



Airgain, Inc.

Fourth Quarter and Full Year 2018 Conference Call

February 14, 2019

C O R P O R A T E P A R T I C I P A N T S

Anil Doradla, *Chief Financial Officer*

Jim Sims, *Interim Chief Executive Officer*

Jacob Suen, *President*

C O N F E R E N C E C A L P A R T I C I P A N T S

Karl Ackerman, *Cowen & Company*

Alessandra Vecchi, *William Blair & Company*

P R E S E N T A T I O N

Operator:

Good afternoon and welcome to Airgain's Fourth Quarter 2018 Earnings Conference Call. My name is Cheryl, and I will be your coordinator for today's call. Joining us today for today's call are Airgain's Interim CEO, Jim Sims; CFO, Anil Doradla; and President, Jacob Suen.

I would now like to turn the call over to Mr. Doradla who will provide the necessary cautions regarding the forward-looking statements made by management during today's call. Thank you.

Anil Doradla:

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 the future events and Airgain's business strategy and future financial and operating performance, including performance for the first quarter and Fiscal 2019. 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 earning release and SEC filings, including its Form 10-K, which we expect to file by March 15, 2019.

This conference call contains time-sensitive information that is accurate only as of the date of this live broadcast, February 14, 2019. 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 may include a discussion of non-GAAP financial measures, including non-GAAP net income, non-GAAP EPS and 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 on the Investor Relations website at www.airgain.com. Following management's prepared remarks, we will open the call for questions from Airgain's publishing sell-side analysts.

Now, with that, I would like to turn the call over to our Interim CEO, Jim Sims. Jim?

Jim Sims:

Thank you, Anil. Welcome, everyone, and thank you for joining us today. After the market close, we issued a press release announcing our unaudited results for the fourth quarter ended December 31, 2018, and Fiscal 2018, which is available in the Investor Relations section of our website. I'm very pleased with our fourth quarter and full year results. Once again, we witnessed another record sales quarter for Airgain. For the fourth quarter 2018, our sales were \$16.6 million, up 5% sequentially and 29% year-over-year. The results in the December quarter marks the fourth consecutive record sales quarter in the Company's history.

Like the last three quarters, the continued strength in our results reflect robust demand across existing and new programs in our consumer, enterprise, and automotive market. Furthermore, customers are increasingly becoming aware of the complexities in delivering gigabit per second data throughput over wireless systems, and this, in turn, is leading them to seek reliable antenna partners with extensive experience in solving RF problems. As we look into 2019 and beyond, our design win momentum combined with our customer engagement pipeline leads us to be positive, and we expect specialists, such as Airgain, will increasingly become important in end-to-end system performance.

Our fourth quarter results mark a milestone in the Company's performance, both on the sales and profitability front. As I highlighted earlier on the sales front, the fourth consecutive quarter of record sales for the Company was driven by a combination of continued robust demand for complex antenna systems combined with strong execution. On a profitability front, our continued effort around efficiency improvements since I stepped in as Interim CEO in May have paid off significantly.

In the past six months alone, we have gone from a net loss of \$3.2 million in the second quarter of 2018 to a net income of \$1.3 million and Adjusted EBITDA of \$1.8 million or 11% of sales in the fourth quarter of 2018. Furthermore, we reported fourth quarter GAAP and non-GAAP diluted earnings per share \$0.13 and \$0.17, respectively, well ahead of our prior expectations of \$0.02 and \$0.03 on a GAAP basis and \$0.07 to \$0.08 on a non-GAAP basis.

As you know, most of our focus during the last year has been around eliminating non-revenue generating spending without impacting our product development pipeline. And in the fourth quarter, we witnessed the combination of those efforts. As we look into 2019, with the completion of the major cost efficiency programs, I believe the Company is back on track of maintaining profitability, along with a healthy top line growth.

I would also like to highlight some of the notable wins and key programs in the fourth quarter across the consumer, enterprise, and automotive market. In Asia, we won a gateway design win with one of the largest service providers to support their fiber-based deployments. We expect revenues to commence in 2020 and we expect to support the customer's products with at least six antennas. In Europe, we won a design win with a large service provider to support their next-generation broadband gateways for their consumers. With multiple wireless access technology such as 4G, Wi-Fi and Bluetooth supported by the product, we expect to provide 10 or more antennas in this offering.

On the automotive front, we won our second infotainment design win with a European-based Tier 1 vendor. We expect revenues to begin in 2021 timeframe. Based on our current level of engagement, I am positive of the prospects of the auto OEM front and look forward to updating you on all of our future wins.

Finally, our ULTRAMAX MIMO antenna product line was selected by two major metropolitan transportation systems to support connectivity needs. We expect revenues here to begin in 2019.

In a moment, I'll be happy to take any questions, but before I do, I'd like to turn the call over to our Chief Financial Officer, Anil Doradla, who will walk us through the financial highlights for the quarter. Anil?

Anil Doradla:

Thank you, Jim, and good afternoon. I will provide key financial highlights for the fourth quarter 2018 and provide some preliminary color around first quarter 2019. As you know, we started providing quarterly guidance in 2018 as we realigned the Company and highlighted the possibility of getting back to our historical practice of providing annual guidance in 2019. Moving forward, we have decided to continue providing quarterly guidance in 2019 and beyond. We believe this will provide more clarity to the investment community and keep us more focused on the execution front. That said, I would also like to remind investors that our business is subject to short lead times, and this may result in short-term quarterly fluctuations and our ability to accurately predict our business.

Now, coming to the fourth quarter 2018 highlights. Sales of \$16.6 million, grew 5% on a sequential basis and 29% on a year-over-year basis versus our guidance of \$16.4 million to \$16.5 million. The strength in the fourth quarter was driven by our service provider business combined with a pickup in our automotive from the third quarter. As a reminder, we completed the Antenna Plus acquisition in May 2017, so the fourth quarter year-over-year growth of 29% was organic in nature.

On a separate note, I would also like to highlight that we are taking steps to prepare us to report our results under the updated ASC 606 revenue recognition rules. We are assessing the impacts across our business, and over the course of the next several quarters, we will provide incremental color, both qualitatively and quantitatively around the impact of these new rules. Fourth quarter gross profit was \$6.9 million or 41% of sales versus \$6.9 million or 43.5% in the third quarter and \$5.9 million or 46% of sales in the same period a year ago. While product mix and new product ramps were the key factors in the decline, our continued focus on restructuring our operations combined with our efforts to streamline our relationships with existing and new contract manufacturers also contributed. We expect our fourth quarter to mark the bottom on the gross margin front and expect an upward trend as we look into 2019.

We believe our efforts over the past several months around operational efficiency improvements combined with favorable product mix leads us to be incrementally positive on the gross margin front in 2019. Our GAAP net income totaled \$1.3 million or \$0.13 per diluted share based on 10 million shares compared to a GAAP net income of \$0.6 million or \$0.06 per diluted share based on 9.7 million shares in the same period a year ago. On a non-GAAP basis, our net income was \$1.7 million or \$0.17 per diluted share compared to \$1 million or \$0.10 per diluted share in the same period a year ago. These results are better than our prior outlook of \$0.02 to \$0.03 on a GAAP basis and \$0.07 to \$0.08 on a non-GAAP basis.

Our continued focus on non-revenue generating expense control combined with lower-than-expected spend towards the year-end resulted in better-than-expected savings and lower operating expenses. As Jim pointed out in his opening remarks, most of the significant cost optimization initiatives have been completed, and as we enter into 2019, we expect to once again start investing to meet our long-term growth aspirations. Once again, we were active during the quarter in terms of our share buyback, which as a reminder, currently expires in August 2019. During the quarter, we purchased roughly 29,000 shares

at \$337,000. Since the share buyback program was implemented, we have repurchased a total of 357,000 shares for \$3.4 million. Going forward, we'll continue to be opportunistic in our repurchase of shares under this program. And finally, our cash, cash equivalents, and short-term investments totaled \$33.8 million, which was up \$2 million from the last quarter.

Now, I would like to provide preliminary outlook for the first quarter 2019. For the first quarter in 2019, we expect sales to be in the range of \$15 million to \$15.25 million. At the midpoint of \$15.13 million, we expect to decline 9% sequentially and grow 14% year-over-year. The decline is largely driven by seasonality or customers combined with macro-related trends. On a GAAP basis, we expect first quarter diluted earnings per share to be between flat to \$0.01; and on a non-GAAP earnings basis, we expect diluted earnings per share to be in the range of \$0.04 to \$0.05.

Finally, I want to note that today we filed a universal shelf statement on Form S-3, which we think is generally good corporate housekeeping to provide future financial flexibility should we ever need it. But to be clear, given our strong cash position, the Company has no current plans to use the S-3. This completes my financial summary.

I will now turn the call over to Jim. Jim?

Jim Sims:

Thank you, Anil, and thanks to everyone for being on the call today. Before I open the call for your questions, I want to share a couple of closing thoughts. Over the course of 2018, we embarked on several initiatives to get the Company back towards healthy profitability and long-term competitiveness. When I took over in May, I embarked on what I typically referred to as course granularity. Where the emphasis is to prioritize a critical and most pressing issues around the organization. I'm happy to say, as we exit 2018, we have made several changes across our marketing, sales, and engineering organizations that lead me to believe that Company being in a much stronger position than when I took over.

Furthermore, we have strengthened our core executive team with the promotion of Jacob Suen to President, Kevin Thill to Senior Vice President of Engineering, combined with our recent hire of Kathy Pearson as Vice President of Global Administration and Human Resources. We believe we have put in place the right organization and leadership team, and as we look into 2019, there are multiple reasons to be positive, and we're excited with the opportunities in the consumer, enterprise, and automotive market. And finally, I'd like to reiterate the continued need for specialized antenna company such as Airgain across the wireless industry, and our belief that our unique product offering and years of experience in solving difficult RF engineering problems are increasingly becoming more valuable across the technology ecosystem.

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

Operator:

We will now take questions from Airgain's publishing sell-side analysts. To ask a question, please press star, one on your telephone keypad.

The first question comes from Karl Ackerman of Cowen & Company. Please proceed.

Karl Ackerman:

Hey. Good afternoon, everyone. Jim or Anil, I wanted to focus on the guidance for the March quarter. How much of the sequential decline in March is coming from channel inventory digestion and perhaps other imbalances in your customer supply chains as they attempt to mitigate tariffs? Secondly, I know it's early in the year, but I'm curious if you have a view yet on the full year revenue run rate. Do you think the net of the seasonality versus those supply chain issues is still a sizable positive for the totality of 2019?

Anil Doradla:

Hey, Karl. Thanks a lot for that question. Good question. There are two parts of it. Let me take the first part. Remember, and this is something we've talked about in the previous several quarters, our lead times are very short. Unlike semiconductor companies that could have lead times as long as 15 to 20 weeks, our lead times tend to be more like 3 to 5, 4 to 6 weeks. In a way, what ends up happening is that, if you look at the channel inventory, at least from our point of view, on our components, that's not much of an issue there. When you take this problem and go across the whole supply chain and look at the inventory issues at our customers that's a second issue. The way I look at it at this stage, based on what we have seen, and as you know, we are uniquely positioned in the component industry because of our focus on more high-end or more cutting edge products, and we're in the midst of a product cycle. At this stage, we are of the opinion that from an inventory point of view, at least from our perspective, that is not much of an issue. That is not what we are looking at.

As we switch into the year, as I pointed out earlier on, based on the investor feedback and based on internal deliberations, what we decided to do is revert to quarterly guidance. I think that is what, more or less, investors wanted. When I look back at the full year, I'll let Jim add some color to it, but in general, our comps are very positive. As we said, we are in a product cycle that kicked off in the second half of 2018, and as we go into 2019, that product cycle continues to move. We did talk about seasonality in the first quarter, but where we are today, and the way we look at 2019, based on what we're seeing on the DOCSIS 3.0 to DOCSIS 3.1, the greater proliferation of AC, in general, we feel that our end markets are growing healthy, and we feel positive.

Jim, I don't know whether you wanted to add something.

Jim Sims:

Yes. I think I will add to the—really starting in the second quarter and beyond because I think Anil addressed the first quarter quite effectively. Our attitude is, sequentially, we become more positive as the year develops second, third, and fourth quarter due both through the transformation and the movement in the AC, we should be on full strength going into the second quarter, and that will incrementally drive our business going forward. Our win rates, as we explained before, both in the consumer and the enterprise continued to strengthen.

A real positive that we had, frankly, was in the auto OEM marketplace are moving into the infotainment area. Originally, when we went after the automotive, it was primarily going to be driven on what's going on in the B2B and the B2E to which we didn't see any real revenues until probably '21, more likely '22. What's happening, there is a movement now in the OEM, and we've been successfully now on two engagements during the last several quarters that it will be moving the OEM, we think, revenue sooner than later. So, we're very pretty positive about that. Going into the second half or the second quarter of the second half, we see nothing but positive trends, and we think we're well positioned for that.

Karl Ackerman:

That's very helpful. I appreciate that. As my follow-up, if I may, one of your ecosystem partners has talked about shifting from single band to dual band routers. While I'm not asking you to comment on that

particular partner, I'm curious how you see the industry broadly adopting dual band as well as the content uplift perhaps from that over the next 12 months? Thank you.

Jim Sims:

I'm going to have Jacob, our President, address that.

Jacob Suen:

Hi, Karl. That's a very good question. As you can see, there's a merge of single band typically on the 2.0 of frequency band. It will be a combinations of 2.0 and five gig. So, you do see that transformation across the industry. And for us, we have the right product that can cover the single band or the dual band. And actually, people are already talking about tri-band, and we are more than well prepared for that That really fits our expertise. Remember what we are known for. The more complex the system, the better off we are, and that fits our model very well.

Karl Ackerman:

Thanks, Jacob.

Jacob Suen:

Thank you very much.

Jim Sims:

Thanks, Karl.

Operator:

Again, if you would like to ask a question, please press star, one on your telephone keypad.

The next question comes from the line of Alessandra Vecchi of William Blair.

Alessandra Vecchi:

Hi, guys. Congratulations on a great quarter. My question is around the Antenna Plus revenue. As you said, it was up pretty significantly year-over-year, and sequentially as well (inaudible) off a slightly lower base in Q3. As we look at that revenue for 2018, I'm estimating it was about 13% of the total. How do we think about that as we start going through 2019 and 2020 in terms of potentially a percentage of total revenue and where you see that business going?

Anil Doradla:

Good. Thanks a lot, and thanks a lot for your congrats to us. I think a couple of things. As we had Antenna Plus, and as we acquired, what we said was kind of low to mid-teens is what we were expecting these guys to kind of contribute. And I think, we more or less feel that we're kind of on track in this year. As we look at 2019 and 2020, we are optimistic. We believe that this asset is going to be a positive on our margin profile, and we believe that it's going to be positive on our growth profile. We are optimistic. We're not going to be giving out the breakdown quantitatively as we go into 2019. But fair to say that we believe Antenna Plus should be a tailwind to our business over the next two years.

Jim Sims:

Maybe I could add something to it. If you recall my remarks earlier about the infotainment area, there is a perfect example of the merger between Antenna Plus and between Airgain that that technology, quite frankly, is derived from both of our organizational structures because it will fit the profile of what Antenna Plus did with the capabilities that Airgain had on custom design. I think you're going to see more and more of that, that some of the complex designs that come out will be an integration between the Antenna Plus acquisition and between the Airgain. What it allows us to do, which quite frankly I'm excited about is; a) our margins improve; b) our ASP increases, and that's always been the goal. It's never been the goal that these will be two independent directed activities. We should see more and more integration and bring the strength of the two companies together to go after problems we couldn't, quite frankly, solve several years ago.

Alessandra Vecchi:

Okay. That's fair. Just on the gross margin front, Anil, you said you sort of felt Q4 was a bottom and margins should improve throughout the rest of the year. How do we think about the long-term target margin there as we look maybe a year or two out?

Anil Doradla:

Good. Alex, before I answer the question, let me also build up a little bit on kind of the moving parts, and this is something I have told in the past, and I kind of repeat myself. There are two or three components of a gross margin, right? There is an engineering component, how efficiently you design a product. There is an operations component, how well you and efficiently you run your contract manufacturers. Then there is a sales component, where you actually price the product. All these three combined contribute to your gross margins. If you hear what Jim and I have been talking about since taking over the Company early in the year, we were going about fixing each of these issues. On the gross margin front, the last part that we were focused on was on the operations front. And what I'm very—I feel confident about at this stage is that we have resolved most of these issues, and we're going to incrementally add one or two contract manufacturers, and it takes a little bit of an investment.

In terms of the cadence or the slope, we believe that there should be an upward trend. I like to believe that our long-term gross margins should revert back to our historical averages, right? That's what our aspiration is; that's what we believe we can get to. If you're wondering the cadence on how we go from Q1 to Q4 and all that stuff, at this point, we're not talking about it, we're not highlighting and providing that level of granularity largely because as we speak there are many decisions I'm making right now where it's a combination of benefiting as well as investing. So, we feel good. We feel that we're going to get back into our long-term gross margin trend, and you'll start seeing the benefits of it in 2019.

Jim, I don't know you if want to add something.

Jim Sims:

Yes. Let me just add to that, Alex. If you take what we said at the beginning of the second quarter on what we're going to focus on operating efficiencies, then our marketing and sales organization, then reengineering, our engineering department, you notice that the results of those were reflected in our business results quickly because they fit themselves into that. At the same time, if you recall in the second quarter, we went over, we spent time in China working with our factories, working on cost downs. The group just went over back several weeks ago picking a new supplier. What you're going to see, in order to get the margins back to where we want them, and we are highly confident this is going to happen, this is a longer-term solution because we got to get it through the inventory, we have to get it

through the process, we got to get it through the factories. But the tight integration now between what we're doing in research and development and a), what we're doing in sales, now we can make sure we're designing products that have the cost effectiveness that we want.

At the same time, we have really worked into the factories to look at the building materials, to look at how we can get cost downs, and how we can drive profitability there. At the same time, we're looking at opening up new factories, which quite frankly, in the new factories we're looking at, we see a substantial improvement in cost. Now, after nine months, I think you're going to start to see the same results that you saw in the operating expenses, you're going to see in the margins going forward between the first, second, third and fourth quarter. And there is no reason we can't get back to our historical margins in the business. We are dedicated and focused on doing that as kind of the last tail of what we had to do to turn this Company around.

Alessandra Vecchi:

That was really helpful. Thank you, Jim and Anil.

Anil Doradla:

Thank you, Alex.

Operator:

At this time, this concludes our question-and-answer session. If your question was not taken, you may contact Airgain's Investor Relations at investors@airgain.com.

I'd now like to turn the call over to Jim Sims for closing remarks.

Jim Sims:

I want to thank all of you for joining us today, and I especially want to thank our employees, partners, and investors for their continued support. We absolutely look forward to updating you on our next call with the continued progress of the Company. Thank you very much.

Operator?

Operator

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