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MRAM - Q1 2018 Everspin Technologies Inc Earnings Call

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Kevin Edward Cassidy *Stifel, Nicolaus & Company, Incorporated, Research Division - Director*

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PRESENTATION

Operator

Good afternoon, and welcome to Everspin Technologies First Quarter 2018 Financial Results Conference Call. (Operator Instructions)

As a reminder, this conference call is being recorded today, Wednesday May 9, 2018. I would now like to turn the call to Brett Perry of Shelton Group Investor Relations. Brett, please go ahead.

Brett Perry

Good afternoon, and welcome to Everspin Technologies First Quarter 2018 Earnings Conference Call. I'm Brett Perry, Vice President of Shelton Group, Everspin's Investor Relations firm. Joining me today are Kevin Conley, Everspin's President and CEO; and Jeff Winzeler, CFO.

Before we begin the call, I want to remind you that this conference call contains forward-looking statements regarding future events, including but not limited to our expectations for Everspin's future business, financial performance and goals, customer and industry adoption of MRAM technology, successfully bringing to market and manufacturing products in Everspin's design pipeline and executing on its business plan. These forward-looking statements are based on estimates, judgments, current trends and market conditions and involve risks and uncertainties that may cause actual results to differ materially from those contained in the forward-looking statements. We would encourage you to review our SEC filings, including the 2017 Form 10-K filed with the SEC on March 15, 2018, and other SEC filings made from time to time in which we may discuss risk factors associated with investing in Everspin. All forward-looking statements are made as of the date of this call, and except as required by law, we do not intend to update this information.

This conference call will be available for audio replay for at least 90 days in the Investor Relations section of Everspin's website at www.everspin.com.

And now, I'd like to turn the call over to Everspin's President and CEO, Kevin Conley. Kevin, please go ahead.

Kevin Conley - Everspin Technologies, Inc. - CEO, President & Director

Thank you, Brett, and good afternoon, everyone. I'm pleased to report that our first quarter results achieved records in revenue and earnings per share. Revenue in the quarter was a new high of \$14.9 million, including \$5.5 million of licensing royalty and other revenue. Total product revenue grew more than 40% year-over-year with MRAM product revenue increasing 60% year-over-year, demonstrating our continued progress in growing MRAM product sales.

We also enjoyed record gross margin of 67%, driven primarily by the exceptionally strong licensing royalty and other revenue. Included in our licensing revenue in the quarter was the upfront license fee associated with the multiyear agreement signed with Alps Electric at the end of the first quarter.



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Under the agreement, Alps and Everspin mutually granted licenses to magnetoresistive-based 3D sensor patent portfolios for sensor products. This agreement demonstrates our ability to monetize our IP assets and generate an additional revenue stream and source of cash for Everspin.

This cash and subsequent revenue, coupled with the funds raised in last February secondary offering have significantly improved our balance sheet and given us more resources to advance our MRAM initiatives.

On the product side, we delivered strong year-over-year growth, driven primarily through increased Toggle MRAM sales, helped by the increasing shipments of our 256-megabit Spin-Transfer Torque or STT-MRAM product. In terms of STT-MRAM production and shipments, we exited Q1 ahead of our internal plan and expect this trend will continue.

We believe that the investments we're making in our operations team and capabilities will help support continued strengthening of our entire business in the coming quarters. These investments not only will strengthen our own captive back-end fab operations, but also position us better for the coming growth we see in our joint operations with GLOBALFOUNDRIES.

One of the demand drivers behind our results was SMART Modular Technologies who recently completed qualification and has started shipping their nvNITRO accelerator card, which is built using our 256-megabit STT-MRAM devices. This product is the world's first entirely STT-MRAM-based storage product and uses NVMe controller technology that was jointly developed by Everspin and SMART Modular. This is the world's first commercially available product using our STT-MRAM's advanced perpendicular MTJ technology, delivering its low latency and high endurance to demanding transaction logging -- logging applications that require power loss data protection. It also addresses the safety and costly maintenance concerns that exist with legacy power back DRAM solutions that use batteries, capacitors or super caps.

As we look to the second quarter, we approach another significant milestone in the growth of our MRAM business. That milestone is the anticipated completion of product qualification by our lead flash array customer who also uses -- utilizes our 256-megabit STT-MRAM in their product. We expect to be able to make more details public as they complete this critical milestone and are able to formally release their product.

On the sales and marketing front, the focus remains squarely on converting our STT-MRAM opportunities into design ins, followed by design wins and ultimately long-term revenue growth. With the nvNITRO product now available for purchase, we're putting greater focus on joint promotional efforts with Smart Modular. As such, we'll be jointly demonstrating the value of this innovative technology at various trade shows, including The Trading Show in Chicago that is taking place today and tomorrow, May 9 and 10. We are providing live demonstrations at the event, showcasing the performance advantages that we published previously in our FinTech white paper.

And coming in the third quarter, Everspin will be lead sponsor at MRAM Developer Day that will occur on August 6, just prior to this year's premier nonvolatile memory trade show, the Flash Memory Summit. This year's MRAM Developer Day is indicative that MRAM technology has finally reached the forefront of emerging memory technologies, a reality that compel the organizers that put on the Flash Memory Summit to organize this special MRAM technology-focused event. This show is attended by system architects and engineers looking at this latest key enabling technology for the industry, not for a distant future, but for today's market needs.

Having this dedicated business-oriented technology form helps further promote MRAM technology to broader industry influencers, partners and potential customers, and we believe will help us move further into mainstream applications.

I will be serving as lead keynote speaker at the event, where our partner, GLOBALFOUNDRIES, also a lead sponsor with a keynote slot of their own, will promote the progress of our joint development efforts on embedded MRAM. We will host joint product demonstrations using our STT-MRAM along with Smart Modular and another significant STT-MRAM customer at the event. Immediately after the MRAM Developer Day, we will transition our messaging into the broader platform of the Flash Memory Summit from August 7 to 9. There, we will showcase with our partners the performance and reliability benefits that our STT-MRAM technology brings to flash memory based storage systems.

In summary, I'm pleased with the progress we're making on our MRAM products and promotions. Longer term, we see trends evolving that are aligned to the value that MRAM brings. And we are strategically targeting these opportunities as future demand drivers of our MRAM products.

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With that, I'd now like to turn the call over to Jeff Winzeler, our CFO, who will review the details of our first quarter results as well as provide our second quarter 2018 guidance. Jeff?

Jeffrey G. Winzeler - Everspin Technologies, Inc. - CFO & Secretary

Thank you, Kevin, and good afternoon, everyone. I'll start by reviewing the first quarter 2018 income statement. Revenue in the quarter was \$14.9 million with product sales representing 63% of total revenue or \$9.4 million, while licensing royalties and other revenue contributed approximately \$5.5 million in the quarter. Total revenue for the quarter increased both year-over-year from \$7.9 million in the first quarter of 2017, and sequentially when compared to the \$10.1 million in the fourth quarter of 2017.

As a result of adopting the new revenue recognition standard, ACS 606, we are now including our back-end foundry revenues, which under the new standard must be recognized over time in licensing, royalty and other revenues on the income statement.

Last year, we recognized our back-end foundry revenues in product revenue, and they were recognized like Toggle and MRAM revenue on a point-in-time basis. On the Form 10-Q, both historic and current revenues are stated under the new rules, enabling like-for-like comparisons of product revenues as well as licensing, royalty and other revenues.

For our MRAM products in the first quarter, which includes Toggle and STT-MRAM, revenue was \$8.9 million, a 60% increase from the \$5.6 million in the first quarter of 2017 and an 18% increase from the \$7.5 million in the previous quarter.

Gross profit for Q1 2018 was \$10 million, up from \$4.2 million from the same period a year ago and also up from \$6.2 million in the fourth quarter of 2017. The increase in gross profit was primarily attributable to the increase in licensing, royalty and other revenue in the quarter.

As we stated on previous calls, this revenue is variable from quarter-to-quarter and is based on the size and terms of each transaction, and as such, can effect gross profit and margins materially.

Gross margin for Q1 2018 was 67%, an increase from 53.5% in the first quarter of 2017 and 61.5% in the fourth quarter of 2017. Product margin in the first quarter was 50%, or lower than our target product margin of 55%, primarily driven by product mix and manufacturing variances.

Operating expenses for the first quarter 2018 were \$11.1 million compared to \$10.1 million in the first quarter of 2017 and \$10.5 million in the fourth quarter of 2017. Breaking down our operational spending for the first quarter, research and development expenses were \$6.5 million compared to \$6.4 million in the same quarter a year ago and \$6.2 million in the fourth quarter of 2017.

SG&A spending was \$4.6 million in the first quarter compared to \$3.7 million in the first quarter of 2017 and \$4.3 million in the fourth quarter of 2017.

Interest expense for Q1 2018 was \$211,000 compared to \$230,000 in the first quarter of 2017 and \$180,000 in the fourth quarter of 2017.

Other gains and losses was \$44,000 of income in the first quarter of 2018 versus \$19,000 of income in the first quarter of 2017 and \$35,000 of income in the fourth quarter of 2017.

GAAP net loss for Q1 2018 was \$1.3 million or \$0.09 loss per share based on 14.8 million weighted average shares outstanding. This compares with the GAAP net loss of \$6.1 million or \$0.49 loss per share during the same quarter a year ago and a GAAP net loss of \$4.4 million or \$0.35 loss per share in the prior quarter.

Now turning to the balance sheet. Cash and cash equivalents were \$33.9 million at the end of the first quarter of 2018 compared to \$13 million at the end of the fourth quarter of 2017. The increase in cash reflects \$24.5 million in net proceeds we raised in our February 2018 secondary offering, providing us the working capital to ramp our 256-meg STT-MRAM product in the market, while continuing the ongoing development of current and new technologies in support of our MRAM initiatives.



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Total assets at the end of the first quarter were \$57.1 million compared to \$31.4 million at the end of the fourth quarter. Total liabilities were \$20.5 million as compared to \$20.6 million in the fourth quarter of 2017.

Stockholders' equity was \$36.7 million compared to \$10.9 million in the fourth quarter of 2017.

Looking ahead to the second quarter of 2018, we expect revenue to range between \$10.9 million and \$11.3 million. We expect the resulting GAAP loss per share will range between \$0.41 loss per share and \$0.37 loss per share based on an average weighted share count of 16.9 million shares outstanding.

With that, I'd like to turn the call back over to Kevin. Kevin?

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

Thank you, Jeff. I'd like to thank the entire Everspin team that is working incredibly hard on the multiple fronts to deliver these notable results, including both strong year-over-year growth as well as stronger cash position. These efforts move us closer to our vision of MRAM as the future of memory technology and more importantly strengthen the focus on Everspin's mission to drive the MRAM revolution.

Now, we will open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Kevin Cassidy with Stifel.

Kevin Edward Cassidy - *Stifel, Nicolaus & Company, Incorporated, Research Division - Director*

On the guidance for the second quarter, can you say what's happening with gross margin? Is product gross margin coming down as the first production of the STT-MRAM is ramping?

Jeffrey G. Winzeler - *Everspin Technologies, Inc. - CFO & Secretary*

Yes, so Kevin, we don't really give guidance on the gross margin. We did say in our prepared remarks that our Q1 gross margins came in -- product gross margins came in at 50% versus our target of 55% that was due to product mix, and also due to some manufacturing variances that we experienced in the first quarter. It takes a while for that material to work itself through the factory, and so we anticipate that will continue to have some manufacturing variance that bleeds over into the second quarter of the year.

Kevin Edward Cassidy - *Stifel, Nicolaus & Company, Incorporated, Research Division - Director*

Okay. And so there's no change to your long-term target of 53% gross margin -- product gross margin?

Jeffrey G. Winzeler - *Everspin Technologies, Inc. - CFO & Secretary*

Our actual target product gross margin for the company used to be 48% to 52%. We raised that at the beginning of 2018 to 55% or greater. So 55% is kind of our minimum target we're shooting for with regard to the whole product portfolio.

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Kevin Edward Cassidy - *Stifel, Nicolaus & Company, Incorporated, Research Division - Director*

Okay, great. And maybe just one other. It's very interesting that you're holding -- hosting a MRAM Developer Day. Will Everspin be the only provider of MRAMs at the conference, or at that Developer Day? Or are some of your MRAM competitors invited too?

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

So there are variety of companies that participate in the MRAM technology ecosystem. We will be the only company with MRAM components in production to our knowledge that will be participating in the show. All the major foundries who have embedded MRAM programs will be presumably presenting their along with their technology partners, and other companies that are familiar names in the MRAM ecosystem are expected to be there as well.

Operator

(Operator Instructions) Our next question comes from Richard Shannon with Craig-Hallum.

Richard Cutts Shannon - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

Maybe I'll follow-up on Kevin's first question regarding your gross margins. He didn't ask the question directly so I'll do that. Is the product mix for product gross margin in the first quarter. Is that related to STT? Or can you give us a sense of the drivers there?

Jeffrey G. Winzeler - *Everspin Technologies, Inc. - CFO & Secretary*

Yes, so we don't really give that type of guidance. Again, we're -- the primary products coming out of the factory today are still Toggle MRAM products. And as we've explained on calls in the past, within that Toggle product family we have roughly 9 different major products, all at different densities and different margin profiles. So our goal across that product portfolio, including STT-MRAM is to achieve 55% plus product margins. As Spin Torque starts to ramp, as STT-MRAM starts to ramp, clearly it will become a bigger part of that product portfolio, but we're trying to manage it as a portfolio.

Richard Cutts Shannon - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

Okay. Fair enough. I think, also question about the sales guidance for the second quarter here. Any sense you can give us of how much growth is coming from Toggle versus STT? I know you haven't in the past, but I'll just ask a question again, where do you're expecting your licensing revenues in the quarter as well?

Jeffrey G. Winzeler - *Everspin Technologies, Inc. - CFO & Secretary*

Yes, so I'm probably going to give you the same answer I had given you in the past. The licensing stuff truly is so sporadic and variable. At some point in time, we expect that the licenses that we worked on both through our sensor products as well as longer term with GLOBALFOUNDRIES on the embedded MRAM piece, that royalty line will start growing and will start becoming a lot more steady. But in the meantime, the licensing portion of it and the NRE portion of it is very sporadic and pretty opportunistic, I would say. So we really -- it's really difficult for us to give specific guidance on what we think that number is going to be.



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Richard Cutts Shannon - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

Okay. One last question from me for Kevin. I think I heard your comments correctly. But I just wanted to verify regarding the tier-1 flash array customer for the 256. Did you say that you expect that to be qualified this quarter?

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

We do.

Richard Cutts Shannon - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

What gives you that confidence level? And assuming that qualification happens, would you expect to start building inventory or that customer starts building inventory immediately afterwards?

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

I'll take that in 2 parts. The first one is, yes, we work very closely with our top OEM customers that includes sharing details about the development schedules. And so that's what gives us the confidence to comment on the timing of that product. With regard to the inventory, we have talked in a general sense that as customers approach the release of products to market, generally the inventory from us is acquired prior to them building their, let's say building their internal inventory of their finished goods products, right. So we tend to be ahead of that curve in terms of the orders that we receive. I don't know if that directly answers your questions, but I hope it's helpful.

Richard Cutts Shannon - *Craig-Hallum Capital Group LLC, Research Division - Senior Research Analyst*

I guess, Kevin, I was just asking where do you expect to inventory build to happen as soon as the qualification is completed? Or there is some lag there?

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

I see. We expect the products to be once it's qualified to start ramping sales in the subsequent quarters.

Operator

And we have a follow-up question from Kevin Cassidy with Stifel.

Kevin Edward Cassidy - *Stifel, Nicolaus & Company, Incorporated, Research Division - Director*

On the Toggle MRAM products, can you talk about the design win pipeline that you have? You know it seems like the product mix of those and, Jeff, as you pointed out there's 9 different types. On the new designs -- is the pipeline filled with more of the higher end, higher gross margin products? Or is it going to be a mix going forward also?

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

I think it's fair to characterize that as a mix, going forward, Kevin.



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Kevin Edward Cassidy - *Stifel, Nicolaus & Company, Incorporated, Research Division - Director*

Okay, great. And just housekeeping. Jeff, could you repeat again the loss per share estimate for next quarter or that guidance?

Jeffrey G. Winzeler - *Everspin Technologies, Inc. - CFO & Secretary*

Yes, sure. So from a loss per share perspective, we said that it will range between \$0.45 loss per share and \$0.41 loss per share. And the average weighted share count we're projecting to be 16.9 million shares, which is reflective of the secondary offering that we did in February.

Operator

At this time, I'm showing no further questions. I'd like to turn the call back to management for closing remarks.

Kevin Conley - *Everspin Technologies, Inc. - CEO, President & Director*

In closing, I'd like to highlight that Everspin will be participating to the upcoming Cowen TMT conference in New York on May 31, and the Stifel Cross Sector conference in Boston on June 12. Please contact our sales representative at the respective firms or the Shelton Group if you would like to schedule a meeting with us. Thank you for your participation on today's call. We look forward to reporting our progress next quarter. Operator, you may now disconnect the call.

Operator

Ladies and gentlemen, thank you for your participation on today's conference. This does conclude the program. You may now disconnect. Everyone, have a great day.

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