FINAL TRANSCRIPT

Baylin Technologies, Inc.

Third Quarter 2020 Conference Earning Call

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PRESENTATION

Operator

Welcome to the Third Quarter 2020 Earnings Conference Call for Baylin Technologies Inc.

At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. To ask a question during the session, you will need to press star, one on your phone. Please be advised today's conference is being recorded. If you require further assistance, please press star, zero.

I'll now turn the call over to Mr. Daniel Kim, Executive Vice President, Corporate Development of Baylin Technologies.

Daniel Kim – Executive Vice President, Corporate Development, Baylin Technologies Inc.

Hello and welcome everyone. Thank you for joining us this morning for the Third Quarter 2020 Earnings Conference Call for Baylin Technologies. Joining me is our President and Chief Executive Officer, Randy Dewey, and our Chief Financial Officer, Michael Wolfe. We will all be available for questions at the end of the presentation.

Before we begin our report, let me make it clear that our comments today will include statements in answers to questions that could imply future events such as our 2020 and 2021 prospects and financial performance and could include the use of non-GAAP and non IFRS measures. Although it is obvious these statements are subject to risk, uncertainties, and assumptions, accordingly, actual performance could differ materially from statements made today so do not place undue reliance upon them. (Inaudible) to disclaim any obligation to update forward-looking statements except as required by law. I ask that you read our legal disclaimers and I refer you to the risks and assumptions outlined in our public disclosures. In particular, the section entitled forward-looking statements and our risk factors in our annual information form for the year ended December 31, 2019 and our other filings which are available on SEDAR. Q3 results were released after market yesterday. The press release financial statements as well as the MD&A are available on SEDAR and our website at baylintech.com.

Before I turn the call over to Randy and Michael, I would like to set the stage for the substance of our discussion. We are navigating unprecedented times, as such, management has selectively restructured the Company to prudently manage its costs throughout this volatility, which Michael will discuss in more detail. Furthermore, our past investments across all of our business units are bearing significant new opportunities, if any of which go into volume production in 2021 could drive significant organic growth and profitability over the near and long term.

I would now like to turn the call over to Randy to provide more commentary on these significant programs and opportunities.

Randy Dewey – President and Chief Executive Officer, Baylin Technologies Inc.

Thank you, Daniel.

After reporting improved quarter-over-quarter financial results in the second quarter of this year, we are pleased to report our third quarter revenue, gross profit, and EBITDA improved again compared to the second quarter. While quarterly financial results have improved, the Corona Virus pandemic continues to have an impact. One very important macro issue is the delay of the C-band auction. It is this new spectrum that is set to be completed in December of this year. The timing is stretched out causing delay in CAPEX in 2020 but is expected to be completed next month.

This important turning point benefits us in two ways. First, our telecommunications customers get the coveted spectrum they need for 5G. Second, our Satcom customers get the influx of almost $10 billion of spectrum that they're giving up. This is exciting news for us. The second piece of exciting news we have received approval to bring in our chamber expert in Vietnam in January; the missing link to our factory completion. The third piece of exciting news is that we want a supplier status with a large U.S. carrier to support our 2021 small cell plan, which appears to be quite aggressive and begins in the first half of ‘21.

Although the short term issues of COVID-19 lockdown in Europe impacting our order book and mobile this quarter, we have made significant progress in some very key areas. I will outline in more detail some of these very positive steps later in my presentation on the long-term contracts we won and the nature of the opportunities we were working on and why is generating a lot of optimism for 2021 and beyond.

I'd like to turn the call over to Michael to provide more commentary and details on our financial result.

Michael Wolfe – Chief Financial Officer, Baylin Technologies Inc.

Thank you Randy.

Revenue in the third quarter of 2020 was $36.6 million, an increase of 19.4 percent compared to the second quarter of this year, and an increase of 35.8 percent compared to the first quarter of this year. The increases were driven by Asia-Pacific and embedded, which were somewhat offset by lower infrastructure and Satcom revenue.

Third quarter revenue was slightly higher compared to the prior period, although the mix was different this year. Asia-Pacific and embedded revenue represented a higher percentage of revenue in the third quarter of this year than the prior year. The change in revenue mix in the third quarter compared to the prior year resulted in a lower gross margin, 31 percent compared to 36 percent. However, due to a continued focus on cost reductions, operating expenses in the third quarter decreased by $3.3 million compared to the third quarter of 2019, resulting in Adjusted EBITDA improving to $3.6 million, an increase of $2.4 million compared to the third quarter of 2019. Adjusted EBITDA for the third quarter of 2020 was the highest reported in the last five quarters.

Operating expenses in the third quarter were slightly higher compared to the second quarter, primarily due to government stimulus relating to COVID-19 received in the second quarter, but offset by the impact of cost reductions in the third quarter. Government stimulus relating to COVID-19 in the third quarter was a very small amount, and as a result had a very small impact on operating expenses. At this point, we are not expecting any further benefit from these programs.

At September 30th, we had a cash balance of $14.9 million and access to approximately $21.5 million of revolving credit facilities, of which $13.5 million was utilized. We had the option to defer the term loan principle repayment on September 30th, and we elected to do so. Quarterly principal repayments of US$750,000, will resume in December. Capital expenditures to September 30th were $6.7 million, of which approximately $5 million was for the new factory in Vietnam. The construction delays have allowed us to fund the capital expenditures incur to date from cash flow rather than additional debt.

I'll now turn the call back to Randy.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc.

Although COVID-19 has impacted us in 2020, we still stand by our earlier comments that the financial performance in the second half of 2020 will be better than the first half. While the impact of the pandemic is creating near term volatility in our business, the long term outlook for all of our product groups is exceptionally robust. For example, Wi-Fi 6 has expanded our opportunities with existing and new customers. Additionally, we have secured automotive contracts with two key OEMs and we are expecting these long life programs to begin volume production in the second half of '21. Combined these wins should accelerate organic growth of our embedded products division.

The reallocation of C-band from satellite operators to telecommunications providers towards 5G spectrum is driving an unprecedented product refresh across both Satcom in the form of C-band filters and infrastructure in the form of small cell base station dash systems, obviously, those products related to us. The delay in the auction has not helped, but the SEC (phon) has come to the final stage and expected to start early December and conclude shortly thereafter. C-band is the new spectrum that we use mostly for 5G and the network operators need this step completed to commence a lot of capital spending.

While small cell deployments stalled in the U.S. during the pandemic, this industry expected to trend steadily upwards beginning in 2021 through 2025. Now that we have secured a second large carrier, we expect our infrastructure projects will enjoy more robust growth and less volatility and deployments in 2021. After years of investment and expanding product portfolio, our base station product group continues to gain significant traction with customers. We have taken a lot more steps in 2020 to cut out further Opex in costs which will position us in 2021 with a lot more torque on new volumes.

The other significant strategic step we announced in the summer was the launch of our Summit Series 2. After three years of heavy investment, that product has hit the market. We have sold and are quoting a lot of business with this industry leading technology. Our first deployment is set for Q1. The key areas of this new product is expected to benefit us is in the areas of 5G backhaul, military, as well positioning for the new LEO Constellation programs that have commenced. To be clear, though, we have one 5G backup and military programs with this system and these are long-term contracts.

Although we have not highlighted LEO as much in the past, we can see from the major industry announcements from Amazon, SpaceX, OneWeb, Telesat, Starlink, that actually the new space race has begun. We've seen 10 years of slow growth in this segment, but we're on the cusp of a major industry shift. I'm excited about 5G and Telecom, but I can tell you that LEO and Satcom is just as exciting. I'm excited, actually, that we're in both.

In closing, I want to keep for you to keep four things really in mind from our call. First, the pandemic has impacted our business this year, but we have not lost any major contracts or key customer relationships. Second, the pandemic is likely to continue into 2021, but the C-band spectrum reallocation completing this quarter sets the stage for significant 5G expansion in the industry. The massive MIMO market in our factory completion was stalled this year due to the pandemic, but we have found a solution that is expected to get this business started in the first half of 2021. The fourth is the opportunities for our Company in 5G, LEO, Wi-Fi 6, automotive, and military are very exciting and we are in an enviable position.

Our immediate challenges are obvious, but our long-term opportunities are exciting. Baylin's (inaudible) and with its position to drive very strong growth and certainly operating leverage.

That concludes my formal remarks. Operator, can we please open up the call for questions.

Q & A

Operator

Thank you.

At this time, I would like to remind everyone, in order to ask a question, press star, then the number one on your telephone keypad. We will pause for just a moment to compile the Q&A roster. Again, if you would like to ask a question, press star, then the number one on your telephone keypad.

Your first question comes from David Quan of PI Financial. Your line is open.

David Kwan – Analyst, PI Financial

Hey guys

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc.

Hi David.

David Kwan – Analyst, PI Financial

Hey, good morning.

I was wondering in terms of the revenue outlook, based on the commentary, it sounds like Q4 is likely to be down sequentially versus Q3 here. The expected declines here in Asia-Pacific (inaudible) a very good quarter in Q3, in the infrastructure side, possibly (inaudible) here. I guess, based on the commentary about the second half being stronger than the first half, it would suggest, I guess, at the bottom end Q4 could be as low as $21 million. At the high end, it could be slightly down from Q3, so maybe about $36 million, so obviously that's a pretty wide range there. Can you provide more colour as to where you might expect revenue to kind of fall in, or is the visibility just not there yet?

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc.

Certainly, that's quite a wide range you've got there. Obviously commentary, I said the second half will be stronger than the first half, that we still stand by. Though this quarter, of course, you've got lockdowns in only one of the two continents that were materially affecting us in the first half of the year, because we had closures in North America as well as in Europe. Here we have just the impact of Europe, so that's creating some near term softness in our order book for mobile only. As you know, we don't give guidance but just trying to help you tighten that very large range you had there.

David Kwan – Analyst, PI Financial

No, no. I understand. I guess maybe another way to ask it is, back after the Q1 results, you said that you expected the revenues in each of the subsequent quarters to be higher than Q1 levels, north of $27 million. Do you still stand by that comment?

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

So, Q4 we're not giving guidance that it's going to be as strong as Q3, obviously it's not. That's not what we're trying to communicate, but we're obviously not going. Specifically to those numbers of the exact, we're talking about one of the four business units having one of their markets softer in the fourth quarter than the prior quarters, and yes that’s takes us—that was the one that was the most strongest in Q3, so having that ship though also creates a similar dynamic, because as you’ve see in the first half of the year, we had a lot of pent up demand because of closures, and then we had a strong Q3. If we're going to have a softer Q4 in the one business segment, that's going to build up some demand that obviously will bring some benefit into Q1. So, on balance, I think you have to kind of balance that in your estimation.

David Kwan – Analyst, PI Financial

Sorry, I guess I wasn't trying to compare to Q3. It sounded like the commentary that it will be down—Q4 will down versus Q3. Back in Q1 when revenues fell to $27 million I think, you had indicated that you expected each of the following quarters to be higher than that Q1 level, so higher than $27 million. I'm just wondering whether you still believe that will be the case.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

That's for you obviously and your model to figure out. We're trying to help you at least kind of come close to where we're looking at, but we certainly don't, as you know, we don't give guidance. As a company, that's been our stance going forward. We are talking about one of the four business segments having a softer quarter, for one of the markets that are softer. It does create some near term volatility I guess in the next couple of months as we closeout the year, but it is building up to demand for the first quarter.

David Kwan – Analyst, PI Financial

Okay, thanks Randy. I was wondering, just given what's gone on with COVID here, just any changes in customer behaviour, maybe particularly as it relates to say inventory levels. Do you find that your customers are carrying lower amounts of inventory, running a little bit leaner just given the demand is a lot different now than it would have been, say a year ago.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

Yes, no doubt, there would certainly be a lot more cautiousness on the end customer perspective on inventory. Of course, anything that’s in mobile (inaudible) need to see, they're being a bit more cautious. So, we do see that certainly playing out. This year though, what's interesting in my view, this year of course, we were all caught by surprise. It’s the first time we had such a global pandemic, but we are seeing a lot more thoughtfulness in 2021 as they're planning to actually have to coexist with this virus for some period of time. No one's expecting the vaccine to be the full silver bullet here, but now you're seeing purposeful planning, and I think that that's what's exciting.

We knew that 5G spectrum was required here and the C-band was maybe a bigger deal than some of the capital markets appreciated, but now that there's a solution that's now there, that’s going to change a lot for us, and so there's going to be a lot of capital being spent by teleco carriers this quarter to buy better slices of that spectrum. The money then flows into Satcom. So, it's going to take two sides of our business that were affected by this and infuse capital into one and provide clarity on spectrum for the other.

Naturally, next year for us is going to be—there’s much more purposeful engineering happening, a lot more things happening right now that set the stage for next year because we know how to live with this virus to some degree, and there's planning going forward. So, we're pretty optimistic as you can tell in the call because of all the things that we see, and the activity level that is happening on the engineering side and the products that we've released. There's certainly near term issues, but when I look at it, I feel very strongly that we've got a very robust order book for next year. We've got a lot of still some uncertainty, but the amount of activity that's going on right now in our spaces is pretty exciting.

David Kwan – Analyst, PI Financial

That's helpful. I guess it kind of ties into my next question. It sounds like there's a lot of stuff going on, positive stuff for next year. Can you maybe talk about what the two, maybe three initiatives that you think could have the most significant impact next year?

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

Sure, clearly it's going to be clearing up this spectrum for small cell. Small cell has been slower this year than expected. We had some issues related to the municipality delays of approval of small cell sites, but then later on that, they had no decision on the actual C-band. Those two things have now cleared up and there's a lot more abilities now in that area. So, we're going to see a natural pick up. I also note earlier in the call that we won a second carrier that has a very aggressive small cell strategy. Take those two and combine it, then our expectations in our infrastructure group are significant for next year, and on the back of two very important things that have cleared the deck a little bit, so that's the first one.

The second one is that we didn't talk so much about Embedded. I did reference Wi-Fi 6 in my earlier comments. However, I should spend a second and explain what that really actually means. So, Wi-Fi 6 has always been—it’s a new unlicensed spectrum, it's got a lot more—because it’s higher frequency, it's got a lot more data transmission and performance capabilities. Wi-Fi 6 was scheduled to be rolling out over a lot more time, but as a result of the pandemic and more people working from home and more bandwidth now coming into homes, they've now pulled in a lot of these Wi-Fi 6 platforms. This year we spent, I think probably be call it April, May, where we had a very stark shift in all the work that we were doing in that division is all slanted towards Wi-Fi 6. Now, those platforms and things are now scheduled to—and have pulled in earlier, and now we're seeing a significant shift into Wi-Fi 6 products as a result of this. Though our embedded group didn't really lose a lot of momentum this year, they were the one division of our four that were really at where we were expecting, but they've had these shifts in Wi-Fi 6 that are setting the stage for them to actually see some improvement next year over what they were maybe currently historically projecting for ‘21. That coupled with the fact that we have now won these automotive contracts, and now that group is now moving into embedded antenna systems inside of cars, and we've won two contracts with two large car OEM's, and those are set to start next year in the second half. So, you couple those two things together for our embedded group and that would be the second one that I'm pretty excited about.

The third is the Summit Series 2. That was a very important and strategic investment that we made as a company two and a half, three years ago when we bought Advantech, that was a very strategic step that we took. It took that much time and effort with a very concentrated group to develop this system. We have launched it, we have—and the initial reaction to it has been very strong, very positive and we are set to deliver our first system in Q1. The momentum of that coupled with the industry changes in LEO and all the new platforms and opportunities that are coming have really given us, I would say very enviable position in the industry, and we are in some respects first to market on some of the things that we can offer.

David Kwan – Analyst, PI Financial

That's helpful, Randy. I guess the last question about—maybe more for Mike about this, just talking about further cost reduction activities, any colour you provide in terms of magnitude and timing would be appreciated.

Michael Wolfe – Chief Financial Officer, Baylin Technologies Inc.

As we've reported, we've been really looking at cost reductions for, really it started at the end of last year, and we're continuing to do that. In terms of magnitude and timing, it gets a little tricky because we are always looking at cost reduction opportunities, obviously, and will continue to do it. It will partly depend on what our ongoing outlook looks like for each one or the first half of next year, and the timing of some of the initiatives that Randy's announced or commented and this ramp up of our new facility in Vietnam. So, all of those things could have an impact on operating expenses, and while we're continuing to look at them, we are being careful that we don't want to make any cuts that will impact or put at risk anything that we've landed and executing on, or anything that we're working on or to try to win. So, it's a bit of a balancing act and we're going to be closely looking at it and continue to closely look at it. Directionally, I think we would say that we expect costs to continue to decrease but in terms of magnitude and timing, it's really uncertain at this time.

David Kwan – Analyst, PI Financial

All right, thanks guys.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

Thank you, David.

Operator

Again, if you would like to ask a question, press star, then the number one on your telephone keypad.

The next question comes from Bill Zhang of Raymond James. Your line is open.

Bill Zhang – Analyst, PI Raymond James Ltd

Hey guys.

For Asia-Pacific, you mentioned it was going to be impacted in Q4. How is it being impacted sequentially, and what are you thinking for 2021? Flattish, up or down? Any colour there.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

I think we've answered that a little bit earlier on David's commentary, but to talk about 2021, this is a business unit that has been at somewhat flat levels for the last number of years, and we don't expect that to change in 2021. What we are certainly expecting is that because of some of (inaudible) that's in Q4, it's going to translate into a pent up demand for Q1. Our expectations is that this change that we're talking about is somewhat temporal, and that Q1, you will see some rebound similar to what we've seen in this year. The same sort of thing happened to us in Q2, and then in Q2, we had a rebound, so we're expecting similar issues for us there.

Bill Zhang – Analyst, PI Raymond James Ltd

Okay, great. For the massive MIMO, you mentioned the engineer will go in for calibrations Q1 operation starting in Q2. So, when can we expect to recognize revenue? In more late Q2 or Q3?

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

Yes, the timing of it is exciting for us because this has been the missing link as I said earlier, so getting that in there and getting that done, we're only getting one engineer in there as opposed to the three that we need. It’ll take a little bit longer but getting it done in Q1 is certainly reasonable, even with what we've got happening today. So, into operations and getting things sort of finalized in early Q2 with an eye to seeing the startup of revenue in the second half of Q2.

Bill Zhang – Analyst, PI Raymond James Ltd

Okay, sounds good. I know this was asked before. The $3.3 million savings for Opex year-over-year, is that a good run rate to use, or should we expect it to decrease or increase?

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

I'll pass it on to Michael.

Michael Wolfe – Chief Financial Officer, Baylin Technologies Inc.

The last three quarters have been roughly $11 million. Some of the cost reduction initiatives that we've made in the last little while haven't been fully realized yet. As I mentioned, we are still looking at other ones.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

I think dramatic decreases in the short term, but again, it's going to depend on timing of certain initiatives and how they play out in 2021 and if things get postponed or if they start earlier, that will impact our decisions on making some cost cuts, but directionally over the next couple quarters, we do expect a downward trend on Opex.

Bill Zhang – Analyst, PI Raymond James Ltd

Okay, great. Thanks.

Operator

There are no further questions at this time. I will now return the call to our presenters for closing remarks.

Randy Dewey – President and Chief Executive Officer**,** Baylin Technologies Inc

Thank you very much. Thank you everybody. I know this obviously was an interesting and difficult year in many respects, but we're glad to give our report today just knowing the exciting four things that I talked about earlier and the trend that things are going. We've moved ourselves into this position that we find ourselves today, in an enviable one with the long term opportunities in tact, customers still in place, contracts still there, and for us, the Opex changes and the things that we've done to make sure that we really grind down our operational costs as best we can. We haven't been bashful whatsoever on that front and now we've got the company positioned for 2021 to see some improvement there.

We're looking forward to reporting those to you in the future. Thank you very much.

Operator

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