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PRESENTATION

Operator

Greetings and welcome to the Juniper Networks third-quarter 2013 earnings results conference call.

(Operator Instructions)

As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Ms. Kathleen Nemeth, Vice President of Investor Relations. Thank you, Ms. Nemeth, you may begin.

Kathleen Nemeth - *Juniper Networks Inc - VP of IR*

Thank you, operator. Good afternoon and thank you, everyone for joining us today.

Here on the call are Kevin Johnson, Chief Executive Officer; Robyn Denholm, Chief Financial and Operations Officer; and Rami Rahim, Executive Vice President, Platform Systems Division. Rami is in Brazil today where he is presenting at the Futurecom Conference.

Please remember when listening to today's call that statements concerning Juniper's business outlook, economic and market outlook, strategy, future financial operating results, and overall future prospects are forward-looking statements that involve a number of risks and uncertainties. Actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including economic conditions generally or within the networking industry; changes in overall technology spending and spending by communication service providers and major customers; the network capacity requirements of service providers; the timing of orders and shipments; manufacturing and supply chain constraints; variation in the mix of products sold; customer perception and acceptance of our products; rapid technological and market change; litigation; and other factors listed in our most recent 10-Q and the 8-K filed with the SEC today.

All statements made during this call are made only as of today. Juniper undertakes no obligation to update the information in this conference call in the event facts or circumstances change after the date of this call.

In discussing the financial results, Robyn will first present results on a GAAP basis, and for purposes of today's discussion, we will also review non-GAAP results. For important commentary on why our Management team considers non-GAAP information a useful view of the Company's financial results, please consult the press release furnished with our 8-K filed with the SEC today. For the detailed reconciliation between GAAP and non-GAAP results, please see the Investor Relations section of our website.

On today's call, Robyn will also be providing forward-looking guidance. As a reminder, guidance is provided on a non-GAAP basis, other than that with respect to revenue and share count.

All guidance is forward-looking and actual results may vary for the reasons I noted earlier. GAAP guidance measures are not available on a forward-looking basis due to the high variability and low visibility with respect to certain charges, which are excluded from the non-GAAP guidance estimate.

Please note that today's call is scheduled to last for 1 hour.

(Operator Instructions)

With that, I'll turn the call over to Kevin.

Kevin Johnson - *Juniper Networks Inc - CEO*

Thanks, Kathleen, and welcome to all of you joining us on today's conference call. I'm pleased with our results this quarter, as we delivered our fifth consecutive quarter of year-over-year growth, reflecting good execution against our strategy. Overall, our results were in line with the expectations we set in the second quarter.

We continue to see strength in the service provider market; the enterprise tracked largely as we expected; and security continued its trend towards stabilization with sequential growth in the third quarter. In each of these areas, we continue to exhibit the strength and innovation of our product portfolio.

Overall, the macro environment remains dynamic. While we are encouraged to see the US government reopen, we are mindful of potential volatility in the federal sector.

There are a few things I'd like to highlight for the third quarter before I turn the call over to Rami for an update on our platforms systems division. First, the response we're getting from customers indicates our SDN and network function virtualization strategy continues to resonate with them.

SDN is a growth opportunity for us in both networking systems and software. Our vision is to unleash innovation and agility in customer IT investments by unblocking the impediment of the static network to their cloud strategies. We're doing this in three ways.

First, we offer a unique advantage through our deep knowledge and proven track record of innovation in high-performance networking, with a focus on systems and software. Second, we provide clarity of choice with software and programmable systems that are based on industry standards and open-source models with open Contrail; customers can buy our product and solutions today. And finally, we have outlined a clear four-step implementation strategy for customers that includes a flexible, cloud-oriented software licensing model, the Juniper Software Advantage.

As we mentioned last quarter, following highly successful beta trials, we launched our Contrail SDN controller earlier than our original 2014 ship date. Contrail works in private and public cloud environments to virtualize the Company's data center network and enable service providers to build new edge networks that significantly reduce the time required to deploy future services.

We have both a commercial and an open license model for Contrail. Open Contrail, our open-source license version, provides access to all aspects of the Contrail source code, offering easy integration, a stable platform, a production-ready code base, and compatibility with both CloudStack and OpenStack. It is our view that the open-source business model of open Contrail will enable maximum reach, while the commercial Contrail business model allows us to monetize Contrail for those customers who look to Juniper for a supported version of the product.

In addition to providing world-class end-to-end solutions across Juniper's routing, switching, and security systems, we have also enabled Contrail to work with competitors' network hardware and software products. This will reduce both the time and risk associated with deploying network virtualization technologies by customers, accelerating the benefits of SDN and network function virtualization.

In other product highlights, we had a strong quarter in routing, which Rami will discuss in more detail. We also saw good growth in our switching bookings that reflect good traction in the data center. You can expect some additional data center announcements later this month.

Looking at our overall markets, we continue to drive innovation in service provider, where we're focused on carrier, including wireless and wire line, along with cable and web 2.0 companies. As I mentioned we're executing as we said we would in SDN and network function virtualization with Contrail and we're continuing our progress in systems and software and data centers and service provider networks.

In addition, we are continuing to focus on advancing the integration of optical and routing. We are well-positioned to take advantage of the continued growth we're seeing in the edge, and the expected growth we've been talking about in the core, with good momentum across our broad product portfolio. Globally we're seeing strength in service provider across all three geographies -- the Americas, EMEA, and APAC.

In the enterprise, we continue to focus on high-performance networking to help transform the SDN-enabled virtualized data center. Within the data center, we help customers virtualize the network and connect their private clouds to commercially provided public clouds. This is also enabled by our Contrail controller.

In security, as we have said consistently in recent quarters, we continue to see signs of stabilization in the product portfolio. For data centers, we are driving the industry agenda on security and today we have the most advanced solution to protect the data centers from attack.

Our campus and branch installed base is significant and we are evolving that technology to meet emerging needs of our customers. And we continue to introduce new features and improved manageability of our security solutions. Although we haven't yet returned to year-over-year growth in this business, the sequential growth we saw in the third quarter is encouraging and we believe our security business is well-positioned for a return to growth in 2014.

Wrapping up, we continue to drive our innovation agenda, offering unique solutions for our customers in each of our markets. While the macroeconomic environment continues to be dynamic, we believe the Business is healthy and momentum is building. We are focused on executing with agility and delivering long-term growth to our stakeholders.

With that, I'll turn it over to Rami.

Rami Rahim *- Juniper Networks Inc - EVP, Platform Systems Division*

Thanks, Kevin. It's great to be here today to discuss the third-quarter results for the platform systems division.

Overall, I'm pleased with this past quarter. Kevin covered the results at a high level so what I'll do is walk through some of the drivers behind this quarter's results for PSD and provide some additional context.

There are two key businesses within PSD -- routing and switching -- and the customers we serve span both service provider and enterprise. I am pleased to report that PSD's revenue came in at $939 million, up 3% quarter-over-quarter, and up 13% year-over-year.

Our PSD product revenues were up 3% quarter-over-quarter and up 17% year-over-year. For Q3, PSD product revenue was at $742 million, our highest product revenue on record, demonstrating solid performance and continued growth in this business.

The sequential increase in PSD revenues overall was driven primarily by growth in routing and strength in service providers globally. This quarter's switching results were mixed, up slightly year-over-year but down sequentially due to lumpiness in service provider demand for data center solutions. While switching revenue declined sequentially, our switching bookings were healthy.

In routing, we saw strong spending among our tier-1 service providers, as well as strength among our cable and web 2.0 customers. In the enterprise, demand is being created by data center consolidation; data center modernization; and the continued adoption of fabric-based architectures.

Let's go a bit deeper on our results. First, routing.

The PSD routing business was up 7% quarter-over-quarter and up 22% year-over-year. Quarterly growth was driven by both core and edge routing and the year-over-year growth in routing was driven primarily by edge routing. We continue to have a diverse customer base and a robust product mix.

We simplified our product portfolio and delivered innovative products and technologies, including the variants of the MX2020 and the MX 2010, and a multiservice line card that delivers high-performance services to the MX. The Junos 13.2 release also came out in Q3 and it was packed with compelling customer features. We had some great routing wins this quarter -- one at a leading Australian provider of home and mobile communications and broadband, and another at a leading Canadian provider of cable and Internet.

The PSD switching business was down 8% quarter-over-quarter and up 1% year-over-year. The quarterly decline was partly due to coming off a strong quarter in Q2 and partly due to the variability in service provider demand for data center solutions.

On the other hand, we did see good bookings growth year-over-year and have a strong backlog going into the next quarter. We continue to see growth in both data center and combined campus and data center deployments.

We saw strength in top-of-rack and 10 gig overall, both sequentially and year-over-year. We also saw good repeat and new business in both service provider and enterprise accounts for switching. Our innovation pipeline was rich in the third quarter as we shipped several new variants of our EX family of fixed switches, as well as new 100 gig line cards for the EX9200.

On the SDN front, Juniper also announced the general availability of our Contrail controller that enables seamless integration between physical and virtual networks for both service providers and enterprises. It has been in trials with roughly 40 customers across the world.

We are very pleased that we were able to pull in the dates of this release and ship a product that supports industry-standard protocols. All credit goes to our hard-working and innovative engineers.

We also joined with VMware at VMworld in August to announce a hardware-accelerated physical to virtual Gateway solution using Juniper's high-performance networking infrastructure and VMware's NSX. The data center is an important focus area for us and you'll continue to hear about our innovations in this domain, as Kevin mentioned earlier.

We had some great wins in switching and wireless, as well. One was with the multi-national industry leader in oil and gas exploration and refining, and the other at a global financial services firm.

So with all of that said, I'd summarize as follows. We are well-positioned in the edge, core, and virtualized data center, with our portfolio today and innovations in the pipeline. Customer feedback around our solutions and recently-launched innovations has been very positive.

We are pleased with the progress we are seeing and I'm satisfied with how we are delivering against our innovation agenda. At this point, I'm going to turn it over to Robyn. Thank you.

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

Thank you, Rami, and good afternoon, everyone. I am pleased to report that our third-quarter results reflect continued momentum in revenue and earnings growth.

Revenue came in slightly higher than our expectations, driven by continued strength in service provider routing. Non-GAAP earnings increased sequentially due to healthy growth margins, partially offset by operating expenses that were at the upper end of our guidance.

Our focus on driving top-line growth and operational excellence is unchanged. With that goal in mind, we continue to work to improve our cost structure.

In the third quarter, we took additional steps to rationalize our product portfolio and rebalance our investments. I will talk more about this and associated restructuring charges later in my prepared remarks.

Looking at our demand metrics we continue to see signs of strength in the service provider market, and for the first time in several quarters, saw bids in all three geographies. We had a good bookings quarter, with book-to-bill greater than 1. Product deferred revenue was up slightly quarter-over-quarter and backlog remained at healthy levels.

Total revenue was $1.186 billion, up 3% sequentially, and 6% year-over-year. Product revenue was up 4% quarter-over-quarter and 7% from a year ago.

Services revenue was down slightly versus the prior quarter, primarily due to the timing of certain renewals. Although we had no 10% customers this quarter, we saw strong revenues from our top-tier carrier customers.

For the quarter, GAAP diluted earnings per share were $0.19, including a $0.02 impact from restructuring charges. Non-GAAP diluted earnings per share were $0.33, up $0.04 sequentially, and increased significantly by $0.11 year-over-year. The sequential growth was driven primarily by high revenue and gross margins, but also included a $0.01 benefit from the lower tax rate.

Now let me provide color on revenue by region, market, and business segment. Americas revenue was down 2% sequentially and up 18% year-over-year.

The sequential decline was due to enterprise. As a reminder, Q2's enterprise results included the recognition of $34 million of government revenue that had previously been deferred. Excluding this, Q3 enterprise revenue in the Americas would have increased by 1% sequentially. Also, enterprise was up 6% year-over-year, reflecting broad-based strengths, partially offset by some softness in the financial services and federal market.

Americas service provider increased sequentially by 4% and had its third quarter in a row of double-digit year-over-year growth, reflecting wins across content, carriers, and cable service provider verticals.

EMEA revenue was up 2% sequentially but down 5% year-over-year. The sequential growth was driven by strong service provider performance as design wins in the UK and Middle East began converting to revenue shipments. Enterprise demand was weak in the quarter relative to a strong performance in Q2 due to some business taking longer than we expected to close.

APAC rebounded sharply from a weak Q2, growing 25% quarter-over-quarter with double-digit increases in both service provider and enterprise. This strong performance was driven by good growth in China, Australia, and South Korea.

Service provider revenue was $788 million, up 9% sequentially, and 12% year-over-year, with broad-based strengths across all three geographies. Enterprise revenue was $397 million, down 6% sequentially and 4% year-over-year.

Excluding the government deferred revenue recognition in Q2, enterprise would have been up slightly quarter-over-quarter. The year-over-year decline was due to weaker financial services and government business globally and the timing of some large switching deals in APAC and EMEA.

Now let me review our revenue by segment. Platform system division revenue was $939 million, up 3% sequentially and 13% year-over-year. Total router product revenue of $609 million was up 5% sequentially and 18% year-over-year.

The MX product line had its second successive revenue record quarter, growing 15% sequentially. The recently released MX2020 and MX2010 products continued to gain traction with customers. Core routing had a good quarter, growing 11% sequentially with the T-series product line having its best quarter in the last four quarters.

Total switching product revenue of $148 million was down 8% sequentially from a record Q2 and up 1% year-over-year. The sequential decline was primarily due to the timing in certain service provider data center deployments and the migration to the new EX9200 switching platform. We did see strong bookings in the quarter and expect switching to regain its momentum.

SSD revenue was $246 million, up 5% sequentially but down 15% year-over-year. Total security product revenue was $144 million, increasing nicely at 14% sequentially. As I mentioned last quarter, we were seeing early signs of the business turning around and this quarter's results are a positive sign.

Service provider security revenue was strong in the quarter with high-end SRX growing double-digits sequentially. Enterprise security continued to stabilize, with a record quarter for branch SRX and good sequential growth for high-end SRX in the data center.

This is still the early stage of our security business recovery and we continue to focus on growing revenue. Our new products continued to secure design wins with revenues greater than $110 million for the quarter.

Moving on to gross margins and operating expenses. Non-GAAP gross margins for the quarter were 64.4% compared to 63.7% last quarter and 65.6% a year ago. Non-GAAP product gross margins were 65.4%, an increase of 1.6% over last quarter and a decrease of 1.4% from last year. As expected, the sequential improvement was largely the result of the non-recurrence of last quarter's federal revenue recognition.

Non-GAAP services gross margins were 61.3%, a decrease of 2% from last quarter, and [a] 0.9% from last year. The sequential decline was the result of lower revenue and higher support-related costs.

Non-GAAP operating expenses were $530 million, an increase of $14 million sequentially, and a decrease of $15 million year-over-year. This increase was primarily due to higher legal expenses. We continue to focus on operational excellence and driving efficiency in our investments.

With that goal in mind, we have taken some restructuring and rebalancing actions in October. That will result in the elimination of approximately 280 positions in the fourth quarter. We have also continued our real estate consolidation.

Looking at headcount, we ended Q3 with 9,714 employees, a sequential increase of 201, primarily in lower-cost regions. Non-GAAP operating margin for the quarter expanded to 19.8% compared to 18.9% last quarter and a significant improvement over the 16.9% last year. The sequential increase was driven by higher revenue and gross margins and an improvement in operating expenses as a percentage of revenue.

The non-GAAP tax rate was 25.5% compared to 27.4% last quarter. This improvement is due to the geographic mix of income and some one-time items.

Looking at the balance sheet, we ended the quarter with $3 billion of net cash and investments. We generated strong operating cash flows of $176 million, in line with our historical patterns. Q3 DSO was 42 days, up from 40 days last quarter.

Capital expenditures were $41 million, down 43% sequentially, as a result of the completion of the first phase of our Sunnyvale campus. While depreciation and amortization expense was $41 million. We repurchased 4.4 million shares for $93 million, at an average price of $20.92, and we have $1.2 billion remaining on our current authorization.

Now I will review our outlook for the fourth quarter. As a reminder, these metrics are provided on a non-GAAP basis except for revenue and share count.

We expect the December quarter to reflect continued strong service provider demand with some improvement in enterprise. However, we are carefully monitoring any impact in federal spending from the recent US government shutdown.

For the fourth quarter, we expect revenues to range from $1.2 billion to $1.23 billion. Gross margins are expected to be in the range of 64.5%, plus or minus 0.5%. Operating expenses are expected to range from $510 million to $525 million.

At the mid-point of guidance, operating margins are expected to be approximately 22%. This is expected to result in non-GAAP diluted EPS of between $0.35 and $0.37 per share, assuming a flat share count and a tax rate of approximately 27.5%. On a GAAP basis, we also expect an additional restructuring charge of approximately $10 million related to the fourth-quarter headcount actions.

To summarize, we anticipate the overall demand to be healthy with some potential challenges in federal. As we drive to close out the year, our product portfolio and focus on execution are very strong.

I would like to thank our employees for their continued dedication and commitment to Juniper's success. And now with that, let me turn the call over for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Rod Hall, JPMorgan.

Rod Hall - *JPMorgan Securities Inc. - Analyst*

I just had a couple. I wanted to go back to security because I thought that was a pretty positive number and to see if you could elaborate a little bit on what's going on there, what should we be thinking about trajectory, et cetera? And where of those revenues coming from customer-wise if you can give us any more color on that?

And then just on the guidance, which is below what we were expecting, it feels like it's probably related to federal enterprise, but can you just clarify what the driver for the slightly weaker revenue expectation is for Q4? Thanks.

Kevin Johnson - *Juniper Networks Inc - CEO*

I'll take the first one and then I'll hand off to Robyn to take the second questions on the guide.

On security, we had a good sequential uptick on revenue in our security business. And I think it's a reflection of the continued progress we're making.

As I've mentioned before, on these calls, there's three categories of scenarios that we're focused on in security. One of them is securing service provider LTE networks and the mobile Internet. The second is data centers, both service provider and enterprise data centers. And the third is campus and branch.

In the area of service providers and securing the LTE networks, we did see some good momentum again this quarter on the service provider side, which was one of the contributors on that uptick, but we also saw very good growth sequentially on our high-end SRX, which is used both for the service providers and the data centers. So the data center solution that we have that provides WebApp Secure, Spotlight, as well as that high-end SRX, we believe is an industry-leading solution, and we're seeing some continued progress, especially with the high-end SRX.

And then for campus and branch, we also saw good sequential growth in our branch SRX. That is also an area that we're doing some additional work for some new capabilities that we'll hear more about in the future.

But overall the SRX business did well. The ScreenOS revenue as a percentage of the total is a lower percentage of the total than it was in the prior quarter, which is a reflection of us continuing to make progress on moving that installed base and migrating from the ScreenOS revenue streams to the SRX and the rest of the security products. So overall it's a good data point that gives us confidence we're executing against the right things.

But that said, we know we still have a lot of work to do. We're very clear about that. We're very focused on that.

We have the resources applied to that. And we believe we are well-positioned for growth on our security business in 2014.

Robyn, I'll let you take the question on guidance.

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

So Rod, on the guidance question, in terms of the service provider momentum that we've been seeing, and we saw in the third quarter, we expect that to continue. We're seeing good design wins in all three [theaters] and we continue to execute really well.

The guidance is tempered by our expectation of federal being weak in the fourth quarter. We did see some signs of that in the third quarter, as we talked about in the prepared remarks, and we do expect that in the fourth quarter.

And so absent that, even for enterprise, we expect things to continue on a good path. But the federal weakness, we're expecting in the fourth quarter.

Operator

Tal Liani, Bank of America Merrill Lynch.

Tal Liani - *BofA Merrill Lynch - Analyst*

On the core side, I have two questions. On that core side, can you discuss where the strength is coming from PTX versus the new T-series?

That's one question. And if you can elaborate, actually, on PTX given that it's a architectural change?

And then this one is a broader question. If I look at your chart, chart number 9, basically the growth is coming from service providers in North America if I combined two pieces.

Is this a spending tide and that's what lifts up revenues, or is this more Company related? That means if we have some slower growth of spending next year on certain projects, is there going to be a reversal of these positive trends or do you have enough product cycle that can lift you up even in a more challenging environment? Thanks.

Kevin Johnson *- Juniper Networks Inc - CEO*

Why don't I take your second question first and then I'm going to hand over to Rami to talk a little bit more about core and the trends that we see there. Your second question had to do around broad growth in the service provider sector.

And what we see unfolding is very consistent with what we outlined in the last earnings call at the end of Q2, which is we continue to see service providers turn their attention and their CapEx investments to their IP networks. And we saw a lot of strength in Edge but this was a quarter where we also saw good sequential uptick in core.

We believe that is going to continue. We believe, if we look at the projects that we have, there are a pipeline of projects that we're working on that will begin deployment in next year. And so we anticipate continued momentum going forward.

Specifically in our Americas service provider business, not only did we see strength with our tier-1 service providers but we also saw it in cable and the web 2.0 content providers. And so -- as well as the tier-2 and tier-3 carriers as well. So it's a broad trend that we believe will continue.

In Europe, with the service provider landscape in Europe, the way I would characterize it is that the large carriers were mixed but stable. There were some that had projects that ended. Others that had project that kicked off.

Some of those service providers have project that ended. We have visibility to the next wave of projects so Europe service provider has stabilized and is at the point they too need to invest CapEx in their IP infrastructure. And there's been some wins that Rami mentioned that we've had there.

And then Asia, we also saw a good sequential uptick in service providers, primarily in countries such as Korea, Australia, China. Other countries were not quite as strong. Japan was also a good performer.

So the net is, on a global basis, this trend that we see of service provider CapEx on the routing infrastructure was evident in the fact that all three theaters showed good sequential growth and we think that that's going to continue into 2014.

With that, let me hand over to Rami. And perhaps Rami, you can take Tal's first question on core and what we're seeing their related to PTX, T, and some strength some trends in core. Rami?

Rami Rahim *- Juniper Networks Inc - EVP, Platform Systems Division*

I'd be happy to, Kevin. First I'll say that the main drivers that are affecting our year-over-year performance in routing are still in the edge and I think that the demand factors there are very strong, whether it be capacity or service delivery or connectivity.

But that said, we are pleased with what we've seen from a sequential standpoint in the core. We've been saying now for a couple of quarters that the core networks are running hotter and therefore there is going to need to be an upgrade cycle. And the fact that we're now seeing some sequential performance gives us conviction in that belief.

As far as the question around T versus PTX, certainly both are performing quite well. PTX year-over-year performance is very healthy. T-series, in fact, I will say is driving a lot of the sequential performance.

You're absolutely right in that PTX is a bit of an architectural transition, which is why we have the T and the MX as other options for our customers to round out our portfolio nature as if we're well equipped to address any sort of core build out.

The T-series remains the best investment protection story in the industry. And the PTX, especially now as we introduce before the end of this year, we've announced this already, our 100 gig DWDM interfaces, is really going to make it a very compelling packet optical solution for operators that are looking to consolidate layers in their network and simplify their network.

Operator

Kulbinder Garcha, Credit Suisse.

Kulbinder Garcha - *Credit Suisse - Analyst*

Maybe first of all, Kevin, just in terms of going back to the previous comments you made, it just feels like many of the service providers -- I'm thinking the telco service providers --are indicating slowly that it seems like they need to invest not only in the US, but Europe is recovering, there are signs of continued life in Asia.

I'm wondering how has your visibility changed over the last 3 or 6 months in your conversation? Any color you could give around that would be helpful.

And my second question is, on the SDN side -- I know it's very early days -- if you were to guess today, in terms of these customers going from the 40 or so trials to an actual stage of relatively meaningful deployment, however you want to describe that, how long is that is that? What is that -- 2 to 5 years, 12 months?

Just the discussions you're having with the products you've launched. How do you see the whole shape of that evolving? Many thanks.

Kevin Johnson - *Juniper Networks Inc - CEO*

I'll take the first question and then perhaps I'll hand off to Rami to talk a little bit about SDN and how he sees that unfolding in the marketplace.

In terms of looking at what we see as the continued building strength of the service provider industry and marketplace, your question specifically was how have we seen visibility change in the last 3 to 6 months? And I would say that the trends that we identified, I would say in Q3 of a year ago, so about 12 months ago, are consistent.

Yet I would say our visibility to the specific projects continues to improve and continues to strengthen and that's a function of bids that customers had, that they were in the process of working, that we have been awarded, and the teams are now engaged working on those projects. And in some cases, it includes new features, new software.

I think the fact that our backlog is up, our deferred revenue is up, the pipeline is strong, all of those are data points that are indicators that the visibility to that service provider spending cycle has improved over the last one to two quarters. Let me hand off to Rami to share a perspective then on SDN and how quickly, Rami, you see deployments unfolding.

Rami Rahim - *Juniper Networks Inc - EVP, Platform Systems Division*

Certainly. So I look at it a number of different layers.

With respect to SDN, it is certainly still in the early stages and there are a lot of customers that we're having discussions with around the journey that they will undertake in order to deploy SDN in their networks. Today, what we are doing in fact is we are implementing the hooks into our systems, into our platforms, and the programmability into our platforms, that gives customers the peace of mind that they are investing in switching, routing, security that will involve through this SDN journey without having to do a wholesale network upgrade. That is very much resonating with our customers and we're seeing momentum in the market as a result of that message alone.

Now, we're also, of course, developing really industry-leading software, like our Contrail controllers that provides unprecedented scale, that provides things like resiliency, and tiering between controllers and so forth, that our customers are starting to really think about how they're going to deploy in order to solve a number of challenges in their networks. I think that this is going to play out over multiple quarters. I think that one of the most prominent applications for it will be in the data center to build out overlay networks for the purpose of virtualizing networks in the data center.

We want to do this both with our own systems and our own controller, as well as with our own systems and partners like VMware. As I said, it's going to take a few quarters for this to pan out, but we're very confident in the solutions that we're developing to address these applications that I mentioned.

Operator

Simona Jankowski, Goldman Sachs.

Simona Jankowski - *Goldman Sachs - Analyst*

I just had two questions. The first one was, I think you commented that China bounced back in the quarter. If you can just dig into that a little bit since some others have commented on weakness there?

And then the second one, back to the core routing dynamics, and perhaps this one for Rami, are you seeing any impact at all from the new product introductions in the market from Alcatel as well as Cisco's CRS-X and the NCS? Whether in terms of market share or pricing or just any other implications?

Kevin Johnson - *Juniper Networks Inc - CEO*

I'll take your first question and then I'll hand off to Rami for the second question.

Just to clarify, in the comments, what we saw, was we saw good sequential growth in APAC, of which China was one of the contributors. And my comments on China, specifically on the service provider side, is that our strategy has always been one that we've been very targeted or very surgical on the opportunities of the areas that we focus on in China, specifically those opportunities that play to our strengths of having differentiated products in the areas of scale, and performance for obviously very high volumes of traffic in China. And there were some opportunities in the quarter that unfolded that generated some revenue for us in China specifically in the service provider routing side of the markets that contributed to the overall APAC results.

China, we work closely with our partner Ericsson in many of the service provider instances. And so Ericsson continues to be a very good partner for us in certain geographies and certainly China is one of them. And that's a contributing factor as well.

Rami, I'll hand over to you for Simona's question on the core.

Rami Rahim - *Juniper Networks Inc - EVP, Platform Systems Division*

I'll say that this market, whether it be core routing or edge routing, has always been a very competitive market. And I certainly don't expect any of our competitors to stand still. I operate and we innovate under the assumptions that both Cisco and Alcatel are going to be releasing new products, as they both have.

It doesn't change the strategy that we are executing towards, and the fact that I remain very confident in the technologies that we're developing and releasing into the market. The fact remains that the PTX is still the only platform of its kind in terms of the efficiency at which it moves packets around, so it appeals to the transport buyer.

T-series remains the best investment [section]. It's been out there for a decade and still growing and still has excellent capacity.

And then as I've also mentioned in the past, the MX2020 now gives us an architectural approach that blends services throughout the entire network -- edge and core. And that also is resonating with many of our customers.

So I remain confident in the technology that we have today. And of course, we're not standing still either. We are working on next-generation silicon, next-generation software to make sure that we maintain our competitive edge.

Operator

Mark Sue, RBC Capital Markets.

Mark Sue - *RBC Capital Markets - Analyst*

You're proactively pruning the headcount. Would you consider extending the pruning to the product portfolio?

If I look at the enterprise, for example, the routers there are down 50%. Security is better now, but it's been somewhat inconsistent, and you even still carry some enterprise Wi-Fi product. So I'm wondering are there benefits to becoming were focused and less broad, or do you feel that with the return of the carrier router cycle, that perhaps you double-down in some of your other investments?

Kevin Johnson - *Juniper Networks Inc - CEO*

Let me comment on that and then I'll let Rami add to it a bit on the product portfolio side. But let me just say, first of all, we have been pruning the product portfolio.

One example of that is MobileNext. And just to give you some perspective there, when we launched the MobileNext project, it was part of an overall strategy to continue to increase our push into the wireless side of the business.

We continue to see good growth in the wireless side, as evidenced by the strong performance we've seen on the MX and some of the core convergence projects that we're doing with PTX. Now with the introduction of the ACX and the Backhaul, all of those things have helped us continue to strengthen our position in the wireless side of service providers.

In addition, the inflection point of network function virtualization and SDN, we believe is going to create a paradigm shift in how evolved packet core solutions are deployed. We believe that's going to become more of an x86 virtualized network function and something like Contrail will play a role in service chaining and help enabling that.

So we took a decision to cancel that project. So that cancellation of that project is pruning the portfolio and is part of this reduction in the headcount that we just spoke of. And there's a number of examples of smaller things like that, that we are doing.

Now specific to your question on routing, and you said enterprise routing was down, keep in mind these are the same routers that we sell to service providers and part of the reason it's down is related to the US federal and other large entities like that, that have similar attributes to their business, like service providers. So unless we took a decision to start to prune the portfolio in our core business of service providers, which I don't think makes sense, these are the same product that we sell to many of our large enterprise customers.

But certainly, we do believe that the strategy we're on is one of narrowing our focus. We've been very clear that our focus is on the service provider and, specifically, the domains of the core and the edge of their networks. And now with ACX, on the access layer of their networks, as well as their data centers. And that data center priority is one that then crosses over into enterprise.

You will hear more about some new things that we'll announce in the data center here later this month. And then certainly there's some areas that we will continue to assess. But we're very committed to the fact that monetizing our investment in R&D across both service provider and enterprise with products that sell to both is the most leveraged way to drive value, both for our shareholders and for our customers.

Rami, let me hand over to you and let you see if there are things you want to add to that, or amplify.

Rami Rahim - *Juniper Networks Inc - EVP, Platform Systems Division*

I'll just add a couple of things. I think you've covered it well, Kevin.

The engineering principles that we're applying to our strategy are really all around focus and high leverage. If you think about what we've done in the past, for example, in focusing all our investments dollars in the MX as opposed to spreading them across multiple different edge platforms, that is an example of the strategy that has worked very well for us and an example of what we are essentially doing now. We want to make sure that we solve our customers' high-performance networking problems with the fewest number of high-quality differentiated platforms possible, and that's essentially what we're doing.

We want to make sure that we're leveraging between our data center and our campus. We've done that in our Organizational design between service provider and enterprise.

We've seen tons of opportunities to do that as enterprises start to seek the same sort of carrier-class capabilities in their platform. We're doing just that as well. So these are just some of the principles that we're applying that worked for us well in the past and will continue to work well for us going forward.

Operator

Subu Subrahmanyan, The Juda Group.

Subu Subrahmanyan - *The Juda Group - Analyst*

My question is on the switching business. Could you talk about, excluding the lumpiness, what are the other drivers you're seeing going forward?

Is it share gain? Is it new products that you're releasing in the data center? And can you talk about the QFabric versus a standalone best-of-breed product strategy, how we should see that play out in 2014?

Kevin Johnson - *Juniper Networks Inc - CEO*

Rami, let me hand this one to you and I'll let you talk a bit about our switching portfolio.

Rami Rahim - *Juniper Networks Inc - EVP, Platform Systems Division*

Certainly. So the major drivers that we're seeing right now for switching are in data center and combined data center campus opportunities. We actually see that a good fraction of our business goes to enterprises that are building common cores that serve both their data center and their campus.

10 gig upgrades are still happening. They are coming [strong] so [we saw good] growth in our 10 gig ports across our portfolio.

SDN, as I mentioned earlier, the discussion now is about making sure that our customers are equipped with the infrastructure that can help them move through their SDN strategy, whether it be one with our own controller, Contrail, or one with our partners' controllers, for example, VMware.

We did not breakout the QFabric versus EX performance. At the end of the day, we have multiple different fabric options that will solve various different problems that our customers need solved. The virtual chassis in the EX, QFabric in the QFabric architecture are both different options and depending on who you're talking to or what problem you're trying to solve, each one will have a sweet spot in terms of its application.

And yes, we did say, whereas revenue was essentially flat year-over-year, the bookings momentum that we saw in terms of growth gives us confidence -- and the backlog that we built, I should say -- gives us confidence in the next quarter. And Kevin did mention that we are going to be announcing somewhat shortly some new innovations in this space that are going to help us and only increase our confidence.

Operator

Ben Reitzes, Barclays.

Ben Reitzes - *Barclays Capital - Analyst*

Could you talk about services expectations for the fourth quarter? You mentioned there were some renewals that didn't get signed and maybe that implied some services revenue pushed into the fourth quarter? I wasn't sure.

And then just on federal, is it still about 4% of sales? And what did it do in the quarter and what's in your guidance for federal? You said qualitatively, if you can quantify any of that around federal, that would be really helpful?

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

On the first question around services, so we did see a slight decline in the revenue quarter-over-quarter. We do expect that to come back over the next couple of quarters.

We also saw a decline in the gross margins by about 2 points. And we do expect that to come back, as well, over the next couple of quarters, as well. So the services business is very healthy.

On the support side, obviously, as our footprint grows, we need to continue to make sure that we're there for our customers in terms of maintaining the products that we have out in the marketplace. So that's why the gross margin came down a little bit.

In terms of the federal revenue, about a year ago, I gave you the percentage of about 4.5% of total Company revenue and that that had come down over the previous year. On a year-to-date basis, including the revenue in the second quarter, the routing revenue that we talked about in the second quarter, we are at about that level, at about 4.5% on a year-to-date basis.

I expect the fourth quarter to be weaker than what we typically see and therefore the percentage of overall total revenue for the year to be lower than the 4.5%. I hope that clarifies it.

Operator

Brian Marshall, ISI Group.

Brian Marshall - *ISI Group - Analyst*

Obviously, service provider continues to move in the right direction, but enterprise is down a little bit. Can you talk a little bit about your partnership with IBM, in conjunction with Pure and what else you're doing to address this pre-configured, pre-integrated stack?

EMC earlier this morning talked about 50% year-over-year growth in there VBox. So I was wondering if you could talk a little bit about that?

Then perhaps a quick update on the CEO search process and where we stand with that? Thank you.

Kevin Johnson - *Juniper Networks Inc - CEO*

Let me handle your second question first and then I'll frame your first question and then hand it off to Rami.

On the CEO search, on our last earnings call, I commented that the Board had put together a search committee and had started a search. I would say that we're in the later stages of that process and I would expect -- there's no news to announce on that today -- but I would expect that when they conclude, we'll make that news available certainly.

And just to remind you that in the interim, I continue to fulfill the role as the CEO, and will make sure that I'm available to have a smooth and thoughtful transition to my successor. So the update is -- I would characterize the Board as being in the late stage of that process.

Your first question around the enterprise -- a couple of things -- certainly as Robyn highlighted there was some weakness in federal and we did see some good results on our SRX sequentially on the security business. And then, as Rami commented, our bookings for switching, we saw some good year-on-year growth with bookings and switching. You put that together and there were some good signs of some progress and momentum there.

The relationship with IBM continues to be a very important one to us. They're a key partner for our go-to-market in the enterprise. I would say much of that relationship is anchored on the services side of their business and what we're doing to help enable their services side of the business and there's certainly opportunities for us to continue to expand that.

Your question specifically then is how are we addressing the integrated stacks of compute, storage, and networking that we are seeing on the market today? And for that, let me hand over to Rami and he can talk a little bit about the work we're doing with IBM in that area. Rami?

Rami Rahim - *Juniper Networks Inc - EVP, Platform Systems Division*

It is certainly an important segment of the market and this is precisely why we have created a partnership with IBM, to make sure that we do have an offering that can satisfy that part of the market. But I will just point out that it's not only about that. There is a large set of our customers, especially the very large customers, that are looking for much more modularity, open interfaces between the various different stack elements in their data center.

And we're well-equipped to have that discussion, especially as a result of partnerships that we have with EMC and VMware and CloudStack and OpenStack and so forth. We want to promote an open ecosystem of the different software and hardware stack elements that will appeal to many of our customers. So [they're] both segments of the data center market are really important to us -- integrated and more disintegrated, if you will.

Operator

Amitabh Passi, UBS.

Amitabh Passi - *UBS - Analyst*

I had a two-part question on security and then one for Robyn. Kevin or Rami, just on security side, can you give us a sense of how the service provider market is?

We're hearing some noise in the market of increasing competitive pressure in that market. Just wondering how you would characterize the environment for your service provider security business?

And then Kevin, just related to your data center strategy, are there any metrics you can give us that give us a sense of how WebApp and Spotlight are developing?

And then Robyn, just one for you on the OpEx front, if we assumed 5%, 6% growth next year for top line, how do we think about OpEx progression for 2014?

Kevin Johnson - *Juniper Networks Inc - CEO*

I'll take the first one and then hand over to Robyn for the second one. The first part of your question was related to security specifically in the service provider market. And the specific area that we are focused on with that is securing the LTE network for the mobile Internet of our large wireless carriers.

And we've had a significant number of wins and success in that area. The key driver is the fact that these require very high-end systems to handle large amounts of traffic. The high-end SRX has been a very strong offering for service providers in securing their LTE networks.

We don't see a lot of competitive threats in that particular area of the service provider, which is where we're focused on security. Certainly service providers have other security needs in other areas whether it's data center or their own campuses.

And certainly there's competitors in those areas but when it comes to securing the LTE mobile Internet, we continue to feel like we've got a strong position and we enhanced the product to have even more scale and the ability to handle more concurrent sessions and more throughput. Some of the evidence is just the sequential growth that we've seen on our high-end SRX is evidence of supporting that.

On the data center side, your question was, what do we see with WebApp Secure and Spotlight? With WebApp Secure and Spotlight, we're now seeing some of the early stages of the deployments and the implementations of those.

But by the same token, we're seeing the high-end SRX that goes into data centers. That's sequential uptick was also contributed by wins in the enterprise. And a number of these enterprise data center wins in the area of security, in many cases, would fall into customer segments like financial services and federal government that also have very large data centers and high-end computing needs.

So there's no specific data that I can give you on WebApp Secure and Spotlight today. I would say we see customers are now in the process of going through the early stages of deploying. We're starting to see deployments increase but it's still early in that cycle.

But those deployments do reinforce the value of the high-end SRX. And we did see good sequential uptick on the high-end SRX. Robyn, I'll hand over to you for the second part.

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

In terms of the OpEx side, obviously as a Company, we are committed to growing revenue and also to continue our journey on the operational excellence front. And we've done a pretty good job, I think, in terms of managing operating expenses and to reduce the overall cost structure of the Company over the last 12 months or so.

As we move into next year, obviously, we're not at a point where we can give you guidance on that, but I will refer you back to our operating model where we've talked about being -- OpEx as a percentage of revenue in the 39% to 42% range. At the mid-point of guidance that I gave you for Q4, we'll be approaching that 42% range -- it's about 42.5% of the mid-point of our OpEx guidance for the fourth quarter. So my view is that's where we're headed into the long-term model range as we move through next year.

Amitabh Passi - *UBS - Analyst*

Okay. Thank you.

Operator

Simon Leopold, Raymond James.

Simon Leopold - *Raymond James & Associates - Analyst*

I wanted to see if you could update us on the target for new products. You mentioned on the call in the prepared remarks that you are at $110 million for that set of new products.

You've in the past talked about exiting the year at $150 million. I'd like to get an update on that target as well, as an update of how the mix has evolved in terms of your expectations on those new products? Thank you.

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

Simon, I'll start and then I'll let Kevin comment as well. So in terms of the third quarter, we were over $110 million of revenue on the new product. And as you will recall, there were five products that I talked about at [SAM] a year ago in terms of what constituted that $150 million target -- it was T4000, the PTX, QFabric, and then we also included ACX and MobileNext.

It is very fair to say that the three products -- T4000, PTX, and QFabric -- make up the bulk of the revenue in the third quarter and they have done over the past year, as I've given you update against that target. We feel very good about the pipeline that we have and about the design wins that we have across-the-board in terms of our T4000, PTX, and QFabric and the momentum on ACX is starting to build.

And so we're 90 days away from the end of the fourth quarter. So we'll report out against that target in the fourth quarter but we feel very good about where we are in the cycle of new products that we've launched.

And don't forget, since we've talked about these five products, we've also launched some pretty compelling new products in the MX2000 series, both the 2010 and 2020. And we've also had quite good revenue against those products, as well as we've developed through the year, as they've been out there for a quarter. I'll let Kevin comment as well.

Kevin Johnson - *Juniper Networks Inc - CEO*

When it comes to the core routing, whether it's PTX or T-series, we saw good sequential uptick on T4000, and we've done a lot of work to lay the foundation for that. And as Rami mentioned earlier, PTX continues to be a good performing product for us.

Key in us achieving that will be continued evidence that service providers are shifting or complementing their CapEx expenditures that we currently see on the edge and complementing those with continued upgrades and continued investment in the core. We saw evidence of that in Q3. We'll see how that unfolds in Q4.

The ACX addresses the access layer of the network. And we're seeing some beginning traction in the ACX and we'll see how that unfolds as well. That's a newer product in the product family, but it does reinforce the strategy we have of focusing on the wireless service providers with the product set that gives us Mobile Backhaul.

In terms of data centers, we had a very strong quarter in Q2 with QFabric. We continue to move forward with some of the key QFabric wins that Rami mentioned and this is both on the service provider side as well as the enterprise side. And there's a number of deployments. I think Q4 will be a function of how many of those new systems get deployed, combined with how many of the existing installed base customers expand their networks.

And then in regards to MobileNext, we commented earlier on the call that we had canceled that project based on what we see happening in the market with a shift more towards network function virtualization. So the mix shift of perhaps what we expected to what we will see, we're probably going to see a higher percentage certainly in core versus the MobileNext and access will be probably about what we expected. And data center will be about where -- perhaps where we expected when we set that target a year ago in June.

So the mix is slightly changed but not too far off. And I think the key factor is going to be what we see in terms of SD CapEx focused on the core, as well as some of these big data center deployments with QFabric.

Kathleen Nemeth - *Juniper Networks Inc - VP of IR*

That is unfortunately all the time we have today. We would like to thank you for your great questions and for your participation. And we look forward to speaking with you again next quarter. Thanks, everyone.

Operator

Thank you. Ladies and gentlemen, this concludes today's teleconference. You may disconnect your lines at this time and thank you for your participation.
