Company: **Finisar Corporation**

Conference Title: **Finisar Corporation Announces Second Quarter Results**

Moderator: **Jerry Rawls**

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Operator: Good afternoon ladies and gentlemen and welcome to the Finisar Corporation Second Quarter Results Conference Call. Today's call is being recorded. And, at this time, I like to turn the conference over to Mr. Jerry Rawls, Chief Executive Officer. Please go ahead, sir.

Jerry Rawls: Thank you, Angela, and good afternoon everyone. We appreciate you taking the time to listen to our conference call today. A replay of this call should appear on our website within eight hours. An audio replay will be available for two weeks by calling area code 888-203-1112 for domestic or area code 719-457-0820 for international, then enter the ID number 7509499.

I need to remind all of you that any forward-looking statements in today's discussion are subject to risks and uncertainties, which are discussed at length in our annual and quarterly SEC filings. Actual events and results can differ materially from any forward-looking statements. In addition, the company undertakes no obligations to update any forward-looking information presented. Unless otherwise indicated, all results discussed today are on a non-GAAP basis. A complete reconciliation of our GAAP to non-GAAP results may be found in our earnings press release and in the Investor Relations section of our website.

We have prepared some slides for today's earnings call. You can view them by connecting to the Investor Relations page of our website at finisar.com. Click on Investors, then scroll down to Webcast Archives and click on it. You'll see a listing for today's Second Quarter 2017's Earning Call.

I am pleased to announce that Finisar achieved all time quarterly records for revenues and profits in our second quarter. We had a very good quarter. Revenues were $369.9 million, an increase of $28.5 million or 8.4% over the first quarter. This growth was primarily driven by strong demand for 100 gigabit per second transceivers. In addition, customer demand was also strong for wavelength selective switches and ROADM line cards.

Our gross margins improved significantly to 37.2% due to our favorable product mix and the leverage we achieved from our vertical integration with larger production volumes. The combination of revenues being at the higher end of our guidance range plus higher gross margins resulted in earnings per fully diluted share of $0.58, which is well above our Q2 guidance range. And now with that, I'll let Kurt review the rest of the numbers. Kurt?

Kurt Adzema: Thank you, Jerry.

Sales of telecom products increased by $9.7 million or 9.9% compared to the first quarter. This increase was due to higher sales of 100 gigabit transceivers, as well as wavelength selective switches and ROADM line cards.

Sales of datacom products increased by $18.8 million, or 7.7%, compared to the first quarter. This increase was primarily due to higher sales of 100 gig transceivers. Sales of 100 gig transceivers for datacom applications increased approximately 30% compared to the first quarter and more than 80% over the second quarter of the prior fiscal year. Sales of 40 gig transceivers were approximately flat compared to the first quarter.

In the second quarter, we had two 10% or greater customers. Our Top 10 customers represented 57.9% of total revenues compared to 60.2% in the first quarter.

Our non-GAAP gross margins improved to 37.2% compared to 33.1% in the first quarter, primarily due to favorable product mix in operational leverage from our vertical integration.

Non-GAAP operating expenses were $69.4 million, compared to $69.3 million in the prior quarter. Non-GAAP operating expenses as a percent of revenue decreased to approximately 18.8% of revenue compared to 20.3% in the first quarter.

Non-GAAP operating income was $68.3 million or 18.5% of revenue compared to $43.5 million or 12.8% of revenue in the first quarter.

Non-GAAP income was $65.2 million or $0.58 per diluted share, compared to $41.8 million or $0.38 in the preceding quarter.

Average diluted shares for non-GAAP purposes totaled 113.2 million.

For non-GAAP purposes interest expense for our $258 million of 0.5% convertible notes was approximately $323,000 in the second quarter. This interest expense is the only impact of these converts on a non-GAAP diluted earnings per share, as no shares are added to the fully diluted share count.

Interest and other income was approximately $500,000 in the second quarter and is expected to be at similar level in the third quarter.

Non-GAAP taxes for the second quarter was approximately $3.6 million. Non-GAAP taxes for the third quarter and the remainder of the fiscal year are estimated to be approximately 5%.

Cash and cash equivalents and short-term investments increased $32.5 million to $626.3 million at the end of the quarter.

Capital expenditures for the upcoming third quarter are estimated to be approximately $40 million. This elevated level of CapEx will continue in the fiscal fourth quarter as well.

Weighted average fully diluted shares for the third fiscal quarter are expected to be approximately 115 million for non-GAAP purposes.

If excluded from our non-GAAP results, a number of charges or benefits that were either non-cash or we consider outside our core ongoing operating results. These totaled $16.4 million in the last quarter. If you excluded all these items, as required under GAAP, we generated net income of $48.8 million or $0.43 per diluted share compared to net income of $23.9 million or $0.22 per diluted share in the first quarter.

That concludes my comments and I'll turn it back to Jerry.

Jerry Rawls: Thanks Kurt.

We continue to believe that the long-term growth prospects of our company and the optical communications industry are positive. Current worldwide demand for optical products is strong and we expect it to remain strong for a long time. Our upcoming third quarter should be another record quarter for Finisar. We anticipate that revenues will be in the range of $378 million to $398 million, primarily from increased sales of 100 gigabit per second transceivers.

We expect third quarter non-GAAP gross margins to improve again to approximately 37% to 38%. This increase will primarily come from a favorable product mix plus the operating leverage from our vertical integration. One partial offset will be the impact of one month of annual telecom price reductions that are typically effective January 1.

We expect operating expenses will be approximately $72 million in Q3 or about 18.6% of revenue.

Non-GAAP operating margins should continue to improve to approximately 18.5% to 19.5%.

Non-GAAP earnings per diluted share are expected to be in the range of $0.58 to $0.64 per share. This would be another new quarterly record for Finisar driven by our growing revenue and improving margins.

We continue to add capacity for a number of products. For QSFP28 in particular, we plan to increase capacity significantly in the third quarter and have plans to continue to increase capacity in the subsequent quarters. We are also adding capacity for the 100 gig and 200 gig coherent CFP2 ACO transceivers and the ROADM line cards for telecom and long haul and metro. We expect the qualification of these products by key customers in the next few months. In addition, we are also adding capacity for our wavelength selective switches. We believe that China will begin significant domestic deployments of ROADM's in calendar 2017. Finally, we are adding capacity over the next couple of quarters in our VCSEL laser fab in Allen, Texas. This will enable us to pursue several new consumer applications for 3D sensing.

Overall, we had an excellent second quarter and are expecting another one in Q3. I would like to thank all our loyal customers for their continued support and I would like to thank all of our 14,000 employees for their hard work, creativity, and attention to detail. I hope all of you listening to this call understand that our success is not a short-term effort. It comes from years of investment in R&D, people, and facilities. But for all of us it is a great time to be in optics.

And with that, I'm going to turn it back over to Angela and open it up for questions.

Operator: Thank you. If you would like to ask a question, please signal by pressing *1 on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off, to allow your signal to reach our equipment. Again, please press * 1 at this time. And we will now go to Michael Genovese with MKM Partners.

Michael Genovese: Hi, great, thanks a lot and congratulations on a great quarter.

Jerry Rawls: Thanks Mike

Kurt Adzema: Thank you.

Michael Genovese: One of your main ROADM competitors, I believe this week said that they already have orders in hand for the ROADM's in China for the near-term. Do you have any commentary along those same lines you could share?

Jerry Rawls: We have orders in hand as well.

Michael Genovese: I mean, would there be revenue from that included in the guidance you just gave?

Jerry Rawls: We will ship wavelength selective switches into China in the next quarter. We also did last quarter.

Michael Genovese: Okay. Any commentary on sort of how that could ramp into a full run rate or how big or how long lasting that project can be?

Jerry Rawls: Well the project could be huge there is a lot of debate about when exactly it's going to kick-off with big orders and deployment is really going to begin in earnest, but the consensus from everybody is that it will be in calendar 2017. So my guess is, there's not going to be big deployments in the first quarter, but any time after that I would not be surprised.

Michael Genovese: Great. And then just one more from me would be on the annual price negotiations, can you share any color there of what it is looking like this year and should we be – how much conservatism should we may be put into our April gross margin estimates, if any?

Jerry Rawls: Generally the price negotiations this year were more favorable for us and they have been in the last several years. So while we have always said that price declines that we see at 1st January every year usually range from the 10% to 15% range. This year they are around 10%.

Michael Genovese: And Kurt, if we are seeing two months of that in April, I know you don't give more than one quarter of guidance at the time, but would you want us to take in that into account or are there other factors where we could be flat in April?

Kurt Adzema: Well there are always a lot of factors that go in the margin as we know. It comes down to revenue growth, product mix, and the competitive environment. I think as Jerry pointed out, the telecom price reductions were less this year than we've seen in prior years. So, obviously that's helpful as you think about having the full three months of impact in the fourth quarter and so that's helpful, but again we're not going to provide guidance for the fourth quarter.

Michael Genovese: Okay. Thanks for taking the questions.

Operator: We will now go to Alex Henderson with Needham.

Alex Henderson: Wow, you guys are really rocking.

Jerry Rawls: You bet.

Alex Henderson: Just a couple of things, so if you could give us some detail on the actual kind of growth rate in the ROADM/wave selective switch quarter-to-quarter and can you give us a little bit of cut at 10 gig SAN and SIPRI?

Kurt Adzema: Yes, I can answer that. I think between WSS and ROADM line card it was about 10% in growth last quarter. I'm sorry you wanted a breakdown of what of datacom?

Alex Henderson: Yes, I mean if you could just give us a little bit more on what 10 gig did and what SAN did and what SIPRI did?

Kurt Adzema: Yes 10 gig was actually up a little bit, wireless was actually down several million dollars. So that helped on the mix side of things.

Alex Henderson: Is wireless now less than 10 million kind of thing, kind of trending on very de minimis amount?

Kurt Adzema: It is in that ballpark.

Alex Henderson: Okay. And then SAN?

Kurt Adzema: I think SAN was relatively flat in the quarter. So, again, as Jerry said most of the growth came from 100 gig.

Alex Henderson: Yes, going back to Mike's next question about the China demand, I think he wasn't asking if ROADMs were – and wavelength selective switches – were going to go into China for sale into China, but rather for use in China, which is a very different question, you have been selling ROADM's into China for years, obviously that's not the issue. The question is, are you shipping in the current quarter product for sale into China that will be used in China?

Jerry Rawls: We believe we are.

Alex Henderson: Perfect.

Jerry Rawls: There is always some uncertainty about where all the products are going to end up. We know some of them have ended up in China and we think some of the ones that we are shipping today are going into the early deployment or trials as we refer to them.

Alex Henderson: So, on the same lines, as the prior question on gross margins, as we look out into the April quarters, we've been bucking the trend here, we have very strong demand and seeing extremely robust situation – ramp in capacity, is it feasible to think about another year where we're not down sequentially on the top line in that quarter. I'm not looking for guidance, just sort of general conceptual thought process there?

Kurt Adzema: Well I think as Jerry mentioned, we hope to not only capacity this quarter for QSFP28 but also in subsequent quarters. I think the hope would be that that product continues to grow, the demand is there, and certainly that will be helpful as you look through the Q3 to Q4 comparison and certainly will make it a lot easier for growth in the fourth quarter.

Alex Henderson: Alright. I've asked enough questions, I'll leave and let somebody else go. Thanks.

Kurt Adzema: Thanks.

Operator: We will now go to James Kisner with Jefferies LLC.

James Kisner: Thanks guys for taking my question. I guess, first question is why don't you give us a status update on the qualification at Cisco for your ROADM line card, also I'd love if you guys would share what the QSFP28 revenue did sequentially in the quarter?

Jerry Rawls: Well we don't talk about specific customers or specific products or situations with particular products. All I can tell you is that we believe that we will achieve qualifications at the key industry OEMs very shortly. Now is shortly weeks or is that months? I can't tell you because there is a lot of stuff that goes into having your qual and your listing on the AVL buttoned up, but we think we are very close.

Kurt Adzema: James what was the second question?

James Kisner: QSFP28.

Kurt Adzema: Yes, I think we said we expected it to more than double and it did more than double.

James Kisner: Think that will happen again next quarter?

Kurt Adzema: To double again? No, I don't think it is going to double again next quarter, but it is going to grow significantly, as Jerry said, I think that 100 gig will be the key driver for growth this quarter.

James Kisner: Just last one. You guys, it sounds like are joining the 3D sensing party potentially here, I am just wondering if you could speak to a little about where you think your revenue opportunity would be, I assume you are looking at that for mobile devices primarily and what you think the dollar per phone could be and when do you think that could ramp up? It sounds like a lot of people think it's going to ramp in the second half of next year, I would just love to hear more on that thanks?

Jerry Rawls: Well it's possible that some of these product projects turn into revenue in 2017 and particularly in the second half of 2017. But I think there is a lot of uncertainty that goes with any of them in terms of consumer products and which ones they will introduce and what features and whatnot. Anyway, I think the numbers are incredibly exciting – but I think it's – and we think it's a good enough bet that we are spending a lot of money on facility expansion. We are spending money to hire people, we are ramping production – or production capability and we think that there are number of places where this 3D sensing is going to be an exciting consumer application.

James Kisner: Okay, thank you very much.

Operator: We will now go to Troy Jensen with Piper Jaffray.

Troy Jensen: Yes, great quarter gentlemen.

Jerry Rawls: Thanks.

Troy Jensen: Just a follow-up on James question on the 3D sensing stuff, could you answer the question about dollar content per phone?

Jerry Rawls: No.

Troy Jensen: Okay. All right. How about – one more for Jerry here just an update on the ACO status, any new certifications, qualifications you got during the quarter?

Jerry Rawls: Well we have achieved a number of customer qualifications and we're still working on a few more. So, we think we are very close to achieving all of the customer qualifications where we are currently engaged.

Troy Jensen: Perfect. And just maybe one for you Kurt, I know historically you talked about 35% being the right gross margin level for this industry and obviously near term you are above that now and looks like we could grow higher, I'd just like to hear your thoughts longer-term about what you think the gross margin profile is for Finisar in this industry?

Kurt Adzema: Sure. So, I'd say first of all I think what I've said is historically we typically have been between 30% and 35%, but certainly we've had quarters where we have been above that and we are above that now. I think in terms of looking to the future, as I have always said, it comes down to revenue growth, product mix, and the competitive environment, and so trying to predict multiple quarters out is challenging in our industry, but obviously we are very optimistic now, and we are very pleased with where our margins were last quarter and with our guidance this quarter, but we don't provide guidance beyond this quarter.

Troy Jensen: All right. Maybe just one follow-up on that, if you think about the 3D sensing opportunity will the margins, gross margins on that be above corporate average?

Jerry Rawls: You know that's a tough one. It depends on the application. I think there are likely to be some that are going to be above the company average, I think it is possible there may be some that are slightly below, I don't know what the average margin for that product line is going to be, I will just tell you that we think it is going to be accretive, very nicely profitable and potentially there's a lot of leverage because it comes from a fixed cost facility, a big fab.

Troy Jensen: Understood. Alright guys keep up the good work.

Operator: We will now move on to Patrick Newton of Stifel.

Patrick Newton: Yes, congratulations Jerry and Kurt on the quarter. Just to ask a little bit more on the CFP2-ACO can you help us understand your shipment levels, are we currently in the hundreds of units, several hundreds of units just a ballpark there?

Jerry Rawls: There are hundreds of units, not thousands.

Patrick Newton: Great. And then I guess on capacity utilization in Wuxi, can you help us understand where you stand there, and from a footprint perspective, should we expect any major facility expansions for Finisar?

Jerry Rawls: Let's see, the answer to the first question is, I am hard pressed to think of a product line where we are not sold out. We are still adding, obviously, a lot of equipment and people in that Wuxi facility. And, yes, we are probably going to add – not probably – we are going to add a third building, which will increase our capacity there by 50%.

Patrick Newton: Okay. And then on the QSFP28 can you give us a little more color on which variants are seeing the most demand or – and then also the pricing dynamics within those products?

Jerry Rawls: The LR4 is still our largest product line in that and the QSFP28. The CWDM4 is next. They are both growing very fast and I don't know, they are competitive products there is other people who can make them, but we think we have very good products and we think our cost structure of making them is extremely competitive in this industry.

Patrick Newton: Great. And just last one, Kurt on G&A, stepped down nicely in the quarter, I believe you had some legal cost that rolled off, correct me if I am wrong there and how should we think about the – just the level of G&A on a go forward basis?

Kurt Adzema: Yes, we had a couple of lawsuits that happened where we went to trial in the first quarter and that rolled off. So, I think hopefully that large expense is behind us and I do expect G&A to continue to grow, but I don't expect legal in the near term to pop back up to the old level. So, I expect it to grow from the levels that we are at now over the subsequent quarters.

Patrick Newton: Great. Thank you for taking my questions. Good luck.

Kurt Adzema: Thanks.

Operator: We will now move onto Doug Clark with Goldman Sachs.

Doug Clark: Great. Thanks for taking my question. First one is on the datacom side, can you give us a sense of how big 100 gig is now as a percentage of datacom? And then question on 3D sensing, I'm curious about kind of the generation of getting into that business this is kind of the first time that we are hearing about you proactively going after it and adding capacity, is this something though that you have been developing or working on or talking to customers or potential customers for a period of time or is this a recent shift in strategy?

Jerry Rawls: 3D sensing is something that we've been working on for years and we've had a number of smaller customers and it really hasn't moved the needle much in terms of revenue, but over the last year, maybe 18 months, discussions in a number of consumer-based industries have really heated up, and as a result, we think that there is likely to be significant revenue and upside for us next calendar year for sure. Now – and the reason we talked about it in this conference call was because all of a sudden we're spending a lot of money on it. And so Kurt thought if we are going to spend a lot of CapEx, we probably ought to tell people why we are spending a lot of CapEx.

Doug Clark: Perfect. That was helpful. And then my question also on 100 gig as a percentage of datacom and then I have one additional follow-up.

Kurt Adzema: Yes, it is about 30% to 35% of datacom.

Doug Clark: Okay, perfect. And then final one is related to the SAN business, but obviously a fairly large customer being acquired by someone that you could consider a competitor alternative source, could we get your early thoughts on what that impact may be and if there are any lessons to kind of glean from the Emulex days

Jerry Rawls: Well, I don't view it as positive for us, long-term Broadcom I mean has said that they are going to be a component supplier and an arms dealer for the optics industry, maybe it has no real long-term impact, but I think short-term, as long as they are the sales arm for Foxconn I think it is likely to have some negative impact on us. But I would tell you that any big equipment company wants two sources for everything. And historically in the SAN industry, Finisar has been the largest supplier in the industry, but Avago was right behind us, so I still think we are going to have substantial sales, and I think really good relationships with not only Brocade, but Emulex as well.

Doug Clark: Thanks. I appreciate the detail. And maybe just a follow-up on that, final one from me, how large is the SAN exposure at this point for the datacom business, just so we can kind of help frame that?

Kurt Adzema: Yes, it is kind of in the low 20’s% of datacom.

Doug Clark: Got it, thanks a lot guys.

Operator: We will now go on to Dmitry Netis with William Blair.

Dmitry Netis: Yes, hi guys thanks for taking the question. I want to shift the discussion a little on the server side optics and with the Tomahawk pushing Cloud operators to 25 gig and 50 gig rates, do you foresee copper still being used in that environment? And my imagination sort of tells me maybe at 100 gig you will have to almost go to fiber, but potentially fiber could exist at 25 gig, 50 gig level as well. So as you go into that [inaudible] server level optics environment, how is Finisar positioned for that opportunity, what's the timing and how are you thinking about the [inaudible], I suppose the opportunity for you in that kind of market that's opening up?

Jerry Rawls: We are positioned very well because we have – we are the biggest supplier in the datacom industry. Most of the server connections, server to server are copper. Some of the server to Top of Rack switch are optics, but most are still copper and this is 10 gig lanes and our 25 gig lanes. The switches from the Top of Rack switch to the aggregation switches are virtually, I won't say all, because I could well be wrong somewhere, but they are predominantly optical, and the rest of the connections in the data center are optical, as we – the question is going to be as Tomahawk goes to third-generation Tomahawk and the lanes become 50 gig PAM4, not 25 gig, the question is, are – will the connections within the server still – can they still be copper at those speeds and the answer is, I don't know. The distances get shorter and shorter and I think optics, the optics share of that business for sure will grow, but it is hard for me to predict the complete demise of copper in some connections, in some cases they're only a foot or two long.

Operator: All right. There are no other questions from this line, we will now move on to Simon Leopold with Raymond James.

Simon Leopold: Thank you for taking my question. A couple of things, one, I'm going to go back to a question I've asked you in the past to get an update. Exposure, you've had direct sales to web scale, how that may have moved around in this particular quarter?

Kurt Adzema: I think we've said in the past it is 15% to 20% of revenue and I still think it's in that ballpark.

Simon Leopold: Great. And in terms of the ROADM opportunity in China, specifically the deployment by Chinese carriers, we've heard some mixed commentary about their choices of architecture whether they would look at a legacy type architecture and a low count 1 by 9 or whether these operators would adopt something similar to the Western vendors maybe 1 by 20 with the CDC and it sounds like maybe there is some mix, I'd like to hear your thoughts, in two parts, in terms of what you expect the Chinese operators will deploy in terms of a mix of technologies for ROADMs and then what does that mean to Finisar? Thank you.

Jerry Rawls: Well I don't think it is clear exactly what will be dominant for Chinese domestic deployment. I think that there will be applications that will be broadcast and select and there are others that will be route and select. I can't tell you exactly which of the carriers might select which one or if there will be a unified approach dictated by the government. There is always a bit of uncertainty that goes with sort of the mysterious operations of the Chinese government and the big Chinese national corporations. So, I don't know, I think you might end up with some of both and I think that for us, well, we make a lot of 1 by 9s, and we make 1 by 9s flex grid on the finest grid spacing that money can buy, and we make the 2 by 1 by 20s for the route and select architectures and they are again flexible grid spacing. And I think we will have a substantial business either way and in both cases.

Simon Leopold: And in terms of the timing on the Chinese operators for the 100 gig opportunities specifically transceiver opportunities for you, what do you expect in terms of any of the seasonal patterns during the course of the year, the timing of the tenders, some of what we've heard is, this tends to be backend loaded because of Chinese New Year and just the time it takes to review and assess tender bids, what's your view on the timing for those opportunities in calendar 2017? Thank you.

Jerry Rawls: Well the only seasonality that I predict in China, is Chinese New Year. And everything sort of slows down and stops before Chinese New Year and it always seems like it takes a while for things to crank back up after Chinese New Year. So, other than that I don't have – there is no seasonal pattern that I would predict, it all has to do with when do RIFs and RFQs come out and when do the deployments get started, but it will be after Chinese New Year, I'm pretty certain.

Simon Leopold: Great, good quarter guys and thank you for taking my questions.

Jerry Rawls: Thank you.

Operator: And as a reminder ladies and gentlemen, it is * 1 if you would like to ask a question. We will now move on to Richard Shannon with Craig-Hallum.

Richard Shannon: Hi Jerry and Kurt thank you for taking my questions, a list here, maybe I will start with a 100 gig QSFP question, can you characterize the growth coming from – is more of it coming from web 2.0 direct sales or through OEMs, can you give some understanding of that would be great please?

Jerry Rawls: Both.

Richard Shannon: Both, okay. How would you characterize your customer base on the web scale side for the QSFP28 products, is it still more of a single customer or very broad based or how would you characterize that Jerry?

Jerry Rawls: Broad based. There is not enough capacity in the industry to supply QSFP28s. There are not enough lasers available. There is not enough capacity. So because we have big factories, we make our own lasers, we are in really good position in that market.

Richard Shannon: To that point Jerry, when do you expect industry constraints to be overcome, could that happen within a quarter or more like a half year or how do you view that?

Jerry Rawls: Well, I have heard people predict that it could be as long as two years, I don't know, I can't tell you, it depends but they have predictions on demands and they have predictions on capacity and balancing the two of these guys said that they thought it might be as long as two years before the capacity equals demand. So, I am very optimistic that it’s going to be a good market for a while.

Richard Shannon: Okay and to follow on that topic, how do you expect that to read into the pricing trends, it seems like LR4 is less competitive space there, where I expect price to be better but how about even on the more CWDM4 format?

Jerry Rawls: Well eventually we think CWDM4 will be a larger market by volume. LR4 is a little more difficult product to make, but the 10 kilometer performance is something that a lot of customers will demand in some part of their networks. So, I think they are both going to be very strong products over time, but the industry analysts that look at this industry predict that CWDM4 will be the largest in volume, but there won't be much difference, I don't think in the TAM.

Richard Shannon: That's helpful. Thanks Jerry. One last question from me, on 100 gig or CFP2 ACO. You talked about some qualifications and more to come, Jerry could you take a venture to guess what kind of share you might expect in this market say in a year’s time, and also you talked about your products being able to do 100 and 200, do you expect you'll be able to do 250 at some point in the near future and how important would that be to do so?

Jerry Rawls: Let's see. In reverse order, yes, we sell a 250 gig product today. We – and in terms of market share, it’s hard to say, but I hope it is big. There aren't many players, there aren't many guys in this industry that really make this product and right now, there is one that makes it in any volume to speak up. So I think that given virtually all the equipment companies that buy these things will want to have two sources, I think we will end up with meaningful share. And define meaningful as been 30% of the industry or 50% of the industry? I am not going to hazard a guess, it depends a lot on performance, it depends on shortages, it depends on quality and price and lots of other things that are yet to come.

Richard Shannon: Okay. Well that's helpful to understand how you're thinking there Jerry, so I appreciate that. That is all the questions from me guys, great job. Keep up the good work.

Jerry Rawls: Thanks Richard.

Operator: We will now go to Dave Kang with B. Riley.

Dave Kang: Thank you good afternoon. Kurt, what was CapEx for the second quarter?

Kurt Adzema: It was about $30 million.

Dave Kang: Okay. And regarding 3D sensing capacity, what is the current capacity and how much are you planning to add next year?

Kurt Adzema: We're not getting into that Dave, we're not at that stage yet.

Dave Kang: Okay and then regarding, Jerry your comments about 3D sensing gross margin, you said some might be above and some might be below, I thought if, correct me if I'm wrong, but if you are selling chips, should they nicely above corporate average, should they be similar to like semiconductor gross margin of say 50% or so?

Jerry Rawls: I think there are some applications that are like that, but the consumer industry is such that, volumes are high, the negotiations are tough and my expectations are that – and many of – in these cases, the OEMs are trying to make sure that they have specifications that are interchangeable between suppliers that is that in many cases the packages are the same, the outputs are the same, the configurations are the same so that you can have multiple sources for a drop-in product and that's a little different than a lot of the IC industry where you go and try to spec in your chip into a slot, in a design, but once you won that design win, then it's very difficult to get you out and almost nobody else in the industry has exactly the same pin out that you do. So it requires a design change to replace you or even to bring in a second source, you have to have a second board design.

Anyway, I don't – I think that most of these consumer companies are trying to make sure that they have design from the beginning so that they have multiple suppliers and interchangeable suppliers. So, I think there is reason to believe that the sky-high margins of the IC industry might not be possible in these consumer applications, but I do think the margins will be quite good and I think the business will be quite profitable.

Kurt Adzema: And it will come down to volume at the end of the day, again, when you're looking at a fixed cost to the extent once you add the capacity it all comes down to how many units go through that fixed cost.

Dave Kang: Okay. Moving to the WSS ROADM business, what is the current mix? I assume WSS is still much bigger than ROADM at this point, what is the current mix at this point?

Kurt Adzema: It is still predominantly WSS. Obviously once we get some of these quals done on line cards we expect that to shift some, but it's predominantly WSS at this point still.

Dave Kang: I assume when you say qual, you're talking about the North American market, but what about China, you think it will be more WSS or ROADMs?

Jerry Rawls: The sales in China are going to be WSS.

Dave Kang: I am talking about the Chinese network, that that will be going to Chinese networks.

Jerry Rawls: That's what I am saying too.

Dave Kang: Okay.

Jerry Rawls: Deals in China for Chinese networks, or for export, makes no different, but the sales will be wavelength selective switches because the Chinese OEMs design and build their own line cards.

Dave Kang: Got it, got it. And then I guess you already talked about whether it is CD, CDC hard to say, but what about the current orders that you have on hand? I mean can you tell us whether they are CD or CDC at this point?

Jerry Rawls: Well we have some for duals that are capable of CDC and we have some that are singles that are, single 1 by 9s that are broadcast and select. So there is both.

Dave Kang: Got it. And then lastly, Acacia are already sampling CFP2-DCO so is there additional pressure for you and other ACO vendors to introduce CFP4 just to keep up with CFP2-DCO?

Jerry Rawls: I don't know, I haven't thought about it that way. I think about the DCO market as being different than the ACO market and the densities that you can achieve on faceplates are higher with ACO than they are with DCO, and so there is a lot of OEMs that are going to prefer ACO.

And there may be more of the data center interconnect kinds of applications that may – but it depends, you know, that may prefer DCO. On the other hand, there are a lot of applications there, where density will be important. So, I don't know how it is going to shake out. I think in the end if you look at the like counting estimates, you will see that there is a significant market for both.

Dave Kang: Got it. Thank you.

Jerry Rawls: Thank you.

Operator: That concludes today's question-and-answer session. Mr. Rawls at this time, I will turn the conference back over to you for additional or closing remarks.

Jerry Rawls: Well Angela thank you very much. And I want to thank everybody for tuning in today. We appreciate you're taking the time to spend with us. And we hope you will be able to join us again, three months from now. Have a good day.

Operator: Ladies and gentlemen, this does conclude today's conference. We thank you for your participation. And you may now disconnect.