

Viavi Solutions Inc. NasdaqGS:VIAV

FQ4 2024 Earnings Call Transcripts

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S&P Global Market Intelligence Estimates

	-FQ4 2024-			-FQ1 2025-	-FY 2024-			-FY 2025-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.07	0.08	▲14.29	0.09	0.32	0.33	▲3.12	0.47
Revenue (mm)	251.83	252.00	▲0.07	252.70	1000.33	1000.40	▲0.01	1053.01

Currency: USD
Consensus as of Aug-06-2024 12:08 AM GMT

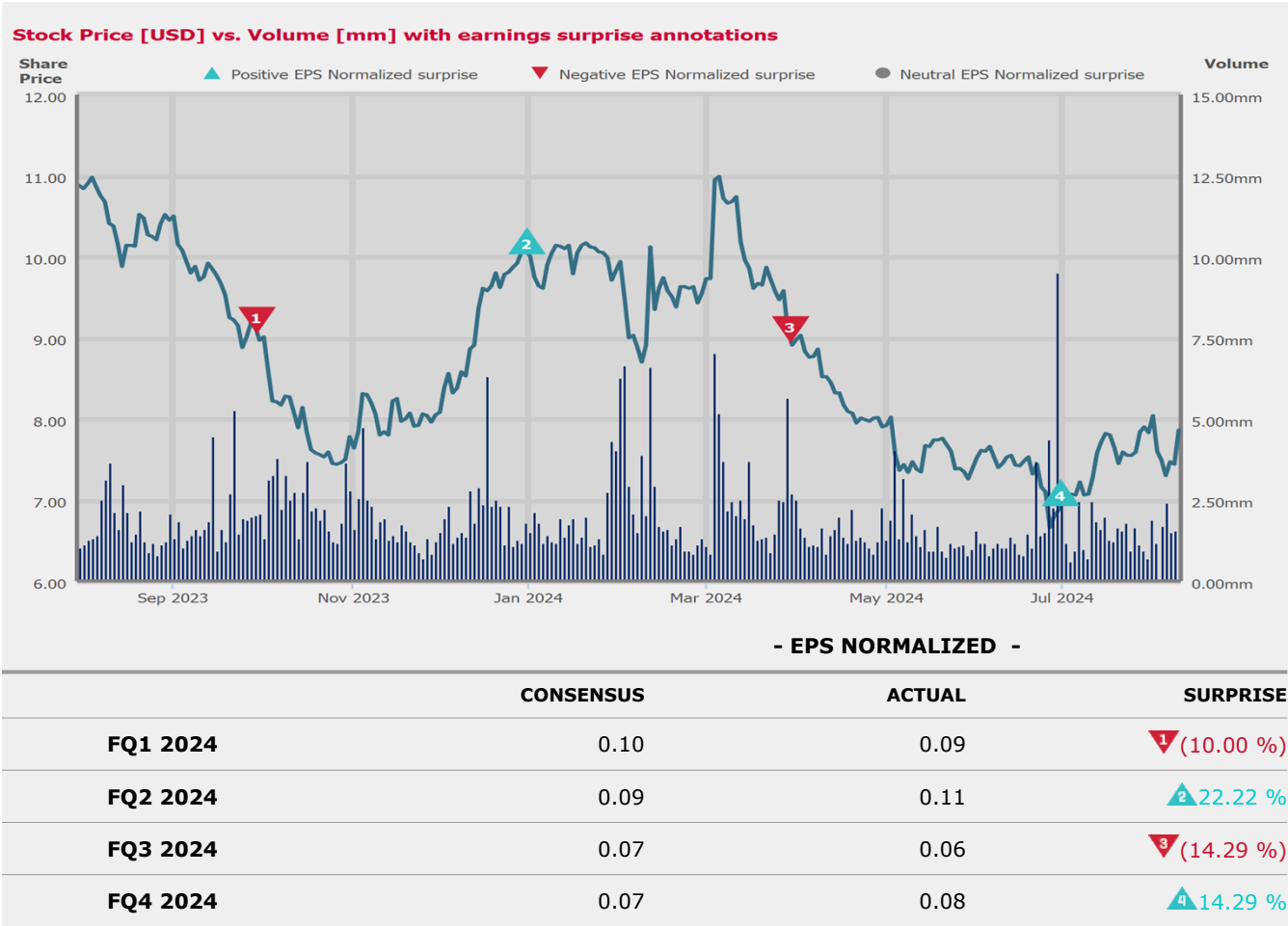


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Call Participants

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Presentation

Operator

Hello, everyone. My name is Emma, welcome to the Viavi Solutions Fourth Quarter and Full Year 2024 Earnings Call. [Operator Instructions] I will now turn the conference over to Vibhuti Nayar, Viavi Solutions Head of Investor Relations. Please go ahead.

Vibhuti Nayar

Director of Investor Relations

Thank you, Emma. Good afternoon, everyone, and welcome to Viavi Solutions Fourth Quarter and Full Year 2024 Earnings Call. My name is Vibhuti Nayar, Head of Investor Relations for Viavi Solutions. And with me on today's call is Oleg Khaykin, our President and CEO; and Ilan Daskal, our CFO.

Please note, this call will include forward-looking statements about the company's financial performance. These statements are subject to risks and uncertainties that could cause actual results to differ materially from our current expectations and estimations. We encourage you to review our most recent annual report and SEC filings, particularly the risk factors described in those filings. The forward-looking statements, including the guidance that we provide during this call are valid only as of today. Viavi undertakes no obligation to update these statements. Please also note that unless we state otherwise, all results discussed on this call, except revenue, are non-GAAP. We reconcile these non-GAAP results to our preliminary GAAP financials and discuss their usefulness and limitations in today's earnings release. The release as well as our supplemental earnings slides, which include historical financial tables, are available on Viavi's website at www.investor.viavisolutions.com. Finally, we are recording today's call, and we will meet the recording available on our website by 4:30 p.m. Pacific Time this evening.

Now I would like to turn the call over to Ilan.

Ilan Daskal

Executive VP & CFO

Thank you, Vibhuti. Good afternoon, everyone. And now I would like to review the results of the fourth quarter of fiscal year 2024. Net revenue for the quarter was \$252 million, which was at the midpoint of our guidance range of \$246 million to \$258 million. Revenue was up sequentially by 2.4% and on a year-over-year basis, was down 4.4%. Operating margin for the fourth quarter was 10.9%, which was above the midpoint of our guidance range of 9.5% to 11.8%. Operating margin increased 160 basis points from the prior quarter and on a year-over-year basis, was down 80 basis points. EPS at \$0.08 at the high end of our guidance range of \$0.06 to \$0.08 and was up \$0.02 sequentially. On a year-over-year basis, EPS was down \$0.02. For the full fiscal year, revenue was \$1 billion, down 9.6% on a year-over-year basis primarily due to conservative spend by service providers and NEMs. Operating margin for the full year was 11.5%, down 410 basis points from fiscal year 2023 and full year EPS was \$0.33, down \$0.22 from the prior year, primarily due to lower year-over-year revenue.

Moving on to our fourth fiscal quarter results by business segment. NSE revenue for the quarter came in at \$182.2 million, which is at the lower end of our guidance range of \$179 million to \$189 million. And on a year-over-year basis, NSE revenue was down 7.9% for the quarter. NE revenue for the fourth quarter was \$158.5 million, which is a 9.7% year-over-year decline as a result of continued conservative spend by service providers and NEMs. SE revenue was \$23.7 million and up 5.8% from the same period last year, partially supported by revenue that was pushed out from Q3. NSE gross margin for the quarter was 62.1%, which is flat on a year-over-year basis. NE gross margin was 61.3%, which is a decline of 40 basis points as compared to the same period last year. SE gross margin was 67.5%, which is an increase of 190 basis points from the same period last year and was driven by product mix. NSE's operating margin for the fourth quarter was 1.8%, which is an improvement of 360 basis points sequentially and 400 basis points lower than the same period last year. NSE's operating margin was at the low end of our guidance range of 1.4% to 3.6% due to lower revenue.

OSP revenue for the quarter came in at \$69.8 million, which was above the high end of our guidance range of \$67 million to \$69 million and was up 6.2% on a year-over-year basis as a result of strength across all products. OSP gross margin was 53%, which is an increase of 640 basis points from the same period last year and was primarily driven by higher revenue, favorable product mix and production ramp at our new manufacturing facility in Chandler. OSP's operating margin was 34.8%, which is up 50 basis points sequentially and 530 basis points increase on a year-over-year basis as a result of the higher gross margin fall through. OSP's operating margin exceeded the high end of our guidance range of 31% to 34%.

Moving on to the balance sheet and cash flow. Total cash and short-term investments at the end of Q4 was \$496.2 million compared to \$486.1 million at the end of the third fiscal quarter of 2024. Cash flow from operating activities for the fourth quarter was \$26.2 million versus \$23.5 million in the same period last year. During the quarter, we purchased 1.3 million shares of our stock for about \$10 million. For the full year, we purchased 2.3 million shares for about \$20 million. We have approximately \$215 million remaining under our current authorized share repurchase program. The fully diluted share count for the quarter was 224.2 million shares, down from 224.6 million shares in the prior quarter and versus 225.5 million shares in our guidance for the fourth quarter.

CapEx for the quarter was \$3.8 million compared to \$7.4 million in the same period last year when we were completing the construction of our new facility in Chandler. In June 2024, we initiated a restructuring and workforce reduction plan to improve operational efficiencies and better align with the current business needs. We expect approximately 6% of our global workforce to be impacted and estimate to incur approximately \$15 million of restructuring charges in connection with this plan. As a result of this initiative, we anticipate to achieve by the end of fiscal 2025 an annualized cost savings run rate of approximately \$25 million, which will mainly benefit our operating expenses.

Moving on to our guidance. We expect that the first half of fiscal 2025 will continue to experience a conservative spend environment by service providers and NEMs. That said, we believe that we are nearing the bottom of the down cycle, and we expect a gradual recovery in demand in the second half of this fiscal year. Given the lingering softness, we are guiding for the first fiscal quarter of 2025 revenue in the range of \$235 million and \$245 million. Operating margin is expected to be 10.8%, plus or minus 90 basis points and EPS to be between \$0.05 and \$0.07. We expect NSE revenue to be approximately \$164 million, plus or minus \$4 million, with a breakeven operating margin plus or minus 100 basis points. OSP revenue is expected to be approximately \$76 million, plus or minus \$1 million, with an operating margin of 34%, plus or minus 100 basis points. Our tax expenses for the first fiscal quarter are expected to be about \$8 million, plus or minus \$500,000 as a result of jurisdictional mix. We expect other income and expenses to reflect a net expense of approximately \$3.5 million, and the share count is expected to be about 224.2 million shares. With that, I will turn the call over to Oleg. Oleg?

Oleg Khaykin

President, CEO & Director

Thank you, Ilan. Viavi end market spend environment continues to be conservative, particularly the North American service providers. Despite these headwinds, our revenue came in at the midpoint of our guidance, with stronger OSP revenue, partially offsetting weaker NSE demand. Our EPS was at the higher end of our guidance range. Starting with NSE. The fiscal fourth quarter NSE revenue came in at the lower end of our guidance range. NSE revenue declined 8% on a year-over-year basis, driven by the softer demand from service providers and wireless NEMs. We believe the decline in NSE demand is bottoming out, and we should start to see a recovery in the second half of the fiscal year. A bit more color on that. The first is field instruments demand remained largely at the maintenance levels due to the absence of major network build-outs and upgrades by Tier 1 service providers, particularly in North America. That said, the investment in data center fiber internetworking by Tier 2 operators, together with recent comments by major service providers regarding their fiber plants leads us to expect a pickup in field instruments demand in the second half of fiscal 2025.

Our wireless demand continues to be impacted by sharply reduced R&D and production CapEx spend by major wireless NEMs to have reduced investments in response to significant cutbacks in 5G deployment by wireless operators. One positive recent trend we are seeing is the emergence of many new customers

pursuing [ORAN] development, however, their cumulative spend is still relatively small. Other parts of NSE are faring much better. Fiber lab and production demand was slightly up. We expect the upcoming transition to 1.6 terabits and ramp of PCI Express 6.0 to drive recovery and growth during the fiscal '25 for Fiber 11 production. Mill/Aero business continues to be a bright spot, seeing year-over-year growth in revenue driven by strong customer demand for communications, avionics and positioning, navigation and timing products. We expect this business segment to enjoy strong demand throughout fiscal '25.

SE segment grew year-on-year, helped by enterprise orders that were pushed out from Q3. We are seeing a lot of interest in our AI Ops products and expected to be a growth driver for fiscal '25 and beyond. As we look at Q1 fiscal '25, we expect a seasonally weaker demand driven by similar dynamics as in Q4. Continued demand weakness from the service providers and wireless NEMs leading to overall weaker NE and seasonally weaker SC revenue, offset by continued strength in fiber 11 production and mill/aero business. Looking ahead at fiscal '25 for NSE, we expect the conservative spend environment to persist for the remainder of calendar '24 and a gradual demand recovery in the first half of calendar '25.

Now turning to OSP. The fiscal fourth quarter OSP grew on a year-over-year basis, mainly driven by higher demand for anti-counterfeiting and 3D sensing products. Overall, OSP results exceeded the higher end of our guidance range. Looking ahead, we expect OSP to be sequentially up in the September quarter, mostly driven by seasonally stronger demand for 3D sensing products. Overall, we expect fiscal '25 OSP demand to be similar to fiscal '24.

To summarize, the fiscal '24 was a challenging year for Viavi in the industry. While we expect the soft market environment to persist for the remainder of calendar '24, we anticipate the start of gradual recovery in first half of calendar '25. I would like to thank my Viavi team for managing through this challenging environment and express my appreciation to our employees, customers and shareholders for their support. With that, I'll turn it over to Vibhuti.

Vibhuti Nayar

Director of Investor Relations

We're ready for the Q&A, Emma?

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Ruben Roy with Stifel.

Ruben Roy

Stifel, Nicolaus & Company, Incorporated, Research Division

Oleg, thanks for the detail around how you're thinking about sort of the near-term environment and then the sort of first half of next calendar year. I guess, can you drill in a little bit on sort of how you're thinking about inventory levels at your customers, I guess, by field instruments and then also lab instruments. And then I had just 1 or 2 quick follow-ups.

Oleg Khaykin

President, CEO & Director

Sure. I mean there's really no inventory to speak of. I mean, all of our deliveries for field instruments to our customers are just in time and it's mainly coincides with whenever they are doing any kind of major expansion projects or technology upgrade or things like that. There's also obviously -- when I say we see our revenue at the maintenance level, there is this constant churn a big chunk of our quarterly revenue is just churn. And it's just basically a lot of large numbers, big installed base, the batteries die, equipment gets damaged, and they periodically replace whatever needs to be replaced. And it's been a fairly consistent number for the past several quarters, which makes me feel a bit better because it just shows you that the first thing customers come back to is they start replacing what's been damaged. And as they start looking at the major new projects and we've heard, obviously, from AT&T, but also we are seeing Tier 2 players like -- there was Lumen recently had a call and there's others. There's a lot of interest for developing fiber internetworking between all those hyperscale data centers. And these are the players that are actually running projects today and they're placing orders. And clearly, so from that perspective, I don't know to what extent they have equipment inventories for networking gear, but I imagine that is also winding down. And clearly, as they start talking about the -- resuming their expansion and technology upgrade that is what we view as a positive news for us.

On the 11 production, that is also pretty much just-in-time type business. So when an R&D organization sees a need for new equipment, and it usually comes in when they are developing next-generation product, they start placing orders in the fiber area and the high-speed compute area, high-speed computer is driving PCI Express 6.0 and the upcoming 1.6 terabits. I mean, the budgets are open and the CapEx is flowing, and we are seeing purely as soon as the equipment is available, they want it. So in that respect, we feel pretty good. But there's also probably further away in the second half of the fiscal year or first half of the calendar '25. The 1.6 terabits is flowing into the module manufacturing, and we're seeing a lot of interest the major AI players to drive upgrades in their contract manufacturing factories to be able to deploy 1.6 terabit modules and products. And for the first time, it's really the data centers that are driving the transition to the higher speeds rather than service providers.

When we saw 400 gig, 800 gig, they were driven by equipment vendors to service providers. This time, it's very much the data centers that are driving the transition to the higher speed speeds of the products. And that's why we're feeling much more bullish on our fiber lab production equipment. So that's kind of more color on those 2 areas.

Ruben Roy

Stifel, Nicolaus & Company, Incorporated, Research Division

Yes. Very helpful again. And you hit my follow-up on the 1.6 terabit side. So I guess then I'll shift over to just a quick follow-up for Ilan the restructuring. Ilan, you talked about the OpEx savings through the fiscal year. Maybe you can put a finer point on sort of how you're thinking about that -- between R&D and projects versus sales and marketing and how we should kind of think about modeling that through the year in terms of the savings as it hits the model.

Ilan Daskal*Executive VP & CFO*

Sure. So thanks for the question. And obviously, as I mentioned earlier in the prepared remarks, most of it will be a reduction of the overall operating expenses. We don't see any of our major R&D projects being impacted or delayed due to this initiative. So these are across the board of the operating expenses, but none of the initiatives that we drive in terms of development will be impacted. And also, as I mentioned earlier, the full realization will be by the end of the year. So it's more of a 2026 kind of net spend there.

Operator

Your next question comes from the line of Ryan Koontz with Needham.

Ryan Boyer Koontz*Needham & Company, LLC, Research Division*

Certainly appreciate your comments about 5G. That doesn't sound like it's coming back around anytime soon. I wanted to double-click a little bit on your comment around data center interconnect for fiber players. Are you seeing demand there from the data center operators who are leasing dark fiber or are they leasing actual connectivity and bandwidth from the service providers on a wholesale basis?

Oleg Khaykin*President, CEO & Director*

So I mean it varies across different data centers, operators. But I mean, for the biggest ones, they basically build data centers and then they pick a vendor who lay fiber and they lease those fibers from them. And what's a little difference is when a service provider lays a fiber, there's a lot of dark fiber and they generally don't connect the dark fiber until they need it maybe years later. What we're seeing with data center, they're laying fiber. And they also initially started doing the same thing, just lay the fiber, connect a few strands and I'm going to lease them. And then when I need it, you turn it on. What they're finding is that they need to turn on additional fibers and additional bandwidth comes a lot faster than everybody thought. And more importantly, it becomes also much more sensitive, the quality of performance of that fiber, right, in terms of the latency, the speeds and things like that. So they're actually putting pretty strict service level agreements as to what performance that fiber needs to deliver. And that actually plays very much to our strength because what they are realizing is traditional build fiber is fairly unreliable and you cannot turn it on as you need it, right?

So we are now working with the data center operators and with the people who provision fiber to bridge this gap to make sure as the fiber gets deployed, you actually characterize it and you know exactly what you're getting for. So -- and then you can monitor it throughout the life. And when you need to turn on the next wavelength, it happens very quickly, which usually means you actually connect everything. And you only -- and by just training on, it becomes a software switch rather than rolling a truck and starting to connect the fibers and then finding out that things may not work or things like that. So we are seeing the level of evolution and forethought in deploying fiber network truly changing the traditional paradigm that the service provider has been doing. And I guess it's the Tier 2 players who are responding more proactively to the demand of data center operators and they're the ones who are winning the business. And I think they view it as their new business model going forward.

Ryan Boyer Koontz*Needham & Company, LLC, Research Division*

And just following up on another big segment, to our -- within the broadband sector, I know that's been pretty depressed. You've talked about previously some pushouts in cable, are you seeing any signs of life in cable? And obviously, we're seeing -- I assume you're seeing some pushouts in fiber and [indiscernible] and these sort of things that will be driving the fiber access industry. Any comments around broadband?

Oleg Khaykin*President, CEO & Director*

Sure. The -- on cable, so the cable upgrade is underway. But unlike in the previous things where they would just buy everything in one quarter and just kind of roll it out. They are doing it over multiple quarters which leads you to a smaller bump up in demand within the quarter but on the other hand, it provides for a smoother shipment over the multiple quarters. And I think part of it is because since the fiber to the home players have slowed down or stopped their deployment, I think the pressure is a bit less. However, I saw comments and AT&T does appear to be serious about resuming their aggressive push fiber to the home next calendar year. I expect the competitive pressure on cable to accelerate, and we will probably see more aggressive spend by them as well.

And the other area that cable was concerned about is the fixed wireless. And so far, it has been -- has not been a factor in terms of competitive pressure on them to do anything. And as you pointed out earlier, I mean, as I said as well, 5G deployment, I think will be the last piece that's going to start recovering. And I think the earliest will be the end of our fiscal year or kind of middle of next year because I'm not seeing any kind of meaningful movement there. And in fact, all the major NEMs have really kind of gone into hibernation mode, where they are continuing to do kind of advanced research, but not much in terms of the accelerating new products to market.

Ryan Boyer Koontz

Needham & Company, LLC, Research Division

That makes a lot of sense. And just one last quick comment on the operations side. Let your inventory on your balance sheet was down quite a bit. Any comments around that? Are you able to kind of sell what you forecasted? And what will be driving the step down in inventory in-house?

Oleg Khaykin

President, CEO & Director

Well, I think the -- as we all know, during the supply chain shortage, you had to agree to a lot of product like kind of [indiscernible], noncancelable, nonrefundable, and of course, a lot of semi-companies have kind of shoved it all down our throats so we built up some component inventory. We have been pretty much working diligently all that inventory down. But also our anti-counterfeiting manufacturing, we are holding quite a bit of raw materials and now as the anti-counterfeiting demand is starting to come back, we've been consuming the raw material as well as the semi-finished goods and we've been bringing inventory more in line with our kind of current run rate demand. We haven't been buying much stuff. Let's put it [indiscernible].

Ilan Daskal

Executive VP & CFO

It's more to categorize it as a more normalized level now. I mean and it will now fluctuate a little bit more to revenue as opposed to kind of the prior cycle.

Operator

Your next question comes from the line of Mehdi Hosseini with SIG.

Mehdi Hosseini

Susquehanna Financial Group, LLLP, Research Division

Yes. The first one has to do, Oleg, can you tell us how the quarter progressed, especially in terms of booking? Was there significant erosion throughout different business units, service providers, CSPs and so forth? Or did you start a week and just carry through. And I have a follow-up.

Oleg Khaykin

President, CEO & Director

Well, the -- actually, I'd say a difference from the prior quarters, and I mean, what we are seeing is the forecast that we kind of assume early in the quarter largely [indiscernible]. So we've been seeing fewer decommits or cancellations. The only big cancellation we had in -- and it was not really cancellation, our major customer reduced their order by 1/3, which is on the wireless NEMs, that order came through,

actually, we would have beaten the high end of our guidance on NSE. And it was really a major wireless NEM decided to take a -- to take a -- less product because of slowness in the market. We don't generally track kind of rely on book-to-ship ratios because the way our market works, demand works, the June quarter and December quarter are usually stronger and we get a lot of bookings within the quarter. and the September and March are generally weaker, and we get a lot less bookings within those quarters. So I look more like -- the way I gauge the relative health of the funnel is that what kind of bookings we enter the quarter and expectations and how well do they hold up or there's a left to go. We forecast the bookings, and then we track how many of the bookings show up as they're supposed to show up. And the way it makes me feel a little better is they're actually showing up. Whereas before, that will get pushed out or get canceled. So I think the booking environment, while the revenue may be lower, the booking environment is now more predictable and more robust, so we can plan better or acquire.

Mehdi Hosseini

Susquehanna Financial Group, LLLP, Research Division

Great. And then if I just double-click on OSP. Should I assume that [indiscernible] sense of what is being reflected in the guidance for the September quarter, would that show any year-over-year growth?

Oleg Khaykin

President, CEO & Director

Are you talking which segment? The 3D sensing or anti-counterfeit?

Mehdi Hosseini

Susquehanna Financial Group, LLLP, Research Division

3D sensing.

Oleg Khaykin

President, CEO & Director

Well, the -- it's actually lower in revenue year-on-year because we have now going to the new ASP schedule. So there is a pricing road map, so the ASP is lower. The volumes are slightly the same, maybe a little higher, but the problem is the volume growth is not enough to offset the ASP erosion that I just want [indiscernible] for the next year. So -- but -- and of course, it's still very much driven by a single customer, which probably have a very high level of penetration of products. So it's very much driven by their demand and volumes.

One thing we are also noticing there that is positive. The demand is now being a little bit better linearized throughout the year. And I think it's mainly driven by contract manufacturers who don't want to be heavily overstressed in the September, December quarter and then having a lot less demand in the March and June but still, I think September, December quarter is a much higher volume. And one other development, I think we are now seeing kind of, if we call them signs of life or interesting new trends, mainly the China Android players are doing with the 3D sensing. It's still very small volumes, just a handful of platforms but if this becomes a major trend and adoption, this will be actually a big positive for us in 3D sensing. And there's also rumors that Samsung may be trying to make other go-ahead. But after having so many years of full start, I will hold off on that one as the outlook.

Ilan Daskal

Executive VP & CFO

It's about \$2.5 million year-over-year for the first quarter. So it would be the pricing, et cetera, that Oleg mentioned, but also we'll have to monitor the supply chain that Oleg just discussed and maybe it kind of more linearized and over the course of 2, 3 quarters, it will kind of offset itself.

Mehdi Hosseini

Susquehanna Financial Group, LLLP, Research Division

Sure. Just for proof of modeling, the implied midpoint of your guide implies about a 9% sequential growth in OSP. Is that driven by both 3D sensing and counterfeit?

Oleg Khaykin*President, CEO & Director*

Well, I think the anti-counterfeiting business is starting to rebound. I mean a lot of the inventories have been consumed. So we have a -- I mean there is an uptick in there, but also 3D sensing has a higher numbers, but you have to discount it for some of the ASP erosion. So you probably would have been closer to an \$80 million range between the churn but of course, it's -- both segments are doing better demand-wise, volume-wise than in the prior year. And when the anti- come for us it's very important for anti-counterfeiting to start recovering because that's where a lot of big irony is sitting in terms of the manufacturing assets. So clearly driving a better absorption on a stronger anti-counterfeiting demand has a bigger impact on the operating margin of the OSP business unit.

Operator

Next question comes from the line of Michael Genovese with Rosenblatt.

Michael Edward Genovese*Rosenblatt Securities Inc., Research Division*

I just have one question, which is, Oleg, you've spoken a lot about how AI and data center investment can improve or help field test over time. I just wanted to kind of more directly connect the dot on how it could help field test? And so is the Lumen announcement about their investment in AI? Is that key to the second half recovery or other things like that, do we expect other service providers to announce something similar? I guess there's a few questions in there, but if you could kind of run unit those thoughts, I would appreciate it.

Oleg Khaykin*President, CEO & Director*

Well, sure. I think all of that is goodness. Actually, those are all positive things. I mean, to be fair, I mean, Lumen to give them credit, even when they were really beaten down in the last 12 months, they've actually been -- when I talk about the Tier 2s being more aggressive, I think Lumen has been one of the more proactive and more innovative companies in that space in terms of how -- what technology they deploy and how they roll out their value proposition. And I mean, we like Lumen because they actually listened to a lot of good innovative ideas and they're one of the more innovative players in terms of implementing things that truly differentiate them from the your run-of-the-mill fiber operator. So I'm not going to say any more on that, but Lumen, they didn't just start it. They've been doing it for the past year, 1.5 years, even when they were beaten down into the pulp. They continued with the innovation.

Michael Edward Genovese*Rosenblatt Securities Inc., Research Division*

I guess just any more. I mean I guess you did touch on this a bit earlier, but any more color or comment a prediction on this AI investment, creating more, whether it's optical or fiber, whether it's [indiscernible] optical kind of core or fiber access demand? So that's why [indiscernible] Lumen there because it seems like their AI investments [indiscernible].

Oleg Khaykin*President, CEO & Director*

Yes. Because -- so what I was talking about is the -- in particular, if you look at 1.6 terabits. I mean, traditionally, driving from 10 gig to 100 gig, 100 gig to 400 gig, 400 gig, maybe to 800 gig, traditionally, the drive to adoption of the higher speeds was driven by NEMs supplying into service providers. 800 gig was kind of like mix between service providers and data centers, 1.6 terabits is being driven all by data centers. And what we are seeing the rate of fiber bandwidth consumption, whereas, let's say, service provider will lay a fiber and then maybe every couple of years, they would turn on another fiber strength and they generally only connect one and then they roll the trucks to connect the others as they need it. What we are seeing with data centers is a, more strands being enabled from get-go. They just may be sitting dark, but they actually pay for connecting all these strands so then as they need it, they turn

them up quicker. And the reason they are doing it is the time between lighting up fiber and lighting up the next fiber, the time is much, much shorter. And the -- as they see their traffic grow much faster than the service providers. So in that respect, I see them looking at the fiber interconnecting between their data centers are completely different than the service provider who would look for their metro and core network. And I view it as a positive for us because that basically means much more frequent changes and need for a much faster responsiveness.

Operator

Your next question comes from the line of Meta Marshall with Morgan Stanley.

Karan Juvekar

Morgan Stanley, Research Division

This is Karan Juvekar on for Meta. So first question, just on the NSE side, I know you're sort of expecting a conservative spend environment throughout the calendar year. I guess as you look into the first half of next year, where you expect some uptick, I guess, are you expecting sort of a step function recovery in revenues or a more gradual recovery? And I guess just parsing out between European and U.S. carriers, just any trends to be mindful in terms of how you're thinking about a recovery? I know North America is the most challenged today and how you expect the recovery there to play out?

Oleg Khaykin

President, CEO & Director

What you said service, what function -- does it mean like NE, NSE or?

Karan Juvekar

Morgan Stanley, Research Division

No, no, just the recovery being a step function or sort of more gradual.

Oleg Khaykin

President, CEO & Director

Step function. Got it. I think it's -- so look at it -- there's the basic things like field instruments. I think that's being a -- I would say, not a big step, but like lots of little steps because those are driven by projects. So I think it's a gradual recovery. And I would say, amazingly, Europe has not been that bad. Yes, they slowed down, but nowhere near as bad as North America. North America has been cricket basically for the last 2 years. So I think in terms of a step function, clearly, if AT&T will continue to proceed with their plans to accelerate and resume their fiber to the home, in a way, it will be a bit of a step function for the fiber instruments. And usually, if somebody as big as AT&T restarts deployment, it sends a shock through the industry, which means the cable guys are going to have to accelerate, the wireless may have to do something more because then it creates a nice competitive whirlwind that everybody needs to start responding. So generally, just when they stop spending everybody else stops spending, when they start spending, others are going to follow usually. So -- but I don't want to create expectation of a step function or I'd rather go with a gradual recovery in the base demand.

Where I see a greater acceleration is really the fiber 11 production, and we do think 1.6 terabits will be a big driver in the first half of next calendar year, okay? And in terms of the -- clearly, as North America starts to recover, I mean, Europe follows pretty quickly. But the good news is Europe never really -- did not really get down as much as North America. So I expect the recovery in Europe to be a bit more mild. But what's also really interesting is we're seeing a lot more aggressive plans in Latin America, which is you think always will be the last ones but they are actually, in many ways, been playing catch up, and we're seeing some of the more interesting opportunities, especially for our AI ops and some of the other products coming out of Central and South America as well. And Asia has been pretty solid all long.

Karan Juvekar

Morgan Stanley, Research Division

Okay. That's very helpful. And then I know you mentioned earlier that sort of on the OSP side, inventories are sort of depleted. But I just wanted to get a little bit more color on trends you're seeing there. What sort of drove the upside? Is it around inventory builds or new prints and just expectations on that moving forward that would be helpful?

Oleg Khaykin

President, CEO & Director

You're talking about our internal inventories, right, not the inventories of the service providers? Which inventories you're talking about?

Karan Juvekar

Morgan Stanley, Research Division

Like the OSP side, inventory [indiscernible].

Oleg Khaykin

President, CEO & Director

OSP, yes. So as I mentioned earlier, the -- we are seeing some recovery in the anticounterfeiting demand, and it's really driven -- I mean, a lot of the inventory that was built up in the channel during COVID because they also order a lot of material and products to keep on hand. Finally, a lot of it has been wound down and consumed. So the orders that are coming back is really more in line with the demand and consumption and less of the restocking or anything like that.

Operator

Your next question comes from the line of Tim Savageaux with Northland Capital.

Timothy Paul Savageaux

Northland Capital Markets, Research Division

A couple of questions. First, on the guide. I think if I heard you right, because you would expect to see kind of a double-digit million sort of sequential increase in OSP. And I guess you're saying you would have seen something closer to that were not for the ASPs in that comment about \$80 million or initially looking at you think maybe something -- so there's some negatives in the currency business, but it sounds like maybe not. Did I get that right?

Oleg Khaykin

President, CEO & Director

No, there's no negatives in the currency business. I think the people are just talking about 3D sensing demand. I mean we have a new pricing in place and clearly, with the ASP erosion, taken down some of the revenue because the volumes are not that much more than they were a year ago. So that was what I was talking about.

Timothy Paul Savageaux

Northland Capital Markets, Research Division

I guess that relative to last year, I was just talking sequential, but I think we're talking about the same thing. And a similar question on NSE coming down sequentially. It looks like there could be some seasonality that you see typically there. But is there any particular product or end markets driving that sequential decline in NSE for Q1 '25?

Oleg Khaykin

President, CEO & Director

I think it's really more seasonality. I mean just weaker demand. But I mean, clearly, we normally would have gotten some orders more -- I think I'd say wireless NEMs is probably one area where the demand is lower. And I would say just general, the service provider field instrumentation, just demand is weaker.

Timothy Paul Savageaux

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Northland Capital Markets, Research Division

Okay. And then back on kind of AI data center side, and I don't know if you break it out or look at it this way, but I think it'd be interesting to get a sense for within the -- any segments what sort of revenue level can you attach to data center overall or fiber-driven data center, whether that's 800 gig test going to 1.6 in lab and production? We assume a good bit of that is probably data center driven. And you've mentioned the potential for more field instrumentation driven by that. But if you had to take a swing at it, would you say data centers has the prospects of getting up towards 10% of your NE business over time or is it there now or some sort of order of magnitude?

Oleg Khaykin

President, CEO & Director

I'm not going to get into this thing -- I mean any number I give you will ultimately be as number anyhow. So I mean there's -- I don't think there's really any good research or understanding because I mean, the one thing I can tell you is the 1.6 terabits is -- next year will be driven all by data center, right? Whereas when we went from 400 gig to 800 gig was primarily driven by carriers and NEM supplying carrier. So I think -- I don't really try to supply this data center or card. I mean, fundamentally, it's all driven by technology. But I would just say that 1.6 terabits will be driven by data center demand. I mean if you want to ascribe that revenue to that, I mean, maybe eventually, we -- as things stabilize, we can start doing segmentation on the end market use. But usually, the same line, just like for 800 gig, the line that was built originally for service providers ended up supplying data centers when the service providers start planning, you can't really -- because it's a multiuse technology. So we think of it more as to who will be the lead customer driving it. And for the first time, I think data centers will drive the next technology node.

And in terms of the build-out of the networks, it is still the service providers fiber, but it's a Tier 2 service providers who are providing those fiber interconnect between all the data centers rather than the big players like, say, AT&T or Verizon. So I mean, whether it's data center today or they take some of that fiber and give it to in the future for 5G towers, I mean it's a multiuse -- so we don't really sweat trying to figure out what's the end market demand.

Timothy Paul Savageaux

Northland Capital Markets, Research Division

Okay. I understand. Let me take one last desperate attempt question and say, Art, if you were to replace 800 gig with let's place data center in my question or AI data center with 800 gig might be a little bit easier to give us a sense of the size of your 800 gig business relative to your overall test business in network.

Oleg Khaykin

President, CEO & Director

I have the numbers, but now you're asking me to go into this segment reporting that we don't report because I mean there is a -- at any given time, we have a 400 gig, 800 gig, and now later this calendar year, we're going to have 1.6 terabits. I mean those things are just like sediment chart, these keeps -- one goes down, the other one goes back up and there is a substitution. So I don't think I'm going to go into that level of detail.

Operator

Your next question comes from the line of Mehdi Hosseini with SIG.

Mehdi Hosseini

Susquehanna Financial Group, LLLP, Research Division

A couple of housekeeping items. Given the fact that the \$25 million of annualized cost savings going to materialize second half of fiscal year '25. Should I keep the OpEx kind of flattish from here? And in flight OpEx for the September is \$120 million. And I'm just wondering how should I model that for the rest of the fiscal year?

Ilan Daskal

Executive VP & CFO

Generally, yes. There are several puts and takes. Obviously, some of it has to do with merit increase in variable employee costs. But generally, yes, you're right.

Mehdi Hosseini

Susquehanna Financial Group, LLLP, Research Division

Okay. And what about the fiscal year tax rate?

Ilan Daskal

Executive VP & CFO

So we guided for about \$8 million then for the remainder of the year, it will depend on the jurisdictional kind of mix. So obviously, as long as the North American kind of region will recover, then obviously, it lowers our effective tax rate. You can see that in the first quarter, it's still \$8 million, which is a higher-than-normal effective tax rate, but that's kind of the thinking.

Oleg Khaykin

President, CEO & Director

Yes. I think you should look at the absolute dollar amount of taxes because they're really driven by statutory kind of things -- and ironically, the more money we make, the lower percentage in taxes we pay because in North America, we have NOLs and a lot of other offsets that will effectively lower our tax rate.

Operator

This concludes our Q&A portion of the call. I turn it back to Vibhuti for final comments.

Vibhuti Nayar

Director of Investor Relations

Thank you, Emma. This concludes our earnings call for today. Thank you for joining everyone. Have a good afternoon.

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