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RDWR - Q4 2018 Radware Ltd Earnings Call

EVENT DATE/TIME: FEBRUARY 06, 2019 / 1:30PM GMT

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PRESENTATION

Operator

Good morning. My name is Sharon, and I will be your conference operator today. At this time, I would like to welcome everyone to the Radware Q4 '18 Earnings Call. (Operator Instructions)

Anat Earon-Heilborn, VP Investor Relations, you may begin your conference.

Anat Earon-Heilborn - *Radware Ltd. - VP of IR*

Thank you, Sharon. Good morning, everyone, and welcome to Radware's Fourth Quarter and Full Year 2018 Earnings Conference Call. Joining me today are Roy Zisapel, President and Chief Executive Officer; and Doron Abramovitch, Chief Financial Officer. A copy of today's press release and financial statements as well as the investor kit for the fourth quarter are available in the Investor Relations section of our website.

During today's call, we may make projections or other forward-looking statements regarding future events or the future financial performance of the company. We wish to caution you that these statements are just predictions, and we undertake no obligation to update these predictions. Actual events or results may differ materially, including, but are not limited to, general business conditions and our ability to address changes in our industry, changes in demand for product, the timing in the amount of orders and other risks detailed from time to time in Radware's filings. We refer you to the documents the company files from time to time with the SEC, specifically the company's last Form 20-F as filed on March 28, 2018.

I would like to remind you that on February 20, Radware will host an investor meeting in New York, where members of the executive team will provide an update on the company's business and outlook. If you'd like to join us, please e-mail me at IR@radware.com.

With that, I will turn the call to Doron Abramovitch.

Doron Abramovitch - *Radware Ltd. - CFO*

Thank you, Anat, and thank you all for joining us. We reported today another good quarter with continued growing revenues and expanding margins. We are closing a strong year, during which we delivered growth, probability and cash generation exceeding our initial guidance for the year and above our long-term CAGR, which we shared last year. Revenues for the fourth quarter were $63.8 million, at the high end of our expectations and up 9% year-over-year. Full year revenues were $234 million and up 11% from 2017. Revenues from the Americas were 44% of total 2018 revenues, an increased 5% from 2017. Revenues from EMEA were up 34% and represented 32% of the total. And revenues from Asia Pacific were down 1% year-over-year and accounted for the remaining 24%.

For the full year revenues from the enterprise vertical represented 69% of total revenues and increased 17% from 2017, and revenues from the service providers vertical remained at the same level as last year. Subscriptions continued to be the fastest-growing type of revenues. Recurring revenues that include subscriptions and support represented approximately 64% of total 2018 revenues compared with approximately 56% in full year 2017.

I will discuss now expenses and profit, all in non-GAAP terms.

Non-GAAP gross margin for the fourth quarter grew to 83% from 82.3% last year, and full year gross margin went up to 82.7% from 82.2% in 2017. Over the long term, we expect gross margin to moderately increase driven by economies of scales of our cloud operations, high utilization rate of our scrubbing centers and an increase in proportion of non-cloud subscriptions. However, product and geography mix differences from 1 quarter to another can cause some fluctuations around the trend.

Q4 non-GAAP operating expenses were $43.2 million, below our guidance, compared with $45 million in Q4 last year, mostly due to benefit from a stronger U.S. dollar compared to last year and ASC 606 impact.

We continue to invest in our business selectively and moderately to support our growth on the one hand, while delivering operating leverage on the other hand. We are very pleased with the balance between these 2 metrics in last couple of years.

Our non-GAAP operating profit in Q4 2018 was approximately $9.8 million, representing a 15.4% margin, which was up from 5.2% in Q4 2017. Full year 2018 operating profit was approximately $21.6 million, up from $3.8 million. And operating margin was 9.2%, up from 1.8% operating margin last year.

Non-GAAP tax rate was 11% for the year, down from 18% in 2017. Tax rate was lower than last year due to impact of the lower federal tax and adjustment related to ASC 606. For 2019, we expect the tax rate to be approximately 11%.

Q4 non-GAAP net income was $11.4 million or $0.24 per share diluted, exceeding our guidance for $0.16 to $0.18 per share. A strong non-GAAP EPS was driven largely by strength in revenues and gross margin, expenses discipline and stable headcount as well as lower tax rate. Revenue growth affected EPS by approximately $0.01 to $0.02; tax and financial income, by another $0.02; and the rest of the upside came from OpEx.

Non-GAAP net income for the full year was $26 million or $0.55 per share diluted, well above net income and EPS for 2017, which were $7.6 million and $0.17, respectively.

Turning to balance sheet and cash flow. As subscription continued to be main growth driver, it positively impacted our total deferred revenues. We ended the year with balance of approximately $167 million, up 13% from December 2017. Our business mix provides us with visibility for future financial performance. In the coming 12 months, we will recognize as revenues approximately $105 million out of the December total deferred revenues balance of 63%. This compares with $91 million or 62% in Q4 last year.

We had a very strong collection from customers in Q4, and we generated approximately $26 million of operating cash flow in the quarter and more than $49 million in the full year, up 57% from last year.

During Q4, we executed on our share buyback program and repurchased approximately 200,000 of our own shares in the amount of $4.3 million. We ended the year with approximately $401 million in cash and financial investments, up from $344 million as of the end of 2017.

In early January, we announced the acquisition of ShieldSquare, a leader in bot mitigation. Roy will discuss this acquisition in more depth shortly. We expect the acquisition to close at the end of Q1, and the total cash consideration that we will pay will be up to $18 million, and part of it will impact the Q1 2019 cash flow. There will be approximately 70 people joining us, the vast majority of whom are based in India. We expect the acquisition to be immaterial for 2019 revenue and dilutive to our fully diluted 2019 non-GAAP EPS by $0.09 to $0.10, starting Q2.

And now to our outlook for the first quarter of 2019. We expect Q1 '19 revenues to be between $58.5 million and $60 million, non-GAAP gross margin to be approximately 82.5% and non-GAAP operating expenses to be between $44 million and $45 million. We expect tax rate to be approximately 12%. Non-GAAP EPS for Q1 is, therefore, expected to be between $0.12 and $0.13. This guidance assumes closure of the ShieldSquare acquisition at the end of Q1, so we didn't take any EPS impact for this quarter. As said, from Q2, we expect the EPS to be impacted by approximately $0.03 per quarter.

As for our outlook for the full year of 2019. We expect it to be in line with our long-term model, which we presented last year, of 9% revenue CAGR between 2017 and 2020.

On the back of our strong 2018 revenue growth, we expect revenue growth in 2019 to be between 7% and 9%. The midpoint of this range leaves 2019 revenues slightly above the CAGR rate from 2017.

We will provide a more detailed 2019 guidance in our investor meeting in New York on February 20.

I will now turn the call over to Roy.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Thank you, Doron. We are pleased with our performance in the fourth quarter and full year 2018. Record quarter revenue closed a record year, reaching $234 million. In addition, we had significant profitability improvement. Net profit rose to $26 million and more than tripled from 2017. Record operating cash generation in the fourth quarter led our cash level to $401 million at the end of the year. We also had record quarterly booking in the fourth quarter, which is reflected in the double-digit growth in total deferred revenues, up 13%.

Overall in 2018, we continued to execute our strategy and deliver on our goals. We have full confidence in our competitive position given the breadth and maturity of our solution portfolio and in the preparedness of the organization for the coming year.

From a geographic perspective, we are very pleased with our underlying performance in the international markets, EMEA and APAC. In the Americas, we were able to grow our revenues against a strong 2017 and in spite of some signs of softness in this region, specifically in the Tier 1 carriers.

Overall, in all aspects and in all geographies, we believe we are in a better position today than we had ever been.

Let me briefly discuss what we are witnessing in our market, data center and cloud application delivery and security solutions. Customer priorities are strongly linked to the ongoing transition of applications to the cloud and the very dynamic cybersecurity space. Our offering is very much aligned with these needs. Through market-leading attack mitigation capabilities and superior quality of detection, we have a complete offering, spanning the private, hybrid and public cloud data centers, coupled with fully managed service offering. The quality of our offering means that we simply provide a higher level of security. Because of that, we are successful with the most demanding customers who have unique and complex requirements that often lead to relatively large deals.

Consequently, our subscription solutions enjoyed strong growth in 2018. Among our new logos acquired this year, a global top-3 car manufacturer, a global top-3 pharmaceutical company as well as banks, carriers, retailers and others.

An example of the quality of our security portfolio is our Emergency Response Team active attacker subscription, which is using intelligence from our Radware Deception Network of honeypot we deployed across the world. We are using this network to identify and block known attackers before they even reach the customer network. We receive fantastic feedback from customers who subscribe to this service. For example, a financial institution in EMEA shared with us that in October 2018 alone, they witnessed 3.7 billion packets and 2-terabyte attack volume being mitigated with zero latency through the ERT active attacker mechanism before our devices had even begun processing any traffic.

In early January of this year, we booked our largest to-date active attackers subscription deal with a long-term customer who upgraded their protection package to include this subscription for more than $500,000.

Another example for the strength in our subscription business in the fourth quarter comes from a cloud security win in a leading European bank. The bank had our DefensePro attack mitigation devices installed in its data centers and an always-on cloud DDoS protection service from one of our competitors. It experienced many DDoS attacks in the past, which were, at times, not mitigated by its existing always-on cloud protection and were only blocked by our on-prem attack mitigation devices. Unfortunately, due to the failure of the always-on cloud protection service, when these attacks became large enough to overwhelm the Internet link, the bank service was disrupted. The bank's zero tolerance towards such attacks and the realization that the existing solution was unable to keep up with the rapidly evolving DDoS threat landscape led it to seek a solution that will protect it in full - always. This multiyear deal was one of our largest cloud security deals to date.

As we announced last month, we further expanded our portfolio with the acquisition of ShieldSquare, a leader in bot mitigation. Today, more than 50% of the Internet traffic comes from bots, and therefore, organization need bot management solutions that not only detect and mitigate bot attacks but also distinguish between human traffic, good bot traffic and bad bots in real time. The ShieldSquare solution does so by applying its own machine learning to analyze behavior and by creating advanced finger printing based on hundreds of parameters. The solution protects websites, mobile applications and API and provides an important expansion of our attack mitigation capabilities.

To summarize, we are in an excellent position in all aspects of our business, and we make consistent progress on all dimensions of our strategy.

Financially, we enjoy revenue growth and increased profitability in line with our 3-year model, affirming our confidence in our strategy. Our portfolio is the widest and most advanced it has ever been, reflecting thought leadership and a close alignment to customer needs. The cloud environment creates new security challenges. We will continue to leverage our advanced algorithms and machine learning capabilities to introduce additional solutions for this environment. We look forward to continue growing our business in 2019 and beyond.

And with that, I will now open the call for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Alex Henderson with Needham & Company.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

I wanted to ask you a couple of quick questions on mechanics. So can you give us the current headcount? And I didn't catch the book to bill.

Doron Abramovitch - *Radware Ltd. - CFO*

Okay, so Alex, so it's in the same level in the last few quarters, approximately 970 people that we now have, what I meant when I said a stable headcount. As for the book to bill, it's -- Roy mentioned it in a different way. It was -- this quarter, it was more than -- significantly more than 1.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

And then you talk about the stats in service revenues being 64% in '18. Do you have a metric of how much you think that might reach over the course of '19? Are you anticipating continued growth in deferred revenues in '19, hence, overall order growth in double digits?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes. So we don't give the specific metric, but given the strength in subscription we're seeing and the fact that we are moving more and more product and solutions to this business model, we obviously see growth, or we expect growth in '19 in the total deferred balance. And we will continue probably to see rise in the percentage of that out of our total revenues, up from the 64% we had for '18.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

Great. I just wanted to talk a little bit about ShieldSquare with you guys for a second. First up, congratulations, it's a great acquisition, superb positioning of that company. Spent a bunch of time talking to some of their competitors, and most of the competition looks like it's growing in the order of 30% to 50% as bot attack metrics become really the most critical element of CDN protection and SaaS protection. So to that extent, how rapidly do you think you can take this bot protection capabilities back to your SaaS customers, back to your service provider customers and monetize the business? I mean, maybe immaterial now, but what does it look like in terms of the ramp?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Okay. So as per Doron comments, assuming we close it towards the end of Q1, I believe it will take us between 3 to 4 months to integrate it into our cloud offering. So our plan is by end of June to have it integrated into our cloud security solutions. And as you mentioned, we think it's an important addition to our cloud security portfolio. We think it plays extremely well with our DDoS, WAF and now anti-bot capabilities. And we believe customers -- and that's the feedback we were getting so far from the customers and prospects we were discussing this acquisition with -- will find it very beneficial to get a unified, complete application security solution from us. So we're entering this market early on, and we are looking to gain a very strong position there.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

Great. Would you think in 2020 that you might be able to fully offset the dilution and have it contribute to earnings? Or how should we think about the fallout or the dilution from it?

Doron Abramovitch - *Radware Ltd. - CFO*

Yes, Henderson, we will probably share some more information in the investor meeting, but we do assume that it will be accretive in a way. It's too early, but we need -- this is the plan right now.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

That's a safe assumption on it.

Operator

Next question comes from George Notter with Jefferies.

George Charles Notter - *Jefferies LLC, Research Division - MD & Equity Research Analyst*

I guess, a few areas of questions. Maybe first, we can just talk about the average duration of the total deferred revenue. I know in times past, you guys have given us that number in terms of years. Just want to make sure the growth in deferred revenues is, I guess, coming more naturally rather than just extension of services contracts?

Doron Abramovitch - *Radware Ltd. - CFO*

Okay. So in terms of the numbers, it's quite stable in last, I think, 2.5 years, and -- since we started to disclose this, so it's approximately 1.8 years. This is the average duration of the contracts that are right now in the total deferred revenues. So as Roy mentioned, assuming that we will continue to grow, I believe we take the assumption it will continue to be in this level of 1.8 years.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

In the last quarter, the duration has shortened actually. The growth you're seeing is in a shorter duration of new booking, and you can see that also in Doron's comments, when he mentioned the percentage of recognition in the coming 12 months has gone up by like 1% from 62% to 63%. That tells you the duration has shortened.

George Charles Notter - *Jefferies LLC, Research Division - MD & Equity Research Analyst*

Okay, great. That's helpful. And then the 64% of revenue coming from recurring sources, that's an impressive number. Just out of curiosity, could you share that number for Q4? I presume it was higher as you exited the year. Is that fair?

Doron Abramovitch - *Radware Ltd. - CFO*

No, unfortunately, we don't share it.

George Charles Notter - *Jefferies LLC, Research Division - MD & Equity Research Analyst*

Okay, no worries. That's fine. Maybe just stepping back just more intuitively, when you go and talk with enterprise customers and you sell deals, I mean, is it fair to say that a higher percentage of those deals are coming in the form of subscriptions, non-cloud types of subscriptions? And, I guess, I'm just curious about what's driving that. Why are enterprises more interested in constructing deals that look like that?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Okay, so a couple of points here. Number one, I think Doron mentioned that subscription is the fastest-growing component of our business. So definitely, we're seeing the trend going there. And as we discussed in previous calls, we have multiple sources today of subscription. Some are coming from product subscription, basically capabilities that we used to sell as perpetual or new capabilities we are bringing to market, and they are only available now in a subscription form. Those are generally capabilities that are add-on or extensions of our product capabilities. I've mentioned, for example, the ERT Active Attackers Feed, it's exactly that, meaning you want this capability of blocking known attackers based on cloud intelligence in your product, you need to subscribe to this add-on capability. And like that, we have a growing set of subscription across both our ADC and security product lines. The second source of subscriptions is all the cloud. The cloud delivered services, the cloud DDoS, the cloud WAF, and now it will be also the anti-bot. And we're seeing very strong growth there as well. And last, but not least, all the managed services. There is a major issue of expertise in customers around the cybersecurity, and we're seeing them more and more subscribing to managed service, ERT, Emergency Response Team under attack services, et cetera, et cetera, renew up the yearly services. So I think if you look on the underlying drivers for the customers to move to subscription, number one is the cloud. They're getting used to consume cloud services. And now -- and as it relates to us, our cloud services. Number two, the lack of expertise moves them to source or outsource some capabilities from the outside. And last, but not the least, as long as we continue to deliver innovative solutions that have clear value like I've mentioned with the -- with this example, although we have several of these that are extremely successful. Customers are buying into it because of the value.

George Charles Notter - *Jefferies LLC, Research Division - MD & Equity Research Analyst*

Yes, that's great. And then just one final question. I just wanted to ask about OEM customers. I think you guys mentioned at one point last year that you expected to sign a new OEM coming through the end of the year. I'm just curious about where that is right now?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes, so we did sign. It did contribute to revenues in '18. The public announcement depends on our partner, and they are not ready yet to do that. But we've execute that and it's started to contribute to the numbers.

Operator

Next question comes from Tavy Rosner with Barclays.

Peter A. Zdebski - *Barclays Bank PLC, Research Division - Research Analyst*

This is Peter Zdebski on for Tavy. Just looking at the Americas growth of 5% for the year, we had understood that subscriptions and deferred was -- growth was stronger in the Americas in the past. Could you give us a sense of how the deferred balance looks in the region in light of that 15% growth in total deferred for the year?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes, so we don't break it by region. But -- so I don't want to go into specifics, but overall, the cloud adoption in North America is the highest. After that, is EMEA and then APAC. Those are global trends. We would see similar aspects of that also in our bookings.

Peter A. Zdebski - *Barclays Bank PLC, Research Division - Research Analyst*

Okay. And just one follow-up on OpEx. You mentioned the stronger dollar was a factor in the OpEx decline in the quarter. Do you have a sense of what the growth in R&D and sales and marketing spend would have been on a constant-currency basis?

Doron Abramovitch - *Radware Ltd. - CFO*

Yes, so if I compare this quarter to 2017, the OpEx was down by $2 million. Out of it, something like $600,000 is the dollar-shekel mainly to the R&D. And if I compare it to Q3, so it's -- we added $700,000. The vast majority from marketing -- sales and marketing activities and a very small portion is the FX. So these are the numbers if I compare to these 2 periods.

Operator

Next question comes from Ittai Kidron with Oppenheimer.

Ittai Kidron - *Oppenheimer & Co. Inc., Research Division - MD*

Couple of questions. Doron, just want to make sure when you say 64% you are including maintenance and subscription revenue. Is that correct?

Doron Abramovitch - *Radware Ltd. - CFO*

Yes.

Ittai Kidron - *Oppenheimer & Co. Inc., Research Division - MD*

Is there a way to give us more color on the subscription component itself? It's hard to get your hands -- our hands around what is the maintenance part, which I assume is probably the majority of the 64%, the relative growth rates of the maintenance versus the subscription. Is the maintenance even growing?

Doron Abramovitch - *Radware Ltd. - CFO*

I'm not sure that your conclusion is definitely correct because 3 years ago, it was 42%. So the growth comes from all the business strengths that Roy mentioned regarding the subscription, and now it turned to be 64%. Unfortunately, we don't break it by quarters, and we don't break it in other ways, between the subscription and maintenance, but you can assume that the growth comes mainly from subscription.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Let me phrase it a bit differently. It took us like 15 years to build a maintenance base of high 30s, low 40s, so to speak, if you look on all our financials, and you know them for many years. And then if you look at the last 3 years, that figure moved once we started with the subscription from 42% to 64%, it's clear where the majority of the growth is coming from.

Ittai Kidron - *Oppenheimer & Co. Inc., Research Division - MD*

Yes. I just think you're doing yourself a little bit of disservice by not splitting it up because my gut tells me is that you're maintenance revenue, Roy, even though it took you 15 years to build all of it, at this point is probably flattish. So the growth would have been even nicer, yes, even worth some spend if you just split them up. Am I, at least directionally, correct in how I'm thinking about this?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

I don't want to say maintenance is flat, et cetera. But again, subscription is the driver absolutely. On that, you are right.

Ittai Kidron - *Oppenheimer & Co. Inc., Research Division - MD*

Okay. Excellent. Now regarding the enterprise revenue, the split there. It's somewhat low on a year-over-year basis in this fourth quarter. I would have expected there's some budget flush to work its way after multiple quarters of very strong year-over-year growth. How do I get my hands around what's going on in the enterprise. And you talked about some softness. Just want to make sure I understand what it specifically relates to.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

The softness I talked about was mainly relating to U.S. Tier 1 carriers. Enterprise trends were very good in the quarter, especially on the booking side. We're very happy with the enterprise business and the trend there. That's where most of the subscription business is going. And the trends are strong.

Operator

The next question comes from Zack Turcotte with Dougherty.

Zack Turcotte - *Dougherty & Company LLC, Research Division - Anlayst*

Zack on for Catherine Trebnick. First, just kind of a follow-up on the Americas growth. It was just under 5%. I know it fluctuates quarterly. But how much of this do you attribute to the softness in the carriers versus just tough compare? How much do you see that rebounding in 2019? Or are you already seeing any sort of bounceback?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes. So -- no, overall I see those 3 factors. One is the tough compare, like you said. Q3 last year, we went up 33% in Americas; Q4, 27%; but like H2 was like 30% year-over-year growth. That was a relatively high bar. Second is the Tier 1 carriers. We don't think it's -- it should be long term. We have very nice projects and so on, but we did see delay, definitely, in Q4, some a bit before that. And the third is our execution. There's always room for improvement. I think we can grow faster. I think we have, based on the comments I shared with you, a very strong portfolio position. And those things, that we always need to improve in our own execution. So those are the 3 factors that I think led to this result.

Zack Turcotte - *Dougherty & Company LLC, Research Division - Anlayst*

Okay, great. And then you had pretty consistent beat and raises throughout 2018, so even despite strong cost controls and sales and marketing as percentage of revenue even declining pretty sharply, so I'm wondering are there different direct sales efforts or channel efforts that you're using to drive the beat and raises. Do you attribute some of this to material revenue from OEM partners that you are finally seeing? Or what's the main driver of these beat and raises consistently?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

It's a combination, I think, of many factors. It's the portfolio, it's the trends in the market that are playing to our favor, the move to cloud, the cybersecurity becoming more and more critical. And I think you know in -- the OEMs are, obviously, assisting us in penetrating new customers, some of the new strategic alliances. But all in all, I think it's consistent execution of the strategy we shared, starting 2 years ago and in more details in the Analyst Day a year ago. We're doing that. It proves itself. And I think we're starting to see the fruits.

Operator

Next question comes from Josh Tilton with Berenberg.

Joshua Alexander Tilton - *Joh. Berenberg, Gossler & Co. KG, Research Division - Associate Analyst*

Can you talk to the type of customers you're seeing adopting the cloud deployments. Aside from the hybrid deployments, are you seeing a situation where the cloud is may be opening up an opportunity for new customers who possibly couldn't afford or manage solutions prior?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes, absolutely. I will give you one prime example. I think it is the cloud WAF, the cloud web security. In -- web application firewalls are not new to the market, but they are considered to be very complicated to manage. You need to understand security, applications. And every time there is a new application version or a capability going out and with DevOps now, it's starting -- and agile, it's becoming a weekly release cycle. You need to adjust your web security to that. That creates a huge cost and operational build-in on even the largest customers, not to mention a midsize customer. Now I can assure you that all the customers that have a Internet-facing application must have a web security solution. Many of them simply cannot afford the complexity and the cost. The cloud WAF is opening up this opportunity for us. And we are seeing very, very strong growth there. And I think this growth can last for years to come because it's one, on one hand, like I mentioned, the critical need of the customer; second, there is a clear displacement of on-prem WAF appliances that are moving to the cloud because of the security cost and operational benefits; and third, because you can build a very, very strong offering, for example, adding anti-bot to the mix. So definitely, we're seeing new markets opening up for us because of the cloud delivery. And we are trying to execute as fast as we can on this opportunity.

Joshua Alexander Tilton - *Joh. Berenberg, Gossler & Co. KG, Research Division - Associate Analyst*

And then just on ShieldSquare. So my understanding is that your security capabilities had bot mitigation capabilities, especially around the issue of the dynamic IP addresses associated with the bots. Is ShieldSquare just to strengthen those capabilities? Or does it bring additional security capabilities to the portfolio?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes. It's much deeper. When you want today to protect against sophisticated bots, it's not enough to look on the IP addressing. The sophisticated bad bots are replacing them. The attacks like account takeover or attacks on inventory and so on are way more complicated. And for that, I mentioned in my comments you need much broader stronger algorithms, machine learning, hundreds of parameters per session that you take into account to distinguish. Again, it's not only between human and bots, you need to differentiate also the good bots like search engines, like performance monitoring and so on, partner API systems. So it's really the ability in real time to differentiate between a good bot, a bad bot and a human. And I think we are very happy with the acquisition, and we believe we will see a significant contribution to our cloud-based services with it.

Joshua Alexander Tilton - *Joh. Berenberg, Gossler & Co. KG, Research Division - Associate Analyst*

I mean, just last one. I believe Cisco added your cloud solutions to its reseller portfolio in Q2. Can we get any updates on how that's going for the business?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

It's progressing. For example, one of the wins I've mentioned on the pharmaceutical top-3 companies that we won was done through Cisco, just as an example.

Operator

Your last question comes from Alex Henderson with Needham & Company.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

I was hoping you could give us some granularity around your penetration of the SaaS customer set, going in and selling to the sales forces of the world. And to what extent (inaudible) CDN in there? That would be quite helpful.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes. Look, so I think at the very high end, we're starting to be with very nice market share. But the SaaS market is huge. And you know the amount of companies is growing by the day. We have significant advantage there, technology advantage there, that we are utilizing, and we are winning more and more of deals. But at least at the high end, we have excellent references, very well recognized names out there.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

One of the other questions, really underneath the surface is: What's going on between the security portfolio and the traditional businesses? I assume that the traditional ADC market is fairly flat and fairly flat in your business. Is that an accurate baselining?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes, we don't break it as you know, Alex. However, I think there are -- there is more strength in the ADC market than people give it credit.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

If we were to look at just the vast portion of the business, I assume that, in terms of orders coming in, it is delivering something in excess of 20%-type clip. My assumption would be that the malware products and other more advanced products that you've added to that are growing faster, and the DDoS is probably around 20% as well. Are those kind of the right mechanics around the security portfolio set?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes, we don't break it to that granularity, but as Doron mentioned, subscription, overall, and obviously, cloud is a major part of it, is the fastest-growing competent of our business. If the average does, they did like, this year, 11%, you can assume the substantial growth in our subscription business and also in cloud obviously.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

And just to go back to Cisco for 1 second, if I could, any thought on actually getting some licensing come out of that partnership with them? Or is this just Waiting for Godot kind of -- I mean, how long have we been talking about this is getting on 3 years I think.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes. It's progressing. You know we always want more, but it is progressing. And we're looking for '19, again, to build that business. But we are not looking into a licensing deal. We are looking for more and more of our solutions being sold by their sales force.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

Right. But didn't you have a licensing deal with respect to the software incorporated on to their boxes?

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

Yes, so it's an OEM deal, where whenever they sell it, we get the license, so absolutely. But It's not a like a onetime software license, maybe, I didn't understand your question, deal that we had with them.

Operator

And at this time, I will turn the call over to Mr. Zisapel.

Roy Zisapel - *Radware Ltd. - Co-Founder, CEO, President & Director*

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Okay. Thank you very much for joining the call. We look forward to seeing many of you in our analyst meeting in New York in 2 weeks' time. Thanks a lot, and have a great day.

Operator

This concludes today's conference call. You may now disconnect.