

# FINAL TRANSCRIPT

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## **JNPR - Juniper Networks Inc at UBS Global Technology and Services Conference**

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## CORPORATE PARTICIPANTS

**Robyn Denholm**

*Juniper Networks Inc - CFO*

## CONFERENCE CALL PARTICIPANTS

**Nikos Theodosopoulos**

*UBS - Analyst*

## PRESENTATION

**Nikos Theodosopoulos - UBS - Analyst**

Okay, thanks, everyone, for joining in this session. We're happy to have in this session Juniper Networks, and with us, we have Kathleen Nemeth from Investor Relations, and Robyn Denholm from the -- well, the Chief Financial Officer. Thank you for attending our conference, and Robyn's going to do a few slides, and then we'll take some Q&A.

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**Robyn Denholm - Juniper Networks Inc - CFO**

Thanks, Nikos, and good morning, everyone. I just wanted to make sure I brought your attention to the Safe Harbor slide before I start the presentation. Obviously, we make some forward-looking statements here, and all the risks and uncertainties are on the filings that we've recently published.

So in terms of Juniper, what I wanted to -- go back one slide. What I wanted to start off with is really the new network. So we've been talking about the new network for a few years now. The two key trends that we are focused on in bringing the new network to life is around the mobile Internet and cloud computing. And what you can see is that we're both transforming the experience as well as the economics. So everything we do as a company is focused on helping service providers and enterprises with their costs, in terms of their networking costs, as well as driving the experience for users, both in terms of the service provider users, and the enterprise users. And what you can see is, everything in our portfolio of products, as well as our solutions, are actually aimed at these areas.

So if you look at our strategy, this means our strategy, on the slide. What we do as a company is, we focus our R&D effort on the key architectural transitions that happen in networking over a prolonged period of time. And we look at those three and five years out. An example of that is what we've done in the data center. We've just recently, in the last quarter, actually brought to market our QFX product, our QFabric products. Those were many years in the making. The architectural transitions that we foresaw were having large scale data centers had a 10 gig inflection point, as well as having massively scaled data centers with service and storage devices, and that type of thing.

So that's an example of an architectural transition. What we're doing in the core with PTX, and our next generation of core routers, T4000, is another example of an architectural transition.

So we actually put the R&D dollars into those architectural transitions. We then expand the footprint, the systems footprint, and we're about platforms as well as software in the network.

And then the third pillar of our strategy is actually driving up the stack with software across the board, whether it's on the device, in the network, or across the network. And we have three developer communities, both in terms of the Junos OS, the Pulse, which is on the client side, and the Space, which is the management layer.

In terms of the new products that we're bringing to the market, we actually had been in a heavy R&D cycle over the last three years. And these are the products that are coming to market. There are obviously others, but these are the main ones. So you



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can see the QFabric products, they're out now, as of the third quarter, and getting very good customer receptivity in terms of the architecture and what we're doing there.

MobileNext is also out. That just started shipping in the second quarter. It's software on top of our MX 3D platform, that we have on the edge router side. PTX will start shipping in the first quarter of 2012, and the T4000 is on track to ship in the fourth quarter, with revenues in the first quarter.

So, in terms of our year to date revenues, we are doing very well. Third quarter year to date, our revenues were up 15% year over year, and we had solid growth in all three geographies. If you look at our operating margins, they're also pretty good in terms of profitability, and our product revenues are up in MX 70% year over year, EX 16% year over year, and SRX was down slightly, 2% year over year.

If you look on a year to date basis, product revenue for routing is up 19% year over year, and switching product revenue is up, at 30% year over year. And a slight decline in our security area.

If you look at what we're doing in our two markets, enterprise is up over 11% year over year, and if you look at our service provider business, it's up 17% year over year. So, pretty healthy results, given the macro environment out there.

So in summary, we're very confident in the strategy that we're on. It's aligned to the markets. Our customers are embracing the technology that we're bringing to market. We do have disruptive innovation, and it's generating momentum with those customers. And we're also executing well in the macroeconomic environment that's out there.

We are pretty agile in terms of our prospects, and we have actually been making sure that we're investing for the long-term as well.

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## QUESTIONS AND ANSWERS

**Nikos Theodosopoulos** - UBS - Analyst

Okay, thank you. Okay, thanks for that, Robyn. I'd just ask a few questions, following up on that. So, you had a slide up there with the new products. What -- if you look at the new products, which ones -- which one do you think is showing the most significant customer interest, that would potentially generate the most positive results for you in 2012?

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**Robyn Denholm** - Juniper Networks Inc - CFO

So, we're pleased with the customer receptivity of all the new products, actually. Obviously, the PTX is not released yet, but even in early evaluations, the customers are quite pleased with it.

So if you look at the products that -- the four new big products that we have coming out over the next period of time, the first three are driving significant architectural change, both in terms of QFabric, MobileNext, and PTX. The T4000, whilst it is a great leapfrog in terms of the core, in terms of performance for any platform that's out there today, it is a seamless upgrade with our T1600 core routers that are out there.

So, I would say the revenue ramp for the core is much more well known to us, given that we've been in that market for quite some time, and this is actually the third generation of seamless upgrade that we've had. So I would say in terms of ramp to revenue, that's obviously the more predictable, the more well known.



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In terms of the QFX, we've had very good customer receptivity to QFabric. We've actually already announced key design wins with some customers, Deutsche Boerse, Bell Canada, Terra, and also Thomson Reuters. And I think those four are actually examples of many other customer engagements that we have in terms of discussions at this point, where some customers are actually deploying the full QFabric straight out the gate, like Bell Canada. And then others are actually taking the QFX 3500 node, the 10 gig (inaudible) node, that's fabric-enabled, that they can then deploy the rest of the fabric solution over time. And some have indicated that they will do that, and others are actually deploying the QFX 3500 and then not necessarily declaring at this point whether they will go full fabric over time.

So we have varying degrees of customer engagement today, on those products. But so far, we are very pleased with the response across the board.

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**Nikos Theodosopoulos** - UBS - Analyst

Okay. Just a question on terminology. You occasionally use the word design win, and then customer, right? So the three or four design wins for QFabric, are these deploying customers, or -- I'm just trying to understand the difference.

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**Robyn Denholm** - Juniper Networks Inc - CFO

Yes. So a design win, for us, is an award of actually -- either a bake-off, a competitive bake-off, or an award of future business. It may not be an order, straight on that way, but it may be an indication that they are going to order at some future point. We look at them as the earliest sign of revenue in the future. So, you will hear us talk about design wins for the new products in particular.

If you look at MX, design wins preceded revenue, right? And so, that's the cycle. You go from customer engagement FRS and then design wins, in terms of the cycle, and then obviously, orders.

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**Nikos Theodosopoulos** - UBS - Analyst

Okay. On the QFabric product, given the -- the product became commercially available recently. Do you have enough feedback from the customers that are looking at it, that the first iteration, in terms of hardware and features, is strong enough in the marketplace to be successful, or are you getting some feedback -- you know, this is a great product, but we would like the tweaks here and there, and in my impact of deployment, what's the feedback you're getting on this first iteration that's in the market?

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**Robyn Denholm** - Juniper Networks Inc - CFO

Yes, I mean clearly, it's still early days, but we're pretty pleased with the feedback. We obviously did some beta trials beforehand, and the feedback from early customers is pretty consistent with the feedback that we were getting through the beta trials. So overall, we're pleased with where we are at the moment. It's very early days, still, obviously, from a sales cycle perspective.

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**Nikos Theodosopoulos** - UBS - Analyst

Okay, shifting gears. So, the service provider router market, which you're one of the significant players, and it's a big part of your revenues, has consistently grown in non-recession years 15% or better. And so far this year, it looks like we're going to hit that, at least through the first three quarters. We'll see what the fourth quarter does, but certainly double digit growth in non-recessionary years.



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Do you see anything different for 2012? Obviously, there's macro risks. Europe might go into a recession, it might not. The US might go into a recession, it might not. But in terms of what you're hearing from customers, assuming we have a non-recessionary environment, would there be anything structurally different that would make demand not grow at least double digit for the market?

**Robyn Denholm** - Juniper Networks Inc - CFO

Yes, I think, given the -- obviously, the exponential growth in traffic, there's a lot of fundamental demand there, from a -- you know, what makes routing grow, in terms of both the quantity of traffic, as well as the type of traffic, with video increasing in terms of penetration. And again, coming back to my prepared remarks, mobile Internet and also cloud computing will continue to drive the traffic volumes over time.

So, in terms of the absolute growth rate, for 2011, we actually thought routing would grow at the beginning of the year, when we were setting up our long-term model and our operating principles for 2011. We actually thought that the routing growth rate would be somewhere between 12% and 15%. We actually think, given the third quarter, and obviously, our guidance for the fourth quarter, that we're growing faster than the market for 2011, and we actually think that the range is actually less than what we thought it would be at the beginning of the year.

So we think that this year is slightly lower than the 12% to 15% growth that we were talking about at the beginning of the year, for the market growth rate.

In terms of next year, it's a little bit too early to call the year, just given the changes in some of the carrier CapEx behavior in the second half of 2011.

**Nikos Theodosopoulos** - UBS - Analyst

Okay. Okay. So, speaking about carrier CapEx, in the most recent quarter, your book to bill was 1.2, very strong. On the other hand, a lot of the -- it was more -- you have a six month backlog on product, so it was more second half weighted than normal, I would say, which led to the very strong book to bill, at least, if I heard that right.

What is it -- what do you think led to that? Are there certain products that are coming out, or configurations that are coming out in the first quarter that customers felt the need to make sure they got in your order pipeline due to lead times or something? Why are they ordering more into the future than they've done in the past?

**Robyn Denholm** - Juniper Networks Inc - CFO

Yes, I think the book to bill in the third quarter was actually, definitely a highlight of the third quarter results. And it was, as you mentioned, quite a bit higher than usual. In fact, it was one of our highest book to bills that we've had, at least in the timeframe that I've been at the Company, for just over four years.

So -- and if you look at that, the thing that was unusual, other than just the straight-out book to bill, was, there was a couple of customers that actually ordered outside of the next quarter. So they were placing orders for us in the third quarter for delivery in the first quarter. None of that was tied to new product. It was all existing product, and on the call, I said it was mainly routing. And it was quite a bit of edge routing in there.

And that's the deployment of both new and existing design wins that we've had without -- you know, in the three leading platforms and the MX 3D. So some of that, I think in the third quarter -- we obviously saw a sequential decline in revenue, so



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some of it was timing, in terms of when some of the new deployment were slated to be -- actually start to roll out, so in the fourth quarter, and going into the first quarter of next year.

So, in terms of the customer's motivation, I don't want to speak for our customers, but I think, given that many of -- you know, some of it was tied to the new design wins that want a certainty of delivery for their deployment in terms of both new deployments that they were rolling out, so that's probably the closest, in terms of why they were doing that. So, a certainty of delivering, over win -- having the equipment win they needed for the deployments, and actually rolling it out then.

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**Nikos Theodosopoulos** - UBS - Analyst

Okay. Does anybody have any questions from the audience? All the way in the back there?

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**Unidentified Audience Member**

Can you talk about the dynamics, going to the network security market, your position versus Cisco and some of the other incumbents, and this sort of generic move towards unified (inaudible) management?

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**Robyn Denholm** - Juniper Networks Inc - CFO

Yes. The security market, overall, is evolving. So if you go back to the two key industry trends that we're following, it applies to security just as it does to other parts of the network. So -- and with a proliferation of devices in enterprises, bring your own device to work, you know, that type of thing, what we're seeing is the need for very robust device security, and that's where our Pulse offering actually plays. And you may have seen, we've announced a couple of significant design wins with the service providers in that space, so one was AT&T in Q2, and a couple of others around the world.

We also, last week, announced an enterprise arrangement with IBM as well, to take that same Pulse offering into enterprises. And we are seeing quite a bit of receptivity with enterprise customers, because it doesn't matter which CIO you talk to, the proliferation of different devices, not having a corporate issued type of device, actually creates a security challenge for CIOs. So that is where Pulse plays.

The other end of that is the data center. So again, mobile Internet, cloud computing, the data center, the high end SRX was designed for high scale traffic firewall, for both the service providers, and we've seen good traction with high end SRX with service providers around the security on the smartphones.

What we are yet to see is that same penetration in the enterprise. We do have many features that CIOs are looking for, particularly in the data center, around virtual security. So, our VGW, our virtual gateway security, provides security on a high end SRX for the virtual machines within a data center.

And so, as we start penetrating the data center with both switching, and obviously, with QFabric, we expect that to increase, in terms of volume as well, from a security perspective.

In terms of overall, the market in terms of security, as I said, is evolving in terms of both key trends.

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**Nikos Theodosopoulos** - UBS - Analyst

Question over there?



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**Unidentified Audience Member**

Yes, thanks. Just wondered if you could talk about R&D. You mentioned how you had quite a few projects that have come to fruition. And as we look into 2012, what you're spending the money on, and what you think the -- sort of run rate of R&D will be next year. Thank you.

**Robyn Denholm - Juniper Networks Inc - CFO**

Yes, I think we're very pleased with the investments that we've made in terms of these large projects, because you can see the fruits of those projects come to market over the last couple of quarters, and then into early 2012. You can be assured that they're not the last products we'll ever bring to market. We are working on other products, in terms of different parts of the market, some of which we've talked about, so Pulse, and the offerings around the security space. We've talked about some of those. And there are other offerings that we haven't spoken about, so more to come on those at some future point.

**Unidentified Audience Member**

Hi. Recognizing US is only one part of your routing business, but do you think the T-Mobile deal and the Verizon strike had any meaningful, noticeable impact on routing demand this year?

**Robyn Denholm - Juniper Networks Inc - CFO**

Yes, I think it's hard to say whether any type of transaction -- obviously, you know, the consolidation in the service provider space is a trend that we've been anticipating for some time. I think it's inevitable, especially when you're talking about cost per bit and the economics around driving volumes and the amount of traffic that's going through a network, so invest in the critical network infrastructure, you have to have scale in order to be able to do that. So the whole trend around consolidation in that space is something that we've been anticipating for quite some time.

Whether that particular deal or not has had any impact, I wouldn't say.

**Unidentified Audience Member**

Thank you.

**Unidentified Audience Member**

On R&D and focus, you know, the Company recently hired Robert Muglia from Microsoft, and --

**Robyn Denholm - Juniper Networks Inc - CFO**

Bob.

**Unidentified Audience Member**

Bob? Sorry. Okay. I don't know him personally, so just went with the press release. So, the question I have is, it seems with Junos Pulse and the creation of this new position, there's going to be more focus on software. Is there going to be a tradeoff between the traditional roots of the Company in ASIC and chip development, and allocating more resources to software, or do you think you can maintain both focuses and still hit the 25% operating margin target?



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**Robyn Denholm** - Juniper Networks Inc - CFO

I think one of the best kept secrets about Juniper are the time -- is -- has been the software focus. I think creating the divisions has actually shone a spotlight on it. But actually, from the beginning of the Company, we've had a strong focus on software. What Pradeep and the very early team at Juniper did was, the developer, the kernel of the OS, that actually we're continuing to develop and have done over some time. So, we have quite a large proportion of the R&D (inaudible) at Juniper that are software related.

And so, I think what's Kevin's done with the organizational structure has actually helped our focus, in terms of the value added parts of the software, so not just the (inaudible) and functionality into the core OS, but also, add on top of that, other parts of the software area that add value to customers, and also obviously adds revenue and margin to Juniper.

You know, one of the examples of that which we don't talk about is some of the router services that we do with our platforms, both MX 3D and other router platforms, where we actually had software that's deployed in the network of router services. That's a different revenue stream. So today, you know, we bundle that together our IPG revenue. As we move forward, you'll then start to see some of the software revenue separately recorded.

So it's sort of like OS, Pulse, as we talked about in some of the security areas, and then other software applications that we've already been in market with, and others that we bring to market that are specifically focused on value add on top of the systems platform.

**Nikos Theodosopoulos** - UBS - Analyst

Okay. One last question, gross margin. The CFO always gets the gross margin question, right? So, you know, if I look at 2Q and 3Q, the product gross margin has trended down a bit, and Cisco has been talking about being more aggressive in emerging markets in the router market. And the expectation is while (inaudible) will try to be more aggressive in the future. Has routing seen its best days in terms of margin profile, or do you still -- and the trend is down, going forward, or can this still be a stable gross margin business for Juniper?

**Robyn Denholm** - Juniper Networks Inc - CFO

Yes, I -- our routing margins -- in fact, our margins overall, from a gross margin perspective, are actually very healthy. And if you look at what's happened over the last couple of quarters, the proportion of either SLT revenue or router revenue in the case of the third quarter, was less as a proportion of total revenue than has been typically the case.

And so, that has been a slight headwind on the gross margin. The other is, we have had some specific period costs in terms of inventory carrying charges that we've borne over the last couple of quarters.

And so, from my perspective, the margins, router and otherwise, are very healthy.

I think innovation and gross margins go hand and hand, so when we're delivering solutions to customers that are actually 10X, or in the case of PTX, 5 to 7 times better than what any competitors have out there, either the performance in terms of any other products that are out there, or actually, you use one third or 50% of the CapEx of a competitor's solution, that actually creates great value to the customers.

So even if you look at the QFabric solution, it might be slightly more in terms of the per box or per solution price, but what it delivers to the customer is many times less than what it would cost them with the competitor's solution.





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So, our viewpoint is that that our margins are healthy because of the innovation and the value that we're delivering to our customers, and it's reflective of how high they are, and will continue to be.

**Nikos Theodosopoulos** - UBS - Analyst

Okay. Okay, with that, we've run out of time. Kathleen, Robyn, thank you for attending, and we hope to see you both next year.

**Robyn Denholm** - Juniper Networks Inc - CFO

Okay. Thank you.

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