



Keysight Technologies Third Quarter 2022 Earnings Conference Call
Prepared Remarks

JASON KARY

Thank you, and welcome everyone to Keysight's third quarter earnings conference call for fiscal year 2022.

Joining me are Keysight's President and CEO Satish Dhanasekaran, and our CFO, Neil Dougherty. In the Q&A session we will be joined by Senior Vice President of Global Sales, Mark Wallace.

You can find the press release and information to supplement today's discussion on our website at investor.keysight.com under the financial information tab and quarterly reports.

Today's comments by Satish and Neil will refer to non-GAAP financial measures. We will also make reference to "core" growth, which excludes the impact of currency movements and acquisitions, or divestitures completed within the last twelve months. The most directly comparable GAAP financial metrics and reconciliations are on our website, and all comparisons are on a year-over-year basis unless otherwise noted.

We will make forward-looking statements about the financial performance of the company on today's call. These statements are subject to risks and uncertainties and are only valid as of today. We assume no obligation to update them. Please review our recent SEC filings for a more complete picture of our risks and other factors.

Lastly, management is scheduled to participate in upcoming investor conferences hosted by Jefferies, Deutsche Bank, Citi, and Goldman Sachs. We hope to see many of you there.

And now I will turn the call over to Satish.

SATISH DHANASEKARAN

Thank you, Jason. Good afternoon, everyone, and thank you for joining us today.

Keysight Technologies delivered another exceptional quarter with both revenue and earnings per share exceeding the high end of our guidance. Our outperformance reflects the effectiveness of our strategy, outstanding execution by our teams around the world, and the strength of our operating model. Keysight's deep customer engagements with industry leaders and high value, differentiated solutions continue to drive broad-based demand across key technology mega trends.

I will focus my comments today on three key headlines.

- First, outstanding execution by Keysight teams around the world resulted in all-time record revenue and earnings per share, as we saw some supply constraints ease as the quarter progressed.
- Second, we saw strong order growth and sustained demand across all end markets and regions.
- Third, we are again raising our full year outlook. We now expect to achieve revenue growth approaching 9 percent and earnings per share growth of approximately 20 percent for the full fiscal year.

Let's now take a deeper look at our results for the quarter.

Third-quarter orders grew 12 percent to \$1.46 billion, and outpaced record revenue, which grew 10 percent to \$1.38 billion. Record EPS of 2 dollars 1 cent grew 31 percent.

Order and revenue growth in both business segments and across all regions is evidence of our ability to deliver value for customers as we manage macro and supply dynamics.

Software revenue achieved an all-time high, outpacing total Keysight revenue growth and expanding our recurring revenue profile to further strengthen the durability of our business. Our software-centric solutions strategy is a key differentiator in rapidly evolving design, systems emulation, and modeling environments. We recently introduced PathWave Advanced Design System 2023 to address growing complexity in ultra-high frequency designs. We also announced that Keysight's Open-RAN solutions are moving to cloud-based deployment to support our customers' needs, as networks evolve to more software-enabled, virtualized architectures.

Turning to our business segments, the Communications Solutions Group delivered all-time record revenue and record third-quarter orders.

Commercial communications achieved record revenue with growth across all industry segments and regions. Innovation dynamics across the communications ecosystem remained strong, driving demand for Keysight's comprehensive end-to-end portfolio for both the wireless and wireline ecosystems.

In wireless, 5G continues to represent an innovation-rich environment for the industry. Our differentiated, software-centric solutions enable customers to address the growing complexity of

use cases, frequency band combinations, real-world connectivity, and mobility challenges. We continue to evolve our 5G platform to meet the requirements of emerging applications and newer versions of the standards. In collaboration with Intel, Radisys, Vodafone, and Wind River, we recently showcased an industry first demonstration deploying Keysight's O-RAN solutions to help reduce power consumption in a multi-vendor Open-RAN network. AI-LINK, a provider of industrial IoT offerings, used Keysight's solutions for end-to-end performance validation of cloud-native radio access network infrastructure.

In wireline, we continued to see strong demand for 400G, 800G, and photonics applications. We recently collaborated with Nokia, to demonstrate the first public 800G interoperability test, validating the robustness of ultra-high data rates in telco networks and data center environments for the expected increase in AI/ML network workloads.

Record Q3 orders in aerospace, defense and government outpaced revenue, which grew one percent on a core basis, versus a strong growth quarter last year. Budget appropriations began to flow as reflected in prime contractor spending in the US, while 5G investments continued to grow to address new use cases, such as radar and 5G coexistence. We also saw strength in satellite and space, including new applications for non-terrestrial networks. Over the next several years, we expect this market will benefit from elevated investments in technology modernization.

The Electronics Industrial Solutions Group delivered double-digit order and revenue growth for the eighth consecutive quarter with momentum from continued investments in next generation technologies across automotive, industrial IoT, and semiconductor end markets.

In automotive, we are pleased with the continued broad adoption of our solutions portfolio with the business nearly doubling over the past two years. Orders grew strong double-digits for the sixth consecutive quarter, and we delivered all-time record revenue. Keysight's contributions to the advancement of EV and AV technologies, which include vehicle intelligence, connectivity, power, and security are fueling momentum with leading car manufacturers and helped us secure wins with gigafactories around the world. Keysight's award-winning Radar Scene Emulator is the only solution on the market to imitate realistic roadway scenarios in a lab environment and was chosen by a leading US auto manufacturer for testing and validation of autonomous drive systems. This quarter we completed another tuck-in acquisition in the automotive space, further adding to our software technology and technical staff focused on vehicle-to-everything communications. We continue to invest as we target evolving opportunities in the future of transportation.

In general electronics, we achieved double-digit order growth and all-time record revenue, as investments continued in digital health, IoT, and advanced research. In educational research, Keysight is partnering with global leaders, such as Nanyang Technological University in Singapore, to advance 6G technology. Together with Sauce Labs, our Eggplant business delivered artificial intelligence-driven testing of enterprise applications. The acceleration in our general electronics business reflects the broad scope of our portfolio of leading technology solutions.

Record orders for our semiconductor solutions resulted in the ninth consecutive quarter of double-digit order growth, driven by capacity expansion in mature foundries to address pent up demand in the market, and investments in advanced processes. Keysight's PathWave design solutions expand

our collaboration with major foundries beyond parametric wafer test into emerging applications like silicon photonics and next-generation design and simulation applications.

While we continue to successfully execute our strategy, we recognize the near-term macroeconomic uncertainties. Keysight's sustained performance over time is evidence of the resilience and durability of our business. Our resilience is an outcome of enduring partnerships with market leading customers, with early engagement to develop software centric solutions that enable them to solve their most critical development challenges and achieve their first to market goals. Durability is a product of our flexible operating model, designed to quickly respond to variations in demand while investing in critical long-term priorities. These strengths give us confidence that we can navigate uncertainties and continue to deliver superior results going forward.

Of course, all of this is made possible by our talented people. Steadfast execution by our teams, especially in a challenging environment, is proof that our Keysight Leadership Model delivers results, empowering our inclusive and diverse culture which fosters collaboration, high performance, and innovation. We recently released our first Diversity, Equity, and Inclusion Report, as we renewed and strengthened Keysight's longstanding commitment to DEI and to being a great place to work for our global workforce of more than 14,000.

With that, I'll now turn the call over to Neil to discuss our financial performance and outlook.

NEIL DOUGHERTY

Thank you, Satish, and hello, everyone. We delivered strong third quarter results, successfully navigating ongoing supply chain and other headwinds.

Third quarter 2022 revenue of \$1 billion 376 million was \$26 million above the high end of our guidance range, and grew 10 percent, or 13 percent on a core basis.

We generated \$1 billion 461 million in orders, up 12 percent, or 14 percent on a core basis, and we ended the quarter with \$2.5 billion in backlog.

Turning to our operational results for Q3, we reported gross margin of 65 percent, holding steady in the face of significant inflation and currency headwinds. Operating expenses were \$480 million, resulting in operating margin of 30 percent. We used a number of strategies to effectively navigate supply chain challenges including product redesign, alternate sourcing, and increased supplier and customer engagement.

We achieved net income of \$363 million and delivered 2 dollars 1 cent in earnings per share, which was 21 cents above the high-end of our guidance. Our weighted average share count for the quarter was 181 million shares. Despite significant currency headwinds on the top line, we saw negligible FX impact to earnings due to the meaningful natural hedge provided by our global footprint that is then supplemented by our financial hedging program.

Moving to the performance of our segments, our Communications Solutions Group generated record revenue of \$970 million, up 11 percent, or 13 percent on a core basis. CSG delivered gross margin of 67 percent and record operating margin of 30 percent.

Within CSG, Commercial Communications generated record revenue of \$694 million, up 17 percent, or 19 percent on a core basis driven by 5G, O-RAN, 400G, 800G, and high-speed digital applications.

Aerospace, Defense and Government revenue of \$276 million was down 2 percent, and up 1 percent on a core basis. Our backlog for this end market remains strong, and we continue to expect increasing defense budgets in the U.S., Europe, and Japan to provide support for higher spending going forward.

The Electronic Industrial Solutions Group generated third quarter revenue of \$406 million, up 10 percent, or 13 percent on a core basis, driven by strong revenue growth across all end markets and regions. EISG reported gross margin of 61 percent, and operating margin of 31 percent.

Moving to the balance sheet and cash flow, we ended the third quarter with \$1.8 billion in cash and cash equivalents, generating cash flow from operations of \$224 million, and free cash flow of \$192 million, or 14 percent of revenue.

Share repurchases this quarter totaled 1.6 million shares at an average price per share of \$139.46, for a total consideration of \$228 million. Year to-date, we have repurchased approximately 4.6 million shares for a total consideration of \$723 million.

Now, turning to our outlook and guidance ...

Demand remains strong for Keysight's solutions, our funnel is near historic high levels, and we exit the quarter with a record backlog.

We now expect full year revenue growth to approach 9 percent, or 11 percent on a core basis, with EPS in the range of 7 dollars 43 cents to 7 dollars 49 cents, representing growth of 20 percent at the midpoint.

Fourth quarter 2022 revenue is expected to be in the range of \$1.38 billion to \$1.40 billion, with earnings per share in the range of 1 dollar 94 cents to 2 dollars, based on a weighted diluted share count of approximately 180 million shares.

In closing, Keysight's resilient business, consistent execution, and flexible cost structure give us confidence in our ability to capitalize on long-term secular growth trends and deliver above-market, profitable growth in 2023 and beyond.

With that, I will now turn it back to Jason for the Q&A.