NASDAQ:NTCT Q1 2026 Earnings Call Transcript

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Margo | Conference Operator:

Please stand by, your program is about to begin. If you need audio assistance during today's program, please press star zero. Ladies and gentlemen, thank you for standing by. And welcome to NETSCOUT's first quarter fiscal 2026 financial results conference call. At this time, all parties are in a listen only mode until the question answer portion of the call. As a reminder, this call is being recorded. Paul Canavan, AVP, Corporate Finance, 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 Paul Canavan to begin the company's prepared remarks.

Paul Canavan | AVP, Corporate Finance:

Thank you, Margo, and good morning, everyone. Welcome to NETSCOUT's first quarter fiscal year 2026 conference call for the period ended June 30th, 2025. Joining me today are Neil Singhal, NETSCOUT's President and Chief Executive Officer, and Tony Piazza, NETSCOUT's Executive Finance President and Chief Financial Officer. There is 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.netscout.com. including the IR landing page under financial results, the webcast itself, and under financial information on the quarterly results page. As discussed in detail on slide number three, today's conference call will include certain forward-looking statements about NETSCOUT's views on expected results of future performance and go-forward business strategy. These statements speak only as of today's date and involve risks, uncertainties, and assumptions that may cause actual results to differ materially, including but not limited to those described in the company's most recent annual report on Form 10-K and subsequent filings with the Securities and Exchange Commission. As discussed in detail on slide number four, today's conference call will also include discussion of certain non-GAAP financial measures that the company believes to be useful for investors. 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 to the nearest GAAP measures are provided in the appendix of the slide presentation in today's financial press release and on our website. I will now turn the call over to Anil for his prepared remarks.

Neil Singhal | President and Chief Executive Officer:

Anil. Thank you, Paul, and good morning, everyone. Thank you all for joining us today. We delivered a solid start to fiscal year 2026 with Q1 performance reflecting strong execution and positive momentum across both our top and bottom lines. Growth in our cybersecurity and service assurance product lines supported these results as we continue to position NETSCOT for long-term success in the market. Let's turn to slide number six to review some non-GAAP financial highlights for the first quarter of fiscal year 2026. Revenue was approximately $187 million, representing a 7% year-over-year increase driven by strong growth in our cybersecurity area and the timing of orders received. We expanded both our gross and operating profit margins during the quarter and delivered non-GAAP diluted earnings per share of 34 cents and increase of approximately 21% year over year. This result reflects the benefit of restructuring and cost management initiatives that we executed in the past fiscal year. As such, These effects will begin to normalize in our year-over-year comparisons starting in the second quarter. Now let's move to slide number seven for some perspective on our business and some market insights. Starting with our service assurance offering, revenue in the first quarter increased approximately 1% year-over-year. The growth was driven by our enterprise customer vertical, which offset a decline in our service provider customer vertical. In the service assurance space, Our enterprise customers are investing in digital transformation initiatives, AI ops, and enhanced visibility at the network edge. We experience solid growth across most of our major sectors in this customer vertical. On the service provider side, we continue to see both domestic and international carriers invest in 5G-related initiatives. They are proceeding at a measured pace, Aligning investment will clearly define monetization opportunities, such as fixed wireless access and private 5G. While we remain mindful of ongoing macroeconomic uncertainty, we believe NETSCOUT is well-positioned to capture further opportunities by delivering differentiated value in this evolving environment. This was recently demonstrated at the TM Forum's Neuronock Catalyst, where our Omni's AI Insight solution showcased how high-value network data can drive closed-loop automation and self-healing of networks. This provided strong validation of our ability to support AI-driven operations in complex 5G environments, reinforcing our role as a technology partner for next-generation telecom transformation. Moving to our cybersecurity operating, revenue in the first quarter increased approximately 18% year-over-year, driven by strong growth in both our enterprise and service provider customer verticals. Customers continue to prioritize spending in this area as they seek to protect themselves against an increasingly complex and expanding cyber threat landscape. We believe cybersecurity continues to represent a strong growth opportunity for NETSCOUT, and we continue to advance our portfolio with new innovations in this area. For example, we recently announced new AI-backed enhancements to our NETSCOT Arbor Edge Defense and NETSCOT Arbor Enterprise Manager adaptive distributed denial-of-service attack solutions to help customers further automate operations, enhance defense, and improve reporting. These powerful enhancements are designed to leverage AI and our Atlas intelligence. Feed to automate defenses against an expanding array of attack vectors, enabling customers to mitigate up to 80% of all DDoS attacks without the need for further analysis. We also announced that our Omni Cyber Intelligence Platform aligns with the NIST Zero Trust Security Framework. We believe this further reinforces our product offerings and strengthens our relevance as a strategic partner for the U.S. federal agencies in both service assurance and cybersecurity. Finally, we introduced adaptive threat analytics, a key enhancement to our Omni Network Detection Response, or NDR, solution. It empowers SOC analysts with faster, smarter incident response through continuous packet capture and enriched metadata. This innovation improves our competitiveness in a market where speed and precision in threat response are critical. Our solution continues to gain strong traction with customers seeking to enhance both visibility and cybersecurity capabilities, leading to robust multi-solution across three verticals. Notably, we secured a high seven-figure order earlier than anticipated with a U.S. government agency that has been a long-standing and loyal customer. This order consisted of both service-assured and cybersecurity solutions including our new Omnis AI and Cyber Intelligence product. This customer values our solution for the smart data we provide, which they are leveraging to enhance user experience and support AI-driven operations and initiatives. We also won a low seven-figure deal with major Latin American financial institutions, where we replaced two incumbent vendors in a competitive situation focused on online banking applications. This customer purchased both service-assured and cybersecurity solutions and is exploring our Omnis AI products. Our clear differentiator was our integrated platform, which combines cybersecurity performance and user experience visibility with valuable smart data to support AI of initiatives. These wins demonstrate the value of our innovative and integrated solutions, solid reputation, and strong customer relationship which help organization address the performance, availability, and security needs of the connected digital world. Additionally, they reflect the momentum we are building as we continue to execute our strategy. With that, let's now move to slide number eight to review our outlook. Looking ahead, we remain cautiously optimizing amid ongoing macroeconomic uncertainty. Our focus remains firmly on driving product innovations Returning to annual revenue growth and enhancing margin through discipline cost management. Based on the first quarter performance and solid pipeline, we are reaffirming our fiscal year 2026 revenue and non-GAAP EPS outlook. Tony will provide a recap of the outlook in his remarks. Looking ahead, during the second quarter, we are hosting our customers and partners at our annual Engage Technology and User Summit in late September in Arlington, Texas. As Engage 2025, we'll be showcasing both our existing solutions as well as our latest AIOps innovations. We'll demonstrate how our highly curated data drives improved business outcomes across key ecosystems, focusing on cybersecurity as well as network and service observability. We'll also be highlighting how our solution provides protection against modern days These are DDoS attacks with our AI-powered Arbor DDoS protection. Longer term, we are committed to empowering our customers to meet the demand of today's connected, complex digital landscape by delivering mission-critical solutions that address performance, ensure availability, and safeguard security. We look forward to sharing our progress with you throughout the remainder of our fiscal year. With that, I'll turn the call over to Tony.

Tony Piazza | Executive Finance President and Chief Financial Officer:

Thank you, Anil, and good morning, everyone. Thank you for joining us. I'll start by walking you through the key financial metrics for the first quarter of fiscal year 2026. After that, I'll share some additional commentary on our outlook for the remainder of the fiscal year, including some color on our expectations for Q2. 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. I will note the nature of any such comparisons accordingly. All comparisons are on a year-over-year basis unless otherwise noted. Now let's turn to slide number 10, which details the results of the first quarter of our fiscal year 2026. Total revenue for the first quarter increased 7% to $186.7 million. Product revenue increased 19.3% to $73 million, while service revenue increased 0.3% to $113.8 million. Gross profit margin increased by 1.6 percentage points to 78.7% in the first quarter, primarily driven by product volume and mix. Quarterly operating expenses were relatively consistent year over year as the final quarter of benefit from the prior year's restructuring helped offset higher employee-related expenses, commissions, and professional fees. Accordingly, we reported an operating profit margin of 14.2% compared with 8% in the same quarter last year. Deluded earnings per share was 34 cents. up 21.4% from $0.28 in the same quarter last year. Both the current and prior year's quarters included unrealized gains related to a foreign investment. In the current quarter, this resulted in a benefit of approximately $0.03 per share compared to a benefit of approximately $0.10 per share in the same quarter last year. Turning to slide 11, 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 first quarter of fiscal year 2026, service assurance revenue increased by 1.4%, while cybersecurity revenue grew by 18.3%. During the same period, our service assurance product line accounted for approximately 63% of our total revenue, and our cybersecurity product line accounted for the remaining 37%. Turning to our customer verticals, for the first quarter of fiscal year 2026, our enterprise customer vertical revenue grew 17.7%, while our service provider customer vertical revenue decreased 5.6%. During the same period, our enterprise customer vertical accounted for approximately 59% of our total revenue, while our service provider customer vertical accounted for the remaining 41%. Turning to slide 12, this slide shows our revenue split between the United States and the international markets. For the first quarter of fiscal year 2026, 54% of our revenue was generated from the United States with the remaining 46% coming from international markets. Additionally, no single customer accounted for 10% or more of our total revenue during the first quarter. Slide 13 outlines select balance sheet items alongside free cash flow for the period. We ended the first quarter of fiscal year 2026 with $543.5 million in cash, cash equivalents, short and long-term marketable securities and investments, representing an increase of $51 million since the end of fiscal year 2025. Free cash flow for the quarter was $71.7 million. During the first quarter, we repurchased approximately 761,000 shares of our common stock for approximately $15 million at an average share price of $19.72 per share. We currently have capacity under our share repurchase authorization. and subject to market conditions, intend to remain active in the market through the rest of fiscal year 2026. From a liquidity perspective, we have no outstanding balance on our $600 million revolving credit facility as of June 30th, 2025, which expires in October 2029. To briefly recap other balance sheet items, Counts receivable net was $92.2 million, representing a decrease of $71.5 million since March 31st, 2025. Day sales outstanding, or DSO, at the end of the first quarter of fiscal year 2026 was 41 days, compared with 63 days in the same period in the prior year. This improvement in the

DSO in the first quarter reflects the timing and composition of bookings. Let's move to slide 14 for commentary on our outlook. I will focus my remarks on our non-GAAP targets for fiscal year 2026. As Anil noted earlier, we are reaffirming our non-GAAP outlook for fiscal year 2026 that we presented during our fourth quarter in full fiscal year 2025 earnings call in May. As a reminder, for our fiscal year 2026, we continue to anticipate revenue in the range of $825 million to $865 million, and non-GAAP diluted earnings per share within the range of $2.25 to $2.40. This full year effective tax rate is expected to be approximately 20%. Our weighted average diluted shares outstanding are assumed to be approximately 74 million shares, which does not incorporate any future share repurchase activities. I would also like to note that on August 4th, we successfully completed the sale of our entire previously disclosed foreign investment for the equivalent of approximately $12 million. Our outlook anticipated that this investment would have a relatively neutral impact on our full fiscal year financial performance, which remains the case as a result of this transaction. Finally, let me now provide some color for our second quarter expectations. We currently anticipate year-over-year second quarter revenue growth in the range of 4 to 6 percent. In terms of non-GAAP earnings per share, we anticipate a range of 43 cents to 45 cents for the quarter. This outlook reflects several key factors. The shift in timing of our engaged customer event, which will occur in Q2 this fiscal year versus Q3 last fiscal year. The normalization of operating expenses in Q2 as benefits from the prior year's restructuring actions lapse. And the impact of the sale of our previously disclosed foreign investment in Q2, which will offset the gain recorded in Q1 and is expected to have a relatively neutral impact on our whole fiscal year outlook. That concludes my formal review of our financial results. Before we transition to Q&A, I'd like to quickly note that our upcoming IR conference participation is listed on slide 15. Thank you, and I'll now turn the call over to the operator for questions.

Margo | Conference Operator:

Thank you. At this time, if you would like to ask a question, please press star 1 on your telephone keypad. If you wish to remove yourself from the queue, press star 2. We do ask in the interest of time that you limit yourself to one question and one follow-up question. We'll take our first question from Matt Hedberg, RBC Capital Markets. Please go ahead.

Simran | Analyst, RBC Capital Markets:

Hey, guys. This is Simran for Matt Hedberg. Congrats on the quarter. So just to start out, could you talk a little bit about what you are seeing in the macro environment relative to 90 days ago? And can you give a little bit more color on the outlook around the service provider spending in fiscal year 26 and compare it to what you were seeing this time last year?

Neil Singhal | President and Chief Executive Officer:

So thanks for your question. So if you're talking about the external environment related to tariffs, I think his jury is still out and we are not seeing any effect at this point. Also, as I mentioned on our last call that We have more of, let's say, mostly a software business, which is less impacted by tariffs. So we still remain to be seen whether they will have any serious impact this fiscal year. The second thing on your question of service provider spending, I would not look at the quarter-over-quarter comparison in any serious way because of lumpy deals in service providers. We think that it's too early to compare this year with last year. Overall, the spending climate looks very similar to what we saw last year.

Simran | Analyst, RBC Capital Markets:

Okay, great. And then just one more from me. Can you talk a little bit more about the security portfolio this year? What keeps it going? Where are you seeing the most demand around the newer products like mobile security, adaptive DDoS, distributed threat mitigation. Yeah, any color on that would be great.

Neil Singhal | President and Chief Executive Officer:

So the biggest thing, as we have talked about over the last couple of years, the Arbor DDoS business is fully integrated into NETSCOUT, the main business. As a result, we are crossbreeding some of the technologies, like we are bringing scalable DPI to the DDoS world, which results in adaptive DDoS, and other feature sets which were not previously available and are big differentiators, even though we are already a big leader and incumbent in this market. So that's one area, and that's obviously the biggest portion and the biggest area of growth also. We have some traction on the OCI product, which is basically in the NDR space, but we are repositioning that into what we call post-incident responses. And third area is that even our new AI sensor product, which sends curated data to third parties, it's not only useful to learn observability, but also used for cybersecurity use cases with partnership with Splunk and likes of Palo Alto. So we think that that's a big area of growth, which has, we have made a big advancement in that area. Plus my spending climate is much better versus service assurance.

Margo | Conference Operator:

Great. Thanks, guys. Our next question comes from Kevin Lu with K. Lu and Company. Please go ahead.

Kevin Lu | Analyst, K. Lu & Company:

Hi. Good morning, guys. Nice start to the year here. First question, I just wanted to ask about how, you know, spending amongst your federal government customers trended within the first quarter. It did sound like you guys got a nice deal that came in earlier than expected. And then, as you look towards, you know, the September quarter, Any initial thoughts on whether you'd expect, you know, kind of the usual federal government budget flush and maybe put that in context for kind of the trillion dollar plus defense bill for next fiscal year as well and how that could benefit you?

Neil Singhal | President and Chief Executive Officer:

Yeah, so I'll let Tony maybe give, add to what my commentary is. Okay, I mean, so yeah, we had a good quarter and pipeline looks good. And it's possible that we will get much better performance in the first half as we exit this fiscal year. But as you know, the timing is always of suspect. So we have a good line of sight for the traction and improvement in the federal area. But whether it exactly happened before September 30th is not clear right now.

Tony Piazza | Executive Finance President and Chief Financial Officer:

Yeah, so Kevin, I would say Fed was strong in the quarter. It grew mid-teens, and we see opportunity in this particular area. As we alluded to in the prepared remarks, we did have an order come in earlier, so that was some of the strength in the quarter. But we do see a lot of opportunity in the federal area, but as you know, it's always subject to – subject to the approvals and the timing of those orders given everything going on in the federal government. But we're cautiously optimistic for that sector right now.

Kevin Lu | Analyst, K. Lu & Company:

Understood. And then more generally, just with the strength you're seeing on the enterprise side of the business right now, can you speak to, you know, how much of a contributor kind of these investments in AI data centers is impacting that? or whether there are other kind of strong secular growth drivers that can help sustain that trend moving forward?

Neil Singhal | President and Chief Executive Officer:

So I think the biggest change which has not impacted the revenue stream yet is that our service assurance market, which was more of a niche market where we had almost 40, 50% market share, is getting expanded into the larger observability market. And so our data is even more useful. So I think it's getting legitimacy to what we used to do in the scalable DPI and smart telemetry area. And we have made corresponding product improvements using this product called Omnis AI Insights, which some of it will contribute to revenue this year also. So that's the biggest, most interesting thing going for us that AI is making some of the things which are very important for our customer into the mainstream. And indirectly increasing our market size, which was one of the challenges in the service assurance area we had.

Tony Piazza | Executive Finance President and Chief Financial Officer:

And, Kevin, I would say that it's early on for this product, and we're seeing good interest and momentum. It did have some contribution because, as we said in the prepared remarks, that we did highlight a customer that did invest in it, but it's small at this point, but we see opportunity in this area.

Kevin Lu | Analyst, K. Lu & Company:

Got it. And maybe just one last one, you know, with the passage of the tax bill last month, wondering, you know, what you're hearing from some of your service provider customers at this point in terms of, you know, potential incremental investments they're making in their network and how that could translate in a business for you.

Neil Singhal | President and Chief Executive Officer:

We have not heard anything specific from those this year so far, and even the past when the changes happened, that didn't necessarily translate into more or less business for us.

Kevin Lu | Analyst, K. Lu & Company:

Got it. Thanks for taking the questions, and good luck during G2.

Neil Singhal | President and Chief Executive Officer:

Thank you.

Margo | Conference Operator:

Thank you, and this concludes our call. We thank you for joining us today. Have a wonderful day.