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IOTS - Q3 2017 Adesto Technologies Corp Earnings Call

EVENT DATE/TIME: NOVEMBER 08, 2017 / 10:00PM GMT

THOMSON REUTERS

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PRESENTATION

Operator

Good Afternoon and welcome to the Adesto Technologies Third Quarter 2017 Financial Results Conference Call. (Operator Instructions). As a reminder, this conference is being recorded today November 8, 2017. I would now like to turn the call over to Leanne Sievers, President of Shelton Group Investor Relations. Leanne, please go ahead.

Leanne K. Sievers - *Shelton Group - President*

Good afternoon and welcome to Adesto Technologies' Third Quarter 2017 Earnings Conference Call. I'm Leanne Sievers, President of Shelton Group, Adesto's Investor Relations firm. Joining me today are Narbeh Derhacobian, Adesto's President and CEO; and Ron Shelton, Chief Financial Officer. Before I turn the call over to Narbeh, I'd like to remind our listeners that during the course of this conference call, the company will provide financial guidance, projections, comments and other forward-looking statements regarding future market developments, the future financial performance of the company, new products or other matters. These statements are subject to the risks and uncertainties that we discuss in detail in our documents filed with the SEC, specifically the final prospectus related to our initial public offering and our most recent 10-Q which identify important risk factors that could cause actual results to differ materially from those contained in the forward-looking statements. Also, the company's press release and management statements during this conference call will include discussions of certain non-GAAP financial measures. These financial measures and related GAAP to non-GAAP reconciliations are provided in the company's press release and related current report on Form 8-K, which can be found at the Investor Relations section of Adesto's website at www.adestotech.com. For those of you unable to listen to the entire call at this time, a recording will be available via webcast on the company's website.

And now I'll turn the call over to Adesto's President and CEO, Narbeh Derhacobian. Narbeh, please go ahead.

Narbeh Derhacobian - *Adesto Technologies Corporation - Co-Founder, President, CEO & Director*

Thank you, Leanne, and welcome to everyone joining us today. As announced today, I am very pleased to report that we achieved another quarter of record revenue increasing 36% year-over-year to $15.3 million, and exceeding our guidance range of $14.3 million to $14.7 million.

Additionally, our non-GAAP operating expenses came in $300,000 below the low end of our guidance range, resulting in the achievement of non-GAAP profitability 1 quarter ahead of plan. The main driving force behind our growth continues to be the transition of our past design wins into mass production with our customers. Meanwhile, this past quarter, we continue to add additional designs into our pipeline that will serve as the future growth drivers. In fact, for the first 9 months of 2017, we almost doubled the number of new design wins over the same period last year. This indicates a healthy pipeline of growth opportunities for our products in the future. More importantly, approximately 65% of the design wins in the last quarter were with new customers, indicating expanded future-growth opportunities for Adesto.

In terms of end markets over 75% of our new design wins in the quarter were within our 2 largest vertical end-markets of industrial and consumer. Notable design wins included new Smart Meter platforms with our leading customers for 3 programs in Europe, as well as a large win from a Smart Meter customer in Japan.

Although we've indicated in the past that these wins may take time to reach full production levels, we see from the results of the past several quarters that they do form the basis of future revenue growth for the company. In the consumer market, we had a notable design win with the leading personal fitness tracker company that we've been engaging with for a while, as well as wins in various smart-home applications. In addition to these design wins, I would like to point out notable engagements with 2 Fortune 50 companies. These are not design wins yet, but we are in qualifying stages with these opportunities. One is in a connected personal health monitor application, and the other one is in a personal-entertainment console.

We also continue to see new IoT edge devices coming to market with new applications such as smartphones, validating our thesis that not one end-application is driving our growth, but rather a wide breadth of deployment and adoptions.

In terms of the details of the actual revenue breakdown for our top 20 customers in the third quarter, 55% came from the industrial market, 29% from the consumer market and the remaining 16% spread across computing, automotive and communications. Examples of applications that contributed to our revenue in the quarter included smart meters, universal and streaming remote controls as well as asset trackers.

Now let me talk about our product family. In our DataFlash family we continue to see strong, sequential and year-over-year revenue and unit-shipment growth as we gain increased traction in the Smart Meter end-market. As you recall last quarter, we introduced our DataFlash-L series of products designed for smart-home applications and also announced that we have secured a reference design win with Sigma Designs for their Z-Wave communications chipset. During the quarter, we have seen a large number of opportunities at end-customers sampling this product. The Z-Wave reference design along with our DataFlash memory solutions enable system designers to build simple, over-the-air or OTA update functions into their smart homes and other wireless devices.

As we began to see this quarter, this opportunity is exposing our solution to hundreds of end-customers who are using this reference design for various products targeted at the smart-home end-market.

Turning to our Fusion family. We continue to generate increasing revenue and interest for this family of products. During the quarter, we sampled our Fusion devices to a high-volume game console manufacture. As part of our efforts to expand our product range for Fusion family, we are working on releasing new higher-density versions of Fusion and expect to sample these parts to customers in mid-2018.

We also continue to make solid progress on our EcoXiP product. The opportunity for EcoXiP continues to grow. During the last quarter, JEDEC released its new xSPI standards for high performance octal flash. We are pleased to say that EcoXiP is fully compatible to this new spec. This new standard provides customers, including system developers and controller designers with assured compatibility. This milestone enables faster and broader deployment of the EcoXiP platform and provides the opportunity for new designs to advance forward. We also continue to highlight the performance advantages and the value proposition that EcoXiP offers, as we recently demonstrated at the Arm Tech conference as well as through embedded system demos.

During the quarter, we also saw MCU supplier NXP continue to press the theme of so called Flashless MCU, or microcontrollers without embedded flash. This emerging trend is primarily due to the cost of integrating flash in very-advanced nodes. EcoXiP was designed exactly to meet this growing trend. As of today, we have provided samples of the 32Mb EcoXiP to over 5 microcontroller and system-on-chip suppliers for their evaluation and design activity. We expect to have higher-density versions of the EcoXiP samples by mid-2018.

We also continue to make progress with our MavriqCM device. This is the Mavriq family design for the camera module. You may remember that we received first silicon back from the foundry in the second quarter, and we began testing the device at the end of the quarter and into the third quarter. I'm pleased to report that all of our characterizations show the device functioning as expected. Silicon samples, therefore are on schedule for fourth quarter customer delivery and we're building demos to showcase the product in the first quarter of 2018.

Also in early October, we announced that Teledyne High Reliability Electronics adopted Adesto's CBRAM memory technology for high-performance applications for use in their semiconductor solutions that sell into the civil aerospace, industrial, medical, defense, scientific and space applications. CBRAM technology offers unique advantages to high-reliability applications due to its tolerance to harsh environments. This is in addition to CBRAM's inherent advantage in very low-power operation and low-energy consumption. CBRAM's resistance to the effects of radiation makes it suitable for use in applications such as satellite, medical products and other high-reliability applications. Although these applications are lower-volume compared to our typical opportunities, they do offer a high gross margin profile. This engagement with Teledyne will serve as an additional channel for selling value-added memory solutions to the high reliability end market.

In terms of the Moneta family, I reported last time that we are seeing increased sampling activity for this product. As a reminder, this is a truly value-added solution for IoT application that offers extreme low-power operation, such that can it be powered with energy harvested directly from ambient power sources, thus excluding the need for batteries. We continue to showcase Moneta with customers who are very early in the design phase of their end-systems for such applications. And I'm pleased to report that we have secured a design win with 1 of these customers. This customer is still in early phases of its system process, but clearly has moved to a more committed engagement characterizing its system and finalizing the design with Moneta. This represents a significant milestone for Adesto. As it demonstrates the enablement that resistive RAM can bring to the sensor nodes by allowing flash functionality, while operating under energy-harvesting mode. This is precisely where the IoT market is heading and speaks volumes to the thesis of our proprietary and smart-memory solutions and our suitability for all of the emerging IoT markets.

Lastly, in terms of our Standard Serial Flash product family, we continue to gain significant traction with these products. And I'm pleased to say that we doubled our unit shipment year-over-year, reflecting a sizable return from the investments we made to build out this product family. A number of our design wins have moved into qualification and full production, as evidenced by our strong unit growth in this product category. Our strategy to leverage these products to gain a foothold with large OEMs and ODMs is proving successful just as we have been saying. The strategy has offered us access to key Tier 1 customers as they establish Adesto as a certified supplier. This allows us to then showcase the value-added features of our other products.

In summary, we're entering the fourth quarter with yet another quarter of record bookings. An increasing number of design wins are ramping into production combined with continued traction. Our new products are driving our expectations to grow revenue 30% over the prior-year period, which is the third consecutive quarter of over 30% year-over-year revenue growth for Adesto.

Additionally, our continued management of operating expenses will further contribute increased profits to the bottom line.

With that, I would like to turn the call over to Ron to review the third quarter financial results followed by more details regarding our fourth quarter guidance. Ron?

Ronald K. Shelton - *Adesto Technologies Corporation - CFO & Secretary*

Thanks, Narbeh, and thanks, everyone, for joining us today. Revenue in the third quarter of 2017 was $15.2 million. That's an increase of 36.3% from the $11.2 million in the third quarter of 2016 and a 13.6% increase from $13.4 million last quarter.

Gross margin in the third quarter was 49%, that's compared to 48.1% in the third quarter of 2016 and 50.1% last quarter, and it remains at the high-end of our long-term model.

As Narbeh mentioned, over the last few weeks, we've embarked on our strategy of using Standard Serial Flash products to rapidly gain or expand our presence in new and existing large OEM customers. And we are happy to announce we've been successful in execution of this strategy and it's now taking hold, which is, in turn, allowing us the opportunity within those customers to sell more value-added products such as Fusion, EcoXiP and DataFlash. In addition, given our success in executing the strategy, we're now seeing increased revenue contribution from these customers, initially from our Standard Serial Flash products, which, again, depending on our overall product mix and consistent with our prior year guidance, could contribute to fluctuations of 100 to 200 basis points in our margins over the near-term.

GAAP operating expenses in the third quarter were $8.3 million. That's compared to $8.8 million in the prior-year quarter, and $8.3 million last quarter. On a non-GAAP basis, operating expenses in the third quarter were $6.9 million, which was below our guidance range of $7.2 million to $7.4 million and compared to the $7.7 million in third quarter of 2016 and $7 million last quarter. For the full year of 2017, we continue to expect non-GAAP OpEx to remain flat relative to 2016.

Now looking at third quarter non-GAAP OpEx in more detail, R&D expenses were $3.1 million, that's compared to $4 million in the third quarter of 2016 and $3.2 million in the prior quarter. We continue to focus resources on market opportunities that we believe can drive near-term revenue contribution as reflected in our revenue results.

Non-GAAP sales and marketing expenses have remained consistent at $2.5 million for the third quarter of 2017. That's flat compared to the year-ago period and last quarter as well. Non-GAAP, G&A expenses were $1.3 million. That's up slightly from the $1.2 million a year ago and $1.2 million last quarter.

Stock-based comp in the third quarter was $1.1 million. Amortization of intangible assets was $309,000, and D&A was $360,000.

Accounting for these items, I am happy to announce that the adjusted EBITDA for the third quarter of 2017 was once again positive and increased to $938,000. That's compared to a loss of $2 million in the third quarter of 2016 and a positive $100,000 last quarter.

GAAP net loss for the third quarter of 2017 was $1.0 million, or a loss of $0.05 per share. That's compared to a net loss of $4.1 million or $0.27 per share in the third quarter of 2016 and a net loss of $1.8 million or $0.11 per share in the prior quarter.

Third quarter non-GAAP net income was $0.4 million or $0.02 per diluted share. That's compared to a net loss of $2.9 million or $0.19 per share in the third quarter of 2016 and a net loss of $500,000 or $0.03 per share in the prior quarter. The share counts used to compute third quarter GAAP and non-GAAP results were 21.1 million and 22 million shares, respectively.

In terms of the balance sheet, we ended the quarter with $30.5 million in cash. That's compared to $31.9 million at the end of the prior quarter.

Inventory at the end of the third quarter was $4.3 million. That's slightly down from $4.4 million last quarter, and our inventory turns remain well above our target of 4x or better.

Accounts receivable is $8.8 million, that's down from $9.1 million last quarter and that works out to an actual weighted average days sales outstanding of a little less than 40 days.

Now let me turn the guidance for the fourth quarter of 2017. As Narbeh stated, we expect to achieve yet another quarter of record revenue ranging between $15.8 million to $16.2 million. At the midpoint of $16 million, this represents year-over-year revenue growth of approximately 30%. Gross margin for the quarter is expected to range between 47% and 50%. GAAP OpEx is expected to range between $8.1 million and $8.3 million and non-GAAP OpEx between $7.1 million and $7.3 million.

Stock-based comp in the fourth quarter will be approximately $700,000. Amortization of intangible assets will be approximately $300,000, and depreciation and amortization will be approximately $400,000.

Weighted average shares outstanding are expected to be approximately 21.3 million for the fourth quarter.

So before opening the call to questions, I'd like to summarize my comments on our operating objectives once again. First, again we grew revenue 36% over the prior-year period and we expect to grow fourth quarter revenue another 30% year-over-year, and that's our third consecutive quarter of 30% or greater growth. Second, we achieved our first quarter of non-GAAP profitability and had adjusted EBITDA of more than $900,000. Third, with the restructuring of our debt agreement, we now have expanded borrowing capacity, a 12-month deferral of principal payments on our term loan and reduced interest rates. The new debt payment structure will defer approximately $6.5 million of principal payments over the next 12 months. And lastly, we continue to demonstrate leverage in our operating model and expect over the near-term that an incremental dollar in revenue will add approximately $0.40 to the bottom line.

So with that, we will open the call to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will be coming from the line of Gary Mobley from Benchmark.

Gary Wade Mobley - *The Benchmark Company, LLC, Research Division - Research Analyst*

Guys, I want to, first of all, congratulate you on some strong performance. You guys deserve it. Good to see it reflected in the share price performance this year.

So I wanted to start out asking about seasonality in the first quarter. Would you expect, based on your current visibility, to see the normal high single-digit percent sequential decrease in revenue typical of any Q1?

Ronald K. Shelton - *Adesto Technologies Corporation - CFO & Secretary*

Yes, hey Gary, it's Ron. Yes, I think -- again in terms of seasonality we expect the consumer segment of our business to, obviously, demonstrate that type of thing; so expect to see a down quarter there. But, half of our business is still in the industrial space, and that's a little less susceptible to seasonality. So I think overall, what you would see is -- you would see that in Q1, and I think at this point, we are not giving guidance, detailed guidance on Q1. But those are the dynamics, right? So little less on industrial and down on the consumer space. So having said that, we certainly expect strong year-over-year growth relative to '17.

Gary Wade Mobley - *The Benchmark Company, LLC, Research Division - Research Analyst*

Sure. So seeing 36% year-over-year revenue growth, the skeptic in me wants to know if this is sustainable? I'm just curious if you have a handle on your customer's inventory levels. Is there any motivation for them to increase the days of their inventory held based on maybe some extended production lead times from your foundry partners, and as well would you I guess, quantify contributors to the growth? Is it all a function of design wins coming to fruition? How much of it is being driven by a buoyant pricing environment for NOR flash? And I can just stop there and let you answer.

Ronald K. Shelton - *Adesto Technologies Corporation - CFO & Secretary*

Yes. Hi Gary. I'll touch on the inventory question and then I'll let Narbeh add a little more color on the where growth's coming from. So with regards to inventory, I think in this environment people may be concerned about customers buying and stocking inventory. And actually, what we've seen at least for our products and product lines is we're seeing turns in our distribution channel increasing. So there's no stocking there. I mean it's moving through the channel. We're not seeing any inventory whether it's at distributors or our customers that's building up. So we feel pretty good about that. I think in terms of pricing, we are really not benefiting. Again, it's -- we are generally not a commodity flash player and don't compete with those guys. I think our business model is a little different.

So we don't feel the fluctuations, both up or down, relative to commodity NOR pricing. So we're not seeing a revenue kick from that at all. I think all the revenues are from our new products, new customers and market demand.

Narbeh Derhacobian - *Adesto Technologies Corporation - Co-Founder, President, CEO & Director*

And Gary, just to add to that. As we indicated in the past, because the way -- because unlike commodity, our opportunities now are very much design-win oriented. Basically if you think about it most of the growth coming from design wins has been accumulated in the past. The price has been negotiated on those. So we're not seeing any impact on that. We're actually seeing very tangible unit growth very similar to revenue growth that you are seeing year-over-year. Although, favorable pricing as we indicated that has occurred recently and tends to be continuing in pockets into 2018. We are taking advantage of that going forward as new contracts, new design wins are being negotiated with some customers. But what we're genuinely seeing here is good old-fashioned unit growth coupled with pushing the top line and maintaining the gross margin basically for the company.

Operator

Our next question comes from the line of Robert Mertens from Needham & Company.

Robert Bruce Mertens - *Needham & Company, LLC, Research Division - Research Assoc of Microcontrollers, Analog & Mixed Signal, Consumer IC & Multi-Market & Computing*

Just sort of going back to the last question, I know you have mentioned in the past that you don't see any specific competitors other than maybe these commodity guys and just customers going with the status quo and deciding not to switch over to your better performing memory. Do you see any people or any customers transitioning over to your solutions potentially at a faster rate with current prices being higher or do you think I am reading into it a little too much?

Narbeh Derhacobian - *Adesto Technologies Corporation - Co-Founder, President, CEO & Director*

No, that's actually a trend that we saw already starting when the prices started to firm up a little bit in the commodity, because our value propositions become a lot more attractive to the end-customer as the commodity counterpart of our solutions is not as inexpensive as it used to be a year ago. So you can see that today basically in the design wins which we are securing. And I mentioned also that during the first 9 months of the year, we pretty much doubled all the design wins we have compared to the 9 months of the prior-year. So indeed, it makes the sales job for our team and our reps easier and we are expecting that to fuel the growth in the future for the company.

Robert Bruce Mertens - *Needham & Company, LLC, Research Division - Research Assoc of Microcontrollers, Analog & Mixed Signal, Consumer IC & Multi-Market & Computing*

And just another follow-up in terms of your design wins, so you're still seeing the trend towards wins going into higher levels in your revenue potential that we have seen in the last couple of quarters?

Narbeh Derhacobian - *Adesto Technologies Corporation - Co-Founder, President, CEO & Director*

The number is trending up, but what we are seeing is it's not -- we are still not in a mode where we have a design win that in a step function of that kind of in a pareto fashion where it becomes very visible; this in a sense is good for us because again, we're not -- it removes the sort of the customers concentration from us. But what we are seeing is, what I touched upon is that we are getting more engagement with Tier 1 high-volume OEMs. I indicated those 2 Fortune 50 companies that we are engaged in. What's interesting is that our engagement, we use the Standard Serial Flash to enter discussions and open the door to become a certified supplier to the customer. But then within those customers, we see a lot more opportunities for different design wins within a particular customer with our other products. So again, if you look at customer concentration we may see some of these new design wins to be high, but the actual design win concentration is not there because they're in completely different applications with some of these Tier 1 OEMs.

Robert Bruce Mertens - *Needham & Company, LLC, Research Division - Research Assoc of Microcontrollers, Analog & Mixed Signal, Consumer IC & Multi-Market & Computing*

And just 1 more before I step back in the queue. In terms of your OpEx going forward, you haven't guided anything out as far as 2018 or anything, but just how should we think about the breakdown with R&D, with new products ramping, do you expect any uptick in that with the designs more in the first half of 2018?

Ronald K. Shelton - *Adesto Technologies Corporation - CFO & Secretary*

No. I think R&D, if you think about new products coming to market that we've been introducing in some of the new families, for example, EcoXiP and the Mavriq. I think the R&D for those types of products are already done, right? So I think R&D -- the relationships you've seen between R&D and SG&A going forward won't change. And again, I think the thing to focus on is what we've been talking about for the last year or so is that we have a strong belief and leverage in this operating model and that's what's starting to show up right now.

Operator

(Operator Instructions) And at this time, I'm not showing any further questions on the phone line. And I would like to turn the call back over to Mr. Derhacobian for any closing comments.

Narbeh Derhacobian - *Adesto Technologies Corporation - Co-Founder, President, CEO & Director*

Thank you. Thank you all for joining us today. Before I conclude today's call, I'd like to let everyone know that we will be attending at the LD Micro Conference in Los Angeles on December 6, and the Benchmark Micro Cap conference in Chicago on December 14. If you would like to request a meeting, please contact your sales rep at respective firms or the Shelton Group. We appreciate your time and look forward to providing an update on our next earnings call. Have a good evening, everyone. Thank you.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program and you may all disconnect. Everyone, have a great day.