



Airgain, Inc.

Third Quarter 2016 Earnings Call

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CORPORATE PARTICIPANTS

Charles Myers, *President and Chief Executive Officer*

Leo Johnson, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Matt Robison, *Wunderlich*

Tom Sepenzis, *Northland Capital Markets*

Scott Billeadeau, *Walrus Partners, LLC.*

Orin Hirschman, *AIGH Investment Partners*

PRESENTATION

Operator:

Good afternoon. Welcome to Airgain's Third Quarter 2016 Earnings Conference Call. Joining us for today's call are Airgain's President and CEO, Charles Myers and CFO Leo Johnson. Following their remarks, we will open up the call for questions.

Please note that certain information discussed on the call today is covered under the Safe Harbor provisions of the Private Securities Litigation Reform Act. I caution listeners that during this call Airgain Management will be making forward-looking statements about the future events and Airgain's business strategy and future financial and operating performance.

Actual results could differ materially from those stated or implied by these forward-looking statements due to risks and uncertainties associated with the Company's business. These forward-looking statements should be considered in conjunction with, and are qualified by, the cautionary statements contained in Airgain's earnings press release and SEC filings, including its S-1 and Quarterly Report on Form 10-Q, which the Company expects to file by November 14, 2016.

This conference call contains time-sensitive information and is accurate only as of the date of this live broadcast, November 10, 2016. Airgain undertakes no obligation to revise or update any forward-looking statements to reflect events or circumstances after the date of this conference call.

This conference call will also include a discussion of non-GAAP financial measures, including Adjusted EBITDA. Please see today's earnings release, which is posted on Airgain's website, for further details, including a reconciliation of the GAAP to non-GAAP results. Any discussion of non-GAAP measures is not intended to detract from the importance of comparable GAAP measures.

Finally, I would like to remind everyone that this call would be recorded and made available for replay via a link available in the Investor Relations section of the Company's website at www.airgain.com.

Now, I would like to turn the call over to Airgain's President and CEO, Charles Myers. Sir, please proceed.

Charles Myers:

Thank you, Tony (phon). Welcome everybody and thank you for joining us today. After the market closed, we issued a press release announcing our results for the third quarter ended September 30, 2016, a copy of that is available on the Investor Relations section of our website.

I'd like to start the call today by welcoming the former COO of Time Warner Cable Media, Joan Gillman, to our Board of Directors. For those of you that did not have an opportunity to read the press release announcing her appointment this week, Joan has served in multiple leadership roles at Time Warner and its media and advertising sales division, Time Warner Cable Media. She not only has a wealth of experience in the connected home market, but also brings a deep insight to the cable industry, one of our core markets, making her an ideal candidate and help shape our strategic roadmap, especially during this time of such rapid growth for our company.

Throughout her career, Joan has proven she is a visionary leader capable of inspiring others and drawing from her talent and experience to help transform major organizations. We are very fortunate to have her on our Board and look forward to her guidance and contributions, as we continue to expand our market share and global footprint.

Transitioning to our results for the third quarter, we are pleased on how our overall numbers came in. Building on the progress we made in second quarter, the third quarter represented another period of strong top-line growth matched by our ability to maintain healthy margins, and ultimately, generate profitability for our shareholders.

Sales, which were partially affected by some seasonal factors, grew by 87% to \$12.4 million, driven by a continued growth in our carrier gateway and set top box segments, but also the emerging prominence of our Smart TV segment. In fact, we recently shipped our 25 millionth antenna to the Smart TV market last month. We believe this, and other positive developments in both our business and the industry as a whole, reflect only a small part of our attractive growth opportunities ahead of us.

But, before I provide any further details about our operational results, growth strategies, and outlook, I'd like to turn the call over to our CFO, Leo Johnson, who will walk us through the financial results for the third quarter and first nine months of 2016. Leo?

Leo Johnson:

Thank you, Chuck, and good afternoon to everyone. Before I begin, I would like to mention that simply looking at our quarterly numbers on a sequential basis may not provide a full picture of the progress and performance of our business. This is primarily due to the natural seasonality of our business, which is reflective of the industry we are in. For those of you who are newer to our story, our results are usually affected by some of our customers make purchasing decisions around holidays.

For example, in China, all businesses observe a national holiday in the first week of November. This, and along with customer demand or product cycles that can impact our top-line, sometimes contribute to strong quarterly sequential growth, since many of our customers purchase ahead of the holiday season to account for higher volume requirements in the fourth quarter.

For the same reason, our historical sequential growth Q4 over Q3 is reflective of lower purchasing days in China, which again also depends on the customer demand and product cycles of that particular quarter and we would expect to see a similar seasonal effect this year.

In addition, the Chinese New Year is another holiday that contributes to the seasonality of our business. During these two weeks of celebration in the first quarter ending March 30, the Chinese businesses are off from work. This creates a temporary drop in the demand for our solutions, causing the results for the first quarter to be down sequentially compared to the fourth quarter of the prior year.

Given the seasonality of our business, we will be providing year-to-date results in addition to quarterly results, whenever appropriate. We believe this practice puts us more in line with the companies in our industry, and it aligns our focus on the long-term growth of the Company, rather than quarter-to-quarter fluctuations that often distort the real measures of our success.

Now, turning to the financial results for the third quarter and the nine months ended September 30, 2016. Our sales for the third quarter increased 87% to \$12.4 million from \$6.7 million in the same period a year ago. For the first nine months, our sales increased 67% to \$30.8 million from \$18.5 million in the same period a year ago. The quarterly and the nine-month increases were primarily driven by increases in our product sales. Our gross margin for the third quarter of 2016 increased 101% to \$5.6 million, or 44.8% of sales, from \$2.8 million, or 41.6% of sales, in Q3 of last year.

For the first nine months of this year, gross profit increased 77% to \$13.8 million, or 44.8% of sales, from \$7.8 million, or 42.3% of sales, compared to the same period a year ago. The increase in gross profit for sales for both Q3 and the nine months ended this year was primarily due to an increase in the sales of our board-mounted antennas, which typically have higher gross margins percentage. As we stated in our last call, our target gross margin is at least 40%, and we expect to continue to achieve this target moving forward.

Now turning to expenses. Our total operating expenses for the third quarter increased 53% to \$4.3 million from \$2.8 million in a year ago. For the nine months, total operating expenses increased 38% to \$11.5 million from \$8.3 million in the same period a year ago. The expenses in both periods were primarily due to higher personnel expenses to support the Company's sales and marketing and R&D initiatives and also includes incremental cost related to the public offering.

For the nine months ended 2016, net income attributable to common stockholders totaled \$1.1 million or \$0.25 per diluted share. This was an improvement from the net loss attributable to common stockholders of \$2.1 million or a loss of \$3.70 per diluted share in Q3 of last year.

Our Adjusted EBITDA, which we define as earnings before taxes, depreciation, amortization, fair market value, and adjustments for warrants, I'm sorry, I'll go back, I skipped a paragraph, and stock-based compensation increased \$1.6 million from \$73 million a year-ago. For the first nine months, our Adjusted EBITDA totaled \$3.2 million, a significant improvement from the \$123,000 from the same period a year ago.

This is the best thing I skipped unfortunately, our net income attributable to common shareholders for Q3 of 2016, totaled \$861,000 or \$0.16 per share on a diluted basis. This was an improvement from net loss attributable to common shareholders to \$617,000 or \$1.05 per share on a per diluted share basis Q3 a year-ago.

This completes my—one other thing to add. Now turning back to the balance sheet. Cash and cash equivalents at the end of the third quarter totaled \$16.8 million, which was up \$5.3 million from the quarter ago. The increase was primarily due to the net proceeds of \$10.8 million received from our IPO in August. This completes my financial summary.

I will now turn the call back over to Chuck. Chuck?

Charles Myers:

Thanks, Leo. I started off at the beginning talking about some of the key areas of our business where we saw encouraging growth for both the quarter and year-to-date thus far. Our carrier gateway and set top box segments continue to represent the core of our business, as many of these carriers, OEMs, and chipset suppliers continue to rely on our high-performance embedded antenna solutions.

In both the connected and the IoT space, we're seeing the rapid proliferation of wireless networking, which, of course, is only made possible by more robust and advanced antenna solutions. We believe very few providers can provide these solutions, given the increasing complexity of both the designing and testing the antenna systems to ensure maximum throughput. These are just some of the reasons why we have continued to grow globally and become a trusted partner in enabling the next-generation wireless networking.

A newer area that has seen some encouraging growth over the past few quarters, and particularly during Q3 when compared to year-over-year basis, has been our Smart TV segment. Over the past two years, we have grown the production of our antennas to be installed in Smart TVs from zero to a current run rate of more than one million a month. We've seen this as a fast-growing and emerging market and is far from showing signs of slowing down. In fact, according to the ABI Research, the market for Wi-Fi enabled TVs is projected to grow to 176 million units in 2021.

Our goal is not only grow within our existing base, as the number and complexity of antennas continue to increase, but also to expand our base both here in the US and across the globe.

Just looking at some of our key performance indicators for Q3 across all of our business segments, will reveal the strong progress we are making on that front. To begin with, the total customer devices nearly doubled in the third quarter to 16.6 million devices from 8.6 million devices in Q3 of last year. As a reminder, our total customer devices metric the number of devices in which our antennas—those are the antennas that are installed. The average number of antennas per device, on the other hand, increased 15% to 2.84. We feel this is also another important metric to track because it measures how we can expand our presence in a single device. Finally, the average selling price per device decreased 5% to \$0.72 for the quarter.

While these metrics are useful in evaluating the performance of our business from a year-over-year perspective, our long-term progress will be measured by our ability to execute on some of the key initiatives we talked about in our S-1, such as expanding our customer base within our current markets and increasing sales to our existing customers.

As an organization, we are committed to continuing growing and pursue opportunities that can strengthen our market position and expand our vertical focus. I spent some time talking about some of the markets which we are already entrenched and looking to penetrate further. But apart from these markets, there are a multitude of others that are in need of technically robust and superior wireless connectivity solutions, which again, are made possible by the high-performing antenna solutions that can enable it all.

Examples of these markets include home security and automation, wearable and healthcare devices, and even automotive with its growing propensity to provide mobile connectivity for the consumer. We will continue to execute on these initiatives and growing as we have done today, by connecting the right solutions with the right sales and engineering teams to meet our customers' exact specifications.

Along the way, there may also be opportunities to acquire complementary technologies, assets, or companies, and we feel—that we feel are confident in helping us pursue these growth opportunities.

So, looking onward it's important to stress again that, though, that we do experience fluctuations in our results from quarter-to-quarter due to seasonality effects, as Leo had mentioned earlier. The Chinese national holiday, for example, that took place in the first week of our Q4 was a positive driver for our strong Q3 results. We also believe our year-to-date results will help show that we have developed a strong foundation for the long-term continued growth of our business and, at that, we're ready and open the call for your questions.

Operator, please provide the appropriate instructions.

Operator:

Thank you, we are now take questions from Airgain's publishing analysts and major institutional shareholders. If you would like to ask a question on the phone please signal by pressing star, one on your telephone keypad. Please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star, one to ask the question.

We'll go first to Matt Robison at Wunderlich.

Matt Robison:

Hey, thanks for taking the question and congratulations. Chuck, if—could you talk a little bit about how customer concentration was relative to the second quarter and maybe what some of the dynamics were related to the—ASP declined slightly as did the number of antennas per device and then...

Charles Myers:

Yeah, I'll... go ahead

Matt Robison:

...and also you had some seasonality commentary, it seems like in some situations you could, you had I guess a little bit of pull in of business into the September quarter because of the November holiday, would you expect a pull in into the December quarter associated with Chinese New Year's, so that would be another question, and I have got some couple housekeeping questions for Leo.

Charles Myers:

Okay. I'll touch on—I'll let Leo touch on the seasonality and the other one. On the ASP, typically when you see our ASP go up especially on a device that has multiple antennas and words where you have 2.84 increased I believe the number was 15% if I'm not quoting that incorrectly. If you look at that, what tends to happen if some of those designs tends to be duplicates. So, as that—the ASP dropping, it might be because we have more of the equivalent antenna in the same device and along that there is a scale, pricing scale that goes with that. The more than one device the little less expensive without it affecting our margins we can deliver that antenna and that's where you primarily see that driver.

As far as the seasonality, I think you can look at our historic numbers and you are going to be able to see that we typically get some fluctuation in the third quarter from the Chinese National Holiday and we always get fluctuation in the first quarter. In our first quarter, always tends to be historically reflective is what you would see in the filings because of the Chinese New Year which affects 10 days of purchasing.

Leo Johnson:

Ten to 12 days of purchasing and with that I want to answer the other piece of the question. Yeah, we probably saw some pull-ins in Q3, but we will not see pull-ins from Q4 for the Chinese New Year because just the timing of it. The New Year doesn't start on January 1, like the National Holiday did this time on October 1.

Matt Robison:

Last year though, if we end to (phon) the December quarter revenue, you had a pretty big sequential uptick in the December quarter last year and more, somewhat more flat comparison in the third quarter last year. So, I understand that we don't expect to see the exact same percentages every year.

Leo Johnson:

Right. Well I mean Matt. Last year, last year in Q4, the TV market was just starting to take off for us in account of what I'll call, 90% ramp started in Q4 and it has been growing since, but prior to that it hasn't been—wasn't nearly as large a piece of business nor was it as big and on an aggregate. So, basically that's the difference between Q3 of a year-ago and Q4 of a year-ago is that actually the Smart TV market kind of took off for us.

Matt Robison:

As far as the concentration goes, was Smart TV as big a percentage in the June, in the third quarter as it was in the second quarter?

Leo Johnson:

Oh, yes. They both were somewhere right around, north of 10%, south of 15%. It's going to fluctuate just by the very nature of the shipments, but both times it stayed right in state right in that range and to your question about...go ahead.

Matt Robison:

No, you continue. Sorry, I didn't mean to interrupt.

Leo Johnson:

All right and then—well you had the one question on the customers, the same three customers that we talked about last quarter came in once again all over 10% and—over 10% of our business and we are not expecting a lot of changes there. At least not in the immediate future. Pardon?

Charles Myers:

The housekeeping questions were cash flow from operation, capital expenditures, and depreciations separate from D&A, just the depreciation alone.

Leo Johnson:

Yes, depreciation alone was right off the top my head it was going to be right around \$300,000 in the depreciation, amortization was about 83 times--amortization 250, I mean I would have to give it to you right at the top of my head Matt, I don't have it right here in front of me.

Matt Robison:

That's fine, rounded numbers are okay they are not that big cap ex and cash flow?

Leo Johnson:

Cap ex was pretty typically light, I mean I think we did about \$275,000 I told you last—that were going to buy a chamber for our APAC group and that's about \$200,000, those types of expenses don't happen that often for us. Exact numbers, that was pretty close on the amortization, depreciation 350, amortization 275.

Matt Robison:

Okay, what was the cash flow from operations?

Leo Johnson:

Cash flow from operations, almost \$2 million, \$1.967 million.

Matt Robison:

Very good. Thank you, very much.

Charles Myers:

Thanks Matt.

Operator:

Once again, that's star one, to signal with questions. Next to Tom Sepenzis with Northland.

Tom Sepenzis:

Yeah, congratulations on the good quarter. Great start. I am just curious what should we be expecting for op ex in Q4, would that come back down without the IPO cost?

Leo Johnson:

It will come down but it will come down slightly. I mean we are continuing to invest in our business Tom and we are not the biggest Company in the world. So, it means—expenses for us is still a stepping stone, it's not a straight line, and in this quarter, we want to invest a little bit more going into it into R&D. So, my expectation's it will go down but not—it won't go down significantly but it will go down some.

Tom Sepenzis:

Got you, and then gross margins you mentioned your target is 40%, but you have been well above that in the mid 40% range. Are you expecting that to go back down because of pricing pressure or is it more likely that you kind of stay in this mid-40 range?

Leo Johnson:

I think we are staying in mid 40 range for the next short-term future, but we have various some switch apps that we are seeing that are going to happen in our—basically in our project base that could impact the gross margin but it's not going to be like we're going to tank it or anything.

Charles Myers:

We never know, but we feel very comfortable at 40% and we are happy being conservative on that number and we'll continue to be conservative on that number.

Tom Sepenzis:

Great, thank you, and the 5% ASP drop was that sequential or year-over-year?

Leo Johnson:

That was, I think it's basically the same I think its sequential drop, right?

Charles Myers:

We're just verifying.

Leo Johnson:

We're just verifying. I think it was...

Charles Myers:

Yeah, that was—I believe that was from last year.

Leo Johnson:

...yeah that's last year. Year-over-year, it may be up.

Tom Sepenzis:

Then your share count, what are you using in the calculation to get to, I think GAAP you said was in (inaudible) cents.

Leo Johnson:

That one's always a killer Tom, but it's in the fully diluted number right now, we used approximately \$6.7 million for this quarter and then on a go-forward basis the numbers--if you want a count, then probably the easiest thing to do is figure out what will be on a go-forward basis because you have the shares are rolling out then, and then you come to the IPO for half the month, we had the—all the preferred shares that were still in there for half the month and all this kind of stuff going back and forth. But, at the end of the day, if you take the number of shares that we have outstanding at the end of quarter which was roughly \$7.5 million, \$7.6 million and add in the roughly a million options that we have and figure the treasury method on that. You're going to come in to—our full diluted EPS for the quarter would've been about \$0.14.

Tom Sepenzis:

Okay, and then going forward its 8.3 million shares?

Leo Johnson:

Yes, slightly more than that I would say probably more in line with about 8.45.

Tom Sepenzis:

Great. Thanks, very much.

Charles Myers:

Thanks, Tom.

Operator:

Next to Scott Billeadeau with Walrus Partners.

Scott Billeadeau:

Hi guys. I just—trying to kind of go through the sequential, so it sounds like because of things—Q3 got some orders sucked from Q4. So, Q4 would that be down sequentially and then Q1 is usually sequentially down from Q4. Did I hear that right?

Charles Myers:

I don't think you heard that right. I think that was maybe a comment that one of the analysts made.

Scott Billeadeau:

Okay.

Charles Myers:

We have no real assessment of whether things got sucked in from Q4 to Q3.

Scott Billeadeau:

Okay. Fair enough.

Charles Myers:

I think historic, just to qualify, historically our quarters Q3 and Q4 tend to be maybe less than Q2 to Q3 because of the seasonality depending on where the Chinese holidays hit.

Scott Billeadeau:

Okay.

Charles Myers:

It doesn't mean they don't just grow, it just means there tends to be less growth.

Scott Billeadeau:

Yes, and then I think you mentioned that 2.8 antennas per device and could you clarify is the—do the Smart TVs have fewer or more than that or as equal as...change that.

Charles Myers:

In general, the growth has been consistently up, because of MIMO requiring more antennas.

Scott Billeadeau:

Okay.

Charles Myers:

So, a couple of years ago, where we might have one or two antennas in a box that definitely grows over time. So, as we implement more and more AC chips for instance we end up with more and more antennas. So, the number of antennas per device does tend to grow over time.

Scott Billeadeau:

Alright, that's it for me. Good quarter.

Charles Myers:

Hey, thank you. Appreciate it.

Operator:

Once again, that is star, one to signal with questions. Next to Orin Hirschman at AIGH Investment Partners.

Orin Hirschman:

Hi, congratulations on the progress.

Charles Myers:

Hey, nice to talk to you again Orin.

Orin Hirschman:

Thank you. Just a couple of quick questions. Can you just go over the seasonality one more time, what's typical and what may have changed over the last year through in terms of seasonality I know it's been asked a few times, I'm still kind of unclear as to what's historic for Q2—what should be the new norm. That's question number one. Question number two is, is the sequential decline in the 5% is that a normal sequential decline, is there any point of reference for that on the prior quarter?

Charles Myers:

Sure. We are not quite sure about sequential decline; I don't know that we have ever seen this sequential decline. So, maybe we'll need some clarity on that. I will turn over the seasonality question to Leo

Leo Johnson:

I mean the seasonality, let me just kind of get it out here because I am not very smart, so I have to explain it to myself. Basically, in Q4, there is one week shut down in China which affects our business. Logic tells you that some business that we got in Q3, would have been in that first week of Q4. It's not the end of the world, it's not the biggest change ever, but it does happen and it does affect the sequential growth quarter-over-quarter of Q3 versus Q4.

Now, the Chinese New Year on the other hand is a two-week period that's just taken out of Q1 and that's the reason that between Q4 to Q1 you will see our business drop because basically two weeks of the—no one is working that time. So, we are not selling basically any product over that two-week period. That's the reason that Q1 has always historically been less than Q4.

Charles Myers:

Which mimics other companies that are building their products in China.

Orin Hirschman:

Yeah. Got it.

Charles Myers:

It's not an unusual phenomenon.

Leo Johnson:

No.

Orin Hirschman:

Just in terms of the normal seasonality or for seasonality from Q3 to Q4, just do that with me one more time?

Leo Johnson:

Q3 to Q4 there is one week that is not nearly the impact of the Chinese New Year. I mean it's not nearly the impact of the Chinese New Year so—but it does have an impact so naturally, if you think about it this way, Q3 has 13 weeks for us, Q4 has 12 so--and then you have the normal course whatever the business grows underneath that to offset that.

Charles Myers:

It doesn't affect our growth. It only affects as Leo, I think he succinctly put it in, we just count less weeks in those quarters that's all.

Orin Hirschman:

Got it. Okay great. Okay, thanks so much.

Operator:

Once again that's star, one to signal. We'll turn to Matt Robison with Wunderlich.

Matt Robison:

I actually answered my own question. I'll defer to the next caller.

Charles Myers:

We always knew that you were a smart Matt so—alright thank you.

Operator:

Once again that's star, one to signal. We will pause a moment to allow everyone a chance to signal.

At this time, this conclude our question-and-answer session. If your question was not taken you may contact Airgain's Investor Relations team at airg@liolios.com.

I would now like to turn the conference back over to Mr. Myers for his closing remarks.

Charles Myers:

This really—thank you for joining us today. I especially want to thank our employees who have worked incredibly hard especially through the IPO process and for getting us up to speed on being a public Company. Our partners and investors that continue to support and we look forward to updating you on our next call. That's all I have. Thank you, Tony.

Operator:

This does conclude today's conference. We do thank you for joining us for today's Airgain's third quarter 2016 earnings conference. You may now disconnect.