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Infinera Corp. *(INFN)*

Q2 2012 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Second Quarter Year 2012 Investment Community Conference Call with Infinera Corporation. All lines will be in a listen-only mode until the question-and-answer session. [Operator Instructions] Today's call is being recorded. If anyone has any objections, you may disconnect at this time.

I would now like to turn the call over to Jenifer Kirtland of Infinera Investor Relations. Jennifer, you may begin.

Jenifer Kirtland
Investor Relations, Infinera Corp.

Thank you, operator. Today's call will include projections and estimates that constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements address the financial condition; results of operations; business initiatives; views on our market and customers, our products and our competitors' products and prospects of the Company in the third quarter of fiscal year 2012 and beyond and are subject to risks and uncertainties that could cause actual results to differ materially from such forward-looking statements.

Please refer to the Company's current press releases and SEC filings, including the Company's annual report on Form 10-K, filed on March 6, 2012 for more information on these risks and uncertainties.

Today's press releases include results of the second quarter of fiscal year 2012 and associated financial tables and investor information summary. It will be available today on the Investor section of Infinera's website at infinera.com.

The Company undertakes no obligation to update or revise any forward-looking statements to reflect events or circumstances that may arise after the date of this call. This afternoon's press release and today's conference call also include certain non-GAAP financial measures.

In our earnings release, we announced operating results for the second quarter of fiscal year 2012, which exclude the impact of restructuring and other related costs and non-cash stock-based compensation expenses. These non-GAAP financial measures are provided to facilitate meaningful year-over-year comparisons. Please see the exhibit of the earnings press release for a reconciliation of these non-GAAP financial measures and the most directly comparable GAAP financial measures, and an explanation of why these non-GAAP financial measures are useful and how they are used by management, which will be available today on the Investor section of Infinera's website.

On this call, we will also give guidance for the third quarter of fiscal year 2012. We have excluded non-cash stock-based compensation expenses from this guidance because we cannot readily estimate the impact of our future stock price on future stock-based compensation expenses.

I will now turn the call over to Infinera's President and Chief Executive Officer, Tom Fallon.

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

Good afternoon, and thanks for joining us on our second quarter 2012 conference call. With me are Chief Financial Officer, Ita Brennan; and VP of Corporate Marketing, Mike Capuano, Chief Strategy Officer, Dave Welch is at a well-deserved family vacation.

First, I will talk about DTN-X progress, and then I will touch briefly on global optical market trends and the competitive environment, before turning it over to Ita for a full review of our Q2 financial results and Q3 outlook.

For the last two years, we have been steadfast on our strategy with regard to DTN-X. We initiated our 500-gig PIC program and exhaustively pursued what we would believe would be the world's highest capacity platform, featuring WDM and OTN switching, integrated without compromise. We further committed to market delivery in Q2 2012.

I am extremely pleased with the team's execution, launching the DTN-X product to the market in September 2011, executing critical customer trials in Q1 and Q2 of this year; and shipping to customers for deployment in June, as promised. We believe that this platform, with abundance of cutting-edge technology and elegant ease of use, is available at the exact right time to enable mass adoption of high bandwidth solutions in the transport market.

The DTN-X reception continues to be very positive. At OFC/NFOEC in March of this year, we announced our first public DTN-X customer, Cable and Wireless Worldwide, who selected DTN-X as the sole platform for the Europe to Persia Express Gateway network, known as EPEG. Subsequently, we announced DANTE's selection of DTN-X for the GEANT optical network, Europe's largest high-speed research and education network, connecting 40 million users in over 8,000 institutions across 40 countries.

In addition to these two announced customers, we've received DTN-X purchase orders from eight other customers, for a total of 10 DTN-X customer commitments to-date. Three of these purchase commitments are from customers new to Infinera.

Equally important to note, based on just these decisions, the DTN-X is now being adopted across a broad cross-section of our markets, including the cable, subsea, Internet content, R&E, and Tier 1 markets. I have every confidence that all of our markets will be well served by this leadership next-gen platform.

In addition, we completed 10 customer trials, as compared to the eight we had planned. These customer trials represent a combination of service providers across North America, EMEA and APAC and consist of Tier 1s, Internet content providers, and bandwidth wholesalers. Like the customers who have made purchase commitments, these represent a mix of existing and potential customers.

I would note that while some of these trials in the last two quarters have resulted in purchase commitments for the DTN-X platform, there has not been a direct correlation between trials and POs. We do business with over 100 customers and not all of them will need to trial the DTN-X before committing to it.

In fact, some of the DTN-X POs we have received are from existing customers who have bypassed the trial process. This is the result of the DTN-X being the next phase of our Digital Optical Networking platform, and the trust that we've earned over the past seven years for reliability, quality, and delivering on our commitments.

Because of this lack of correlation, we will no longer provide an update on the trial pipeline, and instead will focus on DTN-X purchase orders and customer wins going forward.

As we discussed on our first-quarter conference call in April, we are seeing strong demand from existing customers for DTN-X for bandwidth growth and new footprint requirements. Implementing a new platform often includes a process of evaluating, qualifying, and running first office applications, which can take one or more quarters.

As we expected, this transition has adversely affected our DTN revenues, as some customers moved from the DTN to the new DTN-X higher capacity 500-gig platform. While we anticipated this transition, we agree with the market analysts who predict a very substantial 10-gig market for an extended timeframe.

We expect continued demand, from both existing and new customers, for the ATN and DTN as part of the Digital Optical Network family of products. To this point, in Q2 we won two new customers based on the DTN platform, and our invoice customer count now stands at 102.

From an overall perspective, we continue to see aggressive pricing in the market for 100-gig offerings, and an average selling price that is several quarters ahead of both market forecast and typical new technology price curves. We believe that 100-gig today sells for a lower dollar-per-bit than 40-gig, and makes 100-gig a better technology and economic choice for most capacity-constrained customers.

Securing this DTN-X based footprint now allows us to capture those opportunities and enable improved gross margin over time, as we add capacity to the DTN-X deployments. As we increase the volume of our DTN-X product, this will allow us to leverage the scale and cost advantages of our PIC-based vertically integrated model versus our competitors who are using less cost-effective, off-the-shelf optical technology. As a result, we are competing aggressively for these opportunities.

Market forces will continue to drive demand for the DTN-X into the future. Mobility, video, and increasing broadband connectivity are generating significant network traffic growth, while data center and cloud services are creating the need for more meshed architectures.

We believe that this bandwidth growth will continue to accelerate, and regardless of access method, virtually all traffic will be transported over optical fiber networks. Operators need to invest in an architecture that is not only scalable, but also provides a more resilient, flexible, and intelligent solution. We believe that digital optical networks, built upon a foundation of incredible ease of use and field-proven quality, can uniquely provide this balance.

Our DTN-X platform is seeing traction because of this unique combination. We believe that this combination can also help improve operator business models. First, the DTN-X provides investment protection assurance through unparalleled scale.

Today, we deliver 500-gig long-haul super-channels while our competitors are only delivering, or trying to deliver 100-gig. They are only talking about 400-gig metro reach channels via slideware and proof-of-concept demonstrations. Their technologies, even if they are commercialized, will have significant compromises versus the performance of Infinera's 500-gig long-haul super-channels that are available now.

Second, the DTN-X provides lower CapEx and OpEx costs through network efficiency, network convergence, and PIC economics. We have analyzed an 80 node nationwide network, and the results show that the integrated switching and WDM of the DTN-X can produce up to a 60% lower total cost of ownership by using fewer channels, fewer fiber connections, less space, and less power when compared to more conventional architectures.

Finally, the DTN-X gives carriers the ability to increase customer wins and to reduce churn through service delivery velocity and unparalleled reliability. With seven years of field-hardened experience integrating OTN switching, WDM transmission, and a GMPLS control plane, our customers can provision 10-gig, 40-gig and 100-gig e-services in minutes, and have them run extremely reliably for years.

The DTN-X is ushering in a new era of converged network generation transport network architecture. Not only is the DTN-X early in the 100-gig market, it is also creating the de facto standard, with 500-gig super-channels which are shipping today. And, similarly to what the DTN did in the 10-gig market, we believe DTN-X will accelerate mass adoption of both 100-gig and 500-gig super-channels.

From our inception, Infinera's mission has been to transform the way telecommunications networks are built, and to help our customers succeed. Infinera does this through deep innovation. As a reminder, we are the first to design and deliver a large-scale photonic integrated circuit, currently shipping to third generation 500-gig PICS, and successfully demonstrating 1 terabit PICS.

First to design and deliver FlexCoherent, allowing our customers to software select the best modulation format to optimize reach and capacity while reducing cost. First to design and deliver 500-gig long-haul super-channels; and the first to design and deliver a platform that integrates 5 terabits of non-blocking OTN switching and DWDM transmission without compromise.

These industry-leading features help our customers to cost-effectively scale their networks now and into the future, significantly reducing their capital and operating cost, and increasing their top line revenue opportunity. We are executing well on our mission and are confident about our ability to drive adoption of the Digital Optical Network.

Now, before turning the call over to Ita, I want to thank the Infinera team for meeting our commitments and shipping the DTN-X in Q2 as we promised our shareholders and customers. I would also like to thank our customers for their continued business and partnership as we move forward into the terabit age together.

Ita will now provide a detailed financial review.

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

Thanks Tom. This analysis of our Q2 results and our guidance for Q3 is based on non-GAAP. All references exclude non-cash stock-based compensation expenses. Total GAAP revenues in Q2 were \$93.5 million, compared to our guidance of \$92 million to \$100 million. As anticipated on our March conference call, the second quarter reflected significant impacts from demand and initial shipments of our DTN-X platform.

Several existing customers made the decision to shift their demand for new footprint to the DTN-X, resulting in lower DTN revenues for the quarter. While this resulted in revenues for Q2 at the lower end of our guidance, it also allowed us to exit the quarter with a healthy order book, ahead of recognizing DTN-X revenues in Q3.

We added two new customers in the quarter for a total roster of 102. As a reminder, this metric now reflects the completion of a number of previously announced customer mergers, and is based on achievement of invoice shipment. The two new customers added in Q2 deploy Digital Optical Networks based on the DTN platform.

We expect to see new DTN-X customers impact this metric next quarter, as we begin to invoice and take revenue on DTN-X deployments. We had one greater than 10% customer in the quarter, which was a cable operator. The top five also included another cable operator; two Tier 1s; and a bandwidth wholesaler.

International revenues totaled \$28 million or 30% of total revenues for the quarter. EMEA accounted for \$23 million or 25%; with APAC and the Other Americas representing 3% and 2%, respectively. Our service revenues for the quarter were strong at \$15.1 million, up from \$11.8 million in Q1. This included some incremental deployment services in the quarter and some catch-up revenue from the renewal of a number of significant entitlement contracts. Services margins for the quarter were approximately 68%.

The commencement of DTN-X shipments also affected gross margins for the quarter. Overall gross margins in Q2 were 37%, down from 40% in Q1, and in line with our guidance of 36% to 38%. Q2 margins reflected the impact of lower product revenues which was offset to some degree by a higher mix of network fill as customers shifted their new deployment opportunity to Q3 in anticipation of DTN-X.

In addition, we recorded lower of cost or market or LCM adjustments related to initial DTN-X inventory and shipments in the quarter. As a refresher on LCM, if we sell product below cost, we must recognize the projected loss on those items when they are recorded as purchase commitments held in inventory; and finally, when shipped and awaiting customer acceptance, all in advance of taking revenue on the transaction.

We normally incur LCM on initial common equipment deployments when faced with competitive first in pricing. We did, however, record LCM adjustments in the second quarter related to the first DTN-X line modules we manufactured which carry a higher cost due to lower initial yields and volumes associated with ramping production on a new product. We would expect LCM adjustments related to line modules to cease, once we have consumed these early high cost units.

While we had anticipated some of this LCM effect in our gross margin guidance for the second quarter, our DTN-X shipments awaiting customer acceptance at the end of the quarter exceeded our original plan and drove some additional LCM. This had a somewhat negative impact on our gross margins in Q2, but this change should be directly offset by an improvement in anticipated margins for the third quarter, when revenue is recognized on these shipments.

Operating expenses for the quarter were \$52.6 million, an improvement versus our guidance of approximately \$54 million. We remain focused on careful expense management, while balancing the need to fund lab trials and other customer-facing activities. Looking forward to the September quarter, we expect operating expenses to be

approximately \$55 million including ongoing OSMINE certification costs and a rollover of some lab trial related expenses from the second quarter.

Overall head count for the quarter was 1,228 versus 1,210 in Q1. Headcount additions were primarily related to direct labor for manufacturing and there were also a few additions in sales and R&D. Our operating loss for Q2 was \$18.5 million, other income and expense for Q2 was favorable at \$0.4 million, net loss for the quarter was \$18.6 million, resulting in a loss per diluted share of \$0.16, in line with our previous guidance, which called for a loss of \$0.14 to \$0.18 per diluted share; and compared to a loss of \$11.2 million or \$0.10 per diluted share in Q1.

Now turning to the balance sheet. Cash, cash equivalents, restricted cash and investments, ended the quarter at \$210 million versus \$240 million in Q1. We used \$22.7 million of cash from operations in Q2 versus \$5.8 million in Q1. DSOs were 55 days, down from 57 days in Q1. Although DSOs were healthy, at 55 days for the quarter, we may see some upward pressure on this metric next quarter, depending on the timing of acceptance and billing of some larger DTN-X opportunities.

Inventory turns were 2.1 times, versus 2.5 in Q1. Overall inventory levels increased to \$115 million in Q2. While DTN inventories were slightly below normal levels, DTN-X inventories have increased in advance of revenue recognition. This includes increased inventory awaiting customer acceptance, and increased inventory levels throughout the manufacturing cycles.

This near-term increase in working capital requirements is in line with our expectations for the initial DTN-X sales period and our goal is to return to more competitive metrics by the end of the year.

Accounts payable days were 44 days, the same as in Q1. Capital expenditures were \$6.1 million in Q2, versus \$13.6 million in Q1. Q2 CapEx included costs associated with the finalization of our ERP replacement project, which went live in July.

This project was initiated to allow us to better scale our operations and to support multiple product lines; potential increased volume from Tier 1 customers and the expanded international footprint. With the completion of this project, we expect go-forward capital expenditures to return to pre DTN-X levels, and run at approximately \$20 million per annum.

Turning to our outlook for the rest of the year. We exited the second quarter with a strong order book, having received DTN-X purchase commitments from 10 new and existing customers. We expect to begin recognizing meaningful revenue from the DTN-X platform in Q3, with incremental revenue growth expected from the fourth quarter.

There may however be some volatility around the timing of acceptance for some DTN-X deals, given that they involve a new platform and in some cases, new customer engagements. We continue to win new DTN opportunities, and expect to complete a number of new DTN deployments in the third quarter. That said, we are seeing some fall-off in DTN revenues as some of our larger customers transition their new, higher bandwidth deployments to DTN-X.

In addition, as Tom mentioned in his remarks, market conditions remain unpredictable, with competitors and analysts tempering their demand forecast for the second half of the year, based on macro economic and other concerns. Given these factors and our current visibility, we now believe that revenues for the second half of 2012 range from approximately \$230 million to \$245 million, with the higher end of this range representing the midpoint of our previous guidance.

Turning to gross margin. As previously mentioned, we continue to see some aggressive pricing from competitors on 100-gig footprint opportunities. We are responding to these competitive pressures in order to secure the initial footprint and gain access to the future, higher margin network fill.

All things being equal, we believe that this initial 100-gig footprint pricing dynamic, coupled with higher levels of common equipment and the need to absorb some DTN-X ramp-up costs, will result in margins for the year that remain consistent with our previous guidance of somewhat below 40%.

Looking beyond 2012, we believe that with solid revenue growth, our vertically integrated model can deliver significant leverage, and allow for healthy margin expansion. In addition, over time, we would expect to see a more balanced mix of new footprint and network fill that should also improve our gross margin structure.

The following specific guidance for Q3 is based on non-GAAP results, and excludes any non-cash stock-based compensation expenses: revenues of approximately \$106 million to \$115 million, gross margins of approximately 37% to 39%, operating expenses of approximately \$55 million, operating and net loss of approximately \$10 million to \$16 million. Based on estimated average weighted diluted shares outstanding of \$114 million, this would lead to a loss per share of approximately \$0.09 to \$0.14. Please note that the basic share count is expected to be at 111 million for the quarter.

Finally, before we open the call up for questions, I wanted to let you know that we will be holding an Analyst Day in New York City in December. We'll be finalizing the details over the next couple of weeks and you will be hearing more from us about this at that time.

Now, operator, would you please open the call up for questions. Thank you.

QUESTION AND ANSWER SECTION

Operator: [Operator Instruction] And our first question comes from Rod Hall with JP Morgan. Your line is open.

Ashwin Kesireddy
Analyst, JPMorgan Securities LLC

Q

Hey, guys. This is Ashwin filling in for Rod. One question is about your DTN-X customers. You said that you completed 10 customer trials, but you also gave a metric around the number of purchase orders you received. And, also, you mentioned that some of the customers bypass the trial phase, so can you give us a number of how many customers actually bypass that phase? And is there any North American customer in the purchase orders you currently have?

Thomas J. Fallon
President, Chief Executive Officer & Director, Infinera Corp.

A

Well, I think you asked a couple questions. One, can we tell you which customers bypassed the process? I will only tell you that it's been customers that we have been working with for a number of years. They have large installed base of DTN, and it's in markets that we have served for a long time. It's a combination of mostly domestic; but also, at least one international customer that bypassed the typical trial phase.

Ashwin Kesireddy
Analyst, JPMorgan Securities LLC

Q

I was just going to ask about the North American customer trial. There was this one Tier 1 service provider which was present at your Analyst Day, and showed some interest about -- interest in the DTN-X platform. Can you give us an update there?

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

A

I think you're probably referencing Verizon. And we continue to -- as you, I think, probably know, have good interactions with Verizon. They have publicly continued to endorse both the architecture that we are supporting, converged network around both OTN and packet, and they've endorsed the direction we're going. I am not at liberty to discuss any further details about that potential customer engagement.

Ashwin Kesireddy

Analyst, JPMorgan Securities LLC

Q

All right, then final question is on the gross margin. Last quarter, you mentioned that you had seen a lot of pressure on 100-gig pricing to win the initial footprint. Now you are saying, you are continuing to see that pricing pressure. I'm just wondering if the pricing pressure actually increased or is it almost stable?

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

A

Yeah, I mean, it's always hard to kind of create relative measures around that. I think we're continuing to see just similar interest in that initial footprint, and drive to win that initial footprint. So I don't know that anything has changed from last quarter's call.

Ashwin Kesireddy

Analyst, JPMorgan Securities LLC

Q

All right, thanks guys.

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

A

This is Tom, adding one point of clarification. We have said it's a very competitive environment, now, for a number of quarters. A part of that, we have linked to the fact that we were competing with platforms that offered 10-gig and 40-gig against a market that was very focused on 100-gig. So we said, we were making some commercial decisions to afford our customers a good solution around our then-available 10-gig and 40-gig.

Now that 100-gig is available and shipping, we continue to see 100-gig pricing pressure, which, usually for a new technology, there's a period of time where that is less intense. My view is, it's probably been less intense over the last couple of years. But as the market opens up, now, to at least a few people pursuing and delivering 100-gig coherent, the competition for 100-gig technologies is pretty significant.

Ashwin Kesireddy

Analyst, JPMorgan Securities LLC

Q

All right. Thanks, guys.

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

A

Thank you.

Operator: [Operator Instructions] Our next question comes from Ehud Gelblum with Morgan Stanley. Your line is open.

Jeremy David

Analyst, Morgan Stanley & Co. LLC

Q

Hi. Good afternoon. It's Jeremy David speaking on behalf of Ehud Gelblum. I guess a couple of questions on -- so you don't take on the second-half revenue guidance from \$245 million at the midpoint to \$237.5 million. What's the reason? Is it just macro? Is it just a delay in purchase orders for the DTN-X or greater fall off than you expected in DTN orders? Can you give us some visibility into that?

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

A

Certainly. This is Tom. Hey, Jeremy. If I look at -- there's two things that are happening. One, are we creating traction with the DTN-X? And are we winning customers at or above the rate we had anticipated? And, as I stated in my statements, I am extremely excited and enthusiastic about the role I think the DTN-X is going to play in the market, short and long-term. So from a traction perspective, from our customer receptivity perspective, I am extremely bullish.

Having said that, and I think you are seeing this from almost everybody who I hear announcements from, the macroeconomic environment is certainly uncertain. And I think that there is, without question, delays of purchase decisions. And we are also concerned about the ability to control when customers accept any DTN-X platform that they might buy from us and deploy. So the change of the guidance is reflective of our view that the macroeconomics are very uncertain, and there's inherent risk there, and our inability to control when certain customers will be able to recognize revenue from them accepting the product.

Jeremy David

Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great, that's very helpful. And then, could you comment on the revenue mix this quarter between the DTN and DTN-X? I know you just started shipping it in June, so it might be single-digit mix?

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

A

Yes, no, there's no DTN-X revenue, Jeremy, in the...

Jeremy David

Analyst, Morgan Stanley & Co. LLC

Q

There is no DTN-X, okay.

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

A

No.

Jeremy David

Analyst, Morgan Stanley & Co. LLC

Q

What about next quarter? Why is that, can you give us some kind of guidance around the mix between DTN and DTN-X, broadly speaking?

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

A

Yes. We said meaningful. So, I think we will start to see a good ramp on the DTN-X revenues. We're not really going to break that out between the two platforms, because – essentially, for us, a network is a network. And we will be selling DTN and DTN-X as a solution to these customers. So we're not going to try and track that between the two platforms.

Jeremy David

Analyst, Morgan Stanley & Co. LLC

Q

Okay. And, finally, you mentioned you will not be disclosing trials anymore for the DTN-X, going forward. You had mentioned 10 trials last quarter, and you had 10 purchase orders, presumably some of them came from customers who were already using you. Are there any trials that were not successful? And is there anything that we can learn from those trials that may not have led to purchase orders?

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

A

Yes. And I think some of them are still in play. As I look at the list of trials, I don't see anybody where we would say we have absolutely lost out on the opportunity. But some of those opportunities are definitely still in play.

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

A

And I want to be more clear, you ask if any of them were unsuccessful. None of them were unsuccessful and I would qualify that I was very satisfied with the results of the trials, certainly the ones that resulted in POs, but I was also as satisfied that potential customers who have not made a purchase decision yet walked away with an exceptionally good feeling about the product, the architecture, the company. So I think they were all successful.

That's one of the reasons we are going to break apart, not talking about trials, because trials come at many different times. Sometimes customers are about to deploy something, sometimes people are thinking about deploying something; and sometimes people are just evaluating a longer-term architectural direction, and they want to understand what we are doing. It might impact that strategy that could be a year or two years away. I think the most relevant thing to think about is customer wins, and market share of 100-gig, moving forward.

We will talk about customer wins, and we are going to talk about 100-gig market share, because we think we're going to have something we can be very proud of. It just -- for Q3, we do have a number of trials that are scheduled. So I don't want anybody to think that we are walking away because metric wouldn't look good. We have approximately the same number of trials scheduled in Q3 that we had scheduled in Q2, but we just don't think it provides great clarity as a predictor of short-term business.

Jeremy David

Analyst, Morgan Stanley & Co. LLC

Q

Okay, understood. Thanks a lot.

Operator: Our next question comes from Jody Farquhar with Jefferies & Company. Your line is open.

Jody Farquhar

Analyst, Jefferies & Co., Inc.

Q

Hi, guys. This is Jody in for George Notter. On the back of the commentary, on the strong order book, I guess any granularity you could provide around book-to-bill metric. And then, you know, also, I noticed we had a downtick in deferred revenue number on the quarters. Any commentary around those would be greatly appreciated. Thanks.

Ita M. Brennan

Chief Financial Officer, Infinera Corp.

A

Yes, I mean it's difficult to give you a meaningful book-to-bill just because our business tends to be large opportunities that kind of have their own cycle time. I think the best book-to-bill we can give you is to look at the revenue guidance, which essentially is bearing out through the end of the year between both the second half guidance and the Q3 numbers.

The downtick on deferred revenues, we did recognize some deferred services revenues and some deferred product revenue in the quarter. We'll start to see that grow again starting in Q3 as we start to bill kind of service contracts for next year. So it's typical for it to come down. We had a couple of larger amounts come out of that this quarter. And then, we should start to see it build again in Q3 and Q4.

Jody Farquhar

Analyst, Jefferies & Co., Inc.

Q

Okay. Great. Thank you. Final question on DTN and DTN-X overlap, going back to that, I believe the commentary on the last update was that 15% to 20% of this customer base, maybe there's an overlapping customer there, is this -- any update on that number given today's commentary? Does this look like, something like 25%, 30% overlap now? Any further commentary on that?

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

A

I don't remember the commentary saying that there is only a 15% or 20% overlap, so I'm going to have to take a note, Jody, and get back to you. I believe that a substantial portion of the customers that buy from us today at a dollar basis will also be interested in the DTN-X. I don't think that all of their applications necessarily will have the DTN-X be the right answer, because it has such a magnificent scale and magnificent capacity and that costs money. So there's certain applications that the DTN is going to be better suited for. But I would say, at a dollar basis, more like 80% of the purchase dollars we get today would come from customers who would have opportunities for DTN-X.

Jody Farquhar

Analyst, Jefferies & Co., Inc.

Q

Okay, that's helpful. Thank you.

Operator: [Operator Instructions]

Thomas J. Fallon

President, Chief Executive Officer & Director, Infinera Corp.

On behalf of Infinera, I would like to thank you very much for your time. I look forward to giving you updates over the next quarter and look forward to hopefully seeing you in December. Thank you.

Operator: Thank you for participating in today's conference. Please disconnect at this time.

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