



**NETSCOUT SYSTEMS, INC.
First-Quarter Fiscal Year 2018 Financial Results Conference Call
Management's Prepared Remarks**

July 27, 2017

A. Kramer: Introduction

Thank you and good morning everyone. Welcome to NETSCOUT'S first-quarter fiscal year 2018 conference call for the period ended June 30, 2017. As usual, I'm joined today by:

- Anil Singhal, NETSCOUT's co-founder, president and CEO;
- Michael Szabados, NETSCOUT's chief operating officer; and
- Jean Bua, NETSCOUT's executive vice president and chief financial officer

There is a slide presentation that accompanies our prepared remarks, which can be accessed on the investor relations section of our website at www.netscout.com. The slides can be advanced in the webcast viewer to follow our commentary. We will call out the slide number we are referencing in our remarks.

Today's agenda will be consistent with prior quarters. Our CEO, Anil Singhal, will share his perspective on our results and recent highlights. Our COO Michael Szabados will briefly discuss key wins and go-to-market developments. Our CFO Jean Bua will then review our first-quarter results and our fiscal year 2018 guidance.

Slide #3: Safe Harbor Statement

Moving on to slide #3, I would like to remind everybody listening that forward-looking statements as part of this communication are made pursuant to the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended, and other federal securities

laws. Investors are cautioned that statements in this conference call, which are not strictly historical statements, including but not limited to, the statements related to the financial guidance and expectations for NETSCOUT, market conditions and customer demand, anticipated revenue from specific customers and all of the other various product development, sales and marketing, expense management and other initiatives planned for fiscal year 2018 and beyond, constitute forward-looking statements which involve risks and uncertainties. Actual results could differ materially from the forward-looking statements due to known and unknown risk, uncertainties, assumptions and other factors. This slide details these factors, and I strongly encourage you to review each of them. For a more detailed description of the Company's risk factors, please refer to the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2017, which is on file with the Securities and Exchange Commission. NETSCOUT assumes no obligation to update any forward-looking information contained in this communication or with respect to the announcements described herein.

Slide #4: Non-GAAP Reconciliation

Let's turn to slide number 4, which involves non-GAAP metrics. While this slide presentation includes both GAAP and Non-GAAP results, unless otherwise stated, financial information discussed on today's conference call will be on a non-GAAP basis only. This slide, which we also encourage you to read, provides information about the use of GAAP and non-GAAP measures because non-GAAP measures are not intended to be superior to, or a substitute for, the equivalent GAAP metric. Non-GAAP items are described and reconciled to GAAP results in today's press release and those and other reconciliations and supplemental detail are included at the end of the slide presentation, which is available on our website.

As we detailed in our press release today, our first-quarter results were consistent with our expectations entering the quarter. We made excellent progress on our product roadmaps, delivering a slate of new products and capabilities to the marketplace. And, we've been pleased thus far with the strong interest and positive feedback on these offerings from customers and prospects. With that as the high-level background, I will now turn the call over to Anil. Anil ...

Anil Singhal:

Thank you, Andy. Good morning everybody and thank you for joining us. Let's begin on slide 6 with a recap of our non-GAAP results.

Slide #6: Q1 FY'18 Highlights

NETSCOUT's first-quarter performance was generally in line with our plans entering the quarter with revenue coming in at 228.8 million dollars, a gross margin of 75.9 percent, an operating profit margin of 6.3 percent and diluted EPS of eight cents per share.

Jean will review our performance in more detail, but I will share a few observations:

- Total revenue declined by 18 percent, which was consistent with the guidance we provided last quarter. A significant majority of this decrease related to the ongoing moderation in spending by one of our tier-one carrier customers.
- Our gross margin improved by 3 percentage points primarily due to favorable shifts in product mix as we begin to see the benefits of our product strategy.
- In terms of profitability, we balanced ongoing expense management with investment in major development and go-to-market activities.
- Overall, we are very pleased with the progress we made over the past several months to drive innovation and elevate our value proposition. Since holding our annual sales kick-off and user conference events in early April to start the quarter, we have officially introduced a number of exciting new products. Let's move to slide number 7 to cover this progress in more detail.

Slide #7: “Smart Data” Strategy and Product Development Highlights

As many of you know, our approach to collecting and analyzing network traffic or wire data is differentiated by our patented Adaptive Service Intelligence (ASI) technology, which instantly converts high-volume network traffic at the collection point into highly structured, multi-dimensional metadata or what we call “smart data.” We’re using this “smart data” to power an expanding range of analytics spanning network performance, application performance, cybersecurity and big data.

During the past two years, we’ve applied ASI to the technologies and capabilities we acquired as part of the Danaher Communication Business including best-in-class analytics for session trace forensics, radio access network optimization, customer experience management, WiFi monitoring, infrastructure performance management and advanced security threats. We believe that this approach offers compelling value to customers. First, it provides investment protection because our new platform is designed to support their legacy workflows. Just as important, it provides customers with next-generation capabilities that address important new use cases and helps facilitate more pervasive instrumentation of their networks.

The first proof point of our “smart data” strategy occurred last fall with the launch of our real-time information platform, the InfiniStreamNG, which is available in multiple form factors and deployment options. The software only version of this platform continues to gain traction in the service provider market because it enables these customers to maximize the utilization of their service assurance budgets and instrument their network more broadly than using traditional hardware probes. At the same time, these deployments are typically negotiated as multi-year purchase agreements, which helps us fortify our incumbency while also providing us with

improved revenue visibility. We also expect that the deals that we've closed thus far will yield comparable or even higher revenue against prior year spends and superior profitability in terms of absolute gross profit dollars. Additionally, we are seeing that when customers standardize on this new platform, they are more likely to purchase other, complementary products from us.

The list of service providers who are now deploying the InfiniStreamNG software has continued to grow and Michael will recap another win that we secured in the Asia-Pacific region. We continue to expect that the software-only version of our InfiniStreamNG will represent between 8 to 10 percent of product revenue in fiscal year 2018 with much of that contribution coming in the second half of the year. Just as important, we anticipate that the adoption of our new platform will help drive better gross margins this year.

During the past several months, we've launched a range of innovative new offerings that can extend our customers' visibility from the core of their infrastructure out to the edge of their networks, and amplify the value of our "smart data" through new high-value analytics. We first showcased these new products at our annual user conference and have subsequently marketed them at major industry events and in customer briefings. The feedback on these new offerings from customers, prospects, partners and industry experts has been resoundingly positive.

We are very excited about the value proposition for each of these new offerings and we plan to highlight many of them on future quarterly calls as they gain traction. This morning I wanted to briefly review why we are especially optimistic about the potential of our new cloud offerings called vSTREAM, vSCOUT and virtual nGeniusONE. These represent the industry's first products to extend application assurance for off-the-shelf or custom applications, regardless

of whether they run in physical or virtual data centers, or in the cloud. By providing deeper visibility into the interactions of the many components of modern applications regardless of how or where they are deployed, we can help customers simplify and assure the success of cloud migration projects, successfully monitor services running across complex hybrid cloud environments, and efficiently extend visibility into their traditional application infrastructures. We are very pleased to have already closed our first sale of this offering, and Michael will profile this win in a moment.

Slide #8: Outlook

This brings us to our outlook, which is covered on slide 8. Overall, we made substantial progress on our development roadmaps during this past quarter to largely complete our newest product cycle. We are excited about the potential of our “smart data” strategy to help customers fully harness the power of IP networking and position NETSCOUT as a strategic partner with proven business assurance solutions that will help them monitor, manage and protect their technology infrastructure.

To capitalize on the potential we see for these new products, we will continue to advance key sales and marketing initiatives. For example, as we move forward, we intend to cross-sell Arbor’s offerings into NETSCOUT’s installed base of customers, advance campaigns to win new accounts, and leverage our strong position in network operations to sell into different senior-level decision makers within our installed base of customers. Although it will take time for these activities to build momentum, we are confident that our value proposition will resonate in the marketplace over the coming quarters. We are also dedicating resources to help guide our longer-term development roadmaps in ways that will help us capitalize on emerging technologies

and new markets such as the Internet of Things, 5G, virtualization, and machine learning.

Looking ahead, our outlook for fiscal year 2018 is fundamentally unchanged, although our EPS guidance was updated primarily to reflect the quarter's share repurchase activity. While the business has tracked according to plan thus far, we recognize that there is a lot of work left to do in order to achieve our targets in fiscal year 2018. We continue to expect that the majority of our revenue and profits will be delivered during the second half of the fiscal year, which is consistent with the historical trends in our business. Jean will provide some additional details on our outlook in a few minutes and at this point, I will turn the call over to Michael for a recap of key customer wins and go-to-market activities.

Slide 10: COO Highlights

Michael Szabados:

Thank you Anil and good morning everyone. Slide number 10 outlines the areas that I will cover.

Wins / Use Cases:

Moving into this fiscal year 2018, one of our top priorities has been to fortify our incumbency with service providers by driving adoption of our software-only platform. We are continuing to make progress on that front. During the past several months, a major mobile operator in the Asia-Pacific region selected and began deploying our InfiniStreamNG software as part of its strategy to improve overall network quality. The former TekComms business was an incumbent at this account but had seen its revenue drop to insignificant levels in recent years after a multi-year period of aggressive investment to support the build out of the carrier's 4G/LTE network. More recently, this carrier saw service outages spike, which resulted in negative press coverage and higher subscriber churn. After conducting an extensive technical review to evaluate a range of solutions, this customer selected the InfiniStreamNG as its new monitoring platform due to its superior next-generation features, combined with the ability to support legacy workflows and compelling total cost of ownership economics. We expect that this multi-year agreement will generate revenue in excess of five million dollars per year.

In addition to this deal, this customer recently expanded its relationship with Arbor for a major DDoS mitigation capacity expansion to help protect its network, and improve its ability to offer a DDoS managed service to its customers. The frequency, complexity and volume of DDoS attacks continues to rise, and our ability to keep pace is critical to both service providers

and enterprises placing their continued trust in Arbor. We recently announced plans to quadruple the mitigation capacity of the Arbor Cloud DDoS managed service to 8 terabits per second by the end of the calendar year. Having this roadmap in place was critical for one of Europe's largest online travel sites who selected Arbor for both on premise and cloud-based DDoS detection and mitigation. This same customer also purchased Arbor Spectrum, our network traffic analysis solution, to identify and investigate advanced threats. A key driver in the selection process was the planned integration between Spectrum and our ISNG platform, which we announced earlier this week.

In the enterprise, Anil highlighted how our new vSTREAM and vSCOUT offerings provide enterprises with deeper application visibility, regardless of whether they run in the traditional data center or in the various forms of the cloud. I am pleased to report that we recently closed our first order for these new offerings totaling nearly a million dollars with a long-standing customer in the energy sector. These products will be used to support a multi-phased, company-wide IT initiative to achieve end-to-end visibility into the company's top 25 applications. While NETSCOUT is the customer's de facto network tool, winning this project involved extensive testing to validate that our solution was more flexible and cost effective than alternative APM tools, along with substantial collaboration with different application teams who helped further refine the development of key features and functionality.

Thus far, we've been pleased with the market's response to all of our new software products for our enterprise customers. We believe that these new capabilities position us to participate in projects with budgets that we historically could not tap into. Our recently launched nGeniusPULSE product is a great example of this because it extends our nGeniusONE

workflows to identify infrastructure performance issues with unprecedented speed, scale and precision across today's largest, most complex technology infrastructures. As a result, customers can leverage their investment in our technology to track issues all the way from the service to a specific infrastructure element directly rather than using disparate tools from multiple vendors. We are building a robust new sales pipeline for this offering and look forward to an upcoming call when we can highlight this use case.

Go-to-Market Activity:

Overall, we generated good momentum with our go-to-market activities during the past quarter. Our marketing organization did an excellent job in cost-effectively maximizing the impact of events such as our Engage user conference and Cisco Live, driving third-party validation of our technology leadership and producing favorable media coverage. Our global sales force is moving forward with great enthusiasm about our newest products, along with the campaigns that we are implementing to generate, cultivate and close new business with existing customers and prospects.

In closing, we move forward intent on further strengthening and expanding our customer relationships with a strong lineup of innovative new products. That concludes my prepared remarks and at this point, I will turn the call over to Jean.

Slide 11: CFO Review

Jean Bua:

Thank you Michael and good morning everyone. This morning, I will review key metrics for the first quarter of fiscal year 2018. After that, I will review the guidance for fiscal year 2018. As a reminder, this review will focus on our non-GAAP results, which are reconciled with our GAAP results in the appendix of the slide presentation.

Slide 12: Q1 FY'18 Results

Slide number 12 shows our results for the first quarter of fiscal year 2018. For the quarter, total revenue decreased 18 percent to 228.8 million dollars. Our gross margin of 75.9 percent increased by 300 basis points. The improvement in gross margin primarily reflects our progress with product strategy aimed at replacing legacy hardware dependent offerings with our ASI technology. Our operating expenses were essentially flat as we continue to control headcount and selectively backfill attrition in certain areas while we tactically expand our salesforce to capture the market opportunities. We reported an operating profit margin of 6.3 percent. This translated into diluted earnings per share of 8 cents.

Slide 13: Q1 FY'18 Revenue Trends: Customer Verticals & Geographic Mix

Turning to Slide 13, I'd like to briefly review the revenue trends for the quarter.

As we have discussed on prior calls, we are managing through a significant moderation in purchasing by one of our large tier-one service provider customers as they manage their network evolutions. This moderation began in fiscal year 2017 as revenue from this customer declined by

well over 100 million dollars. We expect another substantial decline in this customer's purchasing in fiscal year 2018. Our revenue skew for fiscal year 2018 reflects this purchasing pattern.

Turning to the enterprise, this vertical decreased by 9 percent. The decline reflected the timing of certain large federal deals in the first quarter of last year that did not recur at the same level this past quarter and softness within certain ancillary product lines. With that said, we are pleased with the strength of our federal sales pipeline as we head into the second quarter.

The composition of the first quarter's revenue reflected the decline in our service provider vertical and the mix was 52 percent of total revenue coming from service provider and 48 percent from enterprise.

In terms of revenue by geography, which is calculated on a GAAP basis, international represented 39 percent of total first-quarter revenue versus 37 percent in last year's quarter. The decline in the United States was driven by the decrease in revenue from that large tier-one carrier. Excluding that customer, we had mid-single digit growth across all other US customers. We did not have a 10 percent customer this quarter.

Slide 14: Balance Sheet Highlights, Free Cash Flow and Share Repurchase

Slide 14 details our balance sheet highlights and free cash flow. We ended the quarter with cash, cash equivalents, short-term marketable securities and long-term marketable securities of 409.7 million dollars. Our revolver has \$500 million dollars of available credit under our existing facility, which leaves us with total liquidity of nearly 910 million dollars. We

experienced a very high conversion rate of free cash flow to non-GAAP net income this quarter primarily due to working capital changes. Our free cash flow for the first quarter of fiscal year 2018 was 49.3 million dollars. We still anticipate that our free cash flow for fiscal year 2018 will equate to approximately 100 percent of our non-GAAP net income.

Share Repurchase Activity

During the quarter, we used our free cash flow along with our cash balance to fund our share repurchase activity. In terms of our share repurchase activity, we repurchased 2,780,433 shares of our common stock at an average price of \$35.97 per share, totaling approximately \$100.0 million in the aggregate. While this represented a negligible effect on the first quarter's earnings per share, it represents a 5-cent increase to our earnings per share outlook for the year.

At present, we have approximately 4.0 million shares available for repurchase under our existing 20 million share repurchase authorization. As we head toward the completion of our current authorization, we are working with our Board to update and finalize our financial policies going forward, and determine the vehicles, timing and funding for future share repurchases. We plan to be active in the market with our buyback program this quarter.

To briefly recap other balance sheet highlights, accounts receivable, net, decreased by 108.5 million dollars from the end of the last fiscal year. DSOs were 71 days, which is down from 80 days in the fourth fiscal quarter but up modestly from 66 days in the first quarter of last year.

Slide 15: FY 2018 Guidance

Let's move to slide 15 for guidance. I will focus on the non-GAAP guidance and remind you that the reconciliation of our GAAP guidance to our non-GAAP guidance is in the appendix.

FY'18 Guidance

Our guidance for fiscal year 2018 is fundamentally unchanged. We continue to expect that fiscal year 2018 revenue will be relatively unchanged from fiscal year 2017 levels. We anticipate that adoption of our next-generation real-time information platform will improve our gross margins in fiscal year 2018 and be the primary factor for a 200-basis point improvement in operating profitability over last year to 25 percent. Our net income outlook for fiscal year 2018 on a fundamental basis remains intact. Reducing the average weighted diluted shares outstanding to approximately 91 million shares due to our share repurchase activity through the first quarter provides us with an incremental five cents of EPS. Accordingly, we are now targeting diluted EPS growth over last year on a percentage change basis that will range from the high single digits to the low double digits.

Q2 Revenue & EPS Outlook

We continue to expect that 40 percent of fiscal year 2018 revenue will be generated in the first half of the year with the remaining 60 percent of revenue coming in the second half. Based on our first-quarter revenue performance and our view into the phasing of fiscal year 2018 revenue, the mathematical implication for second-quarter revenue is around 250 million dollars. The anticipated year-over-year decline in second-quarter revenue will be primarily driven by the purchasing pattern change at one tier-one service provider. We remain optimistic about the growth potential we see in the third and fourth quarters.

Other full-year modeling assumptions are outlined on this slide. Based on the quarterly impact of these assumptions, most notably relatively flat operating costs, and roughly 90.6 million diluted shares outstanding, this would translate into second-quarter diluted EPS in the range of 25 to 28 cents.

Slide 16: Upcoming Investor Events

That concludes my formal review of our financial results. Before we transition to Q&A, I will note that slide number 16 highlights the various investor conferences we plan to participate in over the next couple of months.

That concludes our prepared remarks this morning. Thank you again for joining us and we're now ready to answer questions. Operator, you may now begin the Q&A session.