



## Q3 FY19 Earnings Conference Call Prepared Remarks

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### Operator

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Ladies and gentlemen, good afternoon. At this time, I'd like to welcome everyone to QuickLogic Corporation's Third Quarter Fiscal Year 2019 Earnings Results Conference Call. As a reminder, today's call is being recorded for replay purposes through November 13, 2019. I would now like to turn the conference over to Mr. Jim Fanucchi of Darrow Associates. Mr. Fanucchi, please go ahead.

### Jim Fanucchi

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Thank you, Lisa and thanks to all of you for joining us. Our speakers today are Brian Faith, President and Chief Executive Officer, and Dr. Sue Cheung, Chief Financial Officer.

As a reminder, some of the comments QuickLogic makes today are forward-looking statements that involve risks and uncertainties, including but not limited to stated expectations relating to revenue from new and mature products, statements pertaining to QuickLogic's future stock performance, design activity and its ability to convert new design opportunities into production shipments; timing and market acceptance of its customers' products; schedule changes and projected production start dates that could impact the timing of shipments; the company's future evaluation systems; broadening our ecosystem partners, expected results and financial expectations for revenue, gross margin, operating expenses, profitability and cash.

These statements should be considered in conjunction with the cautionary warnings that appear in QuickLogic's SEC filings. For additional information, please refer to the company's SEC filings posted on its website and the SEC's website. Investors are cautioned that all



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forward-looking statements in this call involve risks and uncertainties and that future events may differ materially from the statements made. For more details of the risks, uncertainties and assumptions, please refer to those discussed under the heading “Risk Factors” in most recent annual report on Form 10-K, most recent quarterly report on Form 10-Q, recent Forms 8-K and other documents we periodically file with the SEC. These forward-looking statements are made as of today, the day of the conference call, and management undertakes no obligation to revise or publicly release any revisions of the forward-looking statements in light of any new information or future events.

In today’s call we will be reporting non-GAAP financial measures. These non-GAAP measures should not be considered as a substitute for or superior to financials prepared in accordance with GAAP. You may refer to the earnings release we issued today for a detailed reconciliation of our GAAP to non-GAAP results and other financial statements. We have also posted an updated financial table on our IR web page that provides current and historical non-GAAP data.

Please note, QuickLogic uses its website, the company blog, corporate Twitter account, Facebook page, and LinkedIn page as channels of distribution of information about its products, its planned financial and other announcements, its attendance at upcoming investor and industry conferences, and other matters. Such information may be deemed material information, and QuickLogic may use these channels to comply with its disclosure obligations under Regulation FD.



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A copy of the prepared remarks made on today's call will be posted at QuickLogic's IR web page shortly after the conclusion of today's earnings call.

I would now like to turn the call over to Brian.

### **Brian Faith** – Chief Executive Officer

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Thank you, Jim. Good afternoon everyone and thank you all for joining our Q3 Fiscal 2019 financial results conference call.

I would like to start off today's call updating you on our near-term outlook, including some significant new developments, and then discuss the pathway we will follow with the goal of achieving profitability early next year. Later, Sue will review our financial results.

As I mentioned in our call on August 6th, there were several factors outside our control that caused us to reset our revenue expectations for both the third quarter and all of fiscal 2019. While some of these factors have been rectified, there are still some items taking longer to complete than our customers initially expected. These items will have an impact on our fourth quarter outlook.

In the continued dialogue with our customers, it has recently become clear that some of the programs we believed would come back in Q4 are not going to materialize this quarter. As a result of these evolving conditions, we are taking a conservative approach to our outlook. Currently, our fiscal 2019 guidance is for total revenue of \$10.4M plus or minus \$300K. This translates to annual sales approximately \$3 million lower than the previous outlook. In addition, while we expect Q4 gross profit margin to be approximately 60%, for the full year



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2019 we will see gross margin in the high 50s, slightly lower than the range we thought in August.

While we generally don't give financial outlook more than one quarter at a time, I want to offer the following:

We currently believe that we should see a healthy increase in revenue in Q1, accompanied by a stronger gross profit margin, as our revenue mix should include a higher percentage of SaaS and eFPGA IP sales. When combined with continued cost controls, we should be close to non-GAAP operating income breakeven at the end of Q1 2020, and we anticipate being breakeven or profitable in Q2 2020. Furthermore, as Sue will discuss later, while we will use some cash in Q4, we expect the burn to be minimal in Q1 and close to neutral in Q2.

We are obviously disappointed with these near-term conditions. However, there have been several positive developments that we believe will serve as revenue and gross margin drivers starting at the beginning of fiscal 2020.

I'd now like to expand on some of the items influencing the fourth quarter. There are four specific areas that comprise the majority of the approximately \$3 million delta between our current expectations and the previously forecasted revenue.

First, our EOS™ S3 Hearable business continues to be impacted by changes in how customers are developing products that meet Amazon's AVS specification. Most recently, Amazon has released their own proprietary voice software. This has influenced some of our customers to wait for the integration of that Amazon software onto EOS S3 prior to bringing their products to market. This factor, combined with Amazon releasing their own TWS head phones for this



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holiday season, has resulted in \$1.1 million in lower revenue. To be clear, this is not a lost opportunity; rather, it is just a push out into fiscal 2020 due to the delayed development schedules of our customers.

Second, one of our larger expected eFPGA licenses has pushed out to next year, impacting current quarter revenue by approximately \$750,000. I'll offer additional color on our eFPGA business later in my prepared remarks.

Third, within our mature product revenue, while our business with the US Navy is solid and budgets have been confirmed, some of the other military business we expected in Q4 has also been pushed into the first half of 2020. This will negatively impact fourth quarter revenue by approximately \$400,000.

Lastly, several of the SensiML/QuickAI customers we expected to convert to full SensiML SaaS subscriptions have taken longer to get through their evaluation period, thereby shifting revenue from these two areas to 2020. This resulted in lower than expected Q4 revenue by about \$500,000.

Combined, these four factors account for nearly \$2.8 million of the \$3 million delta.

While each of these areas are below our recent expectations, we are confident the issues are short term. We expect a portion of this revenue to be realized starting in Q1.

I now want to offer some additional color on each area and discuss why we are confident the revenue ramp is imminent.



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Starting with our mature product segment - the push out of shipments to the US military customers that impacted our revenue over the second half of fiscal 2019 is being resolved. While we expect to see some of the military orders starting to come back this quarter, it will not be at the pace we anticipated when we spoke back in August. We expect to see the balance of the delayed military orders come back in Q2 2020.

Moving to our EOS S3 related products, the ongoing trade conflict with China has caused several of our customers to delay their new product introductions. As I mentioned in our last call, a specific Chinese consumer electronics manufacturer pushed out the introduction schedule for one of our largest 2019 design wins that we were originally told would happen for the 2019 holiday shopping season. We still believe this project will be deployed for the 2020 product introduction cycle.

The silver lining with this issue is that we have successfully leveraged this always-on technology for a voice-enabled remote control with a well-known and fast-growing streaming and smart TV provider. They recently gave us a firmer launch date of Q2 2020. The reason I say the date is firmer is that the timing is not dependent on any TV manufacturer bringing it to market; this new design is completely in the hands of the consumer platform provider. The potential could be into the hundreds of thousands of dollars per quarter.

In the Hearables market, we have a clear path forward for Amazon AVS or Alexa Voice Service compliant hearable designs. We have successfully concluded a large suite of tests and believe that we have two viable solutions for customers that pass both Certification and Qualification testing. With these hurdles behind us, and the revised schedules we have



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received from our customers, I believe revenue generated by hearable designs will ramp more significantly in Q1 2020.

Separately, we recently established a partnership with Atmosic™, which is rapidly developing traction for its new ultra-low-power Bluetooth® Low Energy solution. Leveraging this and our new partnership with Retune DSP, we have already won a new design with a large consumer electronics OEM for a 2<sup>nd</sup> voice-enabled TV remote control.

The release schedule for this design has shifted to Q2 2020. The customer expects to ship several hundred thousand units next year. In addition, we are engaged with this customer on a second design that has significantly higher volume potential that is scheduled to launch in 2020.

In addition, our largest ODM customer was the only 3rd party company that we are aware of that was showing Truly Wireless Stereo, or TWS, AirPods-like headphones in Amazon's booth at the September IFA Conference in Berlin. This customer has started several engagements now with OEMs who are interested in white labeling this product as their own AVS-compatible TWS headphones. Our partner is still targeting to be complete with their AVS dev kit and AVS ODM design on the Amazon web pages during this quarter. We believe inclusion on Amazon's AVS web sites will lead to several, new OEM engagements that will result in volume shipments from QuickLogic in the first half of 2020.

On another positive note, I'm very pleased to confirm our Japanese smartphone customer is integrating our technology across a broader range of their products. Their first phone with EOS S3 inside was on carrier shelves in August, and we have now shipped pre-production



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orders of EOS S3 for three additional phones that they expect to launch before year end, bringing our total number of models to four. Since we are meeting this OEM's stringent power requirements, we hope to expand the number of models that include an EOS S3.

In June we announced a new Integrated Alarm System or IAS reference design from Infineon that targets home, commercial and industrial IoT applications. Several well-known consumer-focused companies continue to evaluate the IAS reference design for integration into their products. While it is too early to predict specific launch dates by end customers, we do believe we will generate revenue from this starting in the middle of 2020.

On top of this, a large module manufacturer has already designed a new low-cost module based on the Infineon IAS that OEMs can easily integrate into finished IoT designs. This module is scheduled for introduction in early 2020.

Now, I'd like to cover several positive updates on our eFPGA business. As I mentioned in the last call, in Q2 we finalized a license agreement with a prime military contractor that has been commissioned by the DoD to evaluate and recommend embedded FPGA solutions and suppliers. As an update, they continue to progress with their evaluation of our test chip as well as our eFPGA core through their design flow.

As I have noted before, military contractors already represent a large market for discrete FPGAs, and the Department of Defense is taking steps now that will make it easier for its contractors to incorporate embedded FPGA in ASIC designs. We believe we are well positioned to address this trend for certain ASICs that will use FD-SOI manufacturing processes. As further evidence of this emerging trend, we are now more deeply engaged





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with a separate military contractor for our 22nm FD-SOI eFPGA. We are targeting an evaluation agreement for the first part of fiscal 2020 that could lead to a full license in the second half of the year.

Last quarter I had told you we expected to finalize testing of the ETH Zurich Parallel Ultra-Low Power IC that includes our eFPGA IP. After a longer than anticipated delay, the test chip is up and running now in our labs. I want to highlight that this test chip has led to a new engagement that we will touch on shortly.

In September we announced that Nations Technologies selected our eFPGA to power its Next Generation Low Power IoT SoC. While this agreement generates only modest revenue in the near term, it enables us, and the customer, to fast-track SoC License Agreements that we believe will generate considerably more revenue starting in the 2<sup>nd</sup> half of 2020.

Our eFPGA strategy continues to evolve and we believe the promise it holds for our future is significant. I have often discussed the need for a more scalable go-to-market strategy and we believe that comes through tapping into the reach of more “Platform Companies.” By platform companies, we mean well-known mega-cap sized companies, or ones that have a strategy around connecting a massive number of users with services. These massive users in fragmented markets drive sufficiently large volumes that create a served available market large enough for our SoC business to co-exist with other SoC players where we can license our eFPGA.

Last year, we signed an evaluation license with C-Sky who was acquired by Alibaba to be their SoC company moving forward. C-Sky was subsequently renamed to Pingtogue and now



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is driving all the semiconductor development for Alibaba. Ultimately, Alibaba wants more devices connected to their services. As such, they are creating an ecosystem similar to what SiFive is doing – creating SoC templates such that semiconductor companies and system OEMs can bring derivative products to market quickly and cost effectively.

I am pleased to announce we were selected by Pingtogue to join their IP Ecosystem Alliance, and that we are the only eFPGA company included in their recently announced template SoC, codenamed Swordless. This IoT SoC template is targeted for tape out in 2020. Barring any worsening of trade tensions with China, we believe that it will drive significant eFPGA adoption moving forward.

Pingtogue will use the license we had previously agreed to under our MTLA for this Swordless test chip, and then any future users of the template for their own SoC will generate an IP license and royalties upon unit shipment. We are very optimistic about the potential of this initiative with Alibaba for our eFPGA business.

Another exciting initiative for us related to our more scalable go-to-market strategy for eFPGA has now expanded in the last month to be of much broader scope than originally anticipated. This one is also with a well-known mega-cap sized global company. What started as an eFPGA discussion has broadened significantly.

I am very excited to announce that we have signed an agreement with this company to jointly develop and bring-to-market an IoT development platform that is based on the EOS S3 as the host processor. To enable the broadest served available market, we will launch this



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platform with open source tooling support for both the ARM MCU and the eFPGA core in the EOS S3.

We are now jointly engaged with a 3rd party company who has a track record of delivering open source tools. We also have a commitment from this mega-cap company to launch thousands of low-cost development kits into the market, our largest deployment ever by two orders of magnitude. We are targeting to launch these before the end of Q1 2020.

Moreover, we believe multiple AI Software solutions will be ported to this platform, including SensiML.

We believe this initiative will be a catalyst for each of our business units. First, it could drive an EOS S3 user base two orders of magnitude larger than what we have today. Second, it should drive significantly more exposure for SensiML and subsequent SaaS subscriptions. Lastly, we believe it will drive a more meaningful eFPGA IP license agreement with the same company I alluded to earlier.

One of our assumptions from our previous earnings call was that the above IP license would be executed in Q4 and drive a near 7-digit license fee in the quarter. While the push out of this IP license to next year is disappointing, I firmly believe the resulting agreement we have negotiated with this company is of substantially higher aggregate value to QuickLogic, which will commence in the current quarter. We look forward to updating progress on this initiative during our next call.

I'll conclude with some additional comments on our QuickAI and SensiML business.



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SensiML continues to gain momentum as more companies explore how AI can be integrated into their suite of products. As this macro trend accelerates, and more dollars are invested in this area, we are dedicating more resources to the SensiML team and technology.

The funnel for SensiML continues to expand, including additional Global Fortune 500 companies. SensiML closed Q3 with a total of 26 customers, 7 of which are Global Fortune 500 companies. This total is up from 12 customers in Q2 and 3 in Q1. Currently, the majority of them are still using the low-cost, evaluation version of the product, not yet on the full SaaS product that generates significantly higher revenue. We anticipate increasing that total during Q4 from our initiatives with our distribution partners, as well as with MCU partnerships such as our most recent one with ST Micro.

We currently expect SensiML will end the year with approximately 40 customers, most of which serve the Industrial markets. These types of customers tend to have much longer evaluation and decision-making periods. As a result, we have seen that the conversion time from evaluation to full SaaS license is taking longer than we had anticipated. Therefore, our objective of cash flow and non-GAAP profitability for the SensiML business unit is more likely to be achieved in mid-2020.

The good news is that Industrial customers tend to have a much longer and more predictable revenue stream, which should offset the seasonality of our consumer-oriented business. In order to accelerate scalable growth, we have recently hired a director of software sales, with experience in AI Software and SaaS business models.



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I've covered a lot of ground in these opening remarks. The bottom line is that while there is short term lumpiness in our business, I am confident that we have the levers in place to deliver revenue growth and improved overall financial performance in 2020.

I would now like to turn the call over to Sue for a discussion of our recent financial performance and full Q4 Outlook. Sue:

**Dr. Sue Cheung**– Chief Financial Officer

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Thank you, Brian. Good afternoon and thanks to everyone for joining us.

For the third quarter of fiscal 2019, total revenue was \$2.2 million. This compares with revenue of \$3.5 million in the third quarter last year. The decline from Q3 last year, which was our highest revenue quarter since the fourth quarter of fiscal 2015, was mainly due to lower shipments of our mature and display bridge products.

Within our Q3 revenue, sales of new products were \$1.0 million. This compares with \$1.5 million in the third quarter last year. While we did have higher revenue from other new product sales, they did not make up for the significant decline in display bridge sales.

Our mature product revenue was \$1.1 million, a decrease compared with \$2.0 million in Q3 last year. The change was due to lower shipments to customers in the military and aerospace sectors.

In the third quarter of 2019, we had four customers each accounting for 10% or greater of sales.



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Non-GAAP gross margin in Q3 was 48.9%, compared with 50.5% in the same quarter last year. The flat gross margin profile comes in spite of a nearly 40% lower revenue than Q3 last year, showing the strength of our diversifying product and customer mix.

Non-GAAP operating expenses for Q3 2019 were approximately \$4.5 million, which was the same as Q3 last year. As a reminder, our OpEx from Q3 last year was prior to the expenses associated with the SensiML acquisition that closed earlier this year.

Within our Q3 2019 OpEx, R&D expenses were \$2.6 million and SG&A expenses were \$1.9 million. This compares with R&D and SG&A, both at \$2.2 million in Q3 2018. The approximately \$300 thousand decline in SG&A from the same quarter last year resulted from a combination of items including lower consulting expenses and reduced costs resulting from our facility move earlier this year.

The net total for other income, expense, and taxes in Q3 was a \$78,000 charge, compared with an expense of \$33,000 in the third quarter last year.

Non-GAAP net loss in Q3 was \$3.5 million, or \$0.03 per share. This compares with a net loss of \$2.7 million, or \$0.03 per share in the third quarter last year.

Finally, the total cash at the end of Q3 was \$24.8 million, compared with \$28.2 million at the end of last quarter. Our cash balance at the end of the third quarter also includes the \$15 million draw from the revolving line of credit.

Now moving to our forecast for the fourth quarter of fiscal 2019, which will end on December 29<sup>th</sup>:



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Our revenue guidance for the fourth quarter is \$3.0 million, plus or minus 10 percent. We believe total revenue will be comprised of approximately \$1.3 million of new product revenue and \$1.7 million of mature product revenue.

With our guidance for higher revenue, which includes additional SaaS sales, and the corresponding better absorption of manufacturing overhead, we currently believe our non-GAAP gross margin will improve to approximately 60 percent, plus or minus 3 percent.

We are forecasting total non-GAAP operating expenses will decline to approximately \$4.2 million, plus or minus \$300 thousand. Within operating expenses, we expect our R&D to be approximately \$2.5 million and SG&A to be approximately \$1.7 million. This continued improvement in our OpEx is being driven by ongoing cost controls, the lower costs of our new facility in San Jose, and the roll-off of the one-time moving expenses we discussed last quarter.

After interest expense, other income and taxes, at the midpoint of these ranges, we currently forecast our non-GAAP net loss will be approximately \$2.4 million, or \$0.02 per share based on about 116 million shares outstanding.

Most of the difference between our GAAP to non-GAAP results is our stock-based compensation expense, which we expect to be approximately \$760 thousand. We expect this expense will remain in the mid \$700 thousand range for the foreseeable future.

Finally, in Q4, we expect lower cash usage - in the range of \$2.8 to \$3.2 million. As Brian mentioned earlier, we should be close to non-GAAP operating income breakeven at the end

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of Q1. This, in turn, should translate into minimal cash usage for the first quarter next year, and cash flow breakeven in Q2 of 2020.

With that, let me now turn the call back over to Brian for his closing remarks.

### **Brian Faith** – Chief Executive Officer

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Thank you, Sue.

Before concluding my remarks, I would like to take a moment to discuss the preliminary proxy filing we made on October 7<sup>th</sup> asking for shareholder approval to execute a reverse split of our common stock if this is needed to remain listed on the NASDAQ Capital Market. As I discussed in the blog post that accompanied the filing, there are steps we must take to maintain our compliance for trading on the NASDAQ Capital Market if our stock does not close with at least a \$1.00 bid price for ten consecutive trading days prior to January 13<sup>th</sup>, 2020.

The Board has not made a final decision on whether it will execute a reverse split, nor determined a final split ratio. The special meeting is simply to have shareholder approval should it need to use the reverse split path to remain in compliance with NASDAQ.

In closing, while we are disappointed to not have achieved our fiscal 2019 financial goals that we discussed during the year, I am convinced that the design wins with recognizable OEMs, new ecosystem partnerships, and product introductions addressing new growth markets creates a clear pathway to delivering improved financial performance in fiscal 2020. During this ramp to profitability, I believe we have the balance sheet to support our financial





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objectives. I am again reiterating that we currently do not expect the need to raise further cash via an offering.

While it is too early to discuss a detailed outlook for fiscal year 2020, the commitments we have received from customers, and mix of business we currently expect, gives us greater confidence that we will not only significantly increase revenue, but again deliver a solid increase in our annual non-GAAP gross profit margin for the fourth straight year.

Before opening the call for Q&A, I want to let everyone know QuickLogic will be participating in some upcoming investor events. A few of the highlights include:

- The Craig-Hallum Alpha Select Conference in New York on November 12th
- The LD Micro Conference in Los Angeles on December 11<sup>th</sup>; and
- The Consumer Electronics Show in Las Vegas January 7th through the 10th

All the events we plan to attend will be available on the Events Section of our website. That completes our prepared remarks. Operator, I would now like to open the call for questions.

**Brian Faith** – Chief Executive Officer

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### Post Q&A

Thank you for your participation in today's call and continued support. We look forward to speaking with you again when we report our fiscal fourth quarter results in early February next year. Thank you and good bye!