Q3 FY21 Earnings Conference Call Prepared Remarks

Operator

Ladies and gentlemen, good afternoon. At this time, I'd like to welcome everyone to QuickLogic Corporation's Third Quarter Fiscal Year 2021 Earnings Results Conference Call. As a reminder, today's call is being recorded for replay purposes through November 24, 2021. I would now like to turn the conference over to Mr. Jim Fanucchi of Darrow Associates. Mr. Fanucchi, please go ahead.

Jim Fanucchi

Thank you, operator and thanks to all of you for joining us. Our speakers today are Brian Faith, President and Chief Executive Officer, and Anthony Contos, Interim Chief Accounting 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 production start dates that could impact the timing of shipments; the company's future evaluation systems; broadening the number of our ecosystem partners; and expected results and financial expectations for revenue, gross margin, operating expenses, profitability and cash.

Actual results or trends may differ materially from those discussed today. For more detailed discussions of the risks, uncertainties and assumptions that could result in those differences, please refer to the risk factors discussed in QuickLogic's most recently filed periodic reports with the SEC. QuickLogic assumes no obligation to update any forward-looking statements or information, which speak as of the respective dates of any new information or future events.

In today's call we will be reporting non-GAAP financial measures. 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 business. Such information may be deemed material information, and QuickLogic may use these channels to comply with its disclosure obligations under Regulation FD.

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

Thank you, Jim. Good afternoon, everyone, and thank you all for joining our third quarter fiscal 2021 financial results conference call.

Our Q3 results were among the best QuickLogic has ever reported.

Revenue of $3.9 million was the highest we have generated in 6 years, and due to a higher mix of software and IP-related sales, non-GAAP gross margin was 73%, an all-time record for QuickLogic.

We also made significant progress on our bottom line, with a non-GAAP net loss under $400,000, the lowest since Q4 of 2010.

And when we include our outlook for Q4, which Anthony will provide a bit later, our revenue for the second half of fiscal 2021 alone will be almost the same as we reported for all of fiscal 2020.

These results further validate that our transformation to a platform company focused on enabling more edge artificial intelligence is well underway. We are doing this by marrying our decades of expertise in programmable logic with the power, breadth and continually expanding open-source software and hardware ecosystems. I am very proud of the QuickLogic and SensiML teams for their amazing accomplishments and thank them for their dedication and efforts to get us to where we are today.

Since we embarked on this new path forward nearly two years ago, our commitment to leveraging open source is fueling what I believe to be a once in a multi-decade opportunity to disrupt the mature FPGA market. QuickLogic has quickly established itself as one of the leaders in this fast-moving market. We are now at the tipping point for scaling this new approach more broadly, which is coinciding with accelerating market demand for embedded FPGA IP cores and FPGA devices that are supported by open-source tools.

With our powerful combination of leading-edge products, growing customer and industry relationships, and an increasing network of distribution partners, I am even more confident we are at the beginning of a long-term trajectory that will deliver higher revenue and earnings, which should ultimately lead to improved shareholder value.

Now I want to move into some of the items that drove our third quarter results and developments that will serve as the building blocks for our future success.

First, let's start with a significant development that strengthened our financial position. At the end of September, two of our long-time shareholders approached me about making a strategic investment in the Company. These holders recognize the tremendous opportunities ahead. The transaction was done at no market discount, raising a little over $1 million. The funding should ensure we have the capital to execute on our near-term growth objectives.

We also announced our largest eFPGA contract ever, a $2 million design win. Part of this revenue was captured in Q3 with the remainder expected in Q4.

This was an intense and lengthy process. The customer performed an extensive evaluation of several programmable logic companies. Ultimately, they chose QuickLogic because of our proven track record in delivering high quality programmable logic devices, eFPGA IP and FPGA User Tools combined with our strategic QORC (QuickLogic

Open Reconfigurable Computing) open-source initiatives. This is the first of what we believe will be several seven-digit opportunities, which makes us excited about the prospects for 2022 and beyond.

Also in September, we formally announced the Australis™ eFPGA IP Generator, which is the opening to what I believe is a new era of mass FPGA and embedded FPGA customization. The Australis Tool is going to be a game changer.

The Australis Tool generates eFPGA IP in a highly automated way, including the implementation of customer-specific variants. The Tool is built with scale in mind, with the ability to generate an eFPGA IP core for a new foundry and process node within a few months, and derivatives to currently supported foundry/process node combinations within weeks or even days.

To be clear, we will use the Australis Tool to address multiple challenges and opportunities. Developers will be able to create eFPGA implementations for intellectual property protection, offloading and hardware acceleration of artificial intelligence/machine learning processes, or simply create a range of product variants for fragmented markets. Being able to do all of this quickly and with the flexibility to easily target the same node as the SoC means that these significant benefits come at a very low cost.

We are already seeing the Australis Tool pay dividends. A few weeks ago, we announced our first customer success story in which we used the Australis Tool to generate a customized eFPGA IP for UMC's 22 nanometer process. More importantly, this was a new foundry and process combination for us, and we were able to go from contract to

IP delivery within only four months, substantially faster and with much less development cost than with our previous development methodology.

The specific customer's motivations reflect many of the reasons we believe that using embedded FPGA technology for SoC applications is a smart technical and business decision. Being able to execute quickly and with the flexibility to easily target the same node as the SoC is using means that these significant benefits come with a very low cost and a very fast time-to-IP-delivery.

We are seeing an increase in RFPs and RFQs for our eFPGA IP – and this is exactly what the Australis Tool enables, leading to better market penetration and financial results for us in the coming years.

Those are some of the key announcements we made since our last call. Now I want to offer some comments about what we are seeing near-term for our eFPGA business.

We are currently working on several initiatives that have the potential to generate tens of millions of dollars in revenue over the next three years. Given the sensitivity of these programs, and confidentiality restrictions we are bound to, we can't discuss companies or give granularity on applications. However, from a 50-thousand-foot level let me cover the following:

We recently signed a large, very near seven figures, eFPGA-related contract for a process technology we have not targeted before. We will be using the Australis Tool to go from customer contract to IP delivery in less than two months – a record for us. We believe this will likely lead to a follow-on multi-million-dollar contract in 2022, with additional opportunities in future years.

These types of opportunities would simply not have been possible a couple of years ago. Now, through our eFPGA initiatives, growing presence with the Open-Source FPGA Foundation, and an expanding toolbox of key products, we have the opportunity to bid on significant proposals and execute for revenue.

Outside of our eFPGA business, we announced a strategic partnership with Rubidium Ltd., a leader in voice recognition, and always-on voice trigger software. We are providing Rubidium a complete voice recognition solution based on our very low power EOS™ S3 voice and sensor platform, which they will combine with their own Voice User Interface software. This is very attractive for IoT edge applications – particularly those that are battery powered or lack cloud connectivity.

Our SensiML business continues to gain traction. Recently, we announced that SensiML has teamed with onsemi, one of the semiconductor industry giants, enabling the development and integration of AI-based algorithms into their manufacturing, robotics, or predictive maintenance applications without needing to have expertise in data science or AI. The onsemi RSL10 Sensor Development Kit combined with the SensiML tools has produced a compact but sophisticated platform that's perfectly suited for driving next-generation Industry 4.0 solutions. This is a major win for SensiML.

We once again expanded our distribution channels, signing a worldwide distribution agreement with Digi-Key Electronics. Our EOS S3 low power microcontrollers and PolarPro® 3 low power FPGAs, all supported by 100% open-source software, as well as our dev kits are now available through that channel. This agreement is complementary to the agreement SensiML signed with Digi-Key earlier this year. Our partnership with

Digi-Key is an important milestone in our global growth strategy and increasing our presence worldwide.

Our smartphone related sales came down a little as expected in the third quarter after a very strong Q2, and we expect them to come down a little further in Q4 as our smartphone customer prepares for their next smartphone launches. Despite that sequential drop for the year, we are proud to say that our smartphone revenue will be approximately 60% percent higher than the prior year. We ended the quarter in 10 phones including multiple 5G models. A new smartphone was just launched yesterday that includes our EOS S3, and we believe our lead smartphone customer will continue to use EOS S3 through 2022 and into at least 2023 on multiple models.

With respect to the supply chain issues that have been discussed by many companies, our lead times have increased for the final assembly and test production. What used to be a 6 to 8-week turnaround is now stretching to 6 months or more. We are countering some of the delays by leveraging our inventories of substrates and finished materials. However, this issue is not going away anytime soon and so we may need to build additional inventory ahead of customer shipments to minimize risk.

Finally, in our mature product segment, revenue declined as expected. Ongoing supply chain issues impacting our mature customers, particularly in the civilian aerospace market, in addition to the lingering effects of COVID related business disruptions, continue to hold back revenue in this segment.

Without good clarity it is difficult for us to see how mature revenue will be much different in the first half of fiscal 2022 than it will be in second half of fiscal 2021.

I know I have covered a lot of topics that will be instrumental in our ongoing business and financial improvement. Simply put, 2021 is proving to be the most pivotal time in QuickLogic's long history. It has not been easy, and there may still be bumps in the road in the future. However, the financial results we are reporting today, and the outlook we have for both the near-and long-term, are the proof points validating that our transition is succeeding.

With that I will turn the call over to Anthony.

Anthony – Interim Chief Accounting Officer

Thank you, Brian, and good afternoon to everyone joining us on today's call.

As Brian mentioned, our revenue was the highest since the third quarter of fiscal 2015 and represents the successful progress QuickLogic is making in its business and product transformation.

For the third quarter of fiscal 2021, revenue was $3.9 million. This compares with revenue of approximately $2.9 million in the second quarter of 2021 and $1.8 million in the third quarter of 2020. This reflects an increase of $2.1 million, or approximately 117%, compared with the same quarter last year.

Within our Q3 revenue, sales of new products were approximately $2.8 million, the highest since Q3 2015. This compares with about $1.3 million last quarter and $639,000 in the third quarter of 2020. Our mature product revenue was approximately $1.1 million, compared with $1.6 million last quarter and $1.1 million in the third quarter of last year.

In Q3, we had three customers who each accounted for 10% or more of our revenue.

Non-GAAP gross margin in Q3 was 72.8%, which is an all-time record for QuickLogic. Product mix, which included higher eFPGA and other services revenue, were the main reasons for the improvements. The Q3 gross margin compares with 51.5% in the prior quarter and 53.9% in the same quarter of 2020.

I should remind everyone that second quarter gross margin was primarily impacted by a write-down of Raw Materials of approximately $156,000. This caused a 5% reduction in gross margin. Nonetheless, you can see that gross margin was up substantially from the prior quarter.

Non-GAAP operating expenses for Q3 were approximately $3.2 million. This compares with $3.3 million in Q2 and $2.6 million in the third quarter of last year.

Within our Q3 operating expenses, R&D was approximately $1.5 million and SG&A was $1.7 million. This compares with R&D and SG&A of $1.6 million and $1.7 million respectively in Q2, and $1.3 million for both R&D and SG&A, in the third quarter of last year.

Non-GAAP net loss was $0.4 million, or a loss of $0.03 per share, based on 11.6 million shares.

This compares with a net loss of $1.9 million, or $0.16 per share last quarter, and a net loss of $1.7 million, or $0.15 per share in the third quarter of last year.

The total cash at the end of Q3 was $19.6 million, this compared with $19.0 million at the end of last quarter. Included in the total cash was a net of approximately $1 million received from the direct placement. The cash balance also include the $15 million draw from the revolving line of credit.

Now moving to our guidance for the fourth quarter of fiscal 2021, which will end on January 2, 2022.

The revenue guidance for Q4 is $3.9 million, plus or minus 15%. We believe total revenue in Q4 will be comprised of approximately $3 million for new products, which would be the highest since Q2 of 2015. Mature product revenue is forecasted to be approximately $900,000.

This midpoint of guidance, combined with the results from the first three quarters, would translate into annual revenue growing 50% above fiscal 2020, consistent with our previous estimates.

Based on the expected revenue mix, non-GAAP gross margin for the quarter will be approximately 64%, plus or minus 5%. At the midpoint, this will result in annual non-GAAP gross margin of 62%, consistent with what we have discussed throughout the year. For comparison purposes, non-GAAP gross margin in fiscal 2020 was approximately 51%.

Additionally, the expected decrease in gross margin in Q4 versus Q3, is primarily related to the reclassification of Non-Recurring Engineering expenses to cost of sales in connection with our new eFPGA contracts.

Our non-GAAP operating expenses will be approximately $3.3 million, plus or minus $300 thousand. At the midpoint of the range, we expect R&D expenses to be approximately $1.6 million, and SG&A expenses to be approximately $1.7 million. As

Brian mentioned earlier, with the pipeline of business we see for 2022, we would expect quarterly OpEx will tick up between $200 thousand to $300 thousand, from Q4 levels in order to support the anticipated growth. Just a reminder that the first quarter of each fiscal year is generally a higher spend quarter due to the normal beginning of the year expenses.

After interest expense, other income and taxes, we currently forecast our non-GAAP net loss will be approximately $900,000, or a net loss of $0.08 per share, based on roughly 11.8 million shares outstanding.

Most of the difference between our GAAP and non-GAAP results is our stock-based compensation expense. In Q4 we expect that our stock-based compensation will be similar to Q3. There will be movement in our stock-based compensation over the course of the year and it could vary each quarter based on the timing of grants and estimates related to performance related awards.

For the balance sheet, in Q4 we expect cash usage to be consistent with Q3, in the range of $500,000 and $700,000.

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

Brian Faith – Chief Executive Officer

Thank you, Anthony. Before sharing my closing remarks, I would like to offer a warm welcome to Radhika Krishnan to our Board of Directors. As we announced this morning, Radhika is currently serving as the Chief Product Officer and General Manager at Hitachi Vantara where she is responsible for numerous functions across all product lines. This includes the industry leading Lumada SaaS portfolio targeting data management, analytics, AI/ML, and Industrial IoT market segments. Radhika brings a strong background in software and hardware, and I believe she will have an immediate impact on our AI/ML growth strategy for our SensiML AI Software and eFPGA IP products.

In closing, I have been a part of the QuickLogic team for more than two decades. At no other time have I, or many of our long-term team members, been this excited about the future prospects for the company. Customer interest in our new technologies is accelerating, distribution partnerships are expanding our reach, and our financial position is as strong as we have seen in many years.

Our sales funnel is strong and growing, and we are exiting this year with more signed IP-related deals than ever before. SensiML has expanded its partnership ecosystem to support nearly all of the top microcontroller companies. Our go-to-market strategy has been and will continue to be focused on products that can generate revenue faster, with higher gross margin, and with a high return on investment.

With this being the final earnings call this calendar year I wanted to offer a little more insight into our current thoughts for fiscal 2022.

Our pipeline of what I would call ‘winnable’ opportunities is accelerating, and we continue to balance this knowing that not all of these opportunities will pan out. That said, I can see a pathway for annual revenue in 2022 to grow at the same percentage, if not more, than the growth we foresee in fiscal 2021 over fiscal 2020.

At the same time, with an expected higher mix of software and IP-related sales next year, our gross margin could climb into the mid to high 60 percent range. While operating expenses will grow modestly to support the new customer design wins, we should be on track to reach profitability in the first half of 2022.

It has been several years since we have been able to deliver such positive news and a bright outlook. I want to thank our long-time investors, customers, suppliers and most of all the QuickLogic team for their continued support and trust. This is a new era for QuickLogic and our future could not be brighter.

That completes our prepared remarks. Operator, I would now like to open the call for questions.

Brian Faith – Chief Executive Officer

Thank you for participating in today's call and your continued support. We look forward to speaking with many of you again when we participate in upcoming investor events, and again when we report our fourth quarter fiscal year 2021 results. Have a great day!