communications simplified.

Airgain, Inc.

First Quarter of 2017 Earnings Call

May 03, 2017

CORPORATE PARTICIPANTS

Alexis Waadt, *Director, IR*

Charles Myers, *President and Chief Executive Officer*

Leo Johnson, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Anil Doradla, *William Blair*

Timothy Arcuri, *Cowen & Company*

Peter Warendorf, *Wunderlich Securities*

Josh Goldberg, *G2 Investment Partners*

PRESENTATION

Operator:

Good afternoon. Welcome to Airgain's First Quarter 2017 Earnings Conference Call. My name is Bob and I'll be your Coordinator for today. Joining us for today's call are Airgain President and CEO, Charles Myers; CFO, Leo Johnson; and Director of Investor Relations, Alexis Waadt. I will now like to turn the call over to Ms. Waadt who will provide the necessary cautions regarding the forward-looking statements made by Management during today's call.

Alexis Waadt:

Thank you, and good afternoon, everyone. 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 future events and Airgain's business strategy and future financial and operating performance, including performance for remainder of 2017. 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 Release and SEC filings, including its Form 10-Q, which we expect to file by May 15, 2017. This conference call contains time-sensitive information that is accurate only as of the date of this live broadcast, May 3, 2017. 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 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 will 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.

Following Management's prepared remarks, we will open up the call for questions from Airgain's publishing sell side analysts and major institutional shareholders. Now, with that, I would like to turn the call over to our President and CEO, Chuck Myers. Chuck?

Charles Myers:

Thanks, Alexis. Welcome, everyone, and thank you for joining us today. After the market close, we issued a press release announcing our results for the first quarter ended March 31, 2017. A copy of which is available in the Investor Relations section of our website. Riding our strong momentum of 2016, we continue to expand our core connected home market while adding to our sales funnel in new markets like enterprise and automotive. The Company's sales grew organically by 32% year-over-year, while our margins showed expansion. This led to another strong quarter profitability and Adjusted EBITDA, more than doubling from the same period a year ago.

Complementing our healthy financial performance were several achievements on the operational front. We begin shipping multiple new 802.11ac connected home devices during the quarter. I will highlight two examples. The first is a flagship DOCSIS 3.1 8x8 Wi-Fi gigabit gateway for a tier 1 North American carrier.

The second is a DOCSIS 3.1 set-top box for a major cable operator in Europe. This is a cutting edge 4K Ultra HD device which enables wireless video to be streamed over 2.4 gigahertz and 5 gigahertz Wi-Fi networks. These two new devices join an ever-growing number of design wins we've had that are based on the 802.11ac standard. Additionally, we began shipping and environmentally hardened outdoor Wi-Fi access point for major Tier 1 OEM. This product feeds our expansion into new market with a significant existing customer.

I'll say a few words regarding our recent acquisition. We acquired the assets of Antenna Plus last week for $6.4 million in cash. In 2016, Antenna Plus had unaudited revenues of around $7.5 million in gross margins greater than 60% and positive EBITDA. We expect this transaction to be EBITDA-accretive within 2017. We were able to favorably acquire these assets due to court-ordered resolution of an ownership dispute and not due to financial impairment. The acquired Company, Antenna Plus is an early innovator in the mobile fleet antenna market. We're excited about this unique portfolio of cellular, GPS, Wi-Fi and private radio frequency antenna products.

We also took over an established network of sales distribution and value-added resellers. This provides leverage for Airgain’s existing products into several new markets including the fast-growing automotive fleet in industrial IoT space. We look forward to building our team through the addition of the employees and the leaders of Antenna Plus that have built such a solid Company.

Now before I provide any further details about our operational results as well as our future 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. Leo?

Leo Johnson:

Thank you, Chuck, and good afternoon, everyone. Let's turn to our financial results for the first quarter ended March 31, 2017. Our sales for the first quarter increased 32% to $11.3 million from $8.5 million in the same period a year ago. The increase was driven by our continued growth in product sales. Our gross profit for the first quarter 2017 grew 44% to $5.3 million from $3.7 million in Q1 of last year. Gross margin as a percentage of sales increased to 47.0% in Q1 '17, compared to 43.2% in the first quarter of 2016. This increase in gross profit as percentage of sales is primarily due to the shift in sales mix.

Our total operating expenses for the first quarter grew 37% to $4.9 million from $3.6 million in Q1 of last year. The increase is primarily attributed to higher personnel expenses to court sales marketing and R&D initiatives. We also incurred increases in certain administrative causes of results of being a public Company. Net income attributable to common shareholders for the first quarter of 2017 totaled $385,000 or $0.04 per share on a diluted basis. A significant increase from net loss attributable to common shareholders of $465,000 or a loss of $0.82 per share diluted in Q1 of last year.

Our Adjusted EBITDA more than doubled to $712,000 from $354,000 in the same period a year ago. I'd like to remind everyone, as expected we did experience some seasonality in our quarter because of the Chinese New Year. Now turning to the balance sheet, cash and cash equivalents at the end of the first quarter totaled $41.9 million, compared to $45.2 million at the end of the prior quarter.

This completes my financial summary. I'll now turn it back over to Chuck. Chuck?

Charles Myers:

Thanks, Leo. Before I get into our operational results for the quarter, I'd like to briefly share the results of some of our performance indicators. Our key performance indicators were positive for the quarter. Our total number of customer devices grew 23% for the quarter to $12.9 million. The average number of antennas per unit in these devices increased 5% to $3.12 million. Finally, our average selling price per device increased 8% to $0.86.

Moving on to some of our operational highlights. I started the call by talking about how we began shipping for two new 802.11ac devices during the quarter. The DOCSIS 3.1 set-top box is already ramping up very quickly, while we expect shipments for the Wi-Fi gateways to ramp throughout the year. These new customer engagements expand our geographic footprint especially within North American carriers and diversify our overall sales mix.

In addition, we believe the shipments to these customers demonstrate, after much anticipation, the commercial rule out of the 802.11ac adoption. We continue to focus on driving growth through penetrating new markets as well as widening our sales channels and introducing new products that can increase our market share. We believe the acquisition of Antenna Plus will help accelerate these objectives. This acquisition also allows us to advance our presence in North American in terms of higher margin product mix and geography in the automotive and IoT landscape.

Looking ahead, we will take advantage of our enhanced cash position to opportunistically evaluate attractive technologies and businesses like Antenna Plus that can accelerate our future growth. We'll continue to invest in our sales marketing and R&D initiatives to drive our strong organic growth.

I want to thank all the employees at Airgain for an excellent first quarter and a solid start to 2017. Their hard work has laid a solid foundation for what should be another great year. Building on our past four quarters, we continue to see the market expanding and as a long-time seller, it's nice to feel that market trade winds that are back.

With that, we're ready to open the call for any of your questions. Operator, please provide the appropriate instructions.

Operator:

Thank you. At this time, we'll be conducting a question-and-answer session. If you'd like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star key. One moment while we pool for questions.

Our first question comes from the line of Anil Doradla with William Blair. Please proceed with your question.

Anil Doradla:

Hey, guys. Chuck, Leo, congrats on the great results.

Leo Johnson:

Thank you.

Anil Doradla:

Chuck, you've set the tone very positively, you talked about the 802.11ac you've talked about some of the North American service providers. As we look out in 2017 from a bigger picture trends point of view, whether it's ASPs, whether its unit volumes and so forth, the tone that you've set out in the first quarter should be sustainable. Is that a fair assessment?

Charles Myers:

Well, as you know, we look internally kind of our annual revenue and I think that our past performance should kind of demonstrate what we think about the business, Anil.

Anil Doradla:

So, when you look at again, back for the full year, from your point of view, 802.11ac will be the biggest driver. Is that a fair statement?

Charles Myers:

I think with so much of our business in the IoT and more are going to be in the automotive space, AC is I would say not the biggest right now. As I've stated regularly, AC is really in a nascent stage and it continues to expand nicely and we see strong market push for that and we see that–no reason for that to not continue, we're only in nascent stages.

Anil Doradla:

On Antenna Plus obviously, there are some cross-selling opportunities right away as you expand your channels, but then there's following up, there's going to be integrated product synergy. Can you walk us through, Chuck, how you're looking at 2017 and '18 from this acquisition point of view?

Charles Myers:

Yes. Just be aware, we just closed this in last week. So, as we go through the integration, what we see from the distribution channels that we have there, that within that Company there was a bit of a pent-up demand for other products and probably a larger service capability, which Airgain provides to Antenna Plus, to be able to provide even their existing products to more customers. We hope that we see a lot of pull from that throughout the rest of the year and we continue to see that, those are some introductory products for some of the automotive opportunities that we are currently pursuing.

Anil Doradla:

Great. Leo, switching gears to the balance sheet. DSOs went up. It looks like accounts receivable was the factor, had in fact on free cash flow, too. Can you build up and explain what happened there?

Leo Johnson:

Basically, March was obviously our biggest month of the quarter and because of late Chinese New Year sale, we ended up doing over $5 million on the month of March.

Anil Doradla:

Okay. So, it was just a timing thing?

Leo Johnson:

It's just a timing.

Anil Doradla:

All right. Wonderful. And congrats once again from myself.

Operator

Thank you. Our next question comes from the line of Timothy Arcuri with Cohen & Company. Please proceed with your question.

Timothy Arcuri:

Thank you very much. I had a couple. I guess, Chuck, you don't want to really get too specific about the guidance, but you've now grown an excess of 30% for two quarters in a row. Can I just sort of take that sort of growth and then add Antenna Plus of maybe $8 million so you're in the mid-60s for the year? I know you don't want to put a number out there and guide, but is that completely crazy?

Charles Myers:

You know what I love about the analysts, I never mentioned $8 million, I said that unaudited were $7.5 million and you're already at it at half a million. That's a tough one to add, but as you know, if you have a public Company of our size and we're growing it better than 20%, we feel that's kind of where our business model has been modeled. I think that you can see from our performance in the past, we feel comfortable with our performance with the past.

Timothy Arcuri:

Okay. All right. How about this one? Can you help us sort of what the impact will be from Antenna Plus on antennas for device and maybe total devices? Is there going to be any material change? Do they have different mix that we'd make those numbers a little different?

Charles Myers:

They have a much different mix. They tend to be definitely a significantly higher ASP than what we do. It can go anywhere. Leo, do you want to hit on what that numbers are? It could be anywhere from, these could be…

Leo Johnson:

Some of the antennas are $100.

Charles Myers:

A $100, right? It's going to change. At some point as we build up our automotive and IoT business and outdoor business, our key indicators for what we do on cost per device is going to change significantly and at some point, we'll come out with new direction with how we see our KPIs.

Timothy Arcuri:

Okay, got it. Then can you talk about gross margin? It was obviously a lot better and you guys haven't done 47% before, I don't think. Is that a sustainable number? When I put in Antenna Plus, you should be able to do possibly 50% this year if you're already at 47% without them and they're much higher. Is that rational?

Charles Myers:

Well, as I've said on the other calls, it all comes down to product mix and as we change things in and out, depending on the quarter, the mix changes. This is probably a good time that people always love to touch on LeEco with us. As we said in the fourth quarter call and the end of year call that we didn't put near as much emphasis on LeEco as probably, I don't know, I almost call it the social media impact did.

We don't view them necessarily as a significant customer going forward, although we still ship to them as I said in the last call. We still ship to one of their key vendors. But for instance their margins are lower than some of the margins on some of the other products we shipped. Things as products mix shift can shift our margin. We've had 15 or 16 quarters now straight of greater than 40% margin and there's no reason for us to believe that that's going to change.

Timothy Arcuri:

Okay. Then I guess last question. Can you talk about the top customers in the quarter? Who were they and how much were they?

Leo Johnson:

Tim, I don't think we've ever really called out–we've never called out the top customers. We've always given a percentage of what the top three were and again, this quarter is about the same. This quarter is 47% out of the top three customers.

Charles Myers:

But be cautious because next quarter, it may be a completely different set of three. They tend to switch quarter to quarter depending on the shipping schedules and customer demands. A retail product customer will have very different–they'll ship more in one quarter than they would compared to what another person would. It's important to know when you segment customers, those customers could have multiple products in multiple product lines with multiple end customers in their own right.

Timothy Arcuri:

Right, got it. Okay. Thanks so much.

Leo Johnson:

But there's a lot of diversification there.

Operator

Thank you. Our next question comes from the line of Matt Robison with Wunderlich Securities. Please proceed with your question.

Peter Warendorf:

Hi. This is Peter Warendorf for Matt Robison. Thanks for taking my question. I'm just wondering, based on the order flow that you guys are already seeing, what kind of equipment is going to be driving demand in the June quarter? How does that compare to the previous year?

Charles Myers:

I don't necessarily follow your question. We ship to as many of about 150 different products and I don't know that personally I've seen what the breakdown is on each of those individually. So maybe if you have some clarity on the question, maybe I can help you out a little.

Peter Warendorf:

Just trying to get at if there's any product specifically that you're seeing that's a high percentage? Or if you don't have any clarity, that's all right, too.

Charles Myers:

No, I would say there's no one specific product. I think I understand your question now. There's no one specific product. Our revenues tend to be quite diverse so that's how we see it.

Peter Warendorf:

All right. Thank you.

Charles Myers:

You're welcome.

Operator

Thank you. Our next question comes from the line of Josh Goldberg with G2 Investment Partners. Please proceed with your question.

Josh Goldberg:

Hey, Chuck and Leo. How are you doing?

Leo Johnson:

Hey, Josh.

Charles Myers:

Hey, how are you doing?

Josh Goldberg:

I just had a couple of questions. I guess first of all, can you tell us how much, because you said it's very early stages. I assume that the 802.11ac and the DOCSIS 3.1 modem business is still very, very small, less than 10% of your revenue. Is that fair to assume?

Charles Myers:

You know, it's a tough question without seeing the numbers in front of us. Hang on.

Josh Goldberg:

Okay.

Leo Johnson:

The two projects that Chuck alluded to, under 10%.

Josh Goldberg:

Okay. Based on the comment that the tailwind just starting to come your way and you're seeing further orders. Is it fair to say that you probably entered April and May and are depending on the conference, call, with the better order book than you did starting the year?

Charles Myers:

I would assume so, yes.

Josh Goldberg:

Okay. Also you're comfortable saying that the products, the 802.11ac and the DOCSIS 3.1 are not significantly below corporate average course margins?

Charles Myers:

That would be correct.

Josh Goldberg:

Okay.

Charles Myers:

Or very early products, those are very early products. So, going forward, those tend to be decent margin products and it gets buried over the life of the product.

Josh Goldberg:

As you look out to some of the other opportunities, is it fair to say at least that the DOCSIS 3.1 upgrade can be pretty significant to your top line?

Charles Myers:

I think that DOCSIS 3.1 is in very, very early stages. As a market of a whole, I would absolutely agree with your comment.

Josh Goldberg:

Okay. Is there any comments from customers who are saying they're not or they're delaying the spend or they're holding it back? Or just because you're only seeing the early indications that you're saying it's an early market? There's no cancellations or changes in their buying patterns?

Charles Myers:

To the contrary, I think the designs are all geared–for the most part are geared toward–from that particular product set, the products or the new designs are very much geared towards 3.1 DOCSIS products and AC products.

Josh Goldberg:

Okay.

Charles Myers:

Those are very, very early stages.

Josh Goldberg:

Sure. But it looks like they're going to ramp pretty hard between now and the end of the year according to the customer forecast?

Leo Johnson:

Right. I think as you can see from our numbers, we continue to ramp nicely.

Josh Goldberg:

Okay. Regarding the acquisition, just so everyone is clear. You're going to only have two months of the acquisition in the second quarter and then a full quarter and then third quarter. Is there any seasonality in the business? Is it more backend-loaded to the fourth quarter? Are people looking at the 7.4 and saying, okay, divide that over eight months of it–divided by eight months and it's a pretty good indication of what the revenue will be each quarter?

Charles Myers:

We'll have to see how they operate under us in terms of seasonality. They do have a little seasonality there. As we get into the integrational, we'll be able to going forward, give you some better clarity on that. We will see some revenue from them in the first, two quarters. There will be some cost associated with the integration on that.

Josh Goldberg:

Okay. So, you're saying is that maybe the first two quarters is not as accretive as when you had with the year?

Leo Johnson:

Exactly.

Josh Goldberg:

Okay. In terms of just the balance sheet, fair to say that you think those will normalize again back to the 40-45 day in the second quarter?

Charles Myers:

Yes, I believe so. I have no indication that they're not.

Josh Goldberg:

Got it. Just to dovetail at Leo, it sounds like that the quarter and the order (inaudible) bookings seem to be much more front-end loaded this quarter than last?

Leo Johnson:

They were, yes.

Josh Goldberg:

Okay, great. Thanks so much.

Leo Johnson:

Thanks, Josh.

Operator

Thank you. Ladies and gentlemen, as a reminder, if you'd like to ask a question, please press star, one on your telephone keypad. Our next question comes from the line of Paul Duggan with Jackson Capital. Please proceed with your question.

Paul Duggan:

Good afternoon, guys. Nice quarter. I've got a question. It's a little off-topic from what these gentlemen have been asking. The stocks seem to be overrun by short sellers and the open short interest continues to go higher and higher. Would the Company consider paying a cash dividend or instituting a buyback to kind of combat that? We got a lot of cash in the drawer. A buy back or cash dividend would use a cash and provide some defense against the outstanding short sellers. Any thoughts?

Charles Myers:

We're thinking, Paul.

Leo Johnson:

Actually, we were kind of hoping, Paul, that results would speak for themselves.

Paul Duggan:

Oh, the results are great, but there's a lot of social media negative stories. One way to counteract it is just with facts. The Company has a lot of cash, a more accretive acquisition like Antenna Plus, or a dividend, or a buyback, but I think it would send the stock running.

Charles Myers:

We will bring that up at the Board. I think it's a good comment.

Paul Duggan:

All right. Thank you.

Operator:

Thank you. Our next question comes from the line of Will Hamilton. I'm sorry, that's all the time we have for questions today. If your question was not taken, you may contact Airgain's Investor Relations team at investor@airgain.com.

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

Charles Myers:

Thank you for joining us on the call today. I especially want to thank our employees, partners and investors for their continued support and we look forward to updating you on our next call. Operator?

Operator:

Thank you for joining us today for Airgain's First Quarter 2017 Earnings Call. You may now disconnect.