SONUS NETWORKS SECOND QUARTER 2013 RESULTS

PREPARED REMARKS

JULY 29, 2013

PATTI LEAHY, VICE PRESIDENT, INVESTOR RELATIONS

Thank you and good afternoon everyone. Welcome to Sonus Networks' second quarter 2013 operating results conference call.

As a reminder, today's press release and supplementary financial and operational data have been posted to our IR website at sonus.net. A recording of this call and a copy of our prepared remarks will be available there as well later this afternoon.

Speakers on the call today are Ray Dolan, President and Chief Executive Officer, and Moe Castonguay, Senior Vice President and Chief Financial Officer.

Please note for purposes of Safe Harbor provisions that during this call we will make projections and forward-looking statements regarding items such as future market opportunities and the company's financial outlook. Actual events or financial results may differ materially from these projections or forward-looking statements and are subject to various risks and uncertainties including, without limitation, economic conditions, market acceptance of our products and services, the timing of revenue recognition, difficulties leveraging market opportunities, and the impact of restructuring activities. A discussion of these and other factors that may affect future results is contained in our most recent Form 10-Q filed with the SEC and in today's earnings release, both of which are available on our website. While we may elect to update or revise forward-looking statements at some point, we specifically disclaim any obligation to do so, unless required by law.

During our call we will be referring to certain GAAP and non-GAAP financial measures. A reconciliation of the non-GAAP to comparable GAAP financial measures is included in our press release issued today, as well as in the Investor Relations section of our website.

With that, it's now my pleasure to introduce the President and Chief Executive Officer of Sonus, Ray Dolan.

RAY DOLAN, CHIEF EXECUTIVE OFFICER

Thank you, Patti, and good afternoon everyone. I am very pleased to announce another solid set of results. Sonus delivered a strong quarter in which we exceeded most of the guidance we gave back in April and also raised our revenue and EPS outlook for the full year. We are making steady and significant progress towards our principal goal to transform Sonus to an SBC-centric, profitable growth company.

Moe will take you through the full details of the quarter and our outlook in a moment. But first, I would like provide some comments regarding today's press release in which we announced a number of other important developments at Sonus. I will address our key performance metrics and stock buyback program announced today in my closing remarks.

Turning to the topic of management transitions:

As announced today, Moe will be stepping down as CFO once the Board and I have identified the right successor. I'd like to take this opportunity to express my sincere thanks to Moe who has agreed to stay on through the year-end close period, if that is necessary, to help ensure a smooth transition. Moe has been instrumental in a number of important accomplishments since joining us in the summer of 2011 and I believe our results reflect that. Some of these accomplishments include successfully buying and integrating NET; strengthening our internal processes; improving our forecasting capabilities; and, lowering our cost structure.

With the help of Moe's leadership we have taken decisive steps to drive costs out of our business. One particularly bright spot is in our Services gross margins which have improved dramatically over the past year, and are now at 57% in Q2 -- a full 11 percentage points higher than the second quarter of 2012.

Much of the progress in Services is due to the leader of the Services group, Matt Dillon, who is also stepping down as announced today. Matt's departure comes after 12 years of dedicated leadership at Sonus. He and his team can be very proud of what they've accomplished, knowing that our Global Services organization is in an excellent position to succeed in supporting not only our core carrier customer base, but also a rapidly growing enterprise customer base. So I'd also like to take this opportunity to thank both Matt and Moe and wish them the very best in their future endeavors.

Change, of course, also brings opportunity. Along these lines, I am pleased to announce that Peter Polizzi has been named as Matt's successor. Peter brings a proven track record of success leading technically advanced multinational operations at companies like Motorola. I am thrilled that we have someone of his caliber who can step in immediately to lead the services organization.

Sonus is now a far more focused and successful company, in part due to strong leadership. But, like any prosperous company, our success isn't tied to just a few people; it's the result of the thousand-plus individuals who wake up each day figuring out how we can accelerate our growth, compete more effectively, remain strategic to our customers and partners and, ultimately, drive greater value for ALL of our stakeholders.

Sonus has a firm foundation in place and I am confident that our best days are ahead of us.

I'll now turn the call over to Moe to review our financials and outlook in more detail.

MOE CASTONGUAY, CHIEF FINANCIAL OFFICER

Thank you, Ray, and good afternoon everyone.

Before I provide the results, I want to take a moment to reflect on my planned departure from the company. The past two years have been exciting and highly rewarding for me personally. I have been able to work with a great team and Board and I am deeply grateful for having had that opportunity. It has also been a pleasure speaking with our shareholders and the investment community.

There is a strong foundation in place at Sonus and the time is right for me to explore my next challenge. I look forward to continuing in my role until my successor is named and I am committed to working closely with Ray and the Board to identify a new CFO and ensure a seamless transition.

Now, turning to our Q2 Results:

Total revenue for the second quarter was $69.2 million compared to $63.3 million in the first quarter and $57.6 million in the second quarter of 2012.

Total SBC revenue, including products and services, was $29.0 million in the second quarter, $30.0 million in the first quarter and $19.1 million in the second quarter of 2012.

Our top five revenue customers represented 47% of revenue this quarter, down from 50% in the first quarter and down from 54% in the second quarter of last year.

We reported two 10% customers in the quarter, Verizon and AT&T, both of which purchased SBC products or services.

We reported revenue from 539 customers in the second quarter. This compares to 541 customers in the first quarter.

Looking at revenue geographically, domestic revenue accounted for 74% in Q2, compared to 69% in Q1 and 73% in Q2 of 2012.

Before I go into further details on our financials, I would like to point out, that the following are non-GAAP numbers that exclude stock-based compensation, acquisition costs, restructuring charges, and write off and amortization of intangible assets.

Total gross margin for the second quarter was 64.8% compared to 61.0% in the first quarter and 57.4% in Q2 of 2012. Our second quarter performance reflects improvements in both product and service gross margins.

Product gross margin for the second quarter was 69.9% compared to 64.9% in the first quarter and 66.3% in Q2 of last year. Product gross margins can fluctuate, quarter over quarter, based on software content and product mix but are clearly improving on an annualized basis.

Service gross margin for the second quarter was 56.6%, compared to 55.4% in Q1 and 45.7% in Q2 of last year.

Total operating expenses for the second quarter were $41.5 million, compared to $44.7 million in the first quarter and $41.7 million in Q2 of last year.

Consolidated headcount at the end of the quarter, was 1,039 compared to 1,042 at the end of Q1 of 2013.

Net Income for the quarter was $3.2 million, compared to a net loss of $6.4 million in the first quarter and a net loss of $8.6 million in Q2 of 2012.

We ended the quarter with total cash and investments of $304 million which is significantly better than forecast and a good indication that we are making progress toward our goal of generating cash from operations for the full year.

Our DSO for the quarter was 52 days, as compared to 71 days in the first quarter. The improved DSO in the second quarter reflects excellent collections and improved linearity of shipments.

Now I would like to provide more details for our outlook for the third quarter ending Friday, September 27th and for the fiscal year ending December 31, 2013. I will remind you that the outlook provided in the press release is also available on our IR website.

The total revenue outlook for the third quarter is anticipated to be between $68 and $72 million. We are raising our fiscal year 2013 revenue outlook to between $274 and $278 million.

Included in the third quarter outlook is anticipated Total SBC revenue of $28 to $32 million.

Total SBC revenue for fiscal year 2013 remains unchanged at a range of $120 to $124 million, reflecting year over year growth of approximately 40%.

With regards to the second half of the year, and as we told you on last quarter's call, we continue to expect the fourth quarter to be our strongest quarter, representing over 30% of our SBC product revenue, as was the case in the fourth quarter of 2012.

Turning to our legacy product revenue outlook: We currently expect an annual decline of approximately 25% in our Media Gateway product revenue which implies roughly $65 million of legacy product revenue in Fiscal 2013. This reflects a slight improvement from our prior outlook which called for a decline of approximately 30% for Fiscal 2013.

Turning to gross margins: For the third quarter, we expect total non-GAAP gross margins to range between 64 and 65%. For the full year we continue to expect non-GAAP gross margins of between 64 and 65%, reflecting continued streamlining of manufacturing and service operations and lower component and subassembly costs.

For the third quarter we expect non-GAAP operating expenses to be between $42 and $43 million. The slight increase from Q2 primarily reflects an increase in product development related costs.

Total non-GAAP operating expense outlook for fiscal year 2013 remains in the range of $171 to 172 million.

For the third quarter, we expect non-GAAP earnings per diluted share of $0.01 and for the full year we have increased our profit estimate and now expect non-GAAP earnings per diluted share of $0.01 to $0.02.

Fully diluted share count for the third quarter is anticipated to be approximately 287 million. Full year weighted average diluted shares are expected to be approximately 286 million.

We expect to be cash flow positive from operations in 2013, with third quarter ending cash and investments of $300 to $305 million, excluding any reduction related to possible stock buybacks. We expect year-end cash and investments of $305 million, excluding any reduction related to possible stock buybacks.

With that said, I will now turn the call back to Ray.

RAY DOLAN, CHIEF EXECUTIVE OFFICER

I'd now like to review our progress with the four key performance metrics for 2013 that we identified for you at the start of the year.

Turning first to SBC Growth. SBC product revenue and SBC total revenue were both up over 50% year over year, which is great progress. Looking forward, we have provided a slightly broader range than normal for SBC guidance in the third quarter. This guidance accounts for the possibility that a couple of transactions could score either in Q3 or Q4. Our full year outlook remains the same and for a third straight year, our SBC business is on track to substantially outpace market growth.

The next key operational metric I will discuss is new customer growth. We secured 190 new customers in Q2, 85% of which are new SBC customers. This marks a quarterly record for new customers and further validates that we are winning in the marketplace. I am pleased by the raised awareness not only for the SBC category, but also for Sonus as customers and partners seek to understand how we can help them navigate the rapidly growing world of SIP-based communications. Our relationships with customers continue to expand and are becoming increasingly strategic.

We have also developed a burgeoning set of partnerships with industry leaders such as Microsoft, BroadSoft, Juniper and, most recently, F5. These partnerships, coupled with our solid technology roadmap, position Sonus to take advantage of emerging industry trends including NFV, SDN, cloud-based communications and the rapid growth in UC and mobility.

A third key metric for 2013 is the percent of product revenue we generate from the Channel and Enterprise. These are new areas of growth for Sonus in 2013. The Channel contributed 16% of total product revenue in Q2, and we continue to expect the Channel to contribute between $32 to $40 million for full year total product revenue.

We're seeing strong interest from a cross section of partners ranging from global systems integrators to traditional networking resellers. UC solutions providers, particularly those that resell Microsoft Lync, comprise a significant part of our partner base. We have recently expanded the program to include distributors to make it easier for our partners to buy from us. Recall that just one year ago, our partner program launched with a one-tier channel program, a handful of channel partners and no distributors. Today, we have about 300 channel partners – approximately 40 of which are Sonus Select Partners - and we have a two-tiered program with more than a dozen distributors. We've made solid progress in the channel.

Enterprise was 21% of our total product revenue this quarter. Our momentum here is driven by an increasing number of enterprises making the move to UC, cloud services and SIP Trunking. Sonus has the appropriate portfolio to help them, be it for small branch offices or Fortune 100 corporations. For the full year 2013, we continue to expect Enterprise to contribute $35 to $40 million of our Total Product Revenue. To help you with the math, total product revenue for the full year has increased to a midpoint of approximately $165 million.

The final key operational metric I will discuss is our path toward Profitability. This has been a major focus, and we are making solid progress. We are delighted today to post a profitable quarter and raise our guidance for the full year. We expect to be firmly profitable, on a non-GAAP basis, for full year 2013. We've also raised our year end cash outlook based on strong operating performance.

As you can see, Sonus didn't just deliver a great quarter; we are creating a great company that is driving market-leading SBC growth and long-term profitability. This leads to the final topic in my prepared remarks which is the Stock Buyback Program announced today.

When I joined Sonus almost three years ago, I pointed to three major assets that attracted me to take this role. These included a great customer base, a strong and innovative team, and a solid balance sheet. This combination gave us the opportunity to think clearly about our strategy and make the proper investments in our business. As we see our strategy successfully taking root, we feel very good about our future. Our customer base is growing. Our team is stronger than ever. We have used our balance sheet to turn the company around and create an SBC-based, growth company - both organically and through the NET acquisition. Now is the right time to begin returning excess capital to our shareholders.

That concludes our prepared remarks this afternoon. I'd now like to open the call up for questions.