, we will get the business; very often we have direct visibility into it and we're partnering with them. But the business does not come to us directly from them. And now we'll work on how to we try and quantify some of that a little bit more but the Metro is really how they get to their customers on their clouds.

And that increasingly is international. And it is increasingly through other carriers. And so that dynamic, I think, will continue but if we step back from all of this, these folks are really driving the overall global capacity. That's the point, whether it's direct or indirect or submarine or through a carrier in India, we've got visibility to, the point is these folks are really driving demand.

And it's not just the main sort of five or six big players ; you've got international ICPs now coming into the picture. You've got the, what I would say, the smaller ICPs are now connecting up their data centers. And you're seeing a much greater dynamic that's broader based.

Jim Moylan - *Ciena Corporation - CFO*

And as you say, we have been above that 10% number a couple of times last year. Just to clarify the dynamic as well, the web-scale players often are the chooser of the technology provider even though they're not going to be buying direct. They strongly influence the choice of the optical vendor in many of the international engagements so we wouldn't count that as a direct sale, but in many ways, it's because they are influencing the choice of Ciena.

Jeff Kvaal - *Nomura Securities International - Analyst*

Thanks, guys.

Operator

Jess Lubert, Wells Fargo Securities

Jess Lubert - *Wells Fargo Securities, LLC - Analyst*

First I was seeing data from the Ericsson partnership, how that's going? How material the growth driver that could be for the year? And then secondly, it looks like the Packet Networking business had a really strong quarter so I was hoping you could help us understand the drivers there and if the performance was influenced by any large deals like Verizon? If it's more 8700 upgrades and to what extent you believe the momentum in that product category is likely to continue through the year?

Jim Moylan - *Ciena Corporation - CFO*

Quickly on Ericsson. We'll -- I think we're probably going to see a bit of growth out of Ericsson but they are not one of our major growth drivers for this year. The ICPs, clearly, the Metro, certainly; and internationally, particularly India, significantly outweighed the growth we expect from Ericsson in terms of our outlook for this year. We still like the relationship; it's doing well. It's just not one of our big growth drivers this year.

Gary Smith - *Ciena Corporation - President and CEO*

The only thing I would add to that is the success we've had jointly with Ericsson and Telstra. I mean I think that's a multi-year win; you saw some of the publicity for that around Mobile World Congress. That really is a big win for both Ericsson and ourselves ; and that will be a growth driver for us over multiple years.

In terms of the Packet question, Jess, I think the 8700, particularly first platform of its type in the world, really, with that kind of tight convergence around the optical capability in addition to Packet. We're seeing very strong adoption of that, particularly as you roll out into things like 4G, in places like India; it's an ideal platform for that and I think that's contributing particularly to a lot of the dynamics that we're seeing.

In addition to a strong showing from the ethernet access piece which you sort of expect, but I think as carriers and Jim sort of alluded to this increasingly put capacity closer to the customer, driven by things like getting ready for 5G and putting fiber deeper in, I think we will continue to see good growth in our Packet portfolio.

And that's really where we've targeted these kinds of platforms into that sort of access piece, as you drive fiber closer into the customers. And I think that, that's pertinent both in the cable markets in North America and Europe and also as we see this dynamic around building out capacity for both 4G and in advance, ready for 5G. We're already beginning to see that as a real dynamic.

Jess Lubert - *Wells Fargo Securities, LLC - Analyst*

Thanks, guys.

Operator

Stanley Kovler, Citi Research.

Stanley Kovler - *Citigroup - Analyst*

Just wanted to see if you can comment on particularly the web-scale part of the business, where you're referencing that customer base is driving a lot of the technology decisions and is the driving force for the capacity build-outs. What are you sensing from the standpoint of them pushing the industry more towards merchant silicon type of solutions?

And maybe you can go through your portfolio and how you're positioned from that perspective? And then just as a follow-up, I wanted to see if there's any impact that you're seeing from your customer base related to some of the mergers and acquisitions happening in the space in the telco world? Thank you.

Steve Alexander - *Ciena Corporation - CTO*

Sure, Stanley. This is Steve Alexander. I'll give you some insights into what we see going on there. You're right; they are certainly interested in exploring all of the different ways they can solve what they have in terms of access and transport architectures and such, so they tend to be very interested in what you term merchant silicon and such.

The truth is everybody uses merchant silicon to build products and it's a matter of what you do on the system level, the other features you put around it that really make the difference. And we've seen a continued desire for choice and openness in the marketplace. I mean, that's something we've supported since the founding of the Company, quite honestly.

And so we're responsive to those trends. We participate in things like the Open Road initiative. We're participating in things like TIP. I mean we're engaged in that world ; we've helped create this effects for things like the CP to ACOs and you can expect that we're going to continue in those veins, right, where we see an opportunity to introduce the benefits of open architectures and increased choice, we're going to take advantage of that.

Jim Moylan - *Ciena Corporation - CFO*

And on the M&A question, to this point, we haven't seen any slowdown or any other effect from the deals that have been announced and that's reasonably consistent with what we've seen in the past. I would say that we have been a winner in just about all of the combinations of our customers which have occurred.

And I think it's because once the customer is introduced to our Company, our technology, our services, the way we engage and we tend to be very sticky so we want, in cases where we were incumbent with the target, and we were in cases where we incumbent with the inquirer and hopefully, that will continue to be the case.

Gary Smith - *Ciena Corporation - President and CEO*

The other thing I'd say about that is that we're a very broad-based, diverse business now and that's very, very deliberate on our part. We're not a niche player who is providing a particular technology to a particular customer and got high concentration. We are much more diversified and so we're able to deal with the ebbs and flows of these kinds of things, much more easily than a lot of our competitors.

Stanley Kovler - *Citigroup - Analyst*

Thank you.

Operator

Alex Henderson, Needham & Company.

Alex Henderson - *Needham & Company - Analyst*

I was hoping we could just get a couple of housekeeping. Could you talk about the impact of currency was on the quarter? And I don't think you gave a book to bill and I do have a follow-up.

Jim Moylan - *Ciena Corporation - CFO*

Yes, we were -- on the book to bill, we were slightly less than our revenue in our quarter intake in the quarter but Q1, that's a strong quarter for us. Q1 is a quarter which spans holiday months and before budgets are set and so we were very pleased with our order intake in the quarter that was higher than our plan. The other question was --

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Alex Henderson - *Needham & Company - Analyst*

The impact of currency.

Jim Moylan - *Ciena Corporation - CFO*

Currency was not a huge item for us in the quarter; I don't have a precise number. It's well -- it's in the low single digits in terms of our currency affected and then in terms of our expectations, we just didn't see a lot of movement this quarter.

Alex Henderson - *Needham & Company - Analyst*

So the question I wanted to ask was really on the way the pipeline is built when looking forward. Clearly, the December/January quarter is a -- somewhat of a lockdown for you. You don't get a lot of business in there and you seem to have much better leverage to order flow and transactions in that quarter. Is it fair to characterize the pipeline of activity as accelerating even above normal seasonal patterns at this point?

Gary Smith - *Ciena Corporation - President and CEO*

I think that's a fair characterization. I think we're in a better position coming out of Q1 than we had anticipated. There's another way of expressing that, both in terms of hard data, i.e., orders backlog, et cetera, and on-site inventory and the customers that were recognized. And also in terms of the overall pipeline of expectation and customer engagement. You put those two together and that's how we take visibility read and I think we're in a better position than, frankly, we thought we would be.

Alex Henderson - *Needham & Company - Analyst*

Great. Thank you.

Operator

Tim Long, BMO Capital Markets.

Tim Long - *BMO Capital Markets - Analyst*

Jim, could we just -- excuse me, touch on the gross margin and maybe looking forward a little bit --

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Gregg Lampf - *Ciena Corporation - VP, IR*

Tim, we're losing you.

Jim Moylan - *Ciena Corporation - CFO*

You are cutting in and out, Tim. Tim, are you there?

Tim Long - *BMO Capital Markets - Analyst*

To break out of this mid-40%s range. Thank you.

Jim Moylan - *Ciena Corporation - CFO*

Tim, I didn't get your full question but I think it was around gross margin where we are. Here's what I'd say about our gross margin. We've made a lot of progress, as we've said, over the last few years. We've gone from the low 40%s to mid-40%s. We believe that's where we are today. Now, there's a lot of things that go into our gross margin. We have new deals that are going to be lower than corporate average in the early stages where we're putting out Photonics and Commons and that's a thing.

We have -- as we move through time, and these deals become more mature in their rollouts and we're adding capacity, that tends to improve our margins. If we're attacking particularly internationally where we have to take incumbency from someone, that's going to cost us something. So there's a lot of things that impact our margin. I'm very pleased that if you go back over the past six years, we have grown.

We have increased our market share and we have improved our gross margin. I think that's a heck of a performance and as we move forward in time, there are going to be fluctuations in our gross margin. I don't think we can get, in the near-term, above that mid-40%s range.

But hopefully, as we move through time, as software becomes more important, as Packet becomes more important, then I think we will be able to get above that mid-40%s. In fact, when we said we're going to get to 15% operating margin, as we've said, we have to improve from the mid-40%s by a little bit in order to get to that 15%, we believe.

Tim Long - *BMO Capital Markets - Analyst*

Thank you.

Operator

Catharine Trebnick, Dougherty.

Catharine Trebnick - *Dougherty & Company - Analyst*

I have a question more -- a clarification on Ericsson. You said, Gary, that you'd been in over 10 years in India so is most of the Ericsson business more Telstra in Europe and less so in India?

Gary Smith - *Ciena Corporation - President and CEO*

Yes, Catharine. That's right. That's a good interpretation; in India, we've been direct. Pretty much, we've got some local partners there. But basically, we are direct in India. And the vast, vast majority of the business that we see there is us engaging directly with carriers and other customers, their government, particularly as well. In our Telstra engagement is with exclusively with Ericsson and we partnered over the last couple of years into the Telstra network and that is purely with Ericsson.

Catharine Trebnick - *Dougherty & Company - Analyst*

And then follow-on on Blue Planet, I noticed that global -- the Australian Subsea Global Crossing, I forget the exact name of it, talked a lot in their -- in that press release about Blue Planet and subsea and why is that so important? A couple of thought leaders I've talked to indicated that was a big deal.

Gary Smith - *Ciena Corporation - President and CEO*

I mean you've seen that in a number of submarine engagements, Catharine, where we're actually deploying Blue Planet to manage both our equipment and other folks. Steve, do you want to --

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Steve Alexander - *Ciena Corporation - CTO*

Catharine, a simple way to look at it, right, is the submarine cables open up, right? In other words, as you can procure the cable separately from the SLTE or if y you're in upgrade business, you find yourself needing to orchestrate different domains, right? One domain might be the cable infrastructure; another domain might be the SLTE. The third domain might be the equipment you're using to derive, let's say, or create ethernet services. So Blue Planet fits very well in that environment, right? It can orchestrate amongst any one of those domains, so it fits very nicely.

Catharine Trebnick - *Dougherty & Company - Analyst*

All right. Thank you.

Operator

Patrick Newton, Stifel.

Patrick Newton - *Stifel Nicolaus - Analyst*

First on some data points we're seeing from component vendors. I'm curious if you're seeing any easing of capacities -- capacity constraints or lead times and just understanding your comments that the Verizon rollout is in its early days and going well, we did see some component suppliers pointing to choppy trends currently. I'm just curious if the near-term ramp and what's baked into the April quarter guidance has been somewhat tamped down relative to expectations 90 days or even six months ago?

Gary Smith - *Ciena Corporation - President and CEO*

I would say, overall, I think we're in a reasonable place from a supply-chain point of view around components that -- we're pretty vertically integrated so a note of caution. We're not maybe the best barometer overall of this but I would say that we're not, apart from one or two exceptions, which normal sort of ebbs and flows of things, we're in pretty good shape for going in through Q2 and into Q3.

Jim Moylan - *Ciena Corporation - CFO*

There are so many things that affect the component vendors, it's hard -- I would say that it's -- I'd caution you about trying to read through on us their results. China is a big deal for those guys and the ebbs and flows in China are going to impact their results and not have any impact on us because currently, we don't sell in China.

Patrick Newton - *Stifel Nicolaus - Analyst*

And then on Verizon, any -- on the near-term guidance, has it been changed all relative to expectations a few months out?

Gary Smith - *Ciena Corporation - President and CEO*

No. I think Verizon is going pretty much as per plan. We're executing well on it. I think, generally, I would say the financial community have a view of it being bigger earlier than we have. And I think that's sort of -- that's playing out. Listen, it's a very big deal across multiple years. And we're just beginning that ramp. It's a nice piece of business for us over many, many years.

Patrick Newton - *Stifel Nicolaus - Analyst*

Great and then just -- thank you.

Gregg Lampf - *Ciena Corporation - VP, IR*

Thank you. We appreciate everybody's attention today. We look forward to catching up with everyone over the next days and weeks. Thanks, everyone.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes the program and you may now disconnect. Everyone, have a good day.
