**FINAL TRANSCRIPT**

**Baylin Technologies Inc.**

**Third Quarter Investor Conference Call**

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# Corporate participants

**Randy Dewey**

Baylin Technologies Inc. — Vice Chairman, President, and Chief Executive Officer

**Michael Wolfe**

Baylin Technologies Inc. — Chief Financial Officer

**Conference Call Participants**

**Daniel Kim**

Paradigm Capital — Analyst

**Steven Li**

Raymond James — Analyst

## PRESENTATION

**Operator**

Good morning. My name is Dan, and I will be your conference Operator today. At this time, I would like to welcome everyone to the Baylin Technologies Third Quarter Investor Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers’ remarks, there will be a question-and-answer session. If you would like to ask a question during this time, simply press \*, followed by the number 1 on your telephone keypad. If you would like to withdraw your question, you may press the # key.

Thank you. I’ll now turn the call over to Randy Dewey, President and Chief Executive Officer of Baylin Technologies.

**Randy Dewey** — Vice Chairman, President, and Chief Executive Officer, Baylin Technologies Inc.

Hello, and welcome, everyone. Thank you for joining us today for the third quarter 2017 earnings conference call for Baylin Technologies. Our Chief Financial Officer, Mr. Michael Wolfe, is joining me today on the call, and will provide the Q3 financial overview. We will both be available for questions at the end of the presentation.

Not only our we reporting our seventh consecutive quarter of positive adjusted EBITDA, we are reporting for Baylin record quarterly revenue and profitability.

Before we begin our full report, let me make it clear that our comments today will include statements and answers to questions that could imply future events such as our 2017 and 2018 prospects and financial performance, which could include the usage of non-GAAP and non-IFRS measures.

Notice all of these statements are subject to risks, uncertainties, and assumptions. Accordingly, actual performance could differ materially from statements made today, so do not place undue reliance on them.

We also disclaim any obligation to update forward-looking statements, except as required by law.

I ask that you read our legal disclaimer, and refer you to the risks and assumptions outlined in our public disclosures, and in particular in the section entitled Forward-Looking Information of our MD&A for the interim period ending September 30, 2017, and our filings with the securities commissions of Canada.

Q3 Results were released after market yesterday. The press release, unaudited interim financial statements, as well as the MD&A, are all available on SEDAR and on our website at baylintech.com.

In this third quarter 2017 conference call, we are pleased to report positive EBITDA, our seventh quarter of positive adjusted EBITDA, and positive net income.

I’d like to provide a brief summary of our results for the quarter, and then comment on the market outlook for each of our three product lines, after which I’ll ask Michael to cover the details of the financial results.

Revenue for Q3 2017 increased 21 percent compared to the same quarter last year. The main factors contributing to this increase were a successful product launch of a major Asia Pacific customer and the launch of our small cell antenna product, which is part of the multiyear major rollout of the LD densification efforts in North America by our customer. We did report a slight delay in this effort in Q2, which moved the start date into July, but that effort is fully underway, and we expect this rollout to continue through the balance of 2017 and throughout 2018. The LD densification small cell rollout should continue through to 2020.

Our gross profit continues to trend in the right direction. At 8.4 million, Q3 2017 is the highest gross profit we have achieved as a publicly traded company.

We are particularly positive on the fact that all three product lines made material contribution to the results, and we have achieved a very nice balance.

Operating expenses for Q3 2017 were at 8—sorry, 6.8 million, which was consistent with the same quarter for 2016, and we are in line with expectations.

We are pleased with a positive EBITDA for Q3 2017 of 2.7 million and adjusted EBITDA of 3.1 million. Achieving an adjusted EBITDA margin of 11.3 percent is a function of high revenue in the quarter combined with cost reduction and rationalization efforts implemented over the last two years.

We see the instances of onetime adjustments starting to trend downward and the benefits of the past efforts starting to show through in net income strength. A more balanced revenue stream, coupled with strong EBITDA margins and less onetime events, is evidence of a firm foundation.

Asia Pacific’s revenue in Q3 was positively impacted by a successful product launch of a major Asia Pacific customer, and will continue to contribute to revenue in Q4 and into 2018.

Networking revenue is expected to strengthen in the fourth quarter on the back of increasing customer demand. We see further opportunity in small cell and DAS, as network densification projects are expected to incremental volumes for Baylin.

The order book continues to be strong for both the networking and the small cell DAS business units. The small cell product’s launch delay reported last quarter generated revenue of approximately 1.6 million in Q3, and we expect an increase in Q4 revenue and a larger impact in 2018.

I’d now like to turn the call over to our CFO, Mr. Michael Wolfe, to provide more specific commentary and functions on—or sorry, details of our financial picture.

Mr. Wolfe?

**Michael Wolfe** — Chief Financial Officer, Baylin Technologies Inc.

Thank you, Randy. Good morning, everyone. My first few months with Baylin have been very busy as I increase my knowledge of the business and industry, get an understanding of key priorities, and get more involved in the implementation of the Company’s strategy.

I was fortunate to join Baylin at the start of a quarter with very strong financial performance, and I am pleased to be participating in this morning’s earnings call.

I will start by reiterating that since January 1st of this year, we have been reporting our financial results in Canadian dollars rather than US dollars. Our comparative numbers have also been converted into Canadian dollars in order to provide a better comparison.

I will now discuss the key metrics that we believe are helpful in analyzing the Company’s financial results. Q3 revenue at $27.1 million was $4.7 million higher than the prior-year quarter, which as Randy explained, was primarily due to a successful product launch of a major Asia Pacific customer and the rollout of a small cell antenna product.

Gross profit for the current quarter was $8.4 million and gross margin was 31 percent. Gross margin was higher than the prior-year quarter, but slightly lower than the second quarter of this year, primarily due to higher Asia Pacific sales of products that generate a lower gross margin.

Operating expenses at $6.8 million were consistent with the prior-year quarter. Operating expenses consist of research and development costs, sales and marketing costs, and general and administrative costs.

Research and development costs were 2.4 million in the third quarter of 2017, which is a decrease compared to the same quarter a year ago. This decrease was due to the closure of our Israeli operations.

We remain committed to continued investment in new product development, which includes our base station antenna development, and we are continuing to increase the headcount of our internal engineering team in Ottawa.

Sales and marketing costs were $1.4 million in the quarter, up 30 percent from last year. As noted in previous calls, hiring new salespeople to support growth in our DAS, small cell, and base station antenna products continues.

General and administrative costs were $3.1 million in the quarter, consistent with the prior-year Q2 costs and $1.3 million lower than the Q2 of the current year. The decrease from Q2 was attributable to the $1.5 million nonrecurring restructure and impairment provision that was booked in Q2 relating primarily to the closure of our Israeli operations and some other group restructuring costs.

Included in operating expenses in Q3 2017 were $0.5 million of costs related to the development of base station antennas. Expenses were lower than the projected amount as outlined in the short-form prospectus filed in December 2016; however, we expect the variance to plan to decrease in Q4 2017, and further decrease in 2018 as the headcount of our internal engineering team is built up to full strength.

EBITDA for Q3 2017 was $2.7 million and adjusted EBITDA was $3.1 million, our seventh consecutive positive quarterly result. As Randy mentioned, the significantly improved EBITDA was due to higher revenue in the quarter combined with cost reduction and rationalization efforts implemented over the last two year.

From a balance sheet perspective, our liquidity remains solid. Cash on hand was $13.2 million, a decrease of $1.8 million from the end of Q2 2017. The decrease is primarily due to the increase in accounts receivable, a result of the significantly higher Q3 sales over Q2.

The cash conversion cycle improved by 3 days to 28 days, as we continue to effectively manage working capital.

During Q3 2017, capital expenditures of 0.4 million were incurred for plant enhancements for small cell DAS and base station antenna manufacturing, as well as certain other engineering assets.

I will now briefly comment on our year-to-date results. Total revenue at $67.3 million for the nine months ended September 30, 2017, was 5 percent higher than the comparable period of the prior year. This was achieved despite revenue for the six months ended June 30, 2017, being lower than the prior-year period, and as we have discussed, was due to the launches of a flagship handset model by a major Asia Pacific customer and a product rollout of a small cell antenna.

Gross profit increased 19 percent to $21.2 million for the nine months ended September 30, 2017, compared to the prior-year period. For the same period, gross margin was at 31.5 percent compared to 27.7 percent in the prior year. This is attributed to a better product mix and the results of continuing improvement efforts.

Operating expenses for the nine months ended September 30, 2017, were 23 million compared to 19.5 million for the prior year. The increase was primarily due to significant nonrecurring expenditures in the second quarter of the current year, as well as the increased investment in engineering and sales resources for future anticipated growth.

Adjusted EBITDA at $3.6 million year to date was $1.8 million higher than the prior year due to improved gross margins.

I’ll now turn the call back over to Randy for his concluding remarks.

**Randy Dewey**

Thank you, Michael. So the first half of the year saw slower sales caused mostly by product delays which were all timing issues. We’re now seeing increasing revenue momentum and stronger margins while continuing to invest in the areas that will secure our long-term growth and profitability.

We expect to see a solid fourth quarter in all three product lines. Asia Pacific will continue to benefit from the Q3 product launch somewhat under the pace of Q3.

A newer client in APac had some delays in the first half, H1, and we have seen a pick-up in those volumes towards the end of Q3. And we expect that to continue through the end of the year and as well into 2018.

We will continue to see good sales momentum from our small cell antenna product lines, and somewhat offset by the difficult fourth quarter slowdowns as carriers limit changes to the network in advance of the holiday season. We expect that we’ll have a new small cell—sorry, we expect to have a new small cell product coming into market in the fourth quarter which has sales demand behind it.

The networking product line is expecting a stronger fourth quarter as new platforms begin ramping up.

We are pleased with the continued improvement in our financial results, and we are anticipating a positive adjusted EBITDA for the full year that will be close to our expectations at the beginning of the year even though we did not expect our full year top line to achieve the same levels that we had expected at the start of this year.

We are on track with the development of our first base station antenna. We’re entering into that market as outlined in our short-form prospectus from December of last year. Our engineering team and our new R&D centre in Ottawa have made important strides in our base station antenna product development efforts. We are ahead of schedule to launch our first BSA product to market before Q2.

Our reconstructed small cell, DAS, and base station sales team has made several positive inroads with new customers, which includes new master purchase agreements and new product approvals we had not anticipated in our plan. We are expecting to see a meaningful increase in sales in those products lines as a result in 2018.

Our optimism about Baylin’s future continues to grow.

And this concludes my formal remarks. And, Operator, if we could open up the line to questions.

## Q&A

**Operator**

Certainly. At this time, if you would like to ask a question, please press \*, followed by the number 1 on your telephone keypad.

And your first question comes from the line of Daniel Kim with Paradigm Capital. Please go ahead.

**Daniel Kim** — Paradigm Capital

Good morning. Thank you, and congrats on a great quarter. Randy, my first question would be on just the divisional breakdown. The commentary did provide notional revenue growth sequentially and year over year for some of the divisions, but can you be a little bit more granular in terms of the specific numbers by division, please?

**Randy Dewey**

Well, we don’t do segment reporting, as you know, Daniel, but we did try to allude to some of the direction. Obviously we’ve had a good quarter, and the gain over expectations was primarily due to the two divisions, the growth in the mobile segment product line with the launch to the customer and the small cell launch to market. And that was obviously a delay from Q2, and it got started in about the third week of July. And we’ve been experiencing some good pickup as a result of that.

So I’d say that the gain is split half and half between mobile and infrastructure for the quarter.

**Daniel Kim**

Mobile and infrastructure, great. Okay. Switching gears a little bit, if we look at the commentary with regards to the Asian Pacific, Asia Pacific customer that negatively impacted gross margins, presumably this is a mobile customer. Can you explain why this is a lower-margin profile piece of business for you?

**Randy Dewey**

Well, it’s on the back of some issues that we had at the plant level with some yield issues that we were able to work through. It was a particularly difficult product that we were producing, and we had some heightened scrap rates, higher than expectation. But we’ve since resolved that problem. And so we’re expecting margins to continue to trend in the direction they’ve been.

This quarter was obviously just sort of a setback, but it was lower than expected as a result of the higher scrap rates than anticipating.

**Daniel Kim**

Okay. And has that been now resolved so we should see things improve in Q4?

**Randy Dewey**

Yeah. Yes.

**Daniel Kim**

Okay. Okay. And this is presumably with an existing customer that you’ve talked about, I believe, about a year ago. Is this just a new platform or a new program with that existing customer?

**Randy Dewey**

No, it’s a longer-standing customer, and it was just a particularly difficult profile. So we’re through the lion’s share of that platform that we were doing for that customer, so there’ll be a little bit because the nature of the design of that product will produce a little bit more scrap than normal. But the buy-ins of that platform are—have materially declined.

So the issue’s resolved, but maybe the performance on that one product is going to continue for a little bit through this quarter, but it’s dropping off quite quickly. So I don’t know that it’ll have that much of a material impact on the gross margins for this quarter, but depends on the strength of the demand of that product, so. But we’re not expecting to have that same issue this quarter to the same magnitude.

**Daniel Kim**

Okay. Great. Looking at the small cell contract, I’m just trying to understand how the numbers are going to shake out here. When you talk about delivering 1.6 million in the quarter with an expected increase in Q4 and thereafter against what you had suggested of a negative impact of 6.5 million based on the delay, is that negative $6.5 million impact, do you still stand by that number? Or are things progressing better than expected in terms of how things played out in the quarter in your expectations for Q4?

**Randy Dewey**

I’d say half that number, Daniel, is part of the delay of the 6.5 that we talked about delay. So that … so we were expecting sales in this quarter for that small cell; it was just the Q2 we were expecting a lot higher. So I wouldn’t say we’ve recovered all that 6.5. Some of that will slip into next year for sure.

But we … I would say probably recaptured a 1.5 or so of that number through the second half of 2017 here. So anyways, but what’s good news about that, and I know you’re trying to figure out what that number is, but this is a multiyear platform, 36-month rollout. It started basically as of the third week of July, and it’s going to go for 36 months. Doesn’t mean we are going to be the only competitor in that space, but right now we are still … we still remain the only—we still have the only small cell antenna product that’s approved at the carrier level in North America at this point in time.

Obviously there’s going to be other people wanting to rush into that space and get a product, but right now we’re the only one. So we’re enjoying the benefits of a bit of a captured market, but that will obviously change because if you just read in the commentary of how many small cells are going out and going to be deployed over the next 36 months, the numbers get a little staggering. So there’s going to be obviously people in the space.

So anyways, we’re in a pretty good position today, but we anticipate further competition down the road.

**Daniel Kim**

All right. Okay. And then looking at the base station antenna project, with regards to timing, has anything changed on that front? Would you expect qualifications to begin in Q4? Or is that all going to—is that a Q1 event?

**Randy Dewey**

Well, we are very close to sort of product finalization on one of the products, so we then have to go into what’s called inoperability testing, which is what happens at the carrier level. So we will be doing that through the second half of this quarter and then into the first quarter. So we think we’ll be commercially ready to sell those products by the end of the first quarter into the early part of the second quarter, where last year we reported that we wouldn’t see POs or be commercially ready ‘til the end of the second quarter.

So I would say we picked up a couple of months on the back of a really good, strong team that—we were expecting to have a strong team in Ottawa, but we’ve been really … benefitted from some really exceptional hires and people right out of the base station industry. So it’s been exceptional for us to attract the kind of talent that we’ve attracted in the last four months. So we are ahead of the schedule, and we’re expecting good things out of that group.

**Daniel Kim**

Outstanding. Okay. And last question—I recognize you don’t provide guidance—but based on the commentary, clearly Q4 looks like it could have … it should have a better top line than Q3. But then when we look at the margin profile, assuming that with things—excuse me—with things result on the Asia Pacific customer on the yield issues, but with increased investment in sales and marketing and R&D for the base station project, on balance if you were to look at it, say, perhaps philosophically, could this be a quarter where we can see both improved top and bottom line numbers versus Q3?

**Randy Dewey**

No. No, no, I’m not sure how you read that into what we discussed in the call. Q4 typically has two challenges in it. One, you have the carriers that—and the CapEx spending in some of the major operator markets that start to decline towards the end of the year. So some of the engineering deployments kind of curtail and the outdoor deployments start to move towards indoor deployments, and indoor deployments have lower ASPs, those types of products, where outdoor products have a lot higher ASPs and a lot higher revenue generation.

So they kind of move from the … in the Infrastructure from an outdoor deployment in Q4 to an indoor deployment through the second half of Q4 and the first half of Q1. So infrastructure typically has a bit of a lull in that one period. So we’re not expecting at this point in time infrastructure to outpace Q3. Q3 is kind of the strongest quarter of the four as a result of lots of deployments are happening during that period, particularly outdoor small cell, so that being factor one.

Factor two is that in some of our mobile platform rotations, Q3 is a very large launch period and then Q1 is a very large launch period. So Q4 obviously there’s some sort of rollover from the launches of Q3 into 4, but it’s not at the same magnitude. So we’re still expecting strong positive EBITDA performance, but we’re not expecting it to be at the same magnitude as Q3.

**Daniel Kim**

Okay. Very good. And networking presumably doesn’t have that same type of seasonality. And with the ramp of new platforms, we could see … should see sequentially growth in that division?

**Randy Dewey**

Correct. And we did mention that in our script here that networking had some first half softness, and then that has improved in Q3. And then because of the timing of some launches it comes in Q4. So that business unit has a little bit more sort of stability through all four quarters. It doesn’t ebb and flow as some of the others can. And so it’s a little bit more steady-state.

on track, which we don’t have total influence over, but we … but they definitely are coming to market, so we should see some enhancement there in networking over the quarter, so yeah.

**Daniel Kim**

Terrific. Okay. Thank you very much.

**Randy Dewey**

No. Thank you, Daniel.

**Operator**

And we have—oh, your next question comes from the line of Steven Li with Raymond James. Please go ahead.

**Steven Li** — Raymond James

Thank you. When—the new base station antennas, can you talk about what are the milestones that are left? And is it already exceeding specs?

**Randy Dewey**

So thank you for the question, Steven. So yes, the—we have very strong “in-lab”—I should quote—“in-lab” performance specs on the products that we have developed to this point. That has to get proved out in the field. That’s what’s the inoperability testing and that’s being done at the carrier level. So early days, we’re well on track. We’re not really sweating about the specifications.

There’s just certain pieces of a base station antenna that are very different from a small cell in that the base station antenna has moving parts, right? You have what’s called a phase shifter and a remote electrical tilt, and those two components actually move inside the antenna. Most historically our antennas have always been passive and no movement inside the actual antenna, where base station antennas actually have moving parts to help optimize the network for directional pointing of the beam. So those moving parts require a level of testing that we haven’t gone through historically.

And that’s why I’m encouraged because the team that we’ve hired come from the industry, our ability to get that—sort of de-risk ourselves on the launch of that product is great when you have people that have done it 100 times in their past. So we are very, very bullish on the fact that we’ll get that approved, but that doesn’t come—right now it’s coming over the next couple of months in order for us to be commercially ready by the end of the first quarter.

**Steven Li**

Okay. And, Randy, will they be launched with customer contract in hand?

**Randy Dewey**

Yeah. We had demand behind those products.

**Steven Li**

Okay. All right. And one more question. The cash flow picture, so the working capital investments you referred to, do these reverse next year? Or given these rollouts, you expect to continue to invest in working capital?

**Randy Dewey**

There will certainly be some continued investment. We’re coming out with a series of new products in the base station market. The small cell market continues to evolve. I mentioned in earlier that we had another product come into market in the fourth quarter. So there’s going to be at the baseline continued … our investment like you have seen in our historical financials. Maybe slightly a little bit more because of the base station product line, but I wouldn’t say it’s significantly more.

It’s in line with what you’re seeing this year what you’ll see continuing through next year as we continue to sort of round out the team that we’re developing in Ottawa. So no big chunks of capital coming down the pipe outside of what we normally have. So the CapEx spending, and as you know, we always expense R&D, so the R&D OpEx will continue at the rate that you’re seeing, maybe slight bump up, but not a lot. And then CapEx will be in line with historics.

**Steven Li**

And when do—the other small cell product, so that’s Q4 this year, 2017, right?

**Randy Dewey**

Correct.

**Steven Li**

And in terms of potential opportunities, I mean is it comparable to what you have with the Tier 1 carrier?

**Randy Dewey**

I’m sorry, I missed your question.

**Steven Li**

Is it … in terms of potential opportunities, it’s similar in magnitude to the one you’ve announced with the Tier 1 North American carrier?

**Randy Dewey**

Yes. It is similar, yeah.

**Steven Li**

Okay. Thank you.

**Operator**

And we have no further questions at this time. I would now like to turn the call back over to Mr. Dewey for closing remarks.

**Randy Dewey**

And obviously we’ve had a good quarter, and we’re very excited about the results that we produced in the third quarter of 2017. We continue to work very hard on the growth prospects and the opportunities that we have before us. And we will—we really appreciate everybody’s support.

I know that we’ve had a few years in the past that were a little tougher, but we really appreciate everybody supporting and believing in our company.

So thank you very much, everybody.

**Operator**

Thank you to everyone for attending today. This will conclude today’s call, and you may now disconnect.

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