



# Q3 Fiscal Year 2014 Earnings

Prepared Management Remarks

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NASDAQ: UBNT

## Ubiquiti Networks Third Quarter Fiscal 2014 Financial Results



- Revenues of \$148.3 million, up 78% year-over-year
- GAAP operating expenses of 10.4% compared to 14.4% in third quarter fiscal 2013
- GAAP net income of \$45.2 million, up 119% year-over-year
- GAAP operating profitability of \$50.1 million, up 113% year-over-year
- GAAP and non-GAAP diluted EPS of \$0.50, with non-GAAP up 108% year-over-year
- Average days sales outstanding in accounts receivable ("DSO") of 30 days

### CEO & CFO Commentary

We are pleased to announce another record quarter for Ubiquiti Networks. We believe that our quarterly financial results demonstrate our ability to effectively execute on our next generation business that is built for growth and profitability. We continue to have a focused approach to deliver competitively-priced, proprietary products with outstanding performance to our end customers. In addition to solid financial results, there are a few key business and product-related achievements that we would like to highlight:

- **Sustained growth in Service Provider Technology**, mainly driven by expansion of core infrastructure build-outs in our wireless markets.
- **Strong momentum in Enterprise Technology**, primarily due to product expansion and further adoption of our UniFi® technology platform.
- **Signed new distribution agreements with Ingram Micro and ScanSource Security**, leading technology distributors who will accelerate our expansion into established and emerging markets.
- **Launched Ubiquiti World Network™**, an alliance of independent Internet Service Providers and supporting U.S. advertising and marketing campaign. Visit [www.ubnt.com/uwn](http://www.ubnt.com/uwn) to watch success stories of Ubiquiti World Network™ early adopters.
- **Major extensions of airMAX® and airFiber® product lines**, solutions that offer intelligent design and excellent price performance for fixed wireless deployments.
- **More satisfied Ubiquiti users**, such as the Ubiquiti customer stories that can be viewed at [www.ubnt.com/customers](http://www.ubnt.com/customers).
- **Refinancing of outstanding credit facility**, increasing financial flexibility while substantially lowering our cost of capital.

## Key Quarterly Financial Highlights

These prepared remarks include both GAAP and non-GAAP financial information because we consider non-GAAP information in our planning and management processes. We believe that disclosing these non-GAAP financial measures can provide useful supplemental information that, while not a substitute for GAAP measures, can allow for greater transparency in the review of our financial and operational performance. Non-GAAP financials exclude certain recurring costs, expenses and gains such as stock based compensation expenses and the tax effects of these non-GAAP adjustments.

## Income Statement

Financial Results Summary (\$, in millions, except per share data)

<b>Financials</b>	<b>F3Q14</b>	<b>F2Q14</b>	<b>F3Q13</b>
Revenues	148.3	138.4	83.2
<i>Service Provider Technology</i>	121.0	111.4	75.5
<i>Enterprise Technology</i>	27.3	27.0	7.7
Cost of Revenues	82.7	77.5	47.7
Gross Profit	65.6	61.0	35.5
Total Operating Expenses	15.5	13.9	12.0
Income from Operations	50.1	47.1	23.5
Net Income	45.2	41.8	20.7
Non-GAAP EPS (diluted)	0.50	0.48	0.24

For the quarter, we exceeded our target revenue and posted record revenues of \$148.3 million, up 7.1% from the prior quarter, and up 78.4% over the same period in the prior year.

### **Revenue by Product Category**

#### *Service Provider Technology*

- The Service Provider Technology product category primarily encompasses the airMAX®, airFiber® and EdgeMAX® embedded radio and antenna product lines.
- Revenues of \$121.0 million, an increase of 9% from the prior quarter and a 60% from the prior year.
- Represented 82% of our total Q3 revenues.
- Growth was attributed to the continued infrastructure build-out of Wireless Internet Service Providers (“WISPs”) using airMAX® and complementary products.

#### *Enterprise Technology*

- The Enterprise Technology product category primarily encompasses our UniFi®, airVision® and mFi® product lines.
- Revenues of \$27.3 million, an increase of 1% from the prior quarter and 256% from the prior year.
- Represented 18% of our total Q3 revenues.
- Our UniFi® platform volumes continue to grow quickly as our target market remains focused on the outstanding price/performance characteristics of our enterprise technology solutions.

## ***Revenue by Geography***

We continue to experience a unique mixture of demand for our products from all corners of the globe. This quarter, EMEA represented our largest region with a record percentage of total revenues at 52.5%. Regional results were as follows:

- **North America** represented 19.7% of total revenues for the quarter, compared to 25.3% year-over-year. Revenue was down sequentially 10.4% at \$29.2 million, and up \$8.1 million or 38.6% year-over-year. Revenue for the United States was \$27.7 million and \$19.7 million for the quarter and the same quarter in the prior year, respectively. For the quarter we saw strong incremental demand for our antenna and EdgeMAX® product lines.
- **South America** represented 16.9% of total revenues for the quarter, compared to 22.2% year-over-year. Revenue was down 10.5% sequentially at \$25.1 million, and up \$6.6 million or 35.5% year-over-year. For the quarter we saw an incremental demand increase for our antenna and UniFi® product lines.
- **EMEA** represented 52.5% of total revenues for the quarter, compared to 38.0% year-over-year. Growth in this region outpaced all others in recent months. This quarter, EMEA revenue increased sequentially 32.4% to \$77.9 million, and was up \$46.3 million or 146.3% year-over-year. This increase was primarily driven by increased demand in antenna and airMAX® product lines.
- **Asia-Pacific** represented 10.9% of total revenues for the quarter, compared to 15.4% year-over-year. Revenue was down sequentially 14.9% at \$16.2 million, and up \$4.2 million or 35.2% year-over-year.

Over the last year we have become more sophisticated in our ability analyze channel sales and inventory around the world. We are committed to keeping channel inventory in-line with end market demand and we think you can see our discipline during this quarter. Regions will continue to fluctuate, but we believe this is a reflection of our strategies to keep the channel optimized to turn inventory efficiently. We also continue to monitor geopolitical developments as they materialize because of their potential impact on ports being available to receive goods, but we did not see an impact during our third quarter results.

## ***Gross Margins***

During this quarter, our non-GAAP gross margins slightly increased to 44.3%, and to 44.2% on a GAAP basis. This increase was due to changes in sales product mix, increased manufacturing and supply chain efficiency. We believe that our gross margin range will continue to fluctuate between 43% and 45%.

## ***Research and Development***

Research and Development (“R&D”) expenses were \$8.8 million on a non-GAAP basis, and \$9.4 million on a GAAP basis. Non-GAAP R&D was up 16.7% sequentially, primarily due to the hiring of new engineers as we continue to evolve and expand our family of products. This quarter we increased our R&D headcount by 26% with the objective of accelerating our development release cycles. We believe that we are one of the leaders in translating R&D spend into future revenue, and that our focus on engineering talent is a key competitive advantage. The quest for qualified engineers is one of our highest priorities. We expect to continue the pace of our R&D investment to broaden and evolve our product offerings.

## ***Sales, General and Administrative***

Our non-GAAP selling, general and administrative (“SG&A”) expenses for the quarter were \$6.9 million, or 4.7% of revenue, an increase of \$1.9 million compared to the prior quarter. We continue to run one of the most efficient operating business models, and are focused on delivering maximized returns for our expenditures. We had no additional net headcount for the quarter.

The sequential increase in SG&A spend was primarily due to expenses related to the launch of the Ubiquiti World Network™ (“UWN”), a nationwide advertising and marketing campaign that is focused on building awareness of the WISP market. The campaign was officially launched in late January 2014, and included a series of media placements in national and local markets. Given the early stage of the campaign, we will be in a better position to determine its effectiveness over the next few quarters.

### ***Taxes***

Our effective GAAP tax rate for the quarter decreased to 9% as compared to 11% in the third quarter of fiscal 2013. This reduction in effective tax rate reflects our geographic sales product mix, resulting in a larger percentage of our overall profitability occurring in jurisdictions with lower income tax rates.

### ***Net Income***

GAAP net income for this quarter was \$45.2 million, or \$0.50 per diluted share, compared with a net income of \$20.7 million, or \$0.23 per diluted share, in the third quarter of fiscal 2013. Ubiquiti recorded third quarter fiscal 2014 non-GAAP net income of \$45.2 million, or \$0.50 per diluted share, compared with non-GAAP net income of \$21.1 million, or \$0.24 per diluted share, in the third quarter of fiscal 2013.

### **Balance Sheet**

Total cash and cash equivalents as of March 31, 2014 were \$291.7 million, compared to \$305.6 million as of December 31, 2013, and \$181.7 million as of March 31, 2013. We believe that our cash position will allow us to make investments that will enhance our competitive position and product portfolio. A majority of our cash is held by our foreign subsidiaries.

During the last quarter, we invested heavily in inventory. Our inventory balance at the end of the quarter was \$66.0 million, up substantially from \$32.3 million in the prior quarter. The increase was a result of new products that had not been previously released, and the additional build of existing products. Based upon channel sales data, we believe the last half of the calendar year is typically the strongest period for our end markets, primarily due to favorable weather for outdoor equipment installations. We have had constraints in the past with inventory supply during these periods, and we have prepared accordingly by investing in finished goods and certain pre-paid arrangements with some of our key component suppliers. We expect our higher stock levels to reduce our delivery lead-times and increase supply consistency for our channel partners to support their demand for our products. We expect to hold 7 to 8 weeks of previously introduced product inventory in our warehouse going forward. The total inventory number will fluctuate when we introduce new products because there will be an element of “stocking the shelves” during the initial sell-in period.

We recognize a currently paying distributor is more likely to remain a productive long-term channel partner. Over a year ago, we overhauled the credit process for our distributors and have demonstrated excellent results through a dramatic reduction in our average days sales outstanding in accounts receivable (“DSO”). This quarter we saw DSO of 30 days, compared to 24 days in the prior quarter, and 42 days in the third quarter of fiscal 2013. Going forward, we expect to see our DSOs increase to the low 40s due to the addition of some larger distributors.

## **Cash Flow Statement**

Ubiquiti's net cash outflow from operations for the third quarter of fiscal 2014 was \$14.0 million, compared to an inflow of \$27.6 million in the second quarter of fiscal 2014, and net cash inflow of \$35.2 million in the third quarter of fiscal 2013. The primary driver of the change in net cash from operations in the quarter was increased inventories as described above. Capital expenditures for the period were \$1.2 million and depreciation and amortization was \$0.7 million.

## **Fourth Quarter Fiscal 2014 Outlook**

Based on our analysis of orders received and current channel inventory levels, we expect to generate revenues of \$147 - 153 million in the fourth quarter of fiscal year 2014, representing a 46 - 51% increase over the fourth quarter of fiscal year 2013. We expect sustained growth in Service Provider Technology and Enterprise Technology business segments. While both product categories are expected to grow, over time we believe the Enterprise Technology will grow at a faster pace and become an increasingly larger percentage of our total revenues.

Based on these estimates, we expect GAAP earnings to be in the range of \$0.47 - 0.51 per share, and non-GAAP diluted earnings to be in the range of \$0.48 - 0.52 per share, based on a share count of approximately 90 million.

## **Conclusion**

We continue to rapidly grow our business, and we are committed to executing on our long-term business strategy. We remind investors that, in any given quarter, we may observe fluctuations in specific product categories or geographies for a variety of reasons, and seasonal fluctuations as well. Over the last quarter, we believe that we have continued to lay a strong foundation for long-term value creation, including having taken the following actions:

- **Invested in R&D** designed to broaden and evolve our product offering with the best-and-brightest engineers.
- **Built-out inventory** to reduce the inventory constraints we have experienced in recent quarters.
- **Signed new distribution agreements with Ingram Micro and ScanSource Security**, leading technology distributors who will accelerate our expansion into established and emerging markets.
- **Invested in marketing**, such as Ubiquiti World Network™, designed to create powerful network effects to help drive our customers' businesses, and in turn, our business.
- **Major extensions of our core product lines**, with solutions that offer intelligent design, and outstanding price performance for worldwide deployments.

We look forward to speaking to you on our earnings call. The conference call information is listed below.

**Robert J. Pera**  
CEO, Founder & Chairman

**Craig L. Foster**  
CFO

## Conference Call Information

Ubiquiti Networks will host a Q&A-only conference call to discuss the Company's financial results at 2:00 p.m. Pacific Time today. A transcript of Management's prepared remarks can be found on the Investor Relations section of the Ubiquiti Networks website, <http://ir.ubnt.com>.

To listen to the Q&A-only conference call via telephone, dial (877) 291-1296 (U.S. toll-free) or (720) 259-9209 (International) to be connected to the call by an operator. Participants should dial in at least 10 minutes prior to the start of the call. Investors may also listen to a live webcast of the Q&A-only conference call by visiting the Investor Relations section of the Ubiquiti Networks website, <http://ir.ubnt.com>.

The recording of the Q&A call will be available approximately two hours after the call concludes and will be accessible on the Investor Relations section of the Ubiquiti Networks website, <http://ir.ubnt.com>.

## About Ubiquiti Networks

Ubiquiti Networks (NASDAQ: UBNT) is closing the digital divide by building network communication platforms for everyone and everywhere. With over 20 million devices deployed in over 180 countries, Ubiquiti is transforming under-networked businesses and communities. Our leading edge platforms, airMAX®, UniFi®, airFiber®, airVision®, mFi® and EdgeMAX®, combine innovative technology, disruptive price-performance and the support of a global user community to eliminate barriers to connectivity. For more information, join our community at <http://www.ubnt.com>. *Ubiquiti, the Ubiquiti logo, Ubiquiti Networks, airMAX, airFiber, airVision, UniFi, mFi, EdgeMAX, and World Network are registered trademarks or trademarks of Ubiquiti Networks, Inc. and/or its affiliates in the United States and other countries.*

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## Use of Non-GAAP Financial Information

To supplement the financial information prepared under generally accepted accounting principles, or GAAP, we use non-GAAP measures of net income and earnings per diluted share that are GAAP net income and GAAP earnings per diluted share adjusted to exclude certain recurring costs and non-recurring, expenses and gains. Non-GAAP net income and non-GAAP earnings per diluted share are among the primary indicators used by management as a basis for planning and forecasting future periods, and by management and our board of directors to determine whether our operating performance has met specified targets and thresholds. Management uses non-GAAP net income and non-GAAP earnings per diluted share when evaluating operating performance because it believes that the exclusion of the items described below, for which the amounts and/or timing may vary significantly depending upon the Company's activities and other factors, facilitates comparability of the Company's operating performance from period to period. We have chosen to provide this information to investors so they can analyze our operating results in the same way that management does and use this information in their assessment of our business and the valuation of our Company.

We compute non-GAAP net income and non-GAAP diluted earnings per share by adjusting GAAP net income and GAAP earnings per diluted share to remove the impact of recurring stock-based compensation expense, the gain on the reversal of a charge for an export compliance matter, and the tax effect of these adjustments. Items excluded from net income are:

- Recurring charges and gains, including:
  - Stock-based compensation expense is recognized in accordance with FASB Accounting Standards Codification, Topic 718, Stock Compensation.
- Gain on reversal of charge for an export compliance matter
- Tax effect of non-GAAP adjustments. After adjusting to exclude the items described above, we apply the principles of ASC 740, Income Taxes, to estimate the non-GAAP income tax provision.

### Ubiquiti Networks Inc.

#### Reconciliation of GAAP Net Income to Non-GAAP Net Income

(In thousands, except per share data)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Net income	\$ 45,199	\$ 20,667	\$ 127,519	\$ 51,649
Stock-based compensation:				
Cost of revenues	153	124	445	309
Research and development	630	324	1,679	991
Sales, general and administrative	258	252	1,506	949
Gain on reversal of charge for an export compliance matter	(1,121)	—	(1,121)	—
Tax effect of non-GAAP adjustments	32	(280)	(1,004)	(900)
Non-GAAP net income	\$ 45,151	\$ 21,087	\$ 129,024	\$ 52,998
Non-GAAP diluted EPS	\$ 0.50	\$ 0.24	\$ 1.44	\$ 0.58
Weighted-average shares used in non-GAAP diluted EPS	89,775	88,953	89,667	90,656

## **Usefulness of Non-GAAP Financial Information to Investors**

These non-GAAP measures are not in accordance with, or an alternative to, GAAP and may be materially different from other non-GAAP measures, including similarly titled non-GAAP measures used by other companies. The presentation of this additional information should not be considered in isolation from, as a substitute for, or superior to, net income or earnings per diluted share prepared in accordance with GAAP. Non-GAAP financial measures have limitations in that they do not reflect certain items that may have a material impact upon our reported financial results. We expect to continue to incur expenses of a nature similar to the non-GAAP adjustments described above, and exclusion of these items from our non-GAAP net income and non-GAAP earnings per diluted share should not be construed as an inference that these costs are unusual, infrequent or non-recurring.

For more information on the non-GAAP adjustments, please see the table captioned "Reconciliation of GAAP Net Income to non-GAAP Net Income" included herein.

## Safe Harbor for Forward Looking Statements

Certain statements contained herein are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Statements other than statements of historical fact including words such as “look”, “will”, “anticipate”, “believe”, “estimate”, “expect”, “forecast”, “consider” and “plan” and statements in the future tense are forward looking statements. The statements contain herein that could be deemed forward-looking statements include statements regarding anticipated healthy and strong demand, effectiveness of the Company's business model, growth prospects and goals, expected product offerings, market positioning and anticipated market share and profitability, strategic plans, short and long term opportunities, revenues, GAAP diluted EPS and non-GAAP diluted EPS forecasts for the Company's fiscal quarter ending June 30, 2014, and any statements or assumptions underlying any of the foregoing.

Forward-looking statements are subject to certain risks and uncertainties that could cause our actual future results to differ materially, or cause a material adverse impact on our results. Potential risks and uncertainties include, but are not limited to, fluctuations in our operating results; varying demand for our products due to the financial and operating condition of our distributors and their customers, distributors' inventory management practices and general economic conditions; impact of counterfeiting and our ability to contain such impact; our reliance on a limited number of distributors; inability of our contract manufacturers and suppliers to meet our demand; our dependence on Qualcomm Atheros for chipsets without a short-term alternative; as we move into new markets competition from certain of our current or potential competitors who may be more established in such markets; our ability to keep pace with technological and market developments; success and timing of new product introductions by us and the performance of our products generally; our ability to effectively manage the significant increase in our transactional sales volumes; we may become subject to warranty claims, product liability and product recalls; that a substantial majority of our sales are into countries outside the United States and we are subject to numerous U.S. export control and economic sanctions laws; costs related to responding to government inquiries related to regulatory compliance; our reliance on the Ubiquiti Community; our reliance on certain key members of our management team, including our founder and chief executive officer, Robert J. Pera; adverse tax-related matters such as tax audits, changes in our effective tax rate or new tax legislative proposals; whether the final determination of our income tax liability may be materially different from our income tax provisions; the impact of any intellectual property litigation and claims for indemnification and litigation related to U.S. Securities laws and economic and political conditions in the United States and abroad. We discuss these risks in greater detail under the heading “Risk Factors” and elsewhere in our Annual Report on Form 10-K for the year ended June 30, 2013, subsequent Quarterly Reports on Form 10-Q and other filings filed with the U.S. Securities and Exchange Commission (the SEC), which are available at the SEC's website at [www.sec.gov](http://www.sec.gov). Copies may also be obtained by contacting Ubiquiti Networks' Investor Relations Department, or by email at [IR@ubnt.com](mailto:IR@ubnt.com) or by visiting the Investor Relations section of the Ubiquiti Networks website, <http://ir.ubnt.com>.

Given these uncertainties, you should not place undue reliance on these forward-looking statements. Also, forward-looking statements represent our management's beliefs and assumptions only as of the date made. Ubiquiti Networks undertakes no obligation to update information contained herein. You should review our SEC filings carefully and with the understanding that our actual future results may be materially different from what we expect.