

Operator

Welcome to the PCTEL second quarter 2019 Earnings Release Conference Call.

At this time, all participants are in a listen-only mode. At the conclusion of our prepared remarks, we will conduct a question-and-answer session. As a reminder, this conference is being recorded.

I will now turn the call over to Kevin McGowan, the Company's CFO.

Kevin McGowan

Thank you for joining us on today's conference call to discuss PCTEL's second quarter 2019 financial results. With me today is David Neumann, the Company's CEO.

Before we begin, let me remind you that this call may contain forward-looking statements. While these forward-looking statements reflect PCTEL's best current judgment, they are subject to risks and uncertainties that could cause actual results to differ materially from these forward-looking projections. Risk factors that could cause PCTEL's actual results to materially differ from its projections are discussed in the earnings press release which was issued today and in our most recent annual report on Form 10-K, both of which are available on our website.

Additionally, our commentary will include reference to the following non-GAAP measures: non-GAAP earnings per share and adjusted EBITDA. We believe these non-GAAP measures facilitate comparability of results over different

periods. A full reconciliation of these non-GAAP measures to our GAAP measures is included in our quarterly earnings press release that was issued earlier today.

With that, it's now my pleasure to turn the call over to David Neumann.

David Neumann

Thank you, Kevin.

We're pleased with another strong quarter driven by sequential revenue and antenna margin improvements. Second quarter revenue, gross profit margin, adjusted EBITDA and non-GAAP earnings per share all improved both sequentially and compared to last year. The improved results over the last three quarters are attributed to the R&D investments and actions we took in 2018, a strong demand for our 5G scanning receivers and increased industrial IoT antenna sales.

We issued a press release after the market close announcing our results for the second quarter ended June 30, 2019. For the second quarter 2019, our revenues were \$23.5 million. Increased sales of higher margin scanning receivers and improved gross margins for antennas contributed to improved non-GAAP earnings per share for the quarter. We achieved \$0.13 in non-GAAP earnings per share for the second quarter on gross margins of 45.5%, up 3.5% over the first quarter and up 9.4% over last year. Our focus on higher margin antenna solutions for intelligent transportation and Industrial IoT coupled with

strong demand for our 5G scanning receivers contributed significantly to increased margins for the quarter. We expect to maintain margins at this level through 2019.

Operators have launched more than twenty 5G networks in the US, Europe and Asia with dozens more planned for the remainder of 2019. We believe 5G network construction will continue over the next several years to address capacity and ultimately to support more technically demanding wireless applications. Our R&D investment in 5G scanning receiver technology, which started almost two years ago, has positioned PCTEL as a leader in testing 5G networks. Scanning receiver revenues in the second quarter benefitted from continued demand for our 5G products. More than 50% of our scanning receiver revenue was from 5G sales for new units and upgrades. We hold a dominant position in the US and believe the pending merger between T-Mobile and Sprint will accelerate their 5G rollout and increase the demand for our test and measurement tools. The new DISH 5G network will also provide additional opportunities.

We expanded our 5G scanning receiver portfolio in the second quarter by adding full 5G support to our *MXflex*®. The *MXflex* is the fastest 5G scanning receiver on the market, the only scanner that supports 4X4 MIMO in one unit, and the only scanner that measures 4G and 5G networks concurrently. In addition to purchasing new *MXflex* scanning receivers, customers have the option to purchase an upgrade for their existing units to add 5G measurements.

Upgrading units reduces the cost to support testing 5G and it provides a higher margin revenue stream for PCTEL.

Public safety has always been an important market for PCTEL. The demand for our public safety antennas remains robust and we continue to make progress in providing public safety testing solutions for first responders. The latest version of our inbuilding testing solution includes expanded capabilities to test P25 and LTE/FirstNet networks to include signal quality measurements. We are pleased that a major public safety radio system provider has agreed to feature our Public Safety solutions in their product catalog, which is distributed to their nationwide dealer network. We believe this is a growing market for performance critical antennas and scanning receivers and that we have the best solution to verify inbuilding communications for first responders.

Intelligent transportation systems enabled by multiple wireless technologies require precision RF engineering to provide gain and to limit interference in hostile RF environments. Our customized antenna systems will be deployed at approximately 15,000 traffic intersections in New York City, where urban canyons and reflecting signals can create a challenging RF environment. This opportunity accounted for a significant portion of our incoming antenna orders in the second quarter. Antenna deliveries for this order will begin in the third quarter and continue into 2020, which gives us some visibility of antenna revenue going forward. RF performance is important and in many cases custom mechanical engineering is just as important to meet form and fit requirements for demanding physical environments, such as for aircraft. We recently received an antenna

order for specialized GPS antennas to be used for tracking in commercial aviation as well as for military aerial vehicles and helicopters.

With respect to second quarter revenue, antenna revenue for industrial fleets and specifically, rail and precision agriculture, remained strong.

The Industrial IoT market for antennas, radio devices and systems is the largest long-term opportunity for PCTEL. Our products are used today in systems to provide wireless internet access for utility smart grids, sensor networks and asset tracking. We won a significant order in the second quarter to support a new sensor that monitors high power lines. This is significant because PCTEL designed and will manufacture the entire IoT sensor device, not just the antenna. We expect to launch additional Industrial IoT radio products in the second half of 2019. These product releases will be another step toward our long-term goal of becoming a leading original design manufacturer, or ODM, of customized Industrial IoT devices that include the radio, antennas and supporting systems.

I would like to spend a few moments to talk about China. We continue to support our customers in China and deliver products within the constraints of the executive order issued by the US government. I note, however, that 75% of our second quarter revenue was generated in the United States, up from 67% for the second quarter of 2018 and we expect this trend to continue.

Although our customer base is mainly in the US, China remains attractive for manufacturing our antenna products. We are in the process of transitioning a substantial portion of our manufacturing activities in China to contract

manufacturers in order to increase flexibility and reduce geopolitical exposure. This transition is expected to be substantially complete in late 2020 and result in an estimated 35% reduction in the Company's entire workforce.

Looking forward, I'm pleased with the increased rate and size of incoming orders driven by our high-quality engineered products and improved sales and marketing efforts to win business. Based on incoming orders in the second quarter and the global demand for 5G test and measurement tools, we believe the momentum will continue through 2019. As a reminder, incoming orders for the antenna products provide some visibility for future quarters for larger projects. The scanning receiver business revenue cycle is normally much shorter so entering the third quarter with scanner backlog is significant.

This is our third quarter with improved sequential results and I'm confident that we have the people and processes in place to drive consistent growth to increase shareholder value.

With that, I will now turn the call over to Kevin for a closer look at our second quarter.

Kevin.

Kevin McGowan

Thank you, David.

I will address the financial results for the second quarter ended June 2019 and I will provide third quarter 2019 guidance.

Revenues were \$23.5 million in the second quarter, up 9% compared to the second quarter 2018. Similar to the first quarter 2019, higher test and measurement revenues offset lower antenna product revenues in the second quarter compared to last year. Test and measurement revenues were \$7.5 million in the second quarter, the second highest revenue quarter ever for this product line. As David mentioned, scanning receivers for 5G continue to drive the top line as revenues for test and measurement products were 82% higher in the second quarter 2019 compared to the second quarter 2018 and were 36% higher sequentially. Antenna product revenues were \$16.0 million in the second quarter 2019, 8% lower compared to the second quarter of 2018, but 6% higher sequentially. Second quarter revenues were higher for antennas for public safety and fleet applications but declined compared to last year due to lower revenues for small cell antennas and because we completed a large non-recurring enterprise Wi-Fi project in the second quarter 2018.

The second quarter 2019 gross profit margin improved by 9.4% to 45.5% due to the favorable product line mix of test and measurement products and improved antenna gross margin percentage. The gross margin percentage for antenna products was 6.0% better in the second quarter 2019 compared to the prior year

primarily due to a more profitable mix within the product line, but also because of the cost reduction actions taken in 2018.

Adjusted EBITDA and non-GAAP earnings per share improved both sequentially and compared to last year primarily because of higher revenues and gross margins. Adjusted EBITDA margin as a percentage of revenue was 13% in the second quarter compared to 2% for the second quarter 2018, and 7% in the first quarter 2019. Non-GAAP diluted earnings per share improved to \$0.13 in the second quarter compared to break-even in the second quarter 2018, and \$0.04 in the first quarter 2019.

Cash and investments increased by \$1.7 million to \$36.8 million at the end of the second quarter 2019 as free cash flow was \$2.9 million during the second quarter 2019.

Now let's turn to third quarter 2019 guidance. We expect third quarter revenues will be between \$23 and \$24 million with higher sequential antenna product revenues. The gross margin percentage is projected to be in the range of 45% to 46%, and the non-GAAP earnings per share is projected to be in the range of \$0.12 to \$0.13.

Before we take questions, I would like to turn the call over to David to make a few closing remarks.

David Neumann

Thank you, Kevin.

We're pleased with our performance in the first half of 2019. We are seeing the benefits of the actions that we took in 2018 to reduce costs, realign talent and maintain a healthy R&D investment. Most importantly, I'm proud of our team for driving the necessary changes, executing on a daily basis, and the success they have had in developing new products and winning business for both 5G scanning and Industrial IoT opportunities.

We look forward to meeting with investors at two conferences in August. Kevin and I will be attending the Intellisight investment conference in Minneapolis on August 14th, and the Midwest IDEAS investor conference in Chicago on August 28th.

With that, Kevin and I are available to answer questions.

Operator?

David Neumann: Close

We're pleased with the results to date in 2019 and we look forward to finishing the second half just as strong. It is a real pleasure to see the team win with best in class antenna and scanning receiver products, and I would like to thank the entire team for their dedication and hard work. I've said this before - we are in the right markets and we are developing the right products. It comes down to execution and I'm pleased to see all the hard work is paying off for all stakeholders.

Thank you and have a great afternoon.