FINAL TRANSCRIPT

Baylin Technologies Inc.

Second Quarter 2021 Financial Results Conference Call

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CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Daniel Rosenberg
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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Baylin Technologies Second Quarter Financial Results Conference Call.

At this time, all lines are in listen-only mode. Following the presentation, we will conduct a question-answer session. If at any time during this call, you require immediate assistance, please press *, 0 for the Operator.

This call is being recorded on Thursday, August 12, 2021.

I will now turn the call over to Mr. Daniel Kim, Executive Vice President, Corporate Development of Baylin. Please go ahead.

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

Hello and welcome, everyone. Thank you for joining us this morning for the Second Quarter 2021 Earnings Conference Call for Baylin Technologies. I'm delighted to introduce Leighton Carroll, our new Chief Executive Officer, for this very first earnings call and, indeed, the first opportunity for him to speak publicly with analysts and investors since he joined Baylin around seven weeks ago. Leighton has significant experience in building and growing businesses in the telecom space and in satellite technology. And I'm sure you will all be very interested in what he has to say today.

Also joining us this morning is Cliff Gary, our VP of Finance and Acting Chief Financial Officer. We will all be available for questions at the end of the presentation.

Before we begin, let me make it clear that our comments today will include statements and information and answers to questions that could imply future events, such as our 2021 prospects and financial performance of the business, and could include the use of non-GAAP measures. These statements are subject to risks and uncertainties and assumptions. Accordingly, actual performance could differ materially from statements made or information provided today, so you should not place undue reliance upon them. We also do not intend to update forward-looking statements or information except as required by law.

I ask that you read our legal disclaimers and explanation of the use of non-GAAP measures and refer you to the risks and assumptions outlined in our public disclosures; in particular, the section entitled Forward-Looking Statements and Risk Factors in our Annual Information Form for the year ended December 31, 2020, and our other filings which are available on SEDAR.

Q2 2021 results were released after market close yesterday. The press release, financial statements, as well as the MD&A are available on SEDAR and on our website at baylintech.com.

I would now like to turn the call over to Leighton.

Leighton Carroll — Chief Executive Officer, Baylin Technologies Inc.

All right. Daniel, thank you. Let me begin by saying how thrilled I am to be with Baylin. I've always—I've actually been in telecom for 25 years, and I've known about the Company for some time. The Company has good products, really good engineering talent and manufacturing capability, and good people, and I'm thrilled to be on the team.

You will see from our press release and some other disclosure that we had announced several things yesterday, not the least of which are two important announcements, one about a private placement, and then one about a negotiation that we had conducted with our lenders

On the private placement, Paradigm is leading a best-efforts offering in order to raise a minimum of $10 million from the sale of common shares. As part of this, the Company's largest shareholder—which is actually a company who is controlled—its investment decisions are controlled and directed by our chairman, Jeffrey Royer—has agreed to purchase shares to ensure—enough shares to ensure that we will raise at least $10 million. The net proceeds will be available for use in the Company's business at its discretion, and we expect the private placement will close towards the end of this month.

Secondly, our lenders have agreed to waive compliance to our fixed-charge coverage ratio covenants for June 30th. In addition, they've agreed to make changes on how the covenants will be calculated through the end of the year, as well as to remove the minimum EBITDA covenant. We will, of course, be required to maintain a minimum liquidity of $10 million.

Coupled with the private placement, this agreement with our lenders has really provided the business with the flexibility to address many of the challenges that the business has been enduring, and honestly improve the financial stability and the balance sheet of the Company to get us well into 2022.

With that, I'd like to turn it over to Cliff Gary, our VP of Finance, to comment on second quarter results.

Cliff Gary — VP, Finance and Acting Chief Financial Officer, Baylin Technologies Inc.

Thank you, Leighton. Revenue was $21.6 million in the second quarter of 2021, a decrease of $9 million or 29.4 percent compared to the second quarter of 2020. The decrease was due to softer sales across all business lines in the second quarter, under the combined impact of the COVID-19 pandemic and global chipset shortages.

Gross margin was minus 16.4 percent in the second quarter, compared to 31.6 percent in the corresponding quarter in 2020, and was negatively impacted by inventory provisions relating to the 2018 acquisitions of $5.6 million, a $2 million loss on the consumer product manufactured by the Asia-Pacific business line. And Asia- Pacific revenue as a percentage of total revenue was higher in the second quarter of 2021 compared to the prior-year period. These revenues generate lower gross margins than other business lines.

Operating expenses in the second quarter were $29 million compared to $10.9 million for the second quarter of 2020. These expenses include a $15.9 million goodwill impairment charge relating to the 2018 acquisitions, a one-time adjustment for the lower scientific research and experimental development tax incentive in Satcom, and severance costs. If these items are excluded, our operating expenses are lower than the prior period as a result of continued cost-reduction measures.

The Company's operating loss in the second quarter was $32.6 million compared to a loss of $1.2 million in the second quarter of 2020 as a result of the factors previously discussed, in addition to the impact of lower revenue across all business lines.

Net cash at June 30, 2021, decreased by $3 million from December 31, 2020, primarily due to operating losses and principal and interest payments, which were offset by proceeds from the exercise of common share purchase warrants issued in December 2020, drawdown of the Vietnam loan, and a decrease in non-cash working capital.

Capital expenditures increased over the first quarter with aggregate expenditures to 30 June of $812,000. The Company continues to monitor its capital spending closely in an effort to conserve cash.

Finally, I'd like to comment on the situation with our consumer product program in Asia-Pacific. In Q1, we reported a loss of $2 million and announced we would cease further production and ship a small number of remaining antennas over the next few months.

While there were declining production volumes in the second quarter of 2021, there was a further loss of $2 million, primarily related to return shipments from the first quarter of 2021 and quality issues in inventory at the end of the second quarter.

Since our earlier announcement, our customer has asked us to continue production until the program ends in 2021. We are continuing discussions with our customer to minimize the impact while securing other profitable business with them in 2021 and, importantly, 2022.

I'll now turn the call back to Leighton.

Leighton Carroll

Thank you, Cliff.

The business has obviously been going through a very challenging period, not the least of which is COVID-19. It really has affected and continues to affect the business line. And broadly speaking, we deal with travel restrictions, chipset shortages, and I think it's fairly well known that there's been impacts on the global supply chain that affect not just our industry, but many industries broadly.

Speaking about some of the individual businesses, the commercial side of Satcom continues to feel the downturn of the pandemic. And although there's some signs of recovery, we expect capital spending by our commercial customers to remain somewhat constrained for the remainder of 2021.

Similarly, the recently completed C-band spectrum auction in the United States will eventually provide opportunities with the satellite operators, once they receive the incentive payments for their C-band spectrum, but those payments are made as that C-band spectrum is fully cleared and certified by the US FCC. For that reason, the major benefits to the Satcom business line build-out of the related infrastructure is not expected to be realized until 2022.

The military and other government-related side of satellite, which represents the balance of the Satcom business, has remained firm for much of the year, and we expect will continue so for the third quarter and into the end of the year as well.

Although we experienced a delay in the launch of our new Ultra High-Power Summit II solid-state power amplifier product line, the launch of Summit II demonstrates unique competitive advantage and unique competitive differentiation for our Advantech company.

The first deliveries took place in June of 2021, and we have opportunities for further delivery towards the end of this year and into 2022. Overall, we expect the revenue of the Satcom business to be stronger in the second half, as customers begin to invest and as the world slowly comes out of the COVID-19 pandemic.

In Asia, not only did we experience impact from COVID, but our customer did as well, and not just in terms of the personal side of COVID, but also in terms of supply chain interruptions. This included a temporary shutdown of our factory in Vietnam, which has only recently come back fully online to full capacity.

The COVID outbreak has also caused changes in product mix, due to supplier and customer dependencies over time. And certainly, in Q2, we saw lower-margin product even for the Asia unit.

Along those lines, the MMU factory continues to experience delays in the final commissioning and approval of the facility, in part due to COVID. Over the past 18-plus months' delay, our customer sales of their product line have softened significantly, also due to COVID. This has led to lower forecasts through midyear 2022, as well as our customer redesigning their product to reduce its complexity and their ultimate cost structure.

At this time, we do not perceive the facility being production-ready until sometime in 2022. And in light of the market conditions, the changes to product design, and the investment that's been made, we will be assessing the long-term strategic options for that facility over the next two quarters.

On the wireless infrastructure business side, it too has been affected by delays due to COVID, principally in the in-building and small cell deployment part of that business. We have also seen increases in freight costs and raw materials, as well as supply chain constraints. We expect these constraints to slowly lessen over the second half of 2021 and into 2022.

The Embedded business has been a stable performer in the first half of 2021, and despite chipset shortages that have been impacting our customers' schedules and forecasts, the business line has been a consistent performer. It is expected that as those chipset shortages improve, the second half of 2021 will see increased availability and, as a result, increased revenue growth for that business unit.

So having said all of this, understanding that we've had a lot of COVID impacts, one of the things I wanted to talk about is some of the better things in our business that have happened and are going to happen.

Let me talk about Satcom for a second. The Summit II product is very unique, and I'm very proud of the team in Montreal and what they have accomplished for putting that product together. It really is a uniquely competitively differentiated product and is something that will help set up our future, not just for the rest of this year or 2022, but this will be the future of that business in many respects for years to come.

On the infrastructure side, we had two new macro antennas approved by AT&T, we have new status with T-Mobile in the United States, and we have multiple products that are pending approval with Verizon that we expect to grow sales out of. The infrastructure side actually has a very unique story in front of it. It's going to take work, it's going to take execution, but I'm excited about its future.

On the Embedded side of our business, we have a very strong backlog. It's actually a really good story. And you look at the size of the backlog, and you look at the relative sales volume, and it just tells you there's a chipset shortage, and our customers have been impacted. As that thaws, I expect that business will do better.

And then, obviously, there have been challenges in Asia that we have spoken about. Part of what we are doing and part of the work that we have done in terms of our financial picture is to give us the runway to work out of that situation and to get to 2022 and beyond and more normal profitability for that business line.

I came to Baylin because I believe in the people of this company. Baylin has great technology and has terrific engineering and good customer relationships and reputation.

Wanted to maybe close this off by leaving you with five points about our company and where we're going.

One, we have new leadership. Two, Jeffrey Royer is standing behind this business in a very positive way, and that speaks volumes. It's part of why I'm here. Number three, COVID, the impacts are real. They will not last forever. Number four, we have new products and new products that we will work to gain traction with our customers. And number five, we have identified new customer opportunities. And in some cases, we have new standing (phon) in terms of our customer relationships, that may not have been there previously.

For those five reasons, I'm excited about our future. Clearly, we've had a very challenging 12-, 18-month period. There's a lot of work to do. I'm looking forward to being successful with the team.

Daniel, with that, I'll maybe turn it back over to you.

Daniel Kim

That concludes our formal remarks. Operator, please open the call for questions.

Q&A

Operator

Thank you. Ladies and gentlemen, we now begin the question-and-answer session. Should you have any questions, please press *, followed by 1 on your touch-tone phone. You will hear a three-tone prompt acknowledging your request, and your question will be polled in the order they are received. Should you wish to decline from the polling process, please press *, followed by 2. If you are using a speakerphone, please lift the handset before pressing any keys. One moment for your first question.

Your first question comes from Daniel Rosenberg, Paradigm. Please go ahead.

Daniel Rosenberg — Paradigm

Okay. Thanks. Hi. Good morning. I had a question around the product line, the consumer product that you had mentioned had been a drag last quarter and this quarter. So you had mentioned that the customer wanted to continue with production. So just trying to understand, are we looking at similar orders of magnitude? Or do you see it going downwards? What's the impact for the second half of the year?

Leighton Carroll

So, good question. So we do expect that it will be declining in the second half of the year. Obviously, the product is not a success story that we wanted it to be. However, the customer relationship, for the long term of the business and strategically, it is very important. The customer asked us to do that. We've been working with the customer to minimize our exposure, improve our profitability relative to that product, as well as work with the customer to identify and have allotted to us new projects and products which will drive profitability.

So two-part answer. We actually expect to have other, higher-value products in the second half of the year and certainly into 2022. But the product in question which has caused the losses, it is gliding downwards through the end of the year and will be completely wrapped up, we suspect, by the end of the year.

Daniel Rosenberg

Okay. And then you had alluded to supply chain disruptions, and we've all seen that in the news, especially with chip, but Embedded still being an interesting area for you. Just wondering, any early indications on any relief from disruptions from customers? Or is it still—we're still in the midst of them coping with supply chain disruptions?

Leighton Carroll

So our customers absolutely are continuing. We all still see freight costs. We all still deal with some of the chipset issues. However, there are indications it is progressing and getting better. We have received go-ahead on a few orders that were previously pushed out into—we expected to be pushed out into 2022.

I would characterize it as a slow thaw versus the floodgates have opened, so to speak. So it's going to be a slow process and slowly return to normal levels. But we are seeing the beginning of that.

Daniel Rosenberg

Okay. Thanks for that. And last question for me. Just on the kind of opportunities you see for products. You mentioned Summit II, as well as strong relationships with the telecom—within telecom that you could potentially leverage. What does the sales cycle look like as the US telcos and cable cos deploy 5G? Is this kind of a year sales cycle before kind of boots hit the ground? Is it six months? Longer than that? Any colour there would be appreciated.

Leighton Carroll

Sure. So it's really—it's not just the sales cycle. So a lot of what we're doing and a lot of how the Company has been working to position itself is based on new product and new product capabilities., And new product and new capabilities that we as a company have several things both under development and that have just been released.

Once you've released that product, a carrier must certify it. So I mentioned, as an example, Verizon is currently certifying multiple small cell antennas. Once those small cell antennas are certified, the sales cycle can, in many cases, be very quick depending on the customer needs and their capital build plan. And when I say very quick, in literally a matter of months to have a [substantive] impact. In other cases, you'll have situations, particularly on the in-build and wireless side, the sales cycle can be a year.

So the reality of it is it's a bit of a mixture. Part of our job is to be smart, have the right product for the customer as they're capital spending, and have that customer relationship so we know where the customers' needs are going, which will inform our product development lifecycle, so we have the products and technology capabilities that they need at the time they need it. And that's a big part of our roadmap on the infrastructure side.

Daniel Rosenberg

Okay. Great. Thanks for taking my questions.

Operator

Thank you. Ladies and gentlemen, as a final reminder, should you have any questions, please press *, 1.

It appears there are no further questions at this time. Mr. Kim, you may proceed.

Leighton Carroll

Daniel, if it's okay with you, I just want to reiterate, I am excited to be here. I have greatly enjoyed working with our team. And in my opinion, our best is in front of us. Having the investors that we have and the people who we have standing behind our business is a tremendous support. And I'm looking forward to seeing what we can accomplish in our future.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines.