# > Q3 2006 Financial Results Conference Call

November 7, 2006

NORTEL

Business made simple

# Welcome

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- Further, actual results or events could differ materially from those contemplated in forward-looking statements as a result of the following (i) risks and uncertainties relating to Nortel’s restatements and related matters including: Nortel’s most recent restatement and two previous restatements of its financial statements and related events; the negative impact on Nortel and NNL of their most recent restatement and delay in filing their financial statements and related periodic reports; legal judgments, fines, penalties or settlements, or any substantial regulatory fines or other penalties or sanctions, related to the ongoing regulatory and criminal investigations of Nortel in the U.S. and Canada; any significant pending civil litigation actions not encompassed by Nortel’s proposed class action settlement; any substantial cash payment and/or significant dilution of Nortel’s existing equity positions resulting from the approval of its proposed class action settlement; any unsuccessful remediation of Nortel’s material weaknesses in internal control over financial reporting resulting in an inability to report Nortel’s results of operations and financial condition accurately and in a timely manner; the time required to implement Nortel’s remedial measures; Nortel’s inability to access, in its current form, its shelf registration filed with the United States Securities and Exchange Commission (SEC), and Nortel’s below investment grade credit rating and any further adverse effect on its credit rating due to Nortel’s restatements of its financial statements; any adverse affect on Nortel’s business and market price of its publicly traded securities arising from continuing negative publicity related to Nortel’s restatements; Nortel’s potential inability to attract or retain the personnel necessary to achieve its business objectives; any breach by Nortel of the continued listing requirements of the NYSE or TSX causing the NYSE and/or the TSX to commence suspension or delisting procedures; (ii) risks and uncertainties relating to Nortel’s business including: yearly and quarterly fluctuations of Nortel’s operating results; reduced demand and pricing pressures for its products due to global economic conditions, significant competition, competitive pricing practice, cautious capital spending by customers, increased industry consolidation, rapidly changing technologies, evolving industry standards, frequent new product introductions and short product life cycles, and other trends and industry characteristics affecting the telecommunications industry; the sufficiency of recently announced restructuring actions, including the potential for higher actual costs to be incurred in connection with these restructuring actions compared to the estimated costs of such actions and the ability to achieve the targeted cost savings and reductions of Nortel’s unfunded pension liability deficit; any material and adverse affects on Nortel’s performance if its expectations regarding market demand for particular products prove to be wrong or because of certain barriers in its efforts to expand internationally; any reduction in Nortel’s operating results and any related volatility in the market price of its publicly traded securities arising from any decline in its gross margin, or fluctuations in foreign currency exchange rates; any negative developments associated with Nortel’s supply contract and contract manufacturing agreements including as a result of using a sole supplier for key optical networking solutions components, and any defects or errors in Nortel’s current or planned products; any negative impact to Nortel of its failure to achieve its business transformation objectives, including completion of the sale of its UMTS access business to Alcatel; additional valuation allowances for all or a portion of its deferred tax assets; Nortel’s failure to protect its intellectual property rights, or any adverse judgments or settlements arising out of disputes regarding intellectual property; changes in regulation of the Internet and/or other aspects of the industry; Nortel’s failure to successfully operate or integrate its strategic acquisitions, or failure to consummate or succeed with its strategic alliances; any negative effect of Nortel’s failure to evolve adequately its financial and managerial control and reporting systems and processes, manage and grow its business, or create an effective risk management strategy; and (iii) risks and uncertainties relating to Nortel’s liquidity, financing arrangements and capital including: the impact of Nortel’s most recent restatement and two previous restatements of its financial statements; any inability of Nortel to manage cash flow fluctuations to fund working capital requirements or achieve its business objectives in a timely manner or obtain additional sources of funding; high levels of debt, limitations on Nortel capitalizing on business opportunities because of support facility covenants, or on obtaining additional secured debt pursuant to the provisions of  indentures governing certain of Nortel’s public debt issues and the provisions of its support facility; any increase of restricted cash requirements for Nortel if it is unable to secure alternative support for obligations arising from certain normal course business activities, or any inability of Nortel’s subsidiaries to provide it with sufficient funding; any negative effect to Nortel of the need to make larger defined benefit plans contributions in the future or exposure to customer credit risks or inability of customers to fulfill payment obligations under customer financing arrangements; any negative impact on Nortel’s ability to make future acquisitions, raise capital, issue debt and retain employees arising from stock price volatility and further declines in the market price of Nortel’s publicly traded securities, or the planned share consolidation resulting in a lower total market capitalization or adverse effect on the liquidity of Nortel’s common shares. 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# Agenda

1. General Update
2. Q3 2006 Financials
3. Guidance
4. Plans / Priorities
5. Q&A

# Q3 2006 General Update

> Sales (+17%) with strong revenue growth in next gen products and completion of contracts
  - Deferred Revenue down $171M in Q3'06 and $45M YTD

> Orders (flat)
  - Book To Bill 0.8 with timing of CDMA orders and decreasing UMTS/GSM activity
  - Backlog still strong at $5.2B

> Gross Margin at 38.1% – competitive market drives a sub 40% margin for 5th consecutive quarter

> Material Cost Initiatives: Flextronics Contract Amendments – completed

> Programs to Improve Competitiveness – acceleration of Business Transformation Initiatives

> Increasing customer and employee satisfaction trends

> Promising customer wins

# Customers actively investing in the future with Nortel
## Selected Q3 Wins

> Wireless
- CDMA – Embratel, Brazil
- WiMAX – Craig Wireless, Greece
- GSM-R – Indian Railways, African Railway, Spain

> Metro Ethernet
- Carrier Ethernet – Shanghai Telecom
- OME 6500 – COLT, Golden Telecom, Southern Cross

> Secure Routers
- Hanson Professional Svcs
- Austin Cancer Centers
- Superior Community Credit Union

> Enterprise IP Solutions
- New York Times
- The Economist Group, UK
- Westin Beijing Financial Street
- The Telegraph Group, UK
- Montreal Canadiens

> Carrier VoIP/IMS
- Swisscom and Sunrise,
- KVH Co, Ltd., Japan
- Videotron, Canada
- COMCOR, Russia

> Services
- Rolls Royce
- HOT Telecom
- NRC

# Orders

## US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| North America | 1,235 | 1,179 | 5% |
| EMEA | 569 | 614 | (7%) |
| Asia | 429 | 379 | 13% |
| CALA | 117 | 188 | (38%) |
| **Total** | **2,350** | **2,360** | **--** |

> Book to Bill 0.8 – Drivers:
- Large CDMA Orders in Q2'06
- Decreasing UMTS/GSM activity

> Backlog down $0.6B to $5.2B

# Q3 2006 Financial Highlights

## US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| Revenue | $3.0B | $2.5B | 17% |
| Gross Margin | 38.1% | 38.8% | (1pts) |
| SG&A | 20.5% | 22.5% | (2pts) |
| R&D | 16.2% | 17.6% | (1pts) |
| Operating Expenses | $1.1B | $1.0B | 7% |
| Operating Margin* | 1.4% | -1.3% | 270 BPs |
| Other** | $109M | $53M | ($56M) |
| EBT*** | ($69M) | ($85M) | $16M |
| Net Earnings | ($99M) | ($136M) | $37M |
| Cash Flow from (used in) Ops | ($46M) | ($144M) | $98M |
| Period-End Stock Price | $2.30 | $3.26 | ($0.96) |

***Operating Margin is a non-GAAP measure defined as Gross Margin less SG&A and R&D expenses divided by revenue**
****Amortization of Intangibles, Shareholder Settlement expenses, Special Charges, Gain of Sale of Business, Other Income/Expense, Interest Expense, IPR&D**
*****Earnings from continuing operations before income taxes, minority interests and equity in net earnings (loss) of associated companies**

# Mobility and Converged Core Revenue

US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| **Mobility and Converged Core** | **1,540** | **1,251** | **23%** |
| CDMA | 704 | 514 | 37% |
| GSM/UMTS | 563 | 522 | 8% |
| Circuit and Packet Voice | 273 | 215 | 27% |

> CDMA: Growth driven primarily in N.A. by EV-DO Rev A
- momentum expected for remainder of year
- EV-DO rev A to continue through 2007

> GSM/UMTS: Growth driven primarily by completion of contracts in EMEA
- Sale of UMTS access to Alcatel on track for end of year
- Revenues expected to start declining

> Circuit and Packet Voice: Growth driven primarily by Succession in N.A. and EMEA

> WiMAX Momentum:
- Nortel 4G technology field trail with Russia's Golden Telecom
- deployment with Craig Wireless in Greece

# Metro Ethernet Networks Revenue

## US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| **Metro Ethernet Networks** | **430** | **363** | **18%** |
| Optical Networking | 312 | 259 | 20% |
| Data Networking and Security | 118 | 104 | 13% |

> Optical Networking: Continued profitable growth, #1 in Metro DWDM

- Optical Multiservice Edge 6500 momentum with COLT, Golden Telecom, and Southern Cross
- Optus contract completion

> Data Networking and Security

- Shanghai Telecom Metro Ethernet Networking Solution
- Sole vendor to show live Provider Backbone Transport (PBT) demonstration at Carrier Ethernet World Congress

# Enterprise Networks Revenue

US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| **Enterprise Networks** | **609** | **534** | **14%** |
| Circuit Packet Voice Solutions | 430 | 357 | 20% |
| Data Networking & Security Solutions | 179 | 177 | 1% |

> Circuit and Packet Voice: Highest revenue in last 5 quarters
- Momentum on BCM50, benefits from IPT 123 program
- IP Telephony growth driving 2H06 growth
- NY Times for Nortel IP phones, VoIP, unified messaging, contact center, and data and security solutions

> Data Networking and Security:
- Wireless Mesh for Tokyo's Takamatsu City Shopping Arcade

# Global Services Revenue

## US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| Global Services | 316 | 305 | 4% |

- > First quarter of reporting services revenues
  - Excluded networking implementation services
- > New Operational Model – 4 service product groups, 2 business solution groups
- > Vidéotron multi-year contract as primary VoIP technology and professional services provider
- > Swisscom for carrier-hosted VoIP business solution
- > Microsoft-Nortel Innovative Communications Alliance primary services integrator

# Geographic Revenue

## US$M

| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| North America | 1,535 | 1,414 | 9% |
| EMEA | 809 | 618 | 31% |
| Asia | 474 | 312 | 52% |
| CALA | 137 | 174 | (21%) |
| **Total** | **2,955** | **2,518** | **17%** |

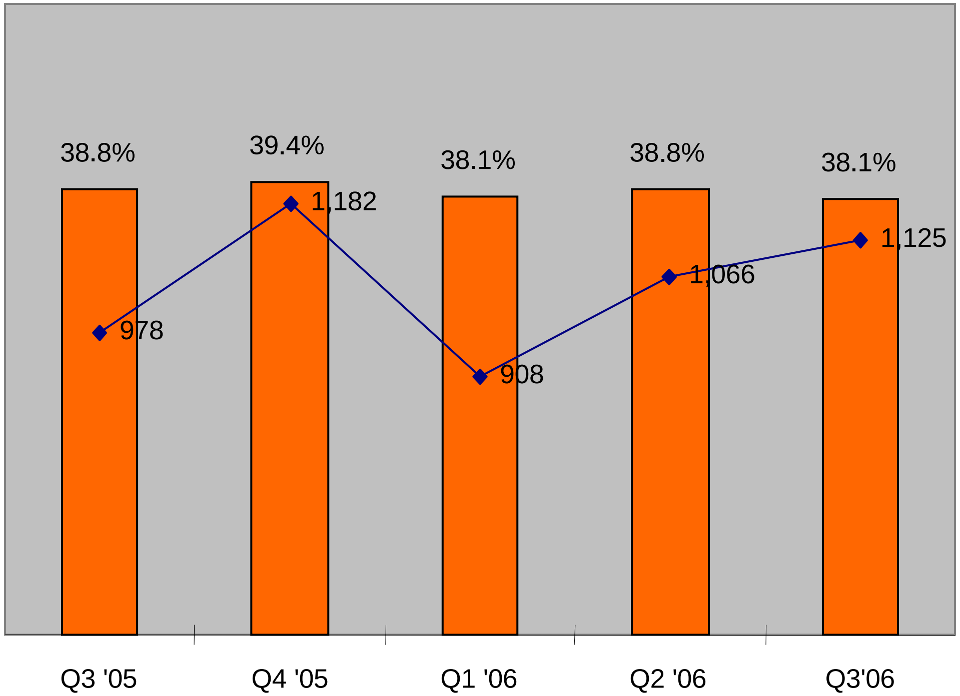
> N. America, EMEA and Asia Pacific comparisons vs. prior year impacted in part by timing of revenue recognition (negative for N.A., positive for others)

> Broad based revenue growth expected for rest of 2006

> LG and NGS produced $86M incremental revenue (partially offset by $16M of lower revenue from exited lines)

# Gross Margin

## US$M

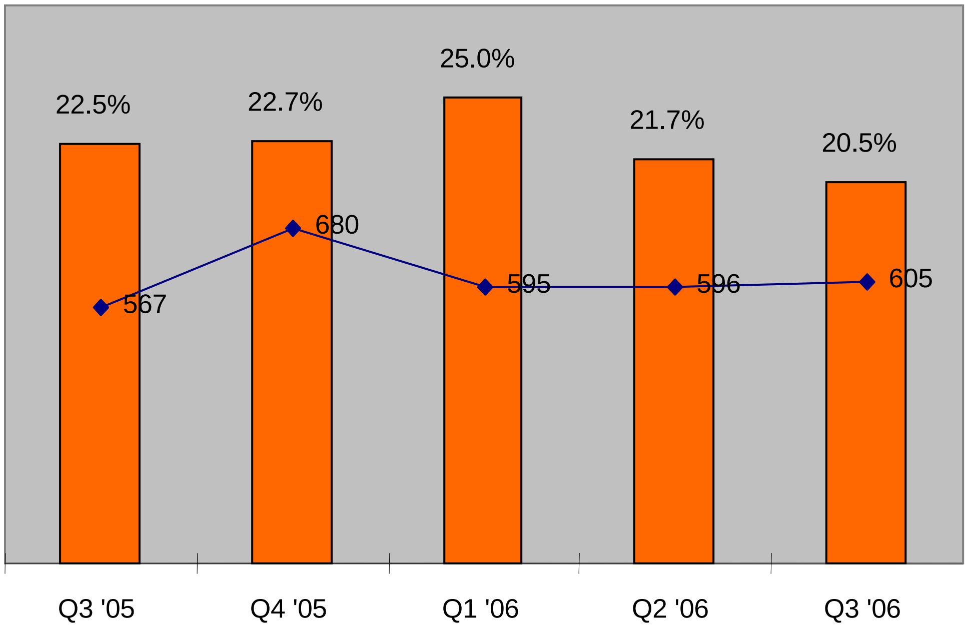



| | Q3'06 | Q3'05 | △ |
|---|---|---|---|
| $ | 1,125 | 978 | 147 |
| % Rev | 38.1% | 38.8% | (1pt) |

- > Sequential and YoY GM% decreased by 70 bps
- > Impacted by higher proportion of next generation product sales
- > Increased pricing pressures in EMEA and emerging markets
- > Regional mix as well EUED Compliance costs

# SG&A

## US$M

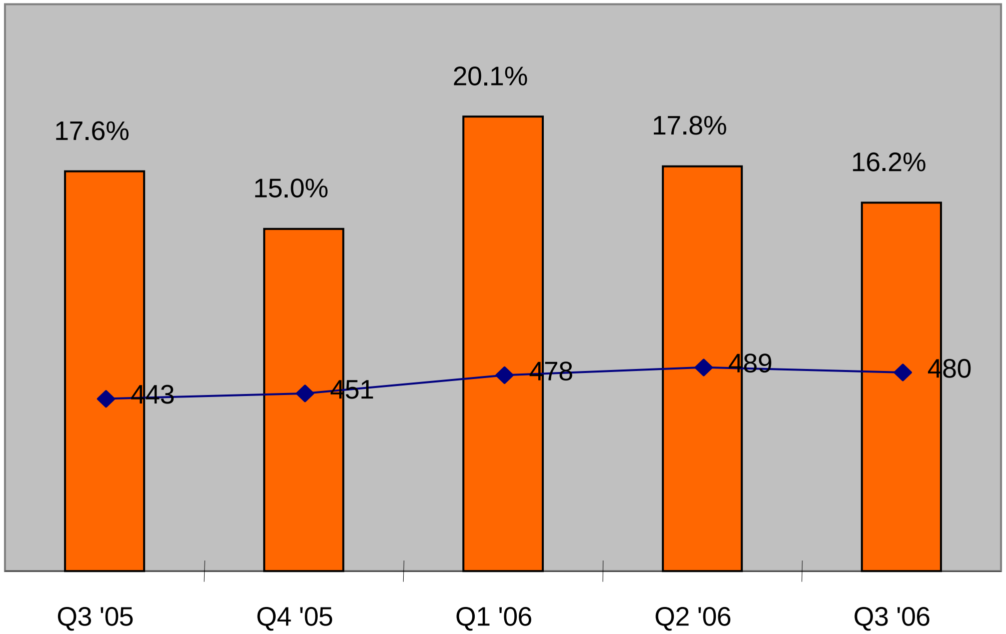



| | Q3'06 | Q3'05 | Δ |
|---|---|---|---|
| $ | 605 | 567 | (38) |
| % Rev | 20.5% | 22.5% | 2pts |

> Q3'06 included:
- Nortel-LG JV SG&A costs
- Business Transformation investment
- Continued impact of cost containment initiatives

# R&D

## US$M




| | Q3'06 | Q3'05 | △ |
|---|---|---|---|
| $ | 480 | 443 | (37) |
| % Rev | 16.2% | 17.6% | 1pts |

> Q3'06 included
- Increased investment in targeted product areas: video, IMS, and WiMAX
- LG JV R&D costs
- Savings associated with 2006 Restructuring

# Q3 2006 Highlights

## US$M

| | Q3'06 | Q3'05 | △ | Q3'06 YTD | Q3'05 YTD | △ |
|---|---|---|---|---|---|---|
| Revenue | $3.0B | $2.5B | 17% | $8.1B | $7.5B | 7% |
| Gross Margin | 38.1% | 38.8% | (1pts) | 38.3% | 41.5% | (3pts) |
| SG&A | 20.5% | 22.5% | (2pts) | 22.2% | 23.0% | (1pts) |
| R&D | 16.2% | 17.6% | (1pts) | 17.9% | 18.7% | (1pts) |
| Operating Expenses | $1.1B | $1.0B | 7% | $3.2B | $3.1B | 3% |
| Operating Margin* | 1.4% | -1.3% | 270 BPs | -1.8% | -0.2% | (160 BPs) |
| Other** | $109M | $53M | ($56M) | ($326M) | $173M | $499M |
| EBT*** | ($69M) | ($85M) | $16M | $166M | ($187M) | $353M |
| Net Earnings | ($99M) | ($136M) | $37M | $100M | ($273M) | $373M |
| Cash Flow from (used in) Ops | ($46M) | ($144M) | $98M | ($328M) | ($297M) | ($31M) |
| Period-End Stock Price | $2.30 | $3.26 | ($0.96) | $2.30 | $3.26 | ($0.96) |

*Operating Margin is a non-GAAP measure defined as Gross Margin less SG&A and R&D expenses divided by revenues
**Amortization of Intangibles, Shareholder Settlement expenses, Special Charges, Gain of Sale of Business, Other Income/Expense, Interest Expense, IPR&D
***Earnings from continuing operations before income taxes, minority interests and equity in net earnings (loss) of associated companies

# Significant Impact Items

## (US$M, except for per share figures)

| | Q3'06 | IMPACT PER DILUTED SHARE |
|---|---|---|
| Pension Restructure Benefit | 43 | $0.01 |
| Shareholder Settlement Expense Mark to Market Adjust | (38) | ($0.01) |
| Restructuring Charges | (25) | ($0.01) |
| Gain on Sale / Lease Back | 16 | $0.004 |

# Cash Flow

US$M

| | Q3'06 | Q2'06 |
|---|---|---|
| **Net Cash - Beginning of Period** | **1,904** | **2,695** |
| From (used in) operating activities | (46) | (108) |
| Investing Activities | 53 | (569) |
| Financing Activities | 683 | (153) |
| F/X Effect | 6 | 39 |
| Change in Cash | 696 | (791) |
| **Net Cash - End of Period** | **2,600** | **1,904** |

# Operating Metrics

## US$M

| | Q3'06 | Q2'06 |
|---|---|---|
| DSO (Days) | 85 | 91 |
| NID (Days) | 27 | 34 |
| DPO (Days) | 43 | 56 |
| Deferred Revenue | $3.5B | $3.7B |
| Book to Bill | 0.8 | 1.1 |
| Order Backlog | $5.2B | $5.9B |

# Guidance

> Fourth Quarter 2006
  - We expect revenue growth in the mid to high single digits compared to the fourth quarter of 2005,
  - gross margin to be between 38 and 39 as a percentage of revenue and
  - spending to be approximately flat compared to the fourth quarter of 2005.

> Full Year 2006
  - We now expect mid to high single digit revenue growth for the full year 2006 compared to 2005,
  - full year gross margin to be between 38 and 39 as a percentage of revenue, and
  - we continue to expect operating expenses to be flat to up slightly from 2005.

# Our Plan and Framework

## Near term, long term and foundational

### BIG—NEAR TERM PRIORITIES

- > **Business Transformation**
- > Integrity Renewal
- > **Growth Imperatives**

### 6-POINT PLAN—LONG TERM

Foundational

- > World-class management team, culture and processes
- > Aggressive focus on the balance sheet, corporate governance and business/financial controls
- > Drive to world-class cost structure and quality levels

Growth

- > Target 20% share for all key activities
- > Invest for profitable growth
- > Increased emphasis on service and software solutions

### OPERATING RHYTHM—FOUNDATIONAL

- > I. People
- > II. Strategy
- > III. Product (MGPD)
- > IV. Budget

# Q3 Update :
# Business Transformation Progress

| BT TEAMS | 3 YEAR TARGET | SAVINGS DRIVERS |
|---|---|---|
| **Direct Materials (Supply Chain)** (J. Hackney/J. Townley) | $425M + | • Flextronics Agreement Amended<br>• Clean Sheet<br>• Design Simplification/Cost Reduction |
| **Service & Operations** (D.Wendt/J. Hackney/S. Chilton) | $250M+ | • COE's launched in Turkey & Mexico<br>• Partner & Maintenance Services<br>• Shared Tech Services (COE's) |
| **Revenue Stimulation & Pricing** (D. Joannou/E. Schoch) | $200M+ | • Go to Market<br>• VoIP initiative<br>• Global Pricing |
| **R&D** (Product presidents/H. Graham) | $225M+ | • Clean Sheet<br>• USDRP<br>• Test Transformation<br>• E2E |
| **G&A/Organization** (D. Carey/B. Donovan) | $200M+ | • Pension<br>• Spans & Layers<br>• Shared Services<br>• G&A supply Initiatives |
| **Financial** (P. Currie/A Bifield) | $200M+ | • SAP Implementation<br>• Finance business and process transformation |
| | $1,500M+ | |

**Thru Q3 2006 delivered $60M recurring savings in year**
**Expect $100M+ total recurring savings by year end 2006**

# Actions to Achieve Business Model

- > More rapid implementation of changes
- > Global Standard Benchmarking
- > Amendment of Flextronics partnership
- > Broaden application of “clean sheet” methodology
- > Acute focus on working capital

# Savings Acceleration -- Goals:

> G&A expenses to benchmark levels (50% by mid 2007 / Balance 2008; Finance 33% by mid 2007 / Balance 2008)
  - 500 BPs improvement by 2008

> R&D run rate to 15% of revenues by mid-2007

> Pull forward Direct Material Savings (nearly 50% in 2007)

> Reduce Real Estate expenses by 20% (2007 exit rate). Approximately $75M vs. 2006

# Working Capital:

Major elements:

- > Accounts Receivables X
- > Inventory X
- > Accounts Payable ✓

Actions:

- > Billing Collection Cycle
- > Contracting
- > Supplier Terms
- > Production/Staging Process

Significant Roll for Lean 6 Sigma Teams

**Target $500M for 2007**

# Growth Imperatives

**ACTIONS WE ARE EXECUTING**

### Enterprise Momentum

Invested in and strengthened channels
Boosted SMB initiatives
IP Solutions momentum
Secure Router momentum

### Services Business

Established new operational model
Invested in tools & Processes

Expanded services portfolio

### Mobility and Convergence

Mobile WIMAX launch
Metro Ethernet momentum
Global Carrier VoIP momentum

### Partnerships

Runcom -- WIMAX
Broadstream – IPTV
Microsoft

**FOUNDATION WE ARE BUILDING**

**Next Generation Mobility**

**Enterprise Transformation**

**Services and Solutions**

**November 15th Analyst Day Discussions**

# Summary

> Solid Revenue Growth
  - Strong foundational business
  - Positive contribution from all regions

> Committed to acceleration of profitability model

> Integrity—forthright and transparent

> Commitment to growth and strong financials

Passionate, Relentless Pursuit of Superior Results and Doing the Right Thing

> Q&A

Business made simple