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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the RadiSys second quarter earnings conference call with Scott Grout, President and CEO of RadiSys. As a reminder, today, Tuesday, July 28th, 2009, this call is being recorded. (Operator Instructions.) Mr. Grout, please go ahead.

Scott Grout - *RadiSys Corporation - President & CEO*

Thank you, Maggie. Good afternoon and thank you for participating in our second quarter conference call. In this call we will review our results from the second quarter, as well as our outlook for the third quarter, and then open the call up for questions.

Participating with me today on this call are Holly Stephens, Finance and Investor Relations Manager, and Brian Bronson, our Chief Financial Officer, as well as myself, Scott Grout, President and CEO.

Before we get started, I'd like to turn the call over to Holly for a caution about forward-looking statements.

Holly Stephens - *RadiSys Corporation - Finance and IR Manager*

Thanks, Scott. Any statements in this call regarding future expectations for the business of RadiSys constitute forward-looking statements that involve a number of risks and uncertainties. We caution you not to place undue reliance on these statements. Factors that could cause actual results to differ materially from those in the forward-looking statements are discussed in our earnings release today and our SEC filings, most recently in our 2008 annual report on Form 10-K.

All information provided in this call is as of today. RadiSys undertakes no duty to update any forward-looking statement to conform the statement to actual results or changes in the Company's expectations. In addition, during the call we will refer to some non-GAAP measures. We provided a GAAP to non-GAAP reconciliation for these measures in our earnings release issued today. Now, I'll turn the call back over to Scott.

Scott Grout - *RadiSys Corporation - President & CEO*

Thanks, Holly. We delivered better than expected results in the second quarter, with revenues of $78.1 million and non-GAAP gross margins of 33.5%, which is up 4.1 percentage points from last year.

We had strong demand for our next generation communications products in the quarter, including a customer-driven acceleration of a network build-out that was originally planned for us in the second quarter.

The growth in our next generation communications revenue, excuse me, has substantially changed our business model over the past couple of years. As a result of our higher gross margin and lower operating expenses, we delivered 7.7% of non-GAAP operating income in the second quarter and further strengthened our cash position.

In the second quarter we launched initiatives within our operations organization to complete our transition to a fully outsourced manufacturing model. We plan to transfer our remaining manufacturing in Hillsboro, Oregon to our manufacturing partners in Asia, including Jabil in Penang and Foxconn in China.

We will be transitioning the majority of our remaining internal production to Jabil, who currently manufactures about 15% of our revenues. Jabil is one of the larger global contract manufacturers, with an excellent reputation for world-class capability and performance.

Foxconn continues to be our largest contract manufacturing partner and we expect to continue to source our production to both Foxconn and Jabil as we move forward. We started transitioning product to Jabil in the second quarter of 2009 and expect to complete the transition by the end of the second quarter of 2010.

Also in the quarter we put in place a plan to consolidate our North American product development into our Hillsboro, Oregon and Vancouver, British Columbia design centers. The plan calls for the transfer of people, technology and programs from our Boca Raton, Florida design center into our other R&D sites in Hillsboro, Oregon; Vancouver, B.C.; Shanghai, China; and Penang Malaysia.

This transfer is expected to increase our new product development capabilities and better enable us to bring more leading new products to market for our R&D investments. Both of these activities are intended to strengthen our ability to develop and deliver more competitive products, while expanding our margin profile over time.

Moving -- excuse me, moving over to design wins. We had another very strong quarter for design wins in each of our target markets, with particular strength in Asia and with our next generation communications products. We won new business that was well-aligned to our strategic goals of increasing the value that we provide and improving our long-term gross margin profile.

In our Media Server product family, we were awarded new business with a North American Tier 1 customer for an interactive voice response, or IVR, program to support an IP teleconferencing application. This application will use our full-featured software Media Server product.

We were also awarded our first Media Server business with a new Tier 1 customer in Asia. This award was for a WiMax application in our customer's home market, and we believe that this win will enable us to expand our Media Server business into these new end markets over time.

In our ATCA portfolio we were awarded new business in deep packet inspection, network security, 3G wireless, packet data and wireless gateway applications. The ATCA wins in the quarter included full platform solutions with both Tier 1 and Tier 2 equipment makers, and were particularly strong in Asia and North America.

Also in the quarter we ramped shipments of our ATCA 7220 packet processing blade to a number of growing Tier 1 and Tier 2 customers. The ATCA 7220 provides the highest level of density of Ethernet interfaces in the industry and offers a complete solution for packet processing applications, such as RNCs, SBC, edge routers, security and media gateway.

In addition, our customers began field deployment of our ATCA platforms into a top North American wireless carrier for a new 3G Femtocell application.

Finally, a recently announced ATCA 4500 processing blade that uses Intel's 5500 series Xeon processors began shipping in production volume in the second quarter. Our customers in Japan and in China awarded us new business for security appliance and packet data applications in the second quarter for this blade.

Finally, in our Commercial business, we were awarded sizeable new rack-mount server business in the second quarter with an existing Tier 1 medical imaging customer.

In addition, we won new COM Express business in the quarter in a wide variety of applications, including military, IP gateway, network analyzer, aircraft video, entertainment and law enforcement.

Moving on to our customers, we continue to make good progress in diversifying our customer base. We expanded our top 10 customer list to include new Tier 1 and Tier 2 customers in both Asia and in North America. Our top five customers in the second quarter, in alphabetical order, were Fujitsu, Miltope, NEC, Nokia Siemens Networks and Philips Healthcare. Collectively, these top five customers represented 68% of our revenue in the quarter.

Our revenues to Nokia Siemens Network in the second quarter were 53% of total company revenues, with a more meaningful percentage now coming from our next generation products. As a reminder, this percentage represents our total revenues to NSN, including our traditional wireless revenues, as well as our ATCA and Media Server revenues sold through NSN.

With that, I'd now like to turn the call over to Brian, who will talk a bit more about our second quarter financial results and projections for the third quarter.

Brian Bronson - *RadiSys Corporation - CFO*

Thanks, Scott. As previously mentioned, our second quarter revenue was $78.1 million, which is down 20% from the prior year, but up 1% from the prior quarter. As expected, revenues were down from the prior year due to reduced demand in our traditional wireless business, as well as softness in our commercial markets. These declines were partially offset by higher revenues in our next generation communications products.

Our GAAP gross margin percentage was 31.1% and was up 6 percentage points year-over-year. While our revenue was down 15% year-to-date, our gross margin dollars were actually up 10%.

Our non-GAAP gross margin rate was 33.5%, up 4.1 percentage points year-over-year, and a point higher than we previously expected. The increases were mainly due to our improving mix of next generation higher-margin products and the customer-requested pull-in that Scott mentioned earlier.

We currently expect our third quarter gross margin percent to be down around 3 points from the second quarter's rate, at the midpoint of the guidance range, due to product mix, increased manufacturing and transition related costs, and lower volume.

GAAP, R&D and SG&A expenses totaled $21.8 million in the second quarter. Non-GAAP R&D and SG&A expenses totaled $20.1 million, which was down $3.8 million or 16% from the prior year, and down $700,000 from the prior quarter. Our expenses were lower than we previously expected due to our ongoing focus on expense control. We currently expect that our total R&D and SG&A expenses will be down again sequentially by approximately $500,000 in the third quarter on both a GAAP and a non-GAAP basis.

In the second quarter we recorded a restructuring charge of $3 million tied to the strategic initiatives in operations and engineering that Scott mentioned earlier. These efforts are expected to result in a workforce reduction of 119 employees, of which 84 are in manufacturing, 28 are in R&D and 7 are in SG&A.

We expect the transitions will be complete in the third quarter of 2010 and are estimated to save $1 million to $2 million a quarter in manufacturing costs, or a full 2 percentage points plus at today's revenue level, reduce inventory levels by $5 million to $10 million, and save $500,000 to $1 million a quarter in operating expenses when complete. The cash payments related to this plan are expected to occur over the next couple quarters.

Our Q1 (sic - see press release) non-GAAP operating income was $6.1 million, or 7.7% of revenues, and was up 2.8 percentage points versus the same quarter last year. As Scott stated previously, with our growing mix of next generation communications revenues and lowered operating expenses, we continue to make meaningful progress on expanding our operating model, despite the ongoing softness in our target markets.

Net non-operating expense, which includes interest income, interest expense and other non-operating items, was $251,000 in the second quarter. We currently expect our non-operating line to be an expense of around $500,000 in the third quarter.

Our non-GAAP tax rate was 15% in the second quarter. As we have stated previously, our tax rates can fluctuate quarter to quarter as changes occur to our projected income by jurisdiction and other discreet items.

In general, our non-GAAP tax rate has come down as more of our income is being generated overseas with lower corresponding tax rates. We currently expect our GAAP and non-GAAP tax rates to be around 10% in the third quarter but, as you guys know, tax projections can vary significantly.

Our basic weighted average shares increased to 23.4 million in the second quarter from 23.1 million in the first quarter. Second quarter non-GAAP diluted weighted average shares were 27.7 million, which includes 3.8 million shares related to our convertible notes.

As a reminder, the net income threshold is $1.8 million to require inclusion of our 3.8 million convertible shares, and associated interest add-back of $291,000 in the EPS calculation. We project our weighted average basic shares to be 23.7 million for GAAP results and our dilutive shares to be around 28 million on a non-GAAP basis.

DSO was 47 days in the second quarter compared to 52 days in the first quarter. Despite an increasingly difficult environment to collect receivables, we've had another great collection quarter. I do expect DSO to gradually increase back up to the mid-50s this year as shipment linearity changes, along with our mix of customer revenues.

Net inventory decreased $2.2 million from the first quarter due to increased scrutiny on supply and demand planning. As we move our remaining manufacturing in Hillsboro to our partners in Asia, we expect that our buffer inventory levels will rise temporarily by about $2 million to $3 million during this transition. However, as I stated previously, we expect to reduce inventory by $5 million to $10 million from today's levels, meaning the second quarter levels, when the transition is complete.

Cash flow from operations in the quarter was $8.3 million and we ended the quarter with $87.6 million of cash and cash equivalents. We currently expect our operating cash flow to be slightly negative to breakeven in the third quarter as we initiate many of our restructuring actions.

Our EBITDA breakeven, excluding restructuring actions, continues to equate to revenue of between $61 million and $64 million, depending on product mix.

With that, I'll turn the call back over to Scott to talk about the revenue and per share outlook for the third quarter.

Scott Grout - *RadiSys Corporation - President & CEO*

Thanks, Brian. Regarding our outlook for the third quarter, please note that this is our view as of today and it is a forward-looking statement subject to risks and uncertainties as discussed previously, and in our press release made available earlier today.

As we have indicated in previous quarters, given the ongoing global economic downturn, our estimates are subject to a higher level of uncertainty than usual. We currently expect third quarter revenues to be between $67 million and $73 million as we expect further softness in our traditional wireless communications markets. We currently expect third quarter GAAP net loss to be between $0.15 and $0.09 per share. Non-GAAP EPS is expected to be between $0.02 and $0.08.

While we continue to make meaningful progress on winning new higher-margin business and deploying our next generation products, we do see continued softness in our more traditional communications and commercial end markets.

In addition to progressing on our core strategies, we are making substantial enhancements to our operating model that will reduce our manufacturing costs, inventory and operating expenses, while growing our overall capabilities to design and deliver market-leading products.

These enhancements, combined with the transformation of our product portfolio to higher value platform products, place us in an even better position to grow our market leadership and resulting financial models.

Before we close, I'd like to invite you to attend our annual Investor Day event on August 25th at 11:00 AM Pacific Time at our company headquarters here in Hillsboro, Oregon. This event is part of the 2009 Silicon Forest Technology and Financial Forum that includes four other neighboring public high-tech companies and several local private companies. I will be presenting, along with other members of the management team, and we will have demonstrations of our latest products.

With that, I'd now like to turn the call over to questions, and I think we're ready to open the call up, Maggie.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions.) Our first question comes from the line of Matt Petkun with D.A. Davidson & Company.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Hi. Good afternoon, guys. Just on the--.

Brian Bronson - *RadiSys Corporation - CFO*

Hey, Matt.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Hey, Brian. On the gross margin mix for next quarter, it sounds like you're seeing more visibility maybe in your mainstream business and less certainty in some of your next generation businesses. Is that fair?

Brian Bronson - *RadiSys Corporation - CFO*

Not necessarily fair. I think what -- the mix can change inside our next gen coms businesses such where, quarter to quarter, we could have gross margin go up or down. So, as you probably have heard, we had a particularly strong first half in Media Servers and I expect ATCA to be up sequentially Q2 to Q3.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Okay. And then when we're looking out beyond this year, is there any visibility -- not visibility, that's probably not fair. But at what point do we start to see more of a contribution from the potential of a 3G ramp in Asia? In China, in particular.

Scott Grout - *RadiSys Corporation - President & CEO*

So, I would say we're seeing a little bit of that now. I would expect as we go out of the end of the year this year and into the beginning of next year, we have a couple of programs that we should start to see some new and incremental revenues on associated with 3G build-out. So, we're experiencing a little bit of that today through our existing customers, existing programs. We've got a couple of new wins that should be relatively short time to money and start ramping up towards the end of the year, beginning of next year.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Okay. And then one other question. I continue to be impressed -- what's that?

Scott Grout - *RadiSys Corporation - President & CEO*

And, I'm sorry, one other point. You probably noticed that, from a geo standpoint, about 44% of our revenues in the last quarter came from Asia.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Right.

Scott Grout - *RadiSys Corporation - President & CEO*

So, it's been particularly strong for us.

Matt Petkun - *D.A. Davidson & Company - Analyst*

It looks like that's more Japan-weighted, but that's still very good.

Scott Grout - *RadiSys Corporation - President & CEO*

Yes.

Brian Bronson - *RadiSys Corporation - CFO*

It is.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Relative to historic.

Scott Grout - *RadiSys Corporation - President & CEO*

Yes.

Matt Petkun - *D.A. Davidson & Company - Analyst*

The other question was just a broader and more strategic question and you can answer it however you want to. You guys have done a great job of controlling the OpEx and R&D continues to go down. I'm wondering, from a broader perspective, where you -- in terms of products specifically -- where you're going to be funneling incremental R&D dollars?

You guys have established a pretty good footprint in advanced ATCA, in Media Server. Is there another area where your customers are seeking help from maybe an outsourced provider of R&D, or is there something else you're focusing on or is it just continue to ramp up using your existing IP portfolio?

Scott Grout - *RadiSys Corporation - President & CEO*

Yes. So, good question, Matt. First of all, we did bring R&D up to a pretty strong level in sort of the '07, '08 timeframe in order to get from no ATCA platform to a big ATCA platform. So inherently, we sort of dialed R&D up quite a bit in order to be able to get to that position.

So, places where we would be putting our R&D dollars on a go-forward basis is, first, we have to keep our ATCA portfolio fresh and competitive, so there'll be upgrades that are done to bring up from 10 gig to 40 gig, increased densities, etc. So, that will be some of the investment.

We're making pretty significant investment in our Media Server business, and then related markets around that Media Server business that are sort of in the video space, a little bit in the gateway space. So, we are trying to put our R&D dollars and investments into places that are consistent with our strategy of more value, more software.

So, CTO team and marketing team have defined a set of products that go a little bit higher up vertically in the stack. We're not in a position yet where we're going to talk an awful lot about that, but that's kind of directionally where we are going.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Okay, great. Thanks so much.

Brian Bronson - *RadiSys Corporation - CFO*

And Matt -- Matt, just to be clear, too, financially for everybody, yes, we did spend $46 million last year in R&D. We're still going to spend $40 million this year. And so, it's all relative, right?

Matt Petkun - *D.A. Davidson & Company - Analyst*

Yes. Oh, no, and I think it's--.

Brian Bronson - *RadiSys Corporation - CFO*

Meaningful.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Yes, it's clearly meaningful. It's just more where the incremental dollars go from a product perspective.

Brian Bronson - *RadiSys Corporation - CFO*

Right. And by the way, we have 250 of our -- call it 550-plus souls in the Company moving forward are engineers.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Right.

Brian Bronson - *RadiSys Corporation - CFO*

So, we're definitely a technology company.

Matt Petkun - *D.A. Davidson & Company - Analyst*

One other question for you and then I'll give it over to everybody else, Brian, just the stock comp decline in the quarter. How should we be looking at that going forward?

Brian Bronson - *RadiSys Corporation - CFO*

I think it was 1.9. I think it was -- we guided to what, 2.3, Holly?

Holly Stephens - *RadiSys Corporation - Finance and IR Manager*

2.1.

Brian Bronson - *RadiSys Corporation - CFO*

2.1. I think it'll be a sub-2 when we get past the Q3 timeframe, Matt.

Matt Petkun - *D.A. Davidson & Company - Analyst*

Yes. Thank you.

Brian Bronson - *RadiSys Corporation - CFO*

Slightly declining.

Scott Grout - *RadiSys Corporation - President & CEO*

Thank you, Matt.

Operator

The next question comes from the line of Ted Jackson with Cantor Fitzgerald.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Thank you. Congratulations on the quarter.

Scott Grout - *RadiSys Corporation - President & CEO*

Thank you, Ted.

Brian Bronson - *RadiSys Corporation - CFO*

Thank you, Ted.

Ted Jackson - *Cantor Fitzgerald - Analyst*

In terms of questions, I wanted to talk first, I guess, about the commercial business. It continues to drop at pretty large sequential rates. And I'm curious when we can expect to see the commercial business bottom out?

Scott Grout - *RadiSys Corporation - President & CEO*

So, as you would expect, that's a question we ask very frequently as well. So the commercial market, I think, is more exposed to some of the economic impact that we're seeing. So, test and measurement's been kind of rugged, healthcare's been kind of rugged, etc.

I don't want to call the bottom, but I'd say the last couple of forecast roles that we've done over the last few weeks it has stopped its rate of decline in terms of what we're seeing internally. So, I think there was probably some channel clearing. We are seeing a couple of upticks in demand, saying, oh, my gosh, late interval requirements.

Brian Bronson - *RadiSys Corporation - CFO*

Right.

Scott Grout - *RadiSys Corporation - President & CEO*

So, the simple answer to your question is my feeling is I think we're probably at the bottom and we'll start to see it gradually rise up again. Like our position in the marketplace, we had a material new win for next generation image server with one of our big customers. So, I think our position remains strong. It's a matter of when the market picks up.

And another thing to mention would be we are starting to see some new business, not just in commercial, but across our product lines in middle aerospace. So, that's an area we're trying to put a little bit more energy to see if we can get deeper penetration there.

Ted Jackson - *Cantor Fitzgerald - Analyst*

So, if I heard you right -- I mean, I'm not sure if I -- it's not that you're expecting necessarily growth in the third quarter, you're just -- like these large double-digit sequential declines maybe you'll -- you're going to -- we're going to see that kind of temper itself out?

Scott Grout - *RadiSys Corporation - President & CEO*

Yes.

Brian Bronson - *RadiSys Corporation - CFO*

Yes. Yes.

Scott Grout - *RadiSys Corporation - President & CEO*

That is correct.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay. And then when you talked about the primary reason for the potential sequential drop in revenue is from your legacy wireless business. And I also heard from the last question you'd said that the ACTA business would actually grow. So, thinking about that in terms of revenue, what you're saying is that the next gen portion we could see some growth and the legacy portion some decline?

Brian Bronson - *RadiSys Corporation - CFO*

So, the legacy definitely will decline sequentially. And that's the biggest driver for the sequential drop. And I think next gen will hang in there.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay. And then you said that the pro forma share count was 27.7?

Brian Bronson - *RadiSys Corporation - CFO*

Correct.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay. Just making sure I had that right. And then I wanted to touch base on ZTE. In the past you've talked about having some success with ZTE in the Media Server business.

Scott Grout - *RadiSys Corporation - President & CEO*

Yes.

Ted Jackson - *Cantor Fitzgerald - Analyst*

And I was curious if you're working with them on -- and you said you were working with them on some newer applications. If you could give an update on that?

Scott Grout - *RadiSys Corporation - President & CEO*

So, that continues to go well. We'll probably continue to remain a little bit oblique on that right now. So, we have one new recent award for a new application. And the funnel looks good, actually, for a couple more. And these particular applications are beyond ZTE, but we're -- continue to grow that relationship pretty nicely.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay. And then my last question, then I'll step out of queue, is in the fourth quarter call, so I'm going back a little bit, in talking about Media Server you had talked about Asia and North America being strong which has, generally speaking, continued to be that way. But you'd said that you'd had a pipeline of activity within Europe that was quite strong. And I was curious if there -- when we might see some of that come through and show itself in your revenue mix.

Scott Grout - *RadiSys Corporation - President & CEO*

I think we will start to see revenue that matters the first half next year and then going in the next year. So, since Q4 of last year, we've turned that pipeline into a number of pretty good wins, pretty attractive wins that should start to grow nicely for us. So, we displaced a major competitor in a big account there that I expect will start turning into revenue first half of next year.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay. Thanks very much.

Scott Grout - *RadiSys Corporation - President & CEO*

Okay. Thanks, Ted.

Brian Bronson - *RadiSys Corporation - CFO*

Thanks, Ted.

Operator

Thank you. The next question comes from the line of George Notter with Jefferies.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Hey, guys. This is Rajiv Jenveja for George Notter.

Brian Bronson - *RadiSys Corporation - CFO*

Hi, Rajiv.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Hey. So, I guess I wanted to start by asking about margins. I heard the comment about the 2 points of incremental profitability from the restructuring. And I guess I'm just wondering, how should we think about the long-term margin profile here? I mean, Nokia Siemens is now 50 -- plus 50% of revenue. As those guys increasingly move over to ATCA and get more active in the Media Server space, how does that -- how do we kind of layer that on top of the 2 points of margin improvement? And where do we ultimately come out in late 2010?

Brian Bronson - *RadiSys Corporation - CFO*

Well, obviously mix aside, you had a taste of the first half. I mean, you got to see our mix of next gen relative to the rest of the business delivered 33.5 points of gross margin. That's without any of the ops improvement.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Yes.

Brian Bronson - *RadiSys Corporation - CFO*

So, if the mix stays similar to what you've seen in the first half, as an example, you can see it going to the lower mid-30s.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Okay. I mean--.

Brian Bronson - *RadiSys Corporation - CFO*

34, 35.

Rajiv Jenveja - *Jefferies & Company - Analyst*

So, the 2 points would be on top of the 33.5, so it'd be at 35.5 and then--.

Brian Bronson - *RadiSys Corporation - CFO*

Yes, if the right mix. And that's why I used the first half because you guys just had a chance to take a peak at the numbers. If the mix stays constant around that, yes. It's as simple as that.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Okay. And then when I look at Nokia Siemens, is there any way to gauge for us how much of that 50%, 53% is next generation revenues right now versus how much of it is more legacy? Just so we can kind of think about what the margin impact can be from that chunk of your business.

Scott Grout - *RadiSys Corporation - President & CEO*

Well, I'll let Brian think about that for a second. I can tell you Q2 was unusually high in terms of next gen content for them.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Okay.

Scott Grout - *RadiSys Corporation - President & CEO*

So -- and that ended up putting them up at a 50% or 53% level.

Brian Bronson - *RadiSys Corporation - CFO*

I would say -- Rajiv, let's leave it that it's relatively small today on a normalized basis, i.e., you think about ATC, you think about Media Server, that's all still to come in a meaningful way.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Okay. Okay. I guess on the -- well, on the China stuff, there's been -- I know you guys have sounded pretty positive on China, both in this call and on the last call. And there's been some chatter of late of inventory build to China Unicom, China Telecom. Are you guys seeing any of that? Does that impact you at all if there is a hiccup there in the next couple months?

Scott Grout - *RadiSys Corporation - President & CEO*

So I mean, we're seeing increasing revenues, an increasing percent of revenue going into Asia in general and China specifically. We try as hard as we can to watch for inventory buildup. I think it's a handful of programs that I think we understand reasonably well. So, I don't think we have a broad-based exposure to it. It's something that we'll have to be careful of, but not something that I'm really worried about in terms of channel buildup and, therefore, having to burn some of that off.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Okay. Okay. And then I guess lastly the broadband seamless package is obviously a hot topic in the industry right now. How do you gauge your exposure to that? Is that a meaningful event for you guys, or what are your thoughts there?

Scott Grout - *RadiSys Corporation - President & CEO*

Well, the nice thing about our business model, ATCA, Media Server in particular, is we get to play in a lot of different applications. So, if it goes WiMax we get to participate in that. If it goes LTE we get to participate in that. If it ends up being DSL to the rural area, we get to participate there. So, I think a general uptick in CapEx, we have a number of different ways to win with that. We're not wedded to any one particular deployment that might end up taking place. So, I think the possibility that it could have a positive impact is definitely there, but it depends on what actually ends up getting funded and spent.

Rajiv Jenveja - *Jefferies & Company - Analyst*

Sure. Sure. Okay, great. Thank you.

Scott Grout - *RadiSys Corporation - President & CEO*

Okay. Thanks, Rajiv.

Brian Bronson - *RadiSys Corporation - CFO*

Thanks.

Scott Grout - *RadiSys Corporation - President & CEO*

Maggie, are you with us?

Operator

I apologize. The next question comes from the line of Greg -- I'm sorry -- Mesniaeff.

Greg Mesniaeff - *Needham & Company - Analyst*

Yes, thank you. This is Greg Mesniaeff at Needham.

Brian Bronson - *RadiSys Corporation - CFO*

Hi, Greg.

Scott Grout - *RadiSys Corporation - President & CEO*

Hello, Greg.

Greg Mesniaeff - *Needham & Company - Analyst*

Hi. A quick question on the geographic breakdown of revenues. It seems that Europe was particularly weak. And I guess that seems to mirror a pattern we've seen with some other equipment providers. I'm wondering if you can comment on what you're seeing, geographically speaking in general; whether the US is starting to show some more positive signs versus different parts of Europe and what you're seeing in those different parts of Europe.

Scott Grout - *RadiSys Corporation - President & CEO*

So, let me answer in two dimensions. One is sort of the design win activity and are decisions getting made and programs funded, and then second on revenue.

We're definitely seeing the US and Asia pick up from where it was the second half of last year with respect to new design initiation and design win awards. So, we went from sort of a locked up period of time where no decisions were being made to pretty healthy in North America and Asia.

I would say Europe right now is in the midst of what was being experienced six or nine months ago in terms of decisions being slowed down a little bit on new program initiatives. So, design wins, North America, Asia pretty strong. Europe I think still some decisions being deferred.

From a revenue perspective, in Asia I'm definitely seeing strength there across a number of different geographies. So for us, Asia means Korea, Japan and China. And then as our customers go into India and other emerging geographies, seeing quite a bit more strength there.

US I think is still a little bit muted, so watching some of the carriers report. They're seeing their earnings down just a little bit because of fixed line deployment. So, it kind of depends on what programs you're in. There are some programs that are growing nicely, others that are contracting. And then finally in Europe, I would say slow from a revenue perspective.

Greg Mesniaeff - *Needham & Company - Analyst*

Thank you.

Scott Grout - *RadiSys Corporation - President & CEO*

Thanks, Greg.

Operator

The next question comes from the line of Ted Moreau with Cardinal Research.

Ted Moreau - *Cardinal Research - Analyst*

Yes, thanks for taking my questions.

Brian Bronson - *RadiSys Corporation - CFO*

Hi, Ted.

Ted Moreau - *Cardinal Research - Analyst*

How's it going, guys?

Brian Bronson - *RadiSys Corporation - CFO*

Good.

Ted Moreau - *Cardinal Research - Analyst*

On the project that was pulled into the quarter, it looks like it was a couple million dollars. Do I have that right? And then can you just kind of comment on what might have caused the pull-in and did this cause any unusual linearity in the quarter?

Brian Bronson - *RadiSys Corporation - CFO*

So, you're right. It's a couple million bucks. And did it cause any unusual linearity in the quarter, not so much.

Ted Moreau - *Cardinal Research - Analyst*

Okay. And then on the gross margin for the Q3 -- and I know you mentioned ATCA shift for Q3.

Brian Bronson - *RadiSys Corporation - CFO*

Plus; volume plus our ops transition costs.

Scott Grout - *RadiSys Corporation - President & CEO*

Ted, are you there? Maggie, did we lose Ted?

Operator

Yes, sir?

Scott Grout - *RadiSys Corporation - President & CEO*

Maggie, did we lose Ted? He was asking a question --.

Operator

We did. I apologize. Yes, we did. Our next question comes from the line of David Nierenberg.

David Nierenberg - *Nierenberg Investment Management - Analyst*

Hi, guys. Can you hear me?

Scott Grout - *RadiSys Corporation - President & CEO*

Yes, I can, David. Sorry for the interruptions.

David Nierenberg - *Nierenberg Investment Management - Analyst*

Congratulations on a very nice quarter.

Scott Grout - *RadiSys Corporation - President & CEO*

Thank you.

Brian Bronson - *RadiSys Corporation - CFO*

Thanks, David.

David Nierenberg - *Nierenberg Investment Management - Analyst*

I just wanted to make two points that stem from my own unfortunate legal training and my own service over the years on the boards of public companies, which is that press releases are carefully written and the numbers in them are carefully written, too. There's a couple things in your press release that I just want to highlight because they wouldn't have gotten in there unless you guys felt pretty good about them.

One of them may be obvious, but that is the enormous change in your net working capital position as a result of the calendar moving forward on the expected timing of your payment from UBS. Your net working capital has grown sequentially from $64.5 million to $132 million. That must reflect the continued expectation and certainty on your part about the probability of the payoff of the ARS's, which I think is terrific.

The second thing I want to note is that you wouldn't have said that the transition would be possibly improving gross profit margin by $1 million to $2 million unless you thought it could be $1 million to $2 million. If you thought it was only $1 million, you would have said $1 million. So, I want to note that $1 million to $2 million is a potential pickup of 200 to 400 basis points in gross profit margin, assuming a similar mix, which is not just 35.5%, but is potentially 37.5%.

So, congratulations on both of those things.

Brian Bronson - *RadiSys Corporation - CFO*

Thanks, David.

Scott Grout - *RadiSys Corporation - President & CEO*

Thank you, David. Good observations.

Operator

Thank you. (Operator Instructions.) And we'll go ahead and take a question from Ted Jackson.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Hey, Brian, what's your outlook for inventory for the third quarter?

Brian Bronson - *RadiSys Corporation - CFO*

Well, it finished up at $26.5 million in the second quarter. I mentioned it'd be up $2 million or $3 million.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay.

Brian Bronson - *RadiSys Corporation - CFO*

So call it $28 million, $29 million. And that should be the peak. And then, more importantly, taking it down $5 million or $10 million from the $26.5 million when we're done.

Scott Grout - *RadiSys Corporation - President & CEO*

And that's to fund a little bit of a buffer to support the transition.

Brian Bronson - *RadiSys Corporation - CFO*

Making sure no disruption to customers.

Ted Jackson - *Cantor Fitzgerald - Analyst*

And then, I know it's an unfair question but I'm going to ask it anyway. The third quarter revenue guidance, a little disappointing. Not really, to be honest, a tremendous surprise given what's going on in the world. But do you think that you could potentially show some sequential growth in the fourth quarter? Top line?

Brian Bronson - *RadiSys Corporation - CFO*

Potentially. But I'll stick to -- I mean, I'd love to be able to know more. Visibility is just enough for us to be able to comment today on the call. So, yes, it's possible.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Okay.

Brian Bronson - *RadiSys Corporation - CFO*

It's possible.

Ted Jackson - *Cantor Fitzgerald - Analyst*

Thanks a bunch.

Scott Grout - *RadiSys Corporation - President & CEO*

Thanks, Ted.

Operator

And I'm showing no further audio questions at this time.

Scott Grout - *RadiSys Corporation - President & CEO*

Okay. Well, thank you, Maggie. And thank you all for participating on our call and looking forward to talking to all of you soon. Thank you.

Operator

Thank you for participating in today's conference. You may now disconnect.
