NASDAQ:NTCT Q4 2025 Earnings Call Transcript

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Gene Bua | Executive Vice President and Chief Financial Officer:

Please stand by.

Operator | Conference Operator:

Your program is about to begin. Ladies and gentlemen, thank you for standing by. And welcome to NETSCOUT's fourth quarter and fiscal year 2025 financial results conference call. At this time, all parties are in a listen-only mode and tell the question and answer portion of the call. As a reminder, this call is being recorded. Tony Piazza, Deputy CFO, and his colleagues at NETSCOUT are on the line with us today. If you require operator assistance at any time, please press star zero. I would now like to turn the call over to Tony Piazza to begin the company's prepared remarks.

Tony Piazza | Deputy Chief Financial Officer:

Thank you, operator, and good morning, everyone. Welcome to NETSCOUT's fourth quarter and full fiscal year 2025 conference call for the period ended March 31st, 2025. Joining me today are Anil Singhal, NETSCOUT's President and Chief Executive Officer, Michael Zavados, Netscouts Chief Operating Officer, and Gene Bua, Netscouts Executive Vice President and Chief Financial Officer. There's a slide presentation that accompanies our prepared remarks. You can advance the slides in the webcast viewer to follow our commentary. Both the slides and the prepared remarks can be accessed in multiple areas within the investor relations section of our website at www.netscouts.com. including the IR landing page under financial results, the webcast itself, and under financial information on the quarterly results page. Moving on to slide number three, today's conference call will include forward-looking statements. Examples of forward-looking statements include statements regarding our future financial performance or position, results of operations, business strategy, plans and objectives of management for future operations, and other statements that are not historical facts. Actual results could differ materially from any forward-looking statements. These statements speak only as of today's date and involve risks and uncertainties, including but not limited to those described on this slide and in today's financial results press release, which are available on the investor relations section of our website, as well as in the company's most recent annual report on Form 10-K and subsequent filings with the Securities and Exchange Commission. NESCow assumes no obligation to update any forward-looking information except as required by law. Let's now turn to slide number four, 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. The rationale for providing non-GAAP measures along with the limitations of relying solely on those measures is detailed on this slide and in today's financial results press release. These measures should not be considered in isolation from or as a substitute for financial information prepared in accordance with GAAP. Reconciliations of all non-GAAP metrics with the applicable GAAP measures are provided in the appendix of the slide presentation in today's financial results press release and on our website. I will now turn the call over to Anil for his prepared remarks.

Anil Singhal | President and Chief Executive Officer:

Anil? Thank you, Tony, and good morning, everyone. Welcome and thank you all for joining us today. We close fiscal year 2025 revenue on a strong note with fourth quarter revenue exceeding our expectations, driven by solid performance in our cybersecurity product lines. We are pleased with our full-year revenue performance, which was in line with our original guidance range provided at the beginning of the fiscal year and consistent with the prior year's revenue after adjusting for the deferred share of the test optimization business. More importantly, we are able to generate approximately $50 million in additional revenue this year and ultimately overcome the challenge of backlog usage from the prior fiscal year. We delivered non-GAAP EPS growth for fiscal year 2025, driven by our continued focus on prudent cost management initiatives. With a strong financial foundation and a clear strategic direction entering fiscal year 2026, we believe NETSCOUT is well positioned to navigate the current macroeconomic uncertainty and deliver sustainable long-term growth. With that as the backdrop, let's now turn to slide number six, for a brief high-level recap of our non-GAAP financial results for the fourth quarter and full fiscal year 2025. Gene will provide more detail on the results later in the call. For the fourth quarter, revenue increased 1% to approximately $205 million, and non-GAAP diluted earnings per share was 52 cents, down approximately 5% on a year-over-year basis. For the full fiscal year 2025, we delivered revenue of approximately $823 million, essentially flat year over year, down less than 1%. As I mentioned earlier, we are happy with this performance given the diversions of the test optimization business and the previously mentioned prior year backlog-driven revenue gains. When adjusting for the sale of the test optimization business, revenue was consistent year over year, and adjusting for the prior year's backlog benefits would have resulted in mid-single-digit revenue growth year-over-year. From a non-GAAP EPS perspective, for the full fiscal year 2025, we delivered $2.22 per diluted share, a $0.02 or approximately 1% improvement over fiscal year 2024. We achieved this performance due to our ongoing focus on efficiency, which has contributed to an improved cost structure. We plan to carry those cost management priorities into fiscal year 2026. Now let's turn to slide number seven, where we'll dive deeper into our key business drivers and share some additional market insights. Starting with our service assurance offerings, in fiscal year 2025, service assurance revenue declined approximately 4% year over year. This was partially attributable to the debauchery of the test optimization business in fiscal year 2024 and the lower level of radio frequency propagation and modeling project revenue compared to last fiscal year. As we consider the demand and mix for the service assurance offering moving forward, we continue to see service provider customer invest in 5G initiatives at a measured space. Customers are also making investment in network performance and new services such as fixed wireless access. We believe we remain well positioned to support both domestic and international carriers as customer demand evolves and innovative network technology trends materialize. We are in active discussion with our service provider customers to demonstrate the critical value of our enhanced smart data generated from deep packet inspection or DPI to accelerate service provider efforts in 5G net ops, AI ops, and mobile network security. In the enterprise vertical, we are cautiously optimistic that the growth we experienced in the second half of fiscal year 2025 will continue into fiscal year 2026 as customers evolve their digital transformation and enhance monitoring at the edges of their networks. However, we recognize that ongoing economic uncertainty may influence customer behavior, and we are actively monitoring these trends. Shifting to our cybersecurity offerings. In fiscal year 2025, our cybersecurity offerings delivered nearly 7% year-over-year revenue growth, driven by strong momentum within our enterprise customer vertical. As I highlighted in our recently released DDoS threat intelligence report, I think geopolitical tensions continue to drive up the number of DDoS attacks. At this time, AIML automation and the abuse of enterprise-grade infrastructure is enabling more sophisticated and agile attacks. This increases the need for proactive and adaptive defense measures to effectively mitigate evolving threats. Attacks have been powered by the Mirai malware-created botnets which cause service provider attacks to surge. With this high activity landscape, companies are increasingly depending on NETSCAR's scalable and real-time adaptable solutions for their cybersecurity protection methods. As we look to fiscal year 2026, we believe the value proposition of our solutions should continue to resonate with customers and expect our core portfolio as well as our newer offerings such as adaptive DDoS, mobile security, and distributed threat mitigation system solutions to fuel continued momentum in this space. Michael will provide more insight regarding customer wins during his remarks. Now let's move to slide number eight regarding our

outlook and summary. As we look ahead to fiscal year 2026, we remain encouraged by the momentum in our cybersecurity offerings. While we remain cautious given the broader economic uncertainty, We are committed to continuing our investments in product-related AI and cybersecurity solutions. We also plan to maintain our disciplined approach to cost management and preserve our strong financial position. Based on our current view, in fiscal year 2026, we expect to achieve year-over-revenue growth, improve our operating margin, and dilute EPS performance, and continue to generate solid free cash flows. Jean will provide more specifics on the outlook in her remarks. Our long-term strategy remains unchanged. We will continue to invest in innovation, deepen relationship with our customers, and leverage our mission-critical solution to support the evolving performance, availability, and security need of today's complex digital environments. With a strong foundation and clear strategic direction, We believe NETSCOUT is well positioned for sustainable long-term success. We look forward to keeping you updated on our progress as we move through the new fiscal year. Now let's move to slide number nine regarding our leadership transition. Before I turn the call over to CEO Michael Sabatos, I want to take a moment to address the announcement we made earlier today. As shared, both Michael and our CFO, Jean Bua, will be retiring and stepping down from their roles effective May 31st, 2025. We appreciate their continued commitment to the company as they transition into advisory roles through June 2026, ensuring a smooth leadership transition. As part of our succession plan, Sanjay Munshi, the company's deputy CEO, and Tony Piazza, next door deputy CFO, will become CEO and CFO respectively and will join the executive team effective June 1st, 2025. On behalf of our board and executive team, I want to thank Jean and Michael for their many contributions in support of NETSCOUT over the years and wish them well in their retirement. We are fortunate to have capable and experienced leaders like Sanjay and Tony ready to take on the roles of CEO and CFO and I look forward to working closely with each of them. With that, I turn the call over to Michael.

Michael Zavados | Chief Operating Officer:

Good morning, everyone, and thank you, Anil, for the kind words. It has been a true pleasure working with you and the outstanding team over these many years. I'm confident that the organization is in great hands with Sanjay Seppin as our new COO. Moving on to our quarterly update, slide 11 outlines the areas that I will be covering customer win highlights. Starting with our service assurance offering, one notable win this quarter was a competitive low seven-figure deal with a new customer, which is a leading financial services company. They were utilizing a competitor's solution that was not satisfying their requirements. During our proof of concept, we demonstrated how our solution delivers end-to-end network from the customer's core network to their external trading partners. This significantly reduced issue resolution times from days to mere minutes, highlighting our clear operational advantage over their existing solution. The power of our service assurance offerings to address issues quickly and accurately at scale was the clear catalyst to this win. In our cybersecurity offering, We extended our relationship with a leading cloud service provider with a mid-seven figure deal that included our sightline detection and TMS mitigation solutions to enhance their security posture at their network edge as well as inside their data centers. The customer recognizes the value of our industry-leading scalability, advanced detection, and surgical mitigation, and it is critical to supporting the growth of their cloud and AI services businesses, and with increasingly larger and sophisticated TDoS attacks. Turning briefly to our go-to-market activities, we continue to actively promote our offerings to both existing and prospective customers. For example, in March, we participated in the Mobile World Congress in Barcelona, where we held a series of productive meetings with both existing and prospective customers. discussion centered around our latest innovations for enhancing our smart data to accelerate service provider efforts in 5G, NetOps, AIOps, and mobile network security. More recently, in May, we participated in the RSA Security Conference in San Francisco, where we demonstrated our visibility without border solutions to deliver next-generation performance management, network security, and DDoS protection to ensure security performance and availability for the most complex and mission-critical network. In June, we will head to San Diego for Cisco Live, where we will showcase our visibility and security solutions, which are designed to ensure organizations are operationally resilient by ensuring every interaction is safer, faster, and flawless from the edge to the cloud. In early August, we will be in Las Vegas participating in the Black Hat USA

Conference, where we will demonstrate our DDoS protection and on-disk network security solutions to ensure performance, security, and availability for the world's most powerful digital ecosystems. That concludes my final update. Thank you for your support over the years. I will now turn the call over to Gene.

Gene Bua | Executive Vice President and Chief Financial Officer:

Thank you, Michael, and good morning, everyone. I will review key metrics for our fourth quarter and the fall fiscal year 2025 and provide some additional commentary on our fiscal year 2026 outlook. As a reminder, this review focuses on our non-GAAP results, unless otherwise stated, and all reconciliations with our GAAP results appear in the presentation appendix. Regardless, I will note the nature of any such comparisons. Additionally, all comparisons are on a year-over-year basis unless otherwise noted. Slide number 13 details the results for the fourth quarter and full fiscal year 2025. Focusing on our quarterly performance first, total revenue for the fourth quarter of fiscal year 2025 was $205 million, up 0.8%. Product revenue was $89.5 million, an increase of 0.1%, and service revenue was $115.5 million, an increase of 1.3%. At the end of the fourth quarter, our total combined product backlog was $33.1 million, consisting of a fillable backlog of $25.1 million, $0.9 million of radio frequency propagation modeling projects, and $7.1 million related to one multi-year customer enterprise license commitment. Additionally, at the end of the fourth quarter, there was $8.3 million of radio frequency modeling projects and deferred revenue. Growth profit margin was 79.2% in the fourth quarter, up two percentage points. Quarterly operating expenses decreased 2.5%, primarily due to the previously announced cost reduction actions and lower variable compensation expense. Accordingly, we reported an operating profit margin of 23.1% compared with 19.2% in the same quarter last year. Diluted earnings per share was 52 cents, which included an unrealized loss on a foreign investment of approximately 3 cents. This was down 5.5% from 55 cents in the same quarter last year. For the full fiscal year 2025, revenue was $822.7 million, which was a decrease of 0.8 percentage points year over year. Normalizing for the test optimization business that we disposed of in fiscal year 24, total revenue would have been consistent year over year. Product revenue was $359.9 million, a decline of 0.2%, and service revenue was $462.8 million, a decline of 1.3%. A gross profit margin was 80%, an increase of 0.6 percentage points. Annual operating expenses decreased 1.9% from the prior year, primarily due to previously announced cost reduction actions. We reported an operating profit margin of 23.7% up 1.1 percentage points compared to the prior year. Diluted earnings per share was $2.22, a 0.9% increase. Our annual tax rate was 19% compared to 17.2% in the prior year. As a reminder, the prior year tax rate was impacted by a valuation gain in a foreign investment with favorable tax treatment. Turning to slide 14, I will review key revenue trends by product lines and customer verticals. Please note that all comparisons here are on a year-over-year basis consistent with our other remarks. For the fiscal year 2025, our service assurance revenue decreased by 4.4%. while our cybersecurity revenues grew by 6.6%. During the same period, our service assurance product line accounted for approximately 65% of our total revenue, while our cybersecurity product line accounted for the remaining 35%. Turning to our customer verticals, for the first fiscal year 2025, our enterprise customer vertical grew 7.5%, while our service provider customer vertical revenue decreased 10.1%. During the same period, our enterprise customer vertical accounted for approximately 57% of our total revenue, while our service provider customer vertical accounted for the remaining 43%. Turning to slide 15, this shows our geographic revenue mix for the fiscal year 2025 57% of our revenue was derived from the United States, with the remaining 43% provided by international markets, which is consistent with the prior year. Also, no customer represented 10% or more of our total revenue in either the fourth quarter or full fiscal year 2025. Slide 16 details certain balance sheet and free cash flow items. We ended fiscal year 2025 with $492.5 million in cash, cash equivalents, short and long-term marketable securities and investments, representing an increase of $68.4 million since the end of fiscal year 2024. Free cash flow for the fourth quarter was $140 million and $211 million for the full fiscal year 2025. From a debt perspective, during the fourth quarter, we repaid the $75 million that was outstanding on our $600 million revolving credit facility. We did not repurchase any of our common stock during the fourth quarter. We currently have capacity in our share repurchase authorization and subject to market conditions intend to be active in the market during fiscal year 2026. To briefly recap other balance sheet items, accounts receivable net was $163.7 million, representing a decrease of $28.4

million since March 31, 2024. The DSO metric at the end of the fourth quarter of fiscal year 2025 was 68 days versus 81 days at the end of fiscal year 2024. the lower DSO metric in the fourth quarter of this fiscal year was due to the timing and composition of bookings. Let's move to slide 17 for commentary on our outlook. I will refocus my review on our non-GAAP targets for fiscal year 2026. I would like to first address the current macro environment and the impact of the proposed tariff policies. As it stands, current global tariff regulations and negotiations are not expected to have a material impact on our business from a direct force perspective. More than 80% of our revenue comes from services and software, which are largely unaffected by these tariffs. On the hardware side, most components for our appliances are sourced either domestically from Canada or from Mexico, and are currently exempt under the USMCA arrangements. As such, our direct cost exposure is currently minimal and could be addressed through pricing adjustments or efficiency initiatives if required. That said, broader tariff-related activity is contributing to some uncertainty in the global macroeconomic landscape. While we haven't seen a meaningful impact on customer demand or revenue so far, we are closely monitoring the situation for any potential shifts in customer behavior or market dynamics that could influence our outlook. Moving on to our fiscal year 2026 outlook, we anticipate our fiscal year 2026 revenue to be in the range of approximately $825 million to $865 million. Additionally, we anticipate non-GAAP diluted earnings per share within the range of $2.25 to $2.40. The full year effective tax rate is expected to be approximately 20%. Our weighted average diluted shares outstanding is assumed to be approximately 74 to 75 million shares. Finally, I would like to provide some color for the first quarter of fiscal year 2026. In comparison to the first quarter of last year, we anticipate our first quarter fiscal year 2026 revenue to grow by approximately 3% to 5%, with approximately the same growth rate for earnings per share. That concludes my formal review of our financial results. I'd like to quickly note that our upcoming IR conference participation is listed on slide 18. As this is my final earnings call, I would like to note that the company is in a strong position thanks to the dedication of our team and the strategic vision that has been built over the years. I would also like to take a moment to express my gratitude to all of my financial team members and company colleagues. It has been an honor to serve alongside you. Thank you again for your trust and support. With that, I'll now turn the call over to the operator for questions.

Operator | Conference Operator:

And at this time, if you would like to ask a question, please press star one on your telephone keypad. If you wish to remove yourself from the queue, press star two. We do ask in the interest of time that you limit yourself to one question and one follow-up. We'll take our first question from Matthew Hedberg with RBC Capital Markets. Please go ahead.

Matthew Hedberg | Analyst, RBC Capital Markets:

Hey, guys. This is Mike Richards. I'm from Matt. Thanks for taking the questions. And, uh, Congrats on the retirement and promotions. It's great to see the continuity in the team. Thank you. And on tariffs, it was great to hear that you guys haven't seen anything yet and you're relatively insulated from a cost perspective. Maybe you could just double click on what you're hearing from customers. And does guidance assume any deterioration in the macro or provide any room for some uncertainty or deal pushes or things like that? Just any color there would be great. Thanks.

Anil Singhal | President and Chief Executive Officer:

Well, at this point, Matt, so right now we see some delayed sales cycles. And so it's maybe quarter to quarter, there might be some issues. We are having broader conferences in Europe, one in Barcelona in June, and then in Asia later in the year. And we'll hear directly sentiments from hundreds of customers. But that's where we see, and I think our, as Gene said, our guidance range covers some of those uncertainties, but it's a little bit wait and see with some customers about timing of the orders.

Matthew Hedberg | Analyst, RBC Capital Markets:

Great. That's super helpful. I guess just maybe my second one would be the cyber momentum has been pretty strong throughout this year. So looking into next year, as we see that momentum continue, are you expecting a step up in any of those newer products that you highlighted? And what are customers most excited about beyond Core DDoS there?

Anil Singhal | President and Chief Executive Officer:

Thanks. I think I'd like to say maybe a little bit broader than that. I think our service assurance business has been tough, but over time, because of AI and other things, that business is becoming part of a broader observability market, which is really... allows us to shine our smart data to a larger set of customers, broader budgets, and all those. So we announced a couple of products in that area also. The DDoS area, we have more automation through our adaptive DDoS announcement, but also we are becoming part of a broader cybersecurity market. So I look at for the next two or three years, our market size in both the service assurance area becoming part of the observability and AI market, as well as DDoS expanding to broader cybersecurity market is a real opportunity. And I think we have a very solid and loyal customer base, and this will be relevant to the same set of people or other departments in the same accounts.

Matthew Hedberg | Analyst, RBC Capital Markets:

Thanks for that, and congrats again, guys.

Anil Singhal | President and Chief Executive Officer:

Thank you.

Operator | Conference Operator:

Thank you. And your next question comes from the line of Kevin Liu with K. Liu and Company. Please go ahead.

Kevin Liu | Analyst, K. Liu & Company:

Hi. Good morning, everyone. Gene and Michael, certainly wanted to wish you well in your retirement and also congrats in order for Tony and Sanjay, of course. On the topic of tariffs, I know you guys haven't seen much impact yet, but I was wondering if you felt there was any sort of pull forward in terms of folks perhaps wanting to get ahead of any potential increases. And if that was reflected in kind of the product backlog exiting the quarter.

Gene Bua | Executive Vice President and Chief Financial Officer:

Hi, Kevin. Thank you for the congratulations. I would say that we did not see any pull forward from the tariffs. If you think about what happened to us during post-COVID when the hardware components were hard to get, and so people focused towards software. you have the potential through FY26 and the future years of the tariffs to have a similar effect where the software companies could be able to see some growth due to the componentry not being affected by the tariffs.

Kevin Liu | Analyst, K. Liu & Company:

That certainly makes sense. And actually, just along those lines, within your own pipelines or maybe customer conversations, are you seeing even more interest from customers today to go to more kind of software-only solutions, or is it still fairly consistent in terms of demand for kind of the traditional systems and appliances?

Anil Singhal | President and Chief Executive Officer:

Yeah, so we have, I mean, our solution does require hardware, but we have unbundled that, and we have been pushing the software solution, and that's one of the reasons we have been able to maintain high margins during the, when we face growth challenges. So, yeah, overall, I think there is, I don't see any change, especially there's no change because of tariffs. And most people buy our software version solution. We do offer a bundle solution, but very few customers are interested because they get us better and user pricing. And we can offer higher discounts on software.

Kevin Liu | Analyst, K. Liu & Company:

Yeah, makes sense. And then if I could squeeze one more in, just as it relates to your government and defense business, I'm wondering if there was any impact from all the DOGE-related headlines on sales cycles within the quarter and just kind of how you're thinking about contribution from federal in your fiscal 26 guidance.

Anil Singhal | President and Chief Executive Officer:

So that was a big, there was some refresh cycle in our product line, and it was contributed to some of the numbers last year. And we are expecting some more, but so far we have not seen any effect. But we'll see as six months left in the federal quarter to close. whether our pipeline really delivers. So, yeah, that's a big question mark going forward. But so far, we have not seen anything.

Kevin Liu | Analyst, K. Liu & Company:

Understood. Well, I appreciate you taking the questions, and congrats on the strong outlook here for 26.

Anil Singhal | President and Chief Executive Officer:

Okay, thank you.

Operator | Conference Operator:

Thank you. And there are no further questions at this time. I will now turn the call back to Tony for any additional or closing remarks.

Tony Piazza | Deputy Chief Financial Officer:

Great. Thank you, operator. That concludes our call for today. Thank you all for joining us, and enjoy the rest of the day.

Operator | Conference Operator:

Thank you. This does conclude today's presentation. Thank you for your participation. You may disconnect at any time.