

THOMSON REUTERS STREETEVENETS

# EDITED TRANSCRIPT

IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

EVENT DATE/TIME: NOVEMBER 05, 2019 / 10:00PM GMT



NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

## CORPORATE PARTICIPANTS

**Joel Achramowicz** Shelton Group - Managing Director

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

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

## CONFERENCE CALL PARTICIPANTS

**Aman Raj Gulani** B. Riley FBR, Inc., Research Division - Associate Analyst

**Anthony Stoss**

**David Neil Williams** Loop Capital Markets LLC, Research Division - VP

**Karl Fredrick Ackerman** Cowen and Company, LLC, Research Division - Director & Senior Research Analyst

**Michael Walkley**

**Rajvindra S. Gill** Needham & Company, LLC, Research Division - Senior Analyst

**Sujeeva Desilva** Roth Capital Partners, LLC, Research Division - Senior Research Analyst

## PRESENTATION

### Operator

Good afternoon, and welcome to the Adesto Technologies Third Quarter 2019 Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded today, November 5, 2019. I would now like to turn the call over to Joel Achramowicz of Shelton Group Investor Relations. Joel, please go ahead.

### Joel Achramowicz - Shelton Group - Managing Director

Thank you, Operator. Good afternoon everyone, and welcome to Adesto Technologies Third Quarter 2019 Earnings Conference Call. I'm Joel Achramowicz, Managing Director at Shelton Group, Adesto's Investor Relations firm. Joining me today are Narbeh Derhacobian, Adesto's President and CEO; as well as 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, our 10-K, 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 in the Investor Relations section of Adesto's website at [www.AdestoTech.com](http://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, it's my pleasure to turn the call over to Adesto's President and CEO, Narbeh Derhacobian. Narbeh.



## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

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

Thank you, Joel. Welcome everyone, and thank you for joining us today. We achieved another quarter of solid execution setting new records for revenue, gross margin and adjusted EBITDA, in addition to achieving non-GAAP profitability.

Revenue of \$32 million increased 6% sequentially and 46% year-over-year. For the first 9 months of 2019, revenue was up 63% from the same period last year, reflecting continuous growth across the business.

Looking at our third quarter revenue in more detail, our top 20 customers represented approximately 62% of total revenue with the remaining 38% of revenue distributed across the rest of our thousands of end customers.

In terms of end market segments, revenue from consumer and computing segment increased to 53% of the total revenue. This increase was primarily driven by a new touch controller ASIC project for a cutting-edge sensing technology, combined with ongoing success of our memory products with our large Tier 1 customer.

The industrial segment represented approximately 39% of total revenue for the quarter, and the remaining 8% was spread across communications, medical and other end markets.

As we have indicated in the past, we continue to expect that the industrial segment will represent approximately 50% of total revenue over time. But on a quarter-to-quarter basis, the end market percentages may fluctuate depending on the ramping of projects with respective customers.

It is important to note that even with the increase in the consumer segment contribution to our overall revenue base, we were still able to achieve record gross margin above 50% as we continue to execute toward our long-term target model of 50% to 55%, reflecting recognition of value proposition of our diverse solutions across different businesses.

Now, to review some recent developments in our business. Starting with the industrial segment, while we saw some demand softness towards the end of the quarter in Europe related to macroeconomic factors and trade tensions, this market is and will remain a long-term growth driver for us as it continues to offer significant upside potential for Adesto as we help our customers address the challenges inherent in transitioning to Industry 4.0.

Our customers require smart, efficient IoT edge devices and gateways to connect their disparate systems and access their data so that they can take advantage of increased efficiencies and cloud analytics. Our FT 6050 smart transceiver and the SmartServer IoT fulfill these needs, and we are seeing growing interest for these products as we continue to expand sample and production deliveries.

Our FT 6050 smart transceiver SOC combines support for the popular LON and BACnet industrial protocols in a single IC that is ideal for complex integration projects where multiple protocols are present in industrial and building networks.

We are seeing rapid growth in the number of FT 6000 family product shipments that started in Q1, continued in Q2 and into Q3. Customer applications include HVAC control, indoor lighting control, transportation and fuel pump monitoring systems. We are also seeing strong traction with our SmartServer IoT which became available in Q2 when we started to ship to selected customers. In Q3, we shipped three times as many units as compared to Q2 and the growth trend is continuing in the current quarter. As we continue to add more capability to the hardware itself via the scheduled software releases, the market opportunity for this product will continue to see further expansion.

As I mentioned last quarter, our go-to-market approach for our SmartServer IoT edge server consists of two main approaches: first, transitioning existing customers who in the past have used Echelon's old server; and second, engaging with new customers in new markets using a variety of partners.

In the past quarter, we managed to expand our partner network and indirect sales channels substantially. In particular, our recent certification as an authorized Microsoft Azure partner ensures that our customer solutions based on our SmartServer IoT will be compatible with Azure-based cloud application systems and vendors.

## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

A large number of potential customers are looking at Microsoft Azure as their cloud provider. This arrangement gives our customers added confidence that they can get their IoT development projects up and running quickly with pretested and verified interoperable solutions.

And to further extend our market reach, we began a soft rollout of our new Adesto SmartServer IoT Partner Program, targeting industrial IoT system integrators, resellers and distributors. We've signed the first partner and are having numerous engagements with others focused on Smart Building, Smart City and Industrial applications.

In Q3 we continued to see strong demand for our memory products in the industrial segment. Roughly half of our memory design wins in the quarter was in the industrial segment. Key applications as always included energy metering, access controls, and broad industrial control systems, among others.

Also as we ended the third quarter -- we achieved another milestone as one of our new FusionHD design wins in the industrial segment started to move into production.

Our ASIC program pipeline continues to grow within the industrial segment due to the active engagement of our network of reps and regional sales teams who are now fully trained to spot and source opportunities. Notable industrial programs in the pipeline for new ASIC opportunities include a second-generation valve controller with an existing customer; an electrical vehicle charging ASIC opportunity; as well as an ASIC for industrial robotics.

Now, let's turn to our business in the consumer segment. Revenue contribution from this segment was stronger than usual in Q3 as compared to our historical trends. This was primarily due to two factors. First, we successfully closed the new ASIC project that I mentioned earlier. This program is a touch controller ASIC for human-machine interface application. This project offers significant up-front NRE revenue to Adesto as well as potential for multi-million-unit per year recurring revenue and ultimately ramping to production.

The second revenue driver in the consumer segment during Q3 was due to successful ramp of our memory products at our large Tier 1 customer.

We also sampled the 128-megabit EcoXiP product in a new smartwatch application with a new Tier 1 customer. Other applications driving revenue in this segment included Bluetooth remote controls and Bluetooth-connected asset trackers.

Finally, I'd like to discuss recent opportunities within the communications market for Adesto. As I indicated in our last quarter, one of our major satellite customers placed pre-production orders in Q3 for the custom ASIC and has already placed production orders for the ASIC units in the fourth quarter. Additionally, another active ASIC project with a different customer in the satellite communications space is on track for production start late in 2020. Finally, during Q3 we also received first ASIC unit orders from our customer in the cellular market, the broadband-to-the-home application, for a pre-production build. We believe this customer will start ramping in 2020.

In short, we are seeing the initial stages of production unit orders for the completed ASIC projects validating our model of recurring revenue that will continue to grow as we complete our ASIC projects and deliver to customers.

Early in October we also announced funding from the European Space Agency that will subsidize our internal efforts to develop a new analog-to-digital converter technology directly applicable to our customers and end markets. In the past, such funding has led to generation of key technologies directly relevant to new ASIC builds with our targeted customer base. We expect this new project to do the same.

Now, before I conclude, I would like to point out another milestone for the company. This past September, we announced that we have shipped more than 1 billion non-volatile memory devices to customers around the world. Today our broad products can be found in smart meters, building automation systems, wearables, asset trackers, glucose monitors, and a host of other connected intelligent devices. As we close 2019 the opportunities we're pursuing across a diverse set of end markets put us in a unique position to be a critical player in the IoT transformation that's taking shape in virtually every industry.

## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

As indicated by our fourth quarter guidance, we expect continued strong growth in revenue of approximately 20% year-over-year at the midpoint and sustained gross margins above 50% which should result in increased profitability as we close the year.

Notably, this is being achieved in what is otherwise an overall challenging market environment, representing strong testament to our team's solid execution.

With that, let me now turn the call over to Ron Shelton to review our third quarter financial results and fourth quarter guidance in more detail. Then we'll open the call for your questions. Ron.

---

### **Ronald K. Shelton** - Adesto Technologies Corporation - CFO

Thanks, Narbeh, and thanks to everyone for joining us today.

As part of my financial review, I'll focus my discussion on non-GAAP financial results and refer you to today's press release for a detailed description of our GAAP results as well as a reconciliation of GAAP to non-GAAP financial results.

The non-GAAP adjustments relate to stock-based comp, purchase accounting adjustments, earnout adjustments, debt amortization and restructuring and other charges.

As Narbeh indicated, we're pleased today to announce record revenue, gross margins and profitability as we continue to make substantial progress toward our long-term financial model that we outlined in our analyst day in March of this year.

Revenue for the third quarter was a record \$32.0 million, increasing 46% over the \$21.9 million in the third quarter of 2018 and up 6.2% sequentially as we continue to generate strong demand for our products across all solution groups and target end markets.

Non-GAAP gross margin expanded in the third quarter to a record 51%, an increase of 530 basis points from 45.7% in the third quarter of 2018 and an increase of 290 basis points from 48.1% in the prior quarter. The significant margin expansion both sequentially and year-over-year reflects the continued benefit from the continued focus on higher-margin products in end markets.

Non-GAAP operating expenses in the third quarter of 2019 were \$14.3 million, that's compared to \$10.2 million during the third quarter of 2018 and \$14.3 million in the prior quarter. As we've noted in the past, our ability to remain disciplined in our spending while continuing to grow revenue has generated significant leverage in our operating model. We will continue to make investments that deliver high ROI and enhance shareholder value. As we've stated previously, our revenue growth will continue to exceed that of operating expenses, thus contributing to continued long-term expansion of our non-GAAP profitability and adjusted EBITDA.

Total other expense in the third quarter is \$5.8 million, almost entirely consisting of interest expense and debt amortization costs related to our recent convertible debt offering and the payoff of a prior term loan. With our new financing in place, we expect interest expense to be approximately \$1 million per quarter going forward, of which \$855,000 would represent cash interest.

On a non-GAAP basis, we achieved profitability and recorded non-GAAP net income of a record \$1.0 million or \$0.03 per diluted share. This compares to a net loss of \$1.2 million or \$0.04 per share in the third quarter of 2018 and net loss of \$0.7 million or \$0.03 per share in the prior quarter.

Non-GAAP adjustments to net income in the third quarter include \$1.8 million of amortization of intangible assets, \$1.6 million of stock-based comp and \$5.1 million of debt amortization cost. Adjusted EBITDA for the quarter was a record \$3.1 million, or 9.7% of revenue, compared to \$0.5 million in the third quarter of 2018 and \$0.9 million in the prior quarter.

For the third quarter of 2019, our fully diluted share count was 32.4 million shares.

## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

Turning to the balance sheet, we ended the quarter with cash, cash equivalents, investments and restricted cash at \$37.7 million compared to \$7.7 million last quarter. The significant increase reflects our successful offering of convertible debentures that we completed in September, and carry a coupon of 4.25% maturing in September of 2024.

The offering generated net proceeds of \$77.3 million, of which we used approximately \$35 million to pay down our prior term debt. By doing so, we decreased the cash flow associated with servicing our debt by approximately \$2.5 million through the end of 2020.

With the higher levels of liquidity and lower cost of debt, we feel we've significantly strengthened the balance sheet relative to where it was just a couple of months ago, providing us with much greater flexibility to not only make the appropriate investments to drive shareholder value, but also to be opportunistic should strategic opportunities arise.

Net inventory ended the quarter at \$16.3 million, which resulted in an inventory turn of greater than our corporate target of four times, and net accounts receivable was \$33.9 million.

Capital expenditures were \$1.2 million for the quarter and depreciation and amortization was \$0.9 million.

Now, let me turn to the guidance for the fourth quarter of 2019. We expect revenue to increase to a range of \$32.0 million to \$35.0 million, which at the midpoint represents growth of 4.6 sequentially and almost 20% year-over-year. This guidance also puts us on track for second half revenue to grow more than 30% compared to the same period last year.

Non-GAAP gross margin for the fourth quarter is expected to range between 50% and 52% and non-GAAP operating expenses are expected to range between \$14.5 million and \$15.5 million. Stock-based comp in the fourth quarter will be approximately \$1.7 million. Amortization of intangible assets will be approximately \$1.8 million. And depreciation and amortization will be approximately \$1 million.

Interest expenses are expected to be approximately \$1.1 million, and weighted average shares outstanding are anticipated to be 30.3 million shares.

Lastly, in my closing comments, I'd like to reiterate a few of the highlights we've just discussed on today's call. We continue to make significant progress towards the long-term financial model targets that we set in our analyst day in March of 2019, and which we believe will drive long-term sustained shareholder value. They include targeted revenue growth rates of 20% annually, which is a growth rate well in excess of the industry in general, and especially notable in this environment. We've obtained this growth rate this quarter and it's in line with our guidance for the fourth quarter of 2019.

We've targeted long-term gross margins ranging between 50% to 55%. We reported 51% this quarter and have guided to remain in that range, demonstrating that our target end markets and new products are aligned with our long-term business model.

We've targeted operating expenses to range between 30% and 35% of revenue, just as here we've seen them decline from 51% of revenue in the first quarter of 2019 to slightly under 45% in the most recent quarter and expect them to continue to trend in a positive direction.

We achieved adjusted EBITDA margins of nearly 10% in the third quarter -- that's significant progress from break-even in the first quarter of 2019 and 3% of revenue in the second quarter of 2019, which is a direct result of increasing revenues, higher gross margins, and disciplined spending.

And lastly, we have the capital structure in place and a strengthened balance sheet to further support our growth objectives going forward.

With that, we'll open the call to questions.

NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Your first question comes from Karl Ackerman with Cowen.

---

**Karl Fredrick Ackerman** - Cowen and Company, LLC, Research Division - Director & Senior Research Analyst

Two questions, please, if I may. You've continued to win new opportunities and expand partnerships for your SmartServer, but as we think about your opportunity over the next 12 to 24 months, what portion of your installed base of Echelon customers do you think have an opportunity for adopting your SmartServer IoT?

---

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

I think a vast majority of the installed base will convert. Because if I look at the installed base, and I historically look at sort of the purchasing habits of the customer base pre-acquisition of Echelon by Adesto, this was essentially a run rate business on a continuous purchasing of the old server. So what we are doing, and we mentioned that in the last call, is that we are creating a structure for transitioning these customers to the new SmartServer. Some of those customers will be using some basic features of the new SmartServer IoT that they need, but as we roll out new software features with the SmartServer, that opens up even further opportunities with those existing customers. So short answer is, in this market, especially the industrial market, change is very painful. And there's a lot of investment that's been done to bring up existing deployments, so we expect the vast majority of those existing customers to switch over.

---

**Karl Fredrick Ackerman** - Cowen and Company, LLC, Research Division - Director & Senior Research Analyst

That's helpful. Just to focus on margins, your margin outlook has held up very well I think, despite some industry softness in memory certainly relative to some of your peers. I know you spoke about focusing on some of the higher density applications within not just NOR, but some of these other niche forms of memory. So I guess how do I think about your margin structure over the next couple quarters? Have you seen a softness in NOR pricing today? Do you expect that to normalize over the next couple quarters? Just any additional color you may provide on just the memory aspect of your business, because I think margins have held up quite well despite some of the softness in the industry and from peers. Thanks.

---

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

Yes, so if you go back 6 months or 9 months, I think you also indicated that we started to see some softness in NOR pricing. We've always said that we're not that immune to that, as compared to the typical commodity NOR suppliers. But nevertheless, it does affect, the overall pricing comes down in terms of us winning new business. But what we are seeing, and I think if you actually do look at some of the recent reporting by Winbond, Macronix, and also Giga Device in China, although they're focused on the commodity side, that we are seeing two things. One is that the NOR pricing is definitely stabilizing and also in terms of on the supply side, the fab capacity of some of these NOR suppliers that have their own fabs that they're talking about tightness on the wafer capacity as well. So I think we've turned the corner, probably sometime in Q3 and my expectation is that the prices for NOR in general will firm up as we enter 2019. Sorry, 2020.

---

### Operator

And your next question comes from Raji Gill with Needham.

## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

**Rajvindra S. Gill** - Needham & Company, LLC, Research Division - Senior Analyst

A question, Narbeh, on the ASIC business. You had mentioned that within industrial, ASIC is growing and you have some new products, particularly on EVs as well as ASICs for robotics. I was wondering if you could kind of break out, number one, within industrial, what percentage is ASIC versus non-ASIC? And you highlighted some demand softness in Europe due to macro and trade issues. Could you be more specific regarding that? Was this, you know, specific kind of customers that you saw slow down, was it due to uncertainty in terms of building new parts? Any clarity on the overall softness in industrial Europe would be helpful as well.

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

Sure. So let me first clarify a comment on the ASIC pipeline. So what I indicated about the opportunities in the industrial segment for the ASIC, it refers to the pipeline. So ASIC, we typically spend time with the end customers to close an ASIC deal, and once the ASIC deal is closed, as you know there's an NRE involved and then there's a back end of the unit revenue. So when I specifically talked about the industrial opportunities that we're sourcing in our ASIC group, it has to do with the pipeline. So one is with an existing industrial customer. I think you know what that -- who that customer is. It's in the industrial control for valve control applications. We're already supplying an ASIC to that customer from previous activity, but they are looking at a second opportunity within that customer. And then the other two, the electrical vehicle as well as the robotics, are brand new opportunities that haven't closed yet but we're working on -- in the pipeline to close. But it basically indicates that our sales channels that opened up to the S3 Semiconductors group, has expanded their footprint in this area. So if I look at the other question is, what percent of our industrial revenue is coming from our ASIC business today. It's a small percentage. It's definitely not a major percentage of that. In terms of softness -- so the softness, what we saw was basically towards the end of the quarter, we saw this broad softness within the industrial base as indicated by some of our end distributors who served there as well as some of the customers. And it's not -- you know, it was not concentrated in one region necessarily within Europe, but it was definitely EMEA-centric. We think there's two things that happened there, as it's specific to us. One is, as we are transitioning the customers from the old FT family to the new FT 6000 family, as well as the old server to the new server, with some adjustments on the pricing that we implemented. And the overall macroeconomic issues that they were experiencing in Europe. It basically had, toward the end of the quarter we saw a slight softness that happened. But we believe that those are temporary as it's indicated in terms of the traction we have entering Q4 and into the market.

**Rajvindra S. Gill** - Needham & Company, LLC, Research Division - Senior Analyst

And Ron, your long-term gross margin target of 50% to 55%, you're at 51%. I know there's not a time frame or a specific time frame, but as we go into next year, going from 51% even though you had a lot of consumer last quarter as well, it seems like there's a lot of tailwinds for that 51% to go higher. What will be the bridge, say, from 51% to 52%, 53%, over the next several quarters? Is this going to be a continuation of a higher mix of industrial, so you're going to wait for a higher mix shift? Or is it also going to be helped by some sort of stabilization of NOR pricing? Is there anything on the back end, test assembly, that you also can do to help bridge that gap from 51% to 52%, 53%, 54%?

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

Yes, sure. So it's a good question. As we look out over the year, Narbeh touched on NOR pricing. So I think some stability there is helpful. I think we do see some cost reductions coming on the memory side that'll be helpful. On the kind of industrial and ASIC side, when you think of, we've talked about recurring revenue models. We'll start to see some of that kick in next year. And then as the ASIC business continues to expand, as you know, that's just generally higher margins. So I think you have a mix shift. You have some recurring revenue models. You have some price stability. And you have little cost reductions. It's really a combination of all of that. It's certainly not a step function, so it's not as if you're going to see 49% last quarter, 51% this quarter and 53% next. It won't be like that. We've guided flattish in Q4 and I think that's the right place to be.

**Operator**

Your next question comes from the line of Mike Walkley from Canaccord Genuity.

---

**NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call**


---

**Michael Walkley**

Just building on an earlier question about Echelon, it's great to hear you expect the vast majority to switch over to the new server product. Can you help us maybe think about how to quantify that opportunity, and what do you think the time frame is for that base to switch over?

---

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

So if you actually look at the timeframe, so the timeframe is going to be measured in multiple quarters. So expectation, again, is that as we roll into 2020 and assuming that the customers are following the same sort of buying habits as they are going forward, I think I indicated in the last earnings call is that the total value expected is north of \$2 million over the next 12 months that -- from a dollar perspective, that we'll be doing the switchover. Just to give you an example, you know, if I look at the SmartServer as we have it today -- and again as I indicated, as we roll out more software features with the pre-planned rollout of the releases of the software -- that universe of the unit opportunities is going to expand because we are adding more features, more capabilities with every new release. And we do that on a regular basis every couple of months.

So as I look at it here today based on sort of the pipeline that I'm looking at, like I indicated last quarter, it's going to be on a revenue basis, will be over [\$2 million] (corrected by company after the call) over the next 12 months.

---

**Michael Walkley**

A follow-up question for Ron. The operating expenses, you guys continue to do a good job managing those. You guided up a little bit sequentially. Are there areas you need to invest to continue to grow the business, and if so, where are you guys investing? But it does sound like you do expect revenue next year to grow faster than OpEx. Just want to clarify that.

---

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

Yes. Sure. So exactly, we will run the business and we I think have been pretty consistent about this over the last year, year and a half, about making sure the top line is growing faster than expenses. But in terms of where we would invest, we would invest -- when you think about the embedded business, you think about getting out recurring revenue streams, new markets, or new products, new features on those products. And you can seek some investment there both on the development and sales and marketing side. On the ASIC side, we've talked about that business model and head counts or capacity. And so you could see additional investment there. But I would caution, we talked about this before. Those design centers are all in Europe and it's a very effective and efficient cost structure there. But yes, you would see investments in areas like that.

---

**Operator**

Your next question comes from Anthony Stoss with Craig Hallum.

---

**Anthony Stoss**

Just a follow-up on the industrial weakness. If it was in line with what you expected it to be in the quarter, how much more in revenue or what's the delta between that and what it was -- what it ended up being. Secondly, the midpoint of your revenue guide is up sequentially a little bit. Can you give us a sense of what segments you expect to be up and what to be down? And then lastly, love to hear more on your design traction on the consumer side for memory, and what you see on ASPs going forward there based on the designs you've won.

---



## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

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

Let me talk about the industrial spend. Again, it's -- you know, there was some like, Narbeh talked about a little bit of weakness in EMEA. But again, in terms of absolute dollars, it's not a huge amount of dollars. I mean, I think we reported record of \$32 million and you know, we guided a midpoint last quarter of \$33 million. So it's not a huge impact but we saw it at the end of the quarter so it's not significant. I'm trying to remember your second question, here.

---

**Anthony Stoss**

What segments do you expect to be up or down sequentially in Q4?

---

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

I think in terms of end market, consumer industrial, those segments.

---

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

We probably expect Q4 to be similar to Q3, so we don't expect much change in terms of the revenue contribution from the different segments. And your other question was about NOR pricing, right, the memory pricing. So like I said in the earlier question, we are seeing -- I think we went through price pressures about 6, 9 months ago on NOR. I think it was widely reported by other commodity suppliers in the same space what we are seeing and what we saw with some of our main competitors reporting in the last month. That seems to have stabilized itself out. So we're not expecting price erosion as we're entering 2020 for sure. So that should bode well for us on the memory pricing side.

---

**Anthony Stoss**

As a follow-up, what I'm trying to get at is the design traction you guys have for your specialty NOR where you're going to see higher ASPs. Any commentary regarding that?

---

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

Yes. So if I look at the specialty NOR opportunities, so if I look at it by product family we have EcoXiP and FusionHD. So we have, as I indicated in the past, design wins with our EcoXiP products, and we were expecting that customer to ramp in Q4 but I think some of you may triangulate to see who that customer is. And they were in the recent news in terms of some strategic engagements that they had. So we don't know -- right now we need to get an update as to where they want to -- you know, that ramp was supposed to be in 2020. So we have to take a look at where that particular design is heading for them. I did report that we have a new opportunity with a smartwatch application in a new Tier 1 customer that we haven't had before, for 128-megabit EcoXiP so that's an opportunity for us in late 2020, in that case. And then the good news was for us that our other new product family, FusionHD, we started to get the production orders within the industrial segment in that case. The first production orders for the FusionHD which also carries a higher gross margin than the commodity prices. In the rest of the memory business, if I look at it again, the old sort of, our DataFlash, our Fusion family, that has broad set of customers especially within the industrial segment. I indicated new wins with our existing customer base in smart meter applications. New wins with existing customers in remote controls, Bluetooth remote controls and asset trackers. So all those are going to start to go into production in 2020.

---

**Operator**

Your next question comes from Sujeeva Desilva with Roth Capital.



## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

**Sujeeva Desilva** - Roth Capital Partners, LLC, Research Division - Senior Research Analyst

So on the S3 business, the ASIC business, can you talk about how many customers you're now shipping units for, or by the end of '19? And then middle of '20 or end of '20 can you talk about how that progresses, how many customers will be actually shipping unit chips for you guys?

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

Yes. So if I look today, we are shipping to two customers. One is industrial control; one is in the satellite comm market. We started to ship pre-production products to the cellular customer that I indicated, this is broadband to the home. This is pre-production, so essentially they're doing a pre-build before the ramp. So my expectation, again, is for that to go into pre-production probably in 2020. And then we have one more satellite customer that we have delivered the ASIC already, so we've done our job. And they're going through their own qualifications. That expectation, again, is for late 2020 for ramp. The new ASIC opportunity that I talked about in the consumer space is just starting, so that one is a 2021 event from a unit perspective. But of course we carry the up-front NRE revenue. So I think in the past, I had talked about sort of if I look at -- if you look at everything we have in the pipeline and you assume all those going to production, what is the annual volume, average annual volume if you think about it. So if you remember in the past, I said that was roughly half a million units per year at \$6 ASP. So if I look at -- so you multiply half a million to -- by I think we had \$6 at the time, until you get -- yes. You get a number in terms of the annual revenue run rate. So today, what I can tell you is that our average annual volume is around 1.1 million. Of course some are, some is the newer customers, that will be late in 2020 with average ASP of \$5, \$5.60. So if you actually do the math, with seven opportunities at that volume, at \$5 million. So that pipeline is more than doubled since the last earning call in terms of recurring unit revenue. But today, we're at the tip of that iceberg in terms of the actual realization. Yes.

**Sujeeva Desilva** - Roth Capital Partners, LLC, Research Division - Senior Research Analyst

Exciting progress. And then on the memory side, you talked about one of the customers potentially going through an acquisition and all that. But how many projects like that, the EcoXiP wearable customer, the large Tier 1 consumer customer you have. How many of those kind of memory customers do you have or will you kind of start having in the next couple of quarters? Is it two or three, or is it more than that?

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

No. So if I look at the same time last year compared to this year, right -- if I just look at our new memory product which includes EcoXiP and FusionHD, right. So last year, at this time we had roughly 21 opportunities we were pursuing at different stages of engagement, design phase, design-ins, design sampling and so forth. So today, that number is 67. So it's definitely expanding.

**Sujeeva Desilva** - Roth Capital Partners, LLC, Research Division - Senior Research Analyst

Fantastic. And the last question on the recent funding, just can you remind us the use of proceeds? Is it inorganic still a near-term priority, and what's the -- you gave us the gross margin target. What's the adjusted EBITDA margin target you guys would do with the OpEx and gross margin where you lay them out?

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

So I think in terms of margins and EBITDA margins, if you look at this quarter, you're right around 10%, right. And we talked about a goal of 10% in the second half, so we're right there. So I think that you know, the way I think about the model is \$32 million in revenue, right around there, gets you to about 10% EBITDA margins. And as you grow from there, I think about incremental revenue dollars, given where we go with OpEx, maybe adding \$0.35, \$0.40 to the bottom line. So that'll give you a sense for how EBITDA can scale going forward. I think with respect to use of proceeds, the test is on the balance sheet today, it's something we've talked about in the past. And we feel really good about the balance sheet. And we would be opportunistic like we were last year. But again -- anything we look at, we've laid out a long-term model. And again, it's revenue growth

NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

rates of 20% annually. Its' margins of 50%, 55%. And the path to get to EBITDA margins of 20%-plus. And if it doesn't feed into that, then it likely wouldn't clear a hurdle that we would have internally to pull the trigger. So we're pretty selective.

**Operator**

(Operator Instructions) Your next question comes from Aman Gulani with B. Riley FBR.

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

Nice to see the lifted margins. Just going back on that question about use of proceeds, I mean, how does the M&A pipeline look now? Are you a little bit more active when it comes to acquisitions?

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

I guess I would characterize it this way. Since we did the two transactions last year, I think we executed really well and integrated well. I think the market understands that we're able, if we commit to doing something, that we'll do it and get it done. We see a lot of inbound activity. So we have a process internally. We've had a process internally for the last couple years, to review opportunities that might look interesting. So I would say we see more now than we did two years ago. And again, we're very discriminating in terms of what we would look at seriously. So that --

(technical difficulty)

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

(technical difficulty) Thank you. I guess turning to memory product mix, I know previously I think maybe last year you talked about 60%, 70% data flash, 10% in the standard product. How does that mix look now, now that you have new products within your memory business? How does that mix look like now? (technical difficulty)

**Operator**

One moment. The speakers are reconnected.

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

Aman, did you get the answer?

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

I think it cut out before I got that answer.

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

So we were talking about, your question was around pipeline, right, on M&A.



## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

Yes. How active is the pipeline? I think you answered that question. I don't know if you heard my next question.

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

No, we didn't. No.

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

Okay. It was about the memory product mix. I think last year, you talked about the memory product mix being about 60% to 70% data flash and 10% standard serial flash. How does that mix look now, now that you have these new products in there?

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

Well again, I would say that if I look at the new product, EcoXiP and Fusion, they're just in the early stages of their sort of ramping up, right. So today, I would say from a revenue perspective, again, probably the combination of the -- the contribution from DataFlash has gone down a little bit, just because our standard flash product our Tier 1 customer has been ramping over the last, especially over the last quarter and a half. But again, it's important to note that even at that point, with that sort of a mix of the products and end markets for us, we still continue to see the gross margin expansion. So we -- all the -- you know, we do manage the business in a way that's trying to target the gross margin and the growth rate at the right place that we want it to be. And so to that extent, the mix and shift will occur within the end markets we serve, and we think the product families of the different divisions.

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

And just the last question from me, how should we think about the growth rate across your three divisions going into the fourth quarter, and then also into next year?

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

I wouldn't look at it as individually, at the division level. I think we guided the overall business to [\$32 to \$35] (corrected by company after the call), about 20% year-over-year at the midpoint. The expectation is that we'll see growth in the different segments. But with respect to any one business unit or something else, I mean, that's not how we see that. Certainly that's not necessarily how you want to think about it. I think 20% year-over-year at the midpoint is pretty strong growth, and I think it's coming from -- you know, it's not one area, right. I mean, you'll see it in different areas. And that may change from one quarter to the next. I think if you look at ASIC, Narbeh called out ASIC this quarter. And that was a transaction. A single deal can kind of drive growth in that from one quarter to the next. So try not to look at it at that level and try to focus at the top level. And again, 20% year-over-year at the midpoint. The long-term model is 20% and that's what we're driving to.

**Aman Raj Gulani** - B. Riley FBR, Inc., Research Division - Associate Analyst

Got it. And just one more question from me. Is it safe to assume that within the ASIC business, it's completely all NRE revenue?

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

Mostly, yes.

## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

### Operator

Your next question comes from David Williams with Loop Capital.

**David Neil Williams** - Loop Capital Markets LLC, Research Division - VP

If we kind of think about the competitive landscape, I wanted to see if maybe you could give us maybe your take on what you're seeing in terms of competition and just thinking about some of the transactions we've seen over the last several quarters in terms of communications being brought into larger-scale companies for the industrial segment. Just how do you think that plays out over time and into your strategy overall?

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

Can you be a little bit specific about the last part of your question in terms of the transactions that you indicated?

**David Neil Williams** - Loop Capital Markets LLC, Research Division - VP

No, I was just mentioning the -- it seems like there's been several transactions to bring in more communications-type product into other companies for specifically within the industrial platform. And just kind of curious if that plays -- how you think about that longer-term, and if that's a competitive disadvantage for you guys.

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

So we play in that space in two areas, including let me first talk about communication in general. And then let me then talk about communication within the industrial segment in particular. So in communication segment in general, our main focus is through our ASIC group and that has to do with satellite communication. So this is primarily driven through applications like cargo tracking, asset management, fleet management sort of applications. So in that respect, our end customers are companies like OrbComm, Iridium, and so forth. And we provide ASICs that goes into these ground modules that then they send to the end customers. Recently we had as I indicated, this one particular ASIC that we delivered to a cellular company that's delivering broadband to the home, so that's a high-volume opportunity, competes in the cellular one. And we've actually -- that's been done. It's an ASIC so we have -- there's no competition there. We sort of won that and delivered it and the customer's in pre-production order. Within the industrial segment, our focus is primarily in wired communication as far as the transceivers are concerned. And this is areas where controlled networks are operating. So this is where machine-to-machine communication is occurring without the human control inside it. So traditionally, this is in the -- behind the walls communicating from sensors, wired communication whether it's twisted pair or ethernet, connecting into a gateway. And then from there it goes out into other, more IP-enabled networks. So in that space, we provide the communication chips that are specifically focused on the LAN protocol and the BACnet protocol which is -- the two together, they are probably 80% of all the building automation protocols that run. And also at the edge gateway level, which is our SmartServer IoT, that sort of aggregates all these connections and then sends the data up into the cloud. Additionally, another area that we do play in is power line communication, sort of the PLC, that's primarily used in smart grid applications, in smart metering applications.

**David Neil Williams** - Loop Capital Markets LLC, Research Division - VP

And just kind of thinking about the revenue synergies and just the distribution channel between the three companies, now that you've had some time to digest and kind of work through that, are you seeing the types of synergies that you would have anticipated early on? And just kind of the progress there.



## NOVEMBER 05, 2019 / 10:00PM, IOTS - Q3 2019 Adesto Technologies Corp Earnings Call

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

Yes. So I would say right now we don't even think ourselves as three separate entities that come together. So as we enter the year and we completed these acquisitions, we really rolled up our sleeves and tried to complete all the synergies. So the vast majority of all the integration has been done. There's a few IP-related things which are really tactical activities in rolling out some new systems and bringing disparate systems together and that's expected to happen as we enter 2020. But it's all going per plan. So from that perspective, let me just say that it doesn't even come to Ron and my attention, at any sort of an operational meeting that we have in the company right now.

**Operator**

There are no further questions. I would now like to hand the conference call back to Narbeh for any closing comments.

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

Thank you. Before closing the call I'd like to let you know that we will be attending two conferences in New York City next week, the Craig Hallum Alpha Select conference on November 12 and the Roth Tech and New Industrials conference on November 13. In December, we'll be attending the Benchmark Discovery Conference on the 4th, also in New York City. If you would like to arrange a meeting with us at any of these events, please contact IR@AdestoTech.com or the Shelton Group. Thank you again for joining us and we look forward to discussing our continued progress on our next earnings call. Operator, you may disconnect now. Thank you.

**Operator**

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

**DISCLAIMER**

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2019, Thomson Reuters. All Rights Reserved.