

Emulex Corporation (NYSE:ELX)

Earnings Call Transcript

Thursday, August 09, 2012 5:00 PM ET

Call Participants

Executives

James M. McCluney

Chief Executive Officer and Director

Jeffrey W. Benck

President and Chief Operating Officer

Michael J. Rockenbach

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Analysts

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Jayson Noland

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Presentation

Operator

Good day, and welcome to the Emulex Corporation Fourth Quarter 2012 Conference Call. This call is being recorded. At this time for opening remarks and introductions, I would like to turn the call over to Chief Executive Officer, Mr. Jim McCluney. Please go ahead, sir.

James M. McCluney

Chief Executive Officer and Director

Thank you, operator. Good afternoon, everybody, and welcome to Emulex's Fourth Quarter Fiscal Year 2012 Conference Call. I'm Jim McCluney, CEO of the company. And with me today are Jeff Benck, our President and COO; and Mike Rockenbach, our CFO. Mike will start off with prepared remarks for the fourth quarter and fiscal year 2012 results. I will follow Mike with my comments on our accomplishments for fiscal year '12 and the current business climate, and Jeff will provide more color on the results for the fourth quarter and an overview of some of the key activities that we're focused on for fiscal 2013. I'll close the prepared remarks with some summary comments and observations, and then we'll open the line for questions.

So with that, Mike, over to you.

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

Thanks, Jim. By now you should have Emulex's fourth quarter 2012 earnings release, which was issued earlier this afternoon. If you do not have a copy, the press release is available in the Investor Relations section of our website at www.emulex.com. The press release and this presentation contain forward-looking statements, including, but without limitations, statements regarding Emulex's business, operations, ongoing patent litigation and the related mitigation effort and the anticipated financial results for our first quarter of fiscal 2013 and beyond. These statements are subject to a number of risks and uncertainties, and our actual results may differ materially from those discussed in the forward-looking statements. Those risks and uncertainties are highlighted in our earnings release and under the heading Risk Factors in Emulex's most recent annual report on Form 10-K and quarterly reports on Form 10-Q. We undertake no obligation to update these forward-looking statements.

During the call, when we use any historical non-GAAP financial measure, you will find the reconciliation to the most directly comparable GAAP financial measure in our earnings release. All of the references we will make today relate to our non-GAAP results unless stated otherwise. Today's conference call is being webcast, and a recording will be available on the Emulex website through August 2013. I would also like to remind participants that if you decide to ask a question, it will be included in both our live transmission as well as any future use of the recording.

Now, let me review our results for the quarter. Sales for our fourth quarter came in at \$129 million, which was in the upper end of our guidance of \$126 million to \$130 million provided on our earnings call in April. Net revenues for the quarter increased 3% sequentially and 5% over the fourth quarter of last year. As a reminder, last year, our fourth quarter had a 14th week, which accounted for an additional \$10 million of revenue. Normalizing that period for a 13-week quarter, our current quarter results showed a 14% increase year-over-year.

Diluted earnings per share in the fourth quarter increased over 60% from a year ago coming in at \$0.26, which exceeded the high end of our April guidance of \$0.21 to \$0.23. This improvement was driven by expense management and lower mitigation expense.

Taking a look at revenues by product line, our Network Connectivity Products, or NCP, represented 68% of our net revenues this quarter. The NCP product line consists of Fibre Channel and Ethernet products that are used to connect servers and storage arrays to a Fibre Channel Storage Area Network or to an Ethernet network. We sell these products in a variety of form factors, including a standalone ASICs, custom mezzanine cards for blade servers and standup cards for rack-mounted servers. NCP revenues totaled \$88 million, a decrease of 3% sequentially and down 7% from the comparable quarter of last year. However our 10Gb Ethernet revenues grew more than 25% from the year ago.

Our second product line, Storage Connectivity Products, or SCP, accounted for approximately 26% of revenues during the quarter. SCP consists of our SOC's, bridges and routers that are used to connect solid-state disks, hard drives and tape drives inside the storage system. As we discussed on our last earnings call, our fourth quarter SCP revenues benefited from the last time purchases of some older legacy products.

Our third product line, Advanced Technology and Other Products, or ATP, accounted for 6% of our net revenues for the quarter. Fourth quarter gross margins of 64% were at the high end of the 63% to 64% gross margins we gave in our guidance. Gross margins for the quarter benefited from the favorable mix of products included the last time purchases in SCP. We are modeling for quarterly gross margins to be between 62% and 63% during the next year.

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Total operating expenses for the quarter came in at \$56 million, a decrease of 6% from the preceding quarter and an 18% reduction from the fourth quarter of last year. As a percent of revenue, OpEx was 43% compared to 47% in Q3 and 55% in the year-ago quarter.

Patent litigation expenses were under \$1 million for the quarter and looking forward, we expect quarterly patent litigation expenses will be in the \$1 million to \$2 million range, until the April 2013 retrial. Year-over-year operating income more than doubled to a total of \$26 million or 21% of revenues. And operationally, this was our best quarterly performance in the past 4 years. Net income for the quarter was \$23 million or 18% of revenues, representing an increase of 26% sequentially and over 60% growth over the last year's comparable period.

Turning to our GAAP results. Preliminary GAAP gross margins included a charge of approximately \$39 million associated with the partial patent litigation settlement that we announced in early July. The balance of the \$58 million settlement, which was paid in July, will be amortized over the 10-year term of the license. GAAP operating expenses for the quarter totaled \$64 million, a decrease of 4% sequentially and 19% from the fourth quarter of last year. GAAP operating expenses included \$3 million of expenses related to the patent mitigation efforts, \$2 million of amortization of intangibles and \$3 million of equity-based compensation charges. We reported an operating loss of \$26 million or 20% of revenues on a GAAP basis compared to a profit of \$8 million in the preceding quarter and a loss of \$8 million in the comparable period of last year.

Now, I'm going to give you a couple of key highlights from the full year results. Top line revenue for the year was \$502 million, an 11% increase over the prior year. Normalizing 2011 to a 52-week year, top line revenue growth was 14% for the year. 10Gb was the fastest growing piece of our business in 2012 growing over 70% on a year-over-year basis. Gross margins for the company remained essentially flat year-over-year at 64%. Operating expenses decreased to \$234 million, representing a 4% decrease in absolute spending. Prudent expense management combined with our strong revenue growth resulted in a 7 point year-over-year reduction from 54% of revenues in 2011 to 47% in 2012. Diluted earnings per share of \$0.86 increased approximately 60% compared to the \$0.54 EPS reported last year.

Taking a look at the balance sheet. We generated approximately \$30 million in cash from operations during the quarter and exited the year with \$230 million in cash and investments.

Before I discuss our outlook for the first quarter fiscal 2013, I want to again remind everyone that there are numerous risks that can affect our future performance causing actual results to differ materially from forward-looking statements. And these risks are noted in our public filings with the SEC in the Safe Harbor statement at the end of our press release.

Based on the current operating environment and the recent forecast from our customers, we are modeling for revenues of \$118 million to \$122 million for our first quarter ending September 30, 2012. This represents a flat to 3% increase in revenues compared to the first quarter of last year. Coming up on the strong fourth quarter, we expect SCP revenues to be down by as much as \$10 million in Q1, which is flat to slightly down year-over-year. Despite the current economic environment, we expect NCP to show better than seasonal growth for Q1. Based on expiring R&D tax credits, we are modeling for a tax rate of 14%, and with a share count of approximately 91.5 million shares, we are guiding for earnings per share in the range of \$0.14 to \$0.16.

Finally, I'd like to note that the partial litigation settlement payments will be reflected in our first quarter cash balances. Excluding this payment, we expect to generate approximately \$10 million in cash from operations during the first quarter, and if we achieve these results, we anticipate having over \$180 million in cash and investments at the end of Q1. We expect our GAAP EPS results to be in the \$0.01 to \$0.03 range. Our first quarter GAAP results will include an impact for stock-based compensation, amortization of intangibles and royalties, mitigation expenses and license fees associated with the patent litigation, as well as the associated tax impact in the U.S. valuation allowance. We estimate these items to be approximately \$0.13.

Now, let me turn the call back to Jim.

James M. McCluney

Chief Executive Officer and Director

Thanks, Mike. The fourth quarter results were an outstanding finish to a record-breaking year for Emulex. Despite a weakening IT spending environment, it's very satisfying to report that we once again came in at the high-end of our revenue guidance. For the second consecutive year, we delivered double-digit year-over-year revenue growth outpacing our nearest competitors. We also achieved an important milestone for the company, exceeding the \$0.5 billion revenue mark for the first time in our history. We not only delivered better than top line growth, but we also stayed focused on expense management. During the year, we reduced total expenses, particularly in engineering and G&A, even while we continue to expand our international investments in sales and marketing to gain market share in both the high-growth 10Gb Ethernet market and in our core Fibre Channel business. We exited the year with quarterly operating income in excess of 20%. It is clear however, that the uncertain IT spending environment is a headwind for

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many high-tech companies, and we are obviously impacted by this as well. But the continuing operational execution and design win momentum in the Romley server refresh, as well as the incremental opportunities with the 16Gb Fibre Channel storage transition, I'm confident that we are well-positioned to continue to gain share in both these important markets over the next year.

Since our last earnings call, we have firmly reestablished the time-to-market momentum in 16Gb Fibre Channel and we are moving quickly to exploit this advantage. Over the past few weeks, we added Dell, IBM and the EMC to a list of OEMs that have launched 16Gb Emulex Solutions. In the Fibre Channel market, switches meet the way in speed transitions, and during the March quarter, 16Gb-ready switch ports grew over 50% sequentially, accounting for more than 10% of all switch ports that quarter. The results for June are not available yet but according to Crehan Research, 20% of switch ports shipped in 2012 will be 16Gb and this is projected to increase to 50% of port shipments in 2013.

From an HBA perspective, we are well-positioned to lead the transition in 16Gb, which is projected to be 30% of the Fibre Channel HBA ports shipped in 2013. Our great momentum continues with 10Gb as well. As Mike mentioned, we grew this product line over 70% last fiscal year, almost double the total industry growth rate, and once again, gained market share. And we expect to continue to grow Ethernet revenues during this coming fiscal year.

Regarding our Q1 guidance, in spite of a weakening IT spending environment and a normally seasonally down quarter, we are modeling for NCP to grow largely fueled by 10Gb products. As we indicated on the last call that our headwinds with SCP, which as Mike mentioned is dropping sharply in Q1. We still see SCP in the \$90 million plus range for the fiscal year. Looking to the rest of the calendar year. As a total company, we expect to see sequential growth returning in the December quarter.

Lastly, on another note, I'd like to welcome Beatriz Infante to the Emulex Board of Directors. Beatriz brings a wealth of industry and management experience to the board and we all look forward to working with her as we continue executing on our strategy. We also announced that Fred Cox will be retiring from the board later this year. I'd like to personally thank Fred for his many years of service to Emulex, first as a Founder of the company and most recently as Chairman Emeritus of the Emulex board. I've had the pleasure of knowing and working closely with Fred for nearly 10 years, and the team and I wish him all the best in his future endeavors.

Now with that, let me turn it over to Jeff to give you some highlights on our operations for the quarter and a look forward into 2013. Jeff?

Jeffrey W. Benck

President and Chief Operating Officer

Thanks, Jim. Today I'd like to provide some further color on our fourth quarter results. Then I'll follow this with a brief update on our strategy and the new markets and growth opportunity this will open up to us.

So let's start with another look at Q4. As Mike mentioned, operationally, this was our best quarterly performance in the past 4 years. In addition to record full year revenues, this was our second highest quarterly revenue in the history of the company. Stable gross margins combined with additional reductions in operating expenses resulted in operating income exceeding 20% of revenues for the first time since the December quarter of calendar 2008. During the quarter, we were also recognized for operational excellence as a supplier to the Lenovo, one of the fastest-growing Chinese server OEMs. We are the only server or storage partner honored as a Perfect Supplier of the Year and this recognition reinforces our commitment to providing high-quality products and achieving outstanding customer satisfaction.

Looking at market share. In the fourth quarter, our board level Fibre Channel product showed modest sequential growth of 4%. With our nearest competitor already reporting June results, I'm confident we gained more than 4 points a share during this quarter versus them. I'm also pleased with the progress we have made in the x86 market over the last 12 months where we have gained almost 3 points a share versus the same Fibre Channel competitor.

Looking forward, the recently signed Broadcom license agreement has reestablished our 9-month time-to-market lead in 16Gb Fibre Channel over our nearest competitor. This time-to-market lead is enabling us to capture more 16Gb OEM design wins on both the host and target sides. In the last few weeks, we announced that we are now shipping 16Gb design wins with Dell, IBM and EMC, in addition to our previously announced win with HP. We're now the growing incumbent in the 16Gb Fibre Channel market and expect us to drive a market share shift to Emulex as customers migrate to 16Gb technology.

Some of you might wonder what's driving the 16Gb transition right now. We see 16Gb being deployed to accelerate application delivery with SSDs, improve Oracle database performance and reliability via our industry-leading data integrity solution, help IT shops deploy virtualization with VMware ESX 5.1 and Windows Server 2012, and provide investment protection for customers deploying new Romley-based servers that are Gen 3 PCI capable. The 8Gb Fibre Channel market took 4 years to reach over 50% of shipments. However, Crehan Research expects that the 16Gb

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transition will be much more aggressive reaching over 50% of port shipments in just 2 years. The Fibre Channel Storage target market is one of the most promising share gain opportunities for Emulex. We expect this segment to be upwards of a \$100 million per year and representing a strong growth proposition for us during this 16Gb Fibre Channel and 10Gb SCOE transition happening in storage arrays. Target storage OEMs typically have a longer development cycle than most server vendors so our early lead in shipping development tools and samples to them is enabling us to capture more of this opportunity than the competition. Look for additional product announcements for us in the 16Gb over the next few quarters, including new storage target-based design wins.

Now, let me share some important updates on our Ethernet strategy. As you may be aware, for several years now, Emulex has had an explicit focus on the rapidly growing 10Gb Ethernet market and we were successful in driving market share leadership with our converged networking strategy that allowed SAN and LAN environments to be combined on a single wire with SCOEs enabling technology. Now, we're forced to be disruptive again with a specific focus on high-performance networking. Customers have asked us to provide a low-cost alternative to InfiniBand that could be used to converge LANs, SANs and HPC workloads while allowing IT managers to leverage a common set of tools and practices in the data center. We see the opportunity to drive the second major phase of network convergence by combining HPC and IP networks on a single wire with software designed networking tools leveraging low latency 40gb Ethernet. This time, the enabling technology is RDMA over Converged Ethernet or RoCE. RoCE is enabling us to now consolidate high-performance networking workloads onto our Converged Network Adapters. Our investment in high-speed 40gb and 100gb Ethernet ASICs combined with our RoCE efforts and our optimized high-performance FastStack buffer offerings will allow us to be -- to very effectively tap into the rapidly growing high performance computing opportunity. This strategy isn't just about pointing into the future as we're starting to make announcements in this space now.

Last quarter, we introduced the new family of high-performance 10Gb Ethernet-based networking solutions to meet the extreme performance needs of the financial trading, fiber security, video streaming and digital content delivery markets. Our OneConnect OCe 12000 family of 10Gb Ethernet high-performance networking solutions further demonstrates our intention to participate in the high performance computing space with low latency Ethernet technology and value-added software offerings.

Now, let me wrap up. I'm really proud of what the Emulex team has accomplished in fiscal 2012, in particular delivering record revenues and growing EPS even faster. And I look forward to the new fiscal year with all of the new capabilities we will be bringing to the market to help customers unlock the value of converged networks, as I/O factors to be an increasingly strategic element of any cloud, HPC or enterprise data center.

Now, let me turn it back to Jim for some closing comments.

James M. McCluney

Chief Executive Officer and Director

Well, thanks, Jeff. So to summarize, despite uncertain IT spend and a bit more muted next generation server launches, we still wrapped up the fiscal year with record revenues of \$502 million, kept gross margins relatively stable, lowered operating expenses and sustained a strong balance sheet. Looking forward, while a meaningful recovery in IT spending remains elusive, we continue to see the Romley transition as a positive catalyst for us. And that, coupled with a great position in 10Gb Fibre Channel, will give us an opportunity to continue to outpace the competition and win share in our core markets, a continued growth in NCP as a reflection of this. Strategically, as Jeff pointed out, we're again focused on expanding our addressable markets through new partnerships and internal innovations. I'm excited by our prospects and look forward to reporting on our progress over the coming quarters.

So with that, Jeff, Mike and I are ready to take your questions. Operator?

Question and Answer

Operator

[Operator Instructions] And our first question will come from Jayson Noland from Robert Baird.

Jayson Noland

Robert W. Baird & Co. Incorporated, Research Division

Mike, the gross margin guidance, was that for F '13?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

That's for the year, yes.

Jayson Noland

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Robert W. Baird & Co. Incorporated, Research Division

And that's down a bit year-on-year with 10GbE and mix, I assume?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

That's correct.

Jayson Noland

Robert W. Baird & Co. Incorporated, Research Division

And it looks like if I moved to the midpoints, you're modeling OpEx up into F Q1, is that right?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

Yes. We expect that the patent litigation expenses will be a little bit higher and then just a little bit of spending is higher in Q1 in G&A, primarily due to the timing of audit and our year end.

Jayson Noland

Robert W. Baird & Co. Incorporated, Research Division

What drove OpEx down so sharply into F Q4?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

Fourth quarter, we benefited from actually the patent litigation expenses were lower than we had modeled for. They came in less than \$1 million. And then just overall, we were being very cautious in terms of what we were spending in really all the functional areas.

Jayson Noland

Robert W. Baird & Co. Incorporated, Research Division

Okay. And last topic for me, 10GbE, in our model we've got F Q3 at about \$27 million, F Q4 at \$21 million, and is that just lumpy with the Romley rollout?

Jeffrey W. Benck

President and Chief Operating Officer

Yes, this is Jeff. We did talk about -- it was down a bit as we have predicted. We did see quite a strong March quarter, pretty pleased with that. When you look at the first half in aggregate, it was a strong first half for us, we are looking for strong sequential growth into the first quarter as you look at the go forward. But I think you're in the right direction.

Jayson Noland

Robert W. Baird & Co. Incorporated, Research Division

And sounds like you've got decent visibility for at least a quarter, Jeff, there?

Jeffrey W. Benck

President and Chief Operating Officer

Yes. We have decent visibility, and we're pretty pleased with. The initial Romley take-up, we said that customers ordered in front of that. We saw a little bit of a pause but we're pretty happy with the backlog right now in the quarter.

James M. McCluney

Chief Executive Officer and Director

Yes, we think that [indiscernible] we've gained market share over the last fiscal year. Not all the results are out yet but based on what we're seeing so far, the momentum just continues.

Operator

And next we'll go to Keith Bachman from Bank of Montreal.

Keith F. Bachman

BMO Capital Markets U.S.

I had a couple too. Mike, just to follow on Jason's comment on OpEx. Did you take a reversal or something on the stock-based compensation -- is that to help lower that number? Were those any kind of change in accruals?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

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No. The stock-based compensation is a number that we exclude from the non-GAAP number. So the numbers that I was talking about in Jason's question was specifically on the non-GAAP numbers.

Keith F. Bachman

BMO Capital Markets U.S.

Okay. Could you give us any sense because OpEx was down so much sequentially. As we look out over the next couple of quarters, is it kind of \$59 million run rate? Is that the way we should be thinking about it? Not just September but a little longer run rate even in December?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

Yes. That's pretty much the area that we've been running. We've been running a little bit below \$60 million. In the March quarter, you see it tick up because of payroll taxes starting over which might take it up a little bit about \$60 million. But based on where we're at today, we had a terrific quarter in terms of OpEx as a percent of revenue in the fourth quarter and we're driving the management expenses to keep it below 60% of revenue -- operating expenses below 50% of revenue on a non-GAAP basis throughout fiscal '13.

Keith F. Bachman

BMO Capital Markets U.S.

Okay. Then just another detail question. Mike, did you say share count 91.5 and if I did hear that correctly, why is it going up?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

The increase is related to the issuing of the shares related to the second milestone in the [indiscernible] acquisition from 1.5 years ago.

Keith F. Bachman

BMO Capital Markets U.S.

All right. Right, okay. Then my final one is taking a step back look and I think you said Ethernet was down a bit. It seems a bit more than a bit. It's by my Math it's 18%. If we look out over the next couple of quarters, what do you see as a sustained growth rate given that you now have some meaningful compares? And then if you could also just talk about the competitive dynamics here with not only Q but the other folks and how you see the pricing changing potentially over the next couple of quarters as more people are now engaged in the market? And that's it for me.

Jeffrey W. Benck

President and Chief Operating Officer

So when we look at the compounding growth rate, it's 37% over the next few years for the 10Gb market. We see the opportunity to grow faster than that in the near term as it will obviously over time it will come down a bit. Jim already talked about, as we looked at the first half of the year, we were pretty pleased with the growth rate being about 50% year-over-year. And then, when you look at the second half, a lot of the Romley systems are now out in the marketplace, some of the high-end Romley systems and some UNIX platforms haven't transitioned to the next generation. So you'll see some of that in the next few quarters, which will be a catalyst for more 10Gb adoption. But when it comes to competition, we like the position that we have. We -- pricing has been pretty stable. Most of this is -- the OEM business obviously is negotiated well in front of the launches and the prices and the takedowns and stuff were sort of a built-in and we kind of know where those sit. There is a competitive market. We know there'll be opportunities to engage on a deal by deal basis. But haven't really witnessed anything that's out of the ordinary there for that market.

James M. McCluney

Chief Executive Officer and Director

Yes, I don't think the competitive dynamic has really changed that much for this. We're competing against the same guys for the LOM business and the same guy for FCOE, really. And I think we're doing pretty well in that regard.

Operator

We'll now take a question from Harsh Kumar from Stephens.

Harsh N. Kumar

Stephens Inc., Research Division

Question on OpEx. What kind of revenue level can you sustain at \$60 million OpEx and I wanted to be clear in understanding this. Is the plan to keep it at 50% of revs or you're kind of managing on an absolute dollar basis at around \$60 million going forward into fiscal '13?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

We're focusing on it on the absolute dollar spending level. But we think based on where we're at, that drives us to be under 50% of revenue. And it doesn't break directly at the end, you've followed us for a while, we got a very OEM based business and our expenses, we don't a lot of expenses that vary directly with revenue. In fact, we have very few expenses that vary directly with revenue. So I think we really feel that depending on how fast Romley ramps with 10Gb and now with 16Gb that we can sustain this level of spending and support higher revenue levels.

Harsh N. Kumar

Stephens Inc., Research Division

Fair enough, that's helpful. And then wanted to get some clarity into your September guidance, which is obviously, I mean, are looking very good relative to your competitors. Could you maybe help us understand in September the split between 10Gb versus Fibre Channel if there's any particular piece of that that's moving in a very abnormal manner than the other?

James M. McCluney

Chief Executive Officer and Director

Well, I think, we're -- as I mentioned on my prepared remarks, we do see HSP grow into the quarter. I think that NCP certainly. But we expect a little bit of normal seasonality in Fibre Channel in the September quarter. So a lot of the growth there is coming from our 10Gb products. As I mentioned and we actually mentioned in the last call as well is we'll get some -- we got a lot of headwinds on SCP as we come off some end of life purchasing that happened in the June quarter.

Jeffrey W. Benck

President and Chief Operating Officer

The only thing to maybe to add to that is we are now shipping 16Gb Fibre Channel so that can be a catalyst for us as we look at the second half and it's early days but having all these customers in market now and having the time-to-market advantage feels pretty good in Fibre Channel space.

Harsh N. Kumar

Stephens Inc., Research Division

That's very helpful. And you talked about a very interesting thing, the HPC opportunities sort of replacing InfiniBand in certain applications. What timing should we think about if possible, any color on that? Any wins, any interesting partners, any kind of color would be helpful.

Jeffrey W. Benck

President and Chief Operating Officer

Yes, I got a couple of things to talk about there. We are starting to put offerings in that space. We announced a new product line, an NX product line, it's a low latency product line with some customization for specific verticals and we're now able to do things like video pumper, entertainment and media. We're able to do a Sniffer for government installations. We're able to do low latency, Hyper due to trading applications with that stack. We did partner with a company called Myricom in that space. It's a new partnership there that we're pretty excited about working on some joint solutions. But going beyond that, what I talked about in the earning remarks was this notion of RDMA over Converged Ethernet is really a unique opportunity. We've had a number of customers that are in the web and cloud space that has been asking us about this as an alternative to native InfiniBand and while we're a little bit early there, we are putting a lot of investment in that segment and be a great growth opportunity because there's a lot of high performance computing solutions being deployed. We're not seeing InfiniBand so much in the storage space. I know there's been a lot of talk about it. We're seeing really just in the clustered high-speed networking space it's in those areas it's doing well and we know Ethernet, particularly as it gets to 40gb, which is not as far away as you might think, 40Gb even thinking into next year, that's going to be a meaningful alternative to the very dominant position that the one guy that plays InfiniBand has today. So that's something that this gives us an explicit focus for us so we just wanted to point that out to you guys.

Operator

And we'll now go to Paul Mansky from Cantor Fitzgerald.

Paul H. Mansky

Cantor Fitzgerald & Co., Research Division

Kind of going back to 10Gb for a minute. Could you provide us whether precise or general, any type of color on the mix of the stands today between LOM and CNA? And then I've got a couple of follow-ups.

Jeffrey W. Benck

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President and Chief Operating Officer

Probably, we can give you a better mix on chip versus card, and we're now seeing our card business actually kind of out -- be larger than our chip business. We haven't broken down all the categories. We're seeing both SCOE and NIC and LOM, all variants, including iSCSI shipping there, but I know there is a lot of focus on, "Is it all going to go to chip?" As we predicted, we're seeing the card business take up nicely and kind of expect more of the same with Romley. Although, we do have more chip down there, so that side will grow as well, but we're pretty happy with the balance in that business, Paul.

Paul H. Mansky

Cantor Fitzgerald & Co., Research Division

Did the card business grow sequentially?

James M. McCluney

Chief Executive Officer and Director

Yes, it did.

Jeffrey W. Benck

President and Chief Operating Officer

Yes, it did.

James M. McCluney

Chief Executive Officer and Director

Yes, I think if you'd remember back when we launched the [indiscernible] platforms, we got an initial surge of chip based business, and then the card business started to take off. So we ended up last year almost a bit more than 50-50 card to chip, and I think we'll see a little bit of surge with Romley that will be chip based and then, particularly on rack-based servers, I think we'd expect a higher I/O penetration, so you might even see more card business coming from the rack-based servers as well for the back standard make on FCP.

Paul H. Mansky

Cantor Fitzgerald & Co., Research Division

Right. Obviously, what I'm just trying to get back to the degree to which any OEM -- initial OEM inventory pre-build, if you will, was the primary corporate on the sequential performance in Ethernet. Now, can you refresh us -- obviously you cleaned up some of the litigation issues on the 16Gb side. Can you refresh us on where we stand vis-à-vis 10GbE in that sunset list, where are we in the process? How are you looking at your risks on that side of the business?

James M. McCluney

Chief Executive Officer and Director

Well, there's a few things there, as you know, Paul, I think we have most of our current customers on the sunset list there but Broadcom is free to challenge that up till the end of this month August 30. And the challenges depend on any evidence of when our OEMs qualified their product and when we signed the production orders and we're getting great cooperation from our customers in providing that evidence, and we're obviously beginning to slowly work to respond to any challenge there. We do have a retrial on one of the patents that's scheduled for -- that wasn't decided on fully by the jury in the last trial. And that retrial is in April 2013. Obviously, the partial settlement, where we announced removed a lot of things from the retrial, so it's a bit simpler now. And as we did before, we'll really vigorously defend our position in the retrial. And obviously, a lot of the chip redesigns we're working on, will be coming out around the time we're preparing for that retrial as well, and work on the mitigation's in full stride there with the intent obviously, and plan to get the redesign product ahead of the sunset period. So a lot of activity, tremendous support from our suppliers and customers alike really [indiscernible] to get our new product into the market.

Paul H. Mansky

Cantor Fitzgerald & Co., Research Division

Thanks for that. And then lastly, I guess by my math, you have about 30% of your market cap in cash at this point. I would imagine you're probably wanting to hold on to some of that in case there's any type of future payment that might be required. But can you talk through just your general thought process around that use of cash? Looks like it's been probably 9 months or so since we've been in the market buying stock.

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

Yes. Well, as I mentioned in the prepared remarks, the payments for the partial settlement was in July, so that will be reflected in our Q1 numbers. We do expect to be cash positive, so we're expecting that within the range of our guidance, we should execute one with about \$180 million in cash. I think our position really hasn't changed. We still

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think that the best use of cash for shareholders is to grow and expand our business, and we're certainly making investments internally, as Jeff talked about in both markets that we're going after our new products. And then we have about \$22 million left available on our share repurchase. And so, yes, we see share repurchases as a good complement to good business execution and so we'll continue to look at both of those opportunities, both investing in the business and repurchasing stock.

Operator

We'll now take a question from Glenn Hanus from Needham & Company.

Glenn Hanus

Needham & Company, LLC, Research Division

Jim, could you comment a little bit on kind of your progress on all the respin activity and your confidence level in kind of making schedules so that there's no negative developments from a timing perspective, can you start there?

James M. McCluney

Chief Executive Officer and Director

Yes, sure. Well, obviously we've been working on the mitigation and redesigns for quite a number of quarters now, and there's a lot of hard work going in to make sure our customers have continued supply and we get the redesigned chips available before the end of the sunset period next year. And we're putting a lot of effort and a lot of experts got their eyes on this one to make sure the redesign is very, very effective. And as I said, we're getting great cooperation from our suppliers, as well as customers to make this a reality for us, and I think, it's a big focus for us but we've got the right people on it and working hard and we're spending the money we need to, to make sure we're successful.

Glenn Hanus

Needham & Company, LLC, Research Division

Can you guys comment a little on kind of the potential down the road for traction within the Web 2.0 space and as they migrate eventually to 10 Gigabit Ethernet, what is -- where are you in terms of potentially cracking that space?

Jeffrey W. Benck

President and Chief Operating Officer

We certainly, through our current OEMs, they're pursuing business there so we can participate that way, we also have relationships with a lot of large web giant end users as you might expect. The injunction under the E3 product did slow us down a bit in that segment because not all of the customers were deployed there. So to be fair, that did slow us down. But we're -- I think, developing some very interesting technologies that customers are very excited about, as well as respin products and the modification make in recurrent products. And while we could participate today with OEMs leading that, we see good opportunity there and that was a little bit. We can go after business in that market right now with NX products that we just launched in partnership with Myricom. So we expect we hit some near-term revenue with that. But some of the new things like RDMA over Ethernet or Converged Ethernet are going to provide us, I think some pretty exciting opportunities as we get into 2013 and more adoption starts to shift in that space. Today, a lot of the web giants are still on 1Gb. But they're certainly looking at 10Gb and starting to go, and you've seen a few pops where a few of those clients have moved there and driven some pretty good opportunities for 10Gb providers in the space.

James M. McCluney

Chief Executive Officer and Director

Yes, I think, our road map I think will be very appealing to the cloud as well as HPC communities.

Glenn Hanus

Needham & Company, LLC, Research Division

Can you comment on the target side? What is the kind of the ramp look like? When will that really start to kick in and kind of be noticeable from a revenue standpoint?

Jeffrey W. Benck

President and Chief Operating Officer

Yes, sure. On the target side, I kind of mentioned it in our remarks. We'll start to ship 16Gb target to customers this year. I know there's been comments about it being a 2013 event for someone else but for us, we expect to launch target customers this year so we're -- while I don't expect we'll see a ton of revenue there-- just getting those launched and out. And we've also, as you can imagine, been feeding a ton of customers with a 15Gb multi-fabric product for the target application opportunity and pretty excited about the number of design wins we already have there. So I think it'll be more material in 2013, but we're starting that activity now. We're going to launch some people that we'll update you in the coming quarter or so year -- you'll hear before the end of the year on the progress there. But we're feeling pretty good about it. As you know, we've been in target a long time but one of our biggest

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competitors stepped away with the transition to 16gb and SCOE, that's really providing a jump ball versus us and our biggest Fibre Channel competitor, and being 6 to 9 months ahead is just a great opportunity for us to go grab a bunch of wins in that space.

Glenn Hanus

Needham & Company, LLC, Research Division

And lastly, just a kind of detail modeling question. The advanced tech kind of lift up this quarter, how should we be modeling that segment? And then did you say, on the Fibre Channel side, you would be a little bit better than seasonal or seasonal?

James M. McCluney

Chief Executive Officer and Director

I think NCP overall will be better than seasonal but that's going to be predominantly driven by 10Gb. And in ATP, it's a collection of a bunch of smaller pieces of the business, including the baseboard management controllers so it tends to vary from quarter-to-quarter. It was, I think, it was up pretty nicely in Q4. We expect it to be down a little bit in Q1.

Operator

[Operator Instructions] And we'll take a follow-up question from Harsh Kumar from Stephens.

Harsh N. Kumar

Stephens Inc., Research Division

Just wanted to get an understanding on how we should think about legal expenses. I know you have a trial coming up in April 2013. But between now and then, what kind of level should we think in terms of legal expenses?

Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

For the part related to that retrial, we expect that it's going to be between \$1 million and \$2 million a quarter. It came a little bit lower than that in Q4. But we expect activity will pick up a little bit over the next couple of quarters going into that April -- April date.

Harsh N. Kumar

Stephens Inc., Research Division

Okay, fair enough. And could you talk about the timing of the work around chip solution as well? When would we get sort of first glimpse or results or any kind of indication if it's on track, on plan or working or not?

James M. McCluney

Chief Executive Officer and Director

I mean, we could tell you that things are on track today. Jim didn't go into too much detail there. Of course, these are kind of unannounced products, so we're not going to give you probably every milestone. You can be fairly confident that we've got a very detailed blow-by-blow, step-by-step project management process and we've got a ton of resource focused on this. But it's a little tough given the competitive environment to give you every in and out other than to say things are on track. We're driving towards the transition that needs to happen with the sunset, as Jim talked about before. So from that standpoint, you probably won't get quite as much visibility because of the competitive nature and the unannounced nature. But the work's been underway, as Jim said, for quite some time. Things are progressing to our plan and we'll have increasing confidence as we get there -- as we get to tape out and things like that. We may share some more milestones but we'll have to see how that plays out.

Harsh N. Kumar

Stephens Inc., Research Division

And then what is the timing of that tape out or the final chip? Is that the end of the year or early part next year or before that?

James M. McCluney

Chief Executive Officer and Director

We've got -- I think, Jeff's been plain but don't want to be rolling out our detailed schedules here. We wouldn't normally do that with any chip, but needless to say the plan is to get working products to our OEMs before the sunset period.

Operator

And at this time, we have no further questions in the queue, and I'll turn the call back over to Mike Rockenbach for closing comments.

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Michael J. Rockenbach

Chief Financial Officer, Principal Accounting Officer, Executive Vice President, Secretary and Treasurer

Thank you, operator. And thanks everyone for your participation in our fourth quarter 2012 conference call. Before I wrap up tonight, just wanted to let you know that we'll be attending quite a number of conferences in the upcoming -- just in the next few weeks. We start off next week on August 11, we'll be at the Oppenheimer conference in Boston. September 4, we'll be at the Citi Technology Conference in New York. On September 11, we'll be presenting at the Deutsche Bank conference in Las Vegas, and then later that week, on September 13, we'll be at the ThinkEquity conference in New York City. And then we'll be back in New York the following week for the Credit Suisse conference on September 20. So hopefully you will be able to join us at one of those upcoming investor events or on our first quarter earnings call in April. So thank you, and good night.

Operator

And that does conclude our conference for today. Thank you for your participation. You may now disconnect.

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