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Q1 2020 SiTime Corp Earnings Call

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PRESENTATION

Operator

Good afternoon, and welcome to SiTime's First Quarter 2020 Financial Results Conference Call. (Operator Instructions) As a reminder, this conference is being recorded today, Wednesday, May 6, 2020. I would now like to turn the call over to Leanne Sievers of Shelton Group Investor Relations. Leanne, please go ahead. .

Leanne K. Sievers ***Shelton Group - President***

Good afternoon, and welcome to SiTime's First Quarter 2020 Financial Results Conference Call. On the call from SiTime are Rajesh Vashist, Chief Executive Officer; and Art Chadwick, Chief Financial Officer. Before we begin, I'd like to point out that during the course of this call, the company may make forward-looking statements regarding expected future results including financial position, strategy and plans, future operations, the timing market, the impact of COVID-19, the company's outlook and the guidance as well as other areas of discussion. It is not possible for the company's management to predict all risks nor can the company assess the impact of all factors on its business or the extent to which any factor or combination of factors may cause actual results to differ materially from those contained in any forward-looking statement. In light of these risks, uncertainties and assumptions, the forward-looking events discussed during this call may not occur, and actual results may differ materially and adversely from those anticipated or applied. Neither the company nor any other person assumes responsibility for the accuracy and completeness of the forward-looking statements. The company undertakes no obligation to publicly update forward-looking statements for any reason after the date of this call to conform these statements to actual results or to changes in the company's expectations. For more detailed information on risks associated with our business, we refer you to the risk factors described in our 10-K filing which we filed with the SEC on March 2, 2020.

Also during this call, we will refer to certain non-GAAP financial measures, which we consider to be an important measure of the company performance. These non-GAAP financial measures are provided in addition to and not as a substitute for or superior to measures of financial performance prepared in accordance with U.S. GAAP. The only difference between GAAP and non-GAAP results is stock-based compensation expense. But please refer to the press release issued today for a detailed reconciliation between our GAAP and non-GAAP financial results.

I'd now like to turn the call over to Rajesh. Please go ahead.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

Thank you, Leanne. Good afternoon, and thank you, everyone, for joining us on today's call, especially in what has become an unprecedented time for the world. Recapping our first quarter, we delivered solid results with both revenue and EPS that were above our original guidance. Revenue of $21.7 million reflected the expected seasonality of mobile, IoT and consumer markets, while achieving a year-over-year growth of 47%.

Turning to how SiTime is doing in the COVID-19 pandemic, our actions, as you can imagine, have been focused on the safety and well-being of our employees worldwide. But we've also successfully transitioned to working from home with high productivity and morale at all our functional groups. Our customer interaction continues to be strong, especially in China and in North America, with good design win activity. Our success and ability to effectively operate in this new virtual environment is a testament to the strength of our team, markets and our products. And finally, it is a testament to the value we bring to our customers as they continue to choose SiTime for their challenging timing problems.

On supply, our multisource strategy has proven effective in maintaining timely product shipments. Our suppliers are operating with no major delays. However, that situation, as you can imagine, can change during these uncertain times. One of our strengths, which is the diversity of our timing and market segments, customers and products, has benefited us in this challenging environment. SiTime's 65 products have been designed into 200 applications across communications-enterprise, mobile, IoT, consumer and industrial, auto, aero and defense markets. Additionally, we serve over 10,000 customers that have chosen SiTime to solve their complex timing problems in industry-leading electronics. I'm happy to note that we are making excellent progress in becoming a trusted adviser and timing to our customers. Even while working from home, we are reaching our customers in many ways, ranging from one-on-one meetings to technical webinars during which we are able to help them design better products with our technical expertise. This approach continues to result in design wins.

As examples, at a Tier 1 customer of high-performance computing, SiTime was selected because we were 60% smaller and the most resilient to vibration. At another Tier 1 customer of data center equipment, one SiTime device integrated the complete clock tree, increasing system performance. In both these cases, SiTime was able to displace entrenched competitors because of the additional value that we provide.

On the technology front, we continue to establish a leadership position in the timing industry through a unique expertise in MEMS, mixed-signal and analog and system-level integration. Over the past 15 years, we have developed and have shipped 2 generations of MEMS resonators that are currently in use in our oscillators. Today, I'm pleased to reveal that our third-generation MEMS resonator, which have up to 2x better stability, are now ready. We have now sampled oscillators that use these resonators and have up to 10x better phase noise, simultaneously reducing power by up to 7x. These are dramatic improvements, and these dramatic improvements build on our history of delivering significant performance enhancements in every generation of the resonators that we produce. Combined with our other advantages such as environmental resilience, size and so on, we're building a new unique class of products that delivers higher value.

In the area of communications and enterprise, we continue to get strong design wins with our 12 Elite and Emerald family of products. I'm particularly excited with the breadth of design wins in 5G, one of the most prominent growth areas for our business. Currently, we're designed into 10 different 5G applications, including radios and test improvements. At a Tier 1 supplier of 5G RRU, remote radio units, we are the preferred provider of timing and have 11 design wins worldwide. We've also designed into multiple mobile edge computing applications, which is a growth area at customers worldwide. In all, 5G continues to be a focus area for SiTime, and we are well positioned to grow our business in this market in 2021 and successive years.

In summary, I'm pleased with our continued progress in our new product and design win activity for future growth. We believe that our focus on high-value applications and products allows us to deliver high growth and predictable revenue. Though there is uncertainty, especially in customer demand in the consumer IoT mobile segment, I believe we are well positioned to navigate this challenging environment with over $71 million in cash and an established leadership position in timing. We remain closely engaged with customers and continue to innovate at a fast pace as we disrupt the $8 billion timing market with our leading silicon MEMS solutions.

With that, I'd like to turn the call over to Art to discuss the financial results for the first quarter and our outlook for the second quarter. Over to you, Art.

Arthur D. Chadwick ***SiTime Corporation - Executive VP & CFO***

Great. Thanks, Rajesh, and good afternoon, everyone. We are very pleased to be holding our second financial results conference call as a public company. During my review today, I will discuss Q1 2020 financial results and will provide guidance for the second quarter. I'll focus my discussion on non-GAAP financial results and refer you to today's press release for a detailed description of our GAAP results as well as a reconciliation of GAAP to non-GAAP results.

First of all, Q1 was an excellent quarter for us. Revenue was $21.7 million, above our guidance range for the quarter. This was down 23% sequentially, reflecting the expected seasonality in our business, but it was up 47% over the same quarter a year ago. To provide some color on revenue by end market, I'll review our 3 major market grouping as I did last quarter.

First is mobile, IoT and consumer, which consists primarily of sales into mobile phones, wearable devices and consumer products. Sales in Q1 were $11.9 million or 55% of sales, down from $18.6 million or 66% of sales in Q4, reflecting typical seasonality for these markets in the first quarter of the year.

Next is industrial, auto and aerospace, which goes into industrial applications, automotive, aerospace and military applications and broad-based sales. Sales in Q1 were $5.5 million or 25% of sales, up from $5.3 million or 19% of sales in Q4.

And third is communications and enterprise, which consists of wireless infrastructure, including 5G, data center and networking. Sales in Q1 were $4.4 million or 20% of sales, up from $4.2 million or 15% of sales in Q4.

We had only one customer in Q1 where sales exceeded 10%, and sales to that customer were 34% of sales. Non-GAAP gross margins for the quarter were 46.1%. Non-GAAP operating expenses were $11.9 million or 55% of sales, almost evenly split between R&D and SG&A expenses. This was higher than in Q4 due to beginning of the year FICA taxes, a full quarter of costs related to being a public company and select new hires. The non-GAAP operating loss was $1.9 million. Net interest and other expense was $0.2 million. This generated a non-GAAP net loss of $2.1 million or $0.14 per share.

Stock-based compensation expense and related payroll taxes were $3.0 million, which are excluded from our non-GAAP results. Accounts receivable were $15.8 million, down from $17.7 million in Q4, with DSOs at 65 days. Inventory was $14.2 million, up from $11.9 million in Q4 as we built some inventory to protect against potential supply chain disruptions resulting from the COVID-19 pandemic.

In regards to cash, we generated $2.0 million in cash from operations and used $3.2 million for the purchase of assets and taxes paid on RSU grants. Out of an abundance of caution, given the current global contraction, we also drew down on a revolving line of credit to ensure increased liquidity during these unusual times. We drew $9 million, which increased our debt from $41 million at the end of Q4 to $50 million at the end of Q1. Our intention is to maintain this approximate level of debt until it's clear the economy is on an upward trend and then pay down some of our debt accordingly. As a result, we ended the quarter with $71.3 million in cash and equivalents.

I'd now like to provide some guidance for the second quarter of 2020. Prior to the COVID-19 crisis, we would have expected sales in Q2 to be up from Q1. But unfortunately, the current economic contraction will have some impact on Q2 revenue. Some of our markets are holding up well, but others are being impacted. We believe revenue in the second quarter will be down between 7% and 13% sequentially to between $18.9 million and $20.2 million, with a midpoint of $19.6 million. I would, however, like to point out that at that midpoint, sales would be 24% higher than the same quarter last year. And that's during this global contraction, which we think clearly shows the strength of our growth story.

I would now like to provide some further color on our various markets. We are seeing strength in communications and enterprise, especially 5G and data center, driven by increased demand from new product ramps in wireless, server and networking. We expect sales into these markets will increase 5% to 10% sequentially. In the industrial, auto and aerospace markets, we have a number of moving parts, but they are all generally positive. Broad-based industrial appears to be holding up well, and we expect sales to increase sequentially. Although the automotive market is a smaller portion of our business, we bring unique value to this market, and new programs are driving increased sales. And it's a similar story for aerospace, where we're also seeing increasing sales. Overall, we believe sales into our industrial, auto and aerospace market segment will increase 5% to 10% sequentially, same type of growth as with comms and enterprise.

The markets most affected this quarter are our mobile, IoT and consumer markets, which is not surprising since so many people are sheltered at home and retail stores are closed. It's difficult to know exactly how significant the impact will be since it is somewhat dependent on how quickly shelter-in-place restrictions are relaxed and how quickly consumers spend again. Our Q2 outlook for this segment is based on orders already booked by our customers as well as recent forecasts received directly from our customers. Needless to say, those forecasts could change as the quarter progresses. However, based on our current data points, we believe sales into our mobile, IoT and consumer segment will be down somewhere between 20% and 30% sequentially.

Gross margins are expected to be relatively flat with Q1, and though we expect an improved product mix, this will likely be offset by the lower overall revenue. We are managing operating expenses closely. We have temporarily slowed hiring and are aggressively managing discretionary expenses. Second quarter non-GAAP operating expenses are expected to be relatively flat with the first quarter, so somewhere between $11.8 million and $12.0 million. Q2 interest expense will be approximately $400,000, an increase over Q1 due to the higher debt level. Q2 share count will be approximately 15.2 million shares. Stock-based compensation expense will be approximately $3.1 million, and income taxes will be nominal.

For the balance sheet, we are planning a modest increase in inventory in order to build a bit more buffer in the event of any supply chain disruptions. Based on this guidance, we expect Q2 non-GAAP EPS will be a loss of between $0.20 and $0.24 per share.

Now we do not plan on providing guidance for the full year, but I will make a few comments. We expect revenue in the second half of the year to be meaningfully higher than revenue in the first half for a variety of reasons. First, we hope and believe the economy will rebound as the world opens back up over the next few months. However, more specific to SiTime, we expect a strong bounce back in our mobile, IoT and consumer business due to new programs and seasonality of that business. Sales will also be fueled by growth from specific design wins in targeted higher-growth markets. Furthermore, we expect gross margins to improve in the second half as we ship more of our newer, higher-margin products and as overall revenue increases. Gross margin should improve 2 to 4 points in the second half over margins in the first half.

So these are unusual times, but we believe SiTime is well positioned for strong growth in the future. We have an exceptional workforce, differentiated products that address large and growing markets, an enviable list of Tier 1 customers and a strong balance sheet. We firmly believe these strengths will allow us to manage through these truly unusual times and emerge stronger than ever.

And with that, I'd like to turn the call back to the operator for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Chris Caso with Raymond James.

Christopher Caso ***Raymond James & Associates, Inc., Research Division - Research Analyst***

I guess the first question is regarding what you're seeing in the IoT, consumer segment. I guess perhaps you could put that in perspective of the amount of -- the extent to which that is reflecting reduction in end market sales by your customer. If the customer is doing anything with regard to inventory, kind of how that plays in the second half. And again, you did talk about that improving as you go into the second half and perhaps talk about some of the visibility that you have there.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

Yes. Well, first of all, Chris, we do expect, as Art indicated, that the mobile, IoT business and consumer, to a slightly lesser extent, is going to show up for a couple of reasons. One is that it always does because Q3, Q4 are, in fact, the right time for that. The second is that we continue to get significant design wins in this space of -- that are pretty prominent in all the hearables, the wearables and consumer products that you would expect, such as the remote cameras and doorbells and all of that. So we think that our pipeline of design wins is very solid and growing quite nicely.

As far as what we hear from our customers on this, frankly, some of it is us just being cautious and some of it are pushouts by some of our customers who have --- some of the smaller ones in the space, in the wearable space, are seeing relatively low traction in these times. Some of the bigger guys have newer products that are waiting to come out. So I think that combination is what allows us to sort of say that it's lower in the coming -- in this Q2, but we're pretty confident about growth in Q3, Q4.

Christopher Caso ***Raymond James & Associates, Inc., Research Division - Research Analyst***

Got it. As a follow-up, I wanted to ask about the potential for supply disruptions, what you're seeing and perhaps how the customers might be reacting. I guess, firstly, have you seen any supply disruptions yourselves? We've obviously heard a lot of that in the space, particularly in back-end manufacturing. And then secondly, we've seen, in some cases, customers tend to pull forward some orders to protect against potential supply disruptions. I'm sure you guys would be watching for that. If you can give any visibility as to what your customers may be doing and the extent to which you can monitor that.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

Right. So there are really 3 questions: One is what have we seen in our suppliers, what have we seen behavior with our customers and the third one I'll throw in as one on competitors. So first and foremost, on the suppliers, we did have some rocky behavior in late Q1, particularly in regards to Malaysia, where there was a pretty sort of an overnight shutdown of the business. And that was a little bit scary. But it was deemed -- semiconductor business, as you may know, was deemed essential business and Carsem, which is a primary supplier, opened up and has done quite well for us since. The side point about competitors is that you will note that, in many places, of course, crystal is not -- crystal technology is not semiconductor technology. So in Malaysia, for example, they were not deemed as essential. So their plants continued to be shut down while SiTime continued to be able to ship. That kind of behavior has just seen -- has given us an added importance as a supplier because of supply chain. Other than that, our supply chain with Bosch on the MEMS side is solid, and we've been in constant contact with them. They have no issues whatsoever. They're continuing to operate the fab in a mostly normal way. TSMC continues in a very, very solid way. And then ASE and UTAC, our 2 other suppliers, have seen no change, no issues at all. And finally, the Carsem hiccup, which is in the end of Q1, resolved itself pretty quickly by the early part of April and so on. So I feel very confident about that.

On our customers, we have not seen any big concerns about pulling in so that they can have product. To the extent some of them did pull in, we know that they are trying to do this from -- with an abundance of caution, but we've reached out to them and explained to them how different our supply chain is from other timing products. And that appears to have had a significant amount of impact. We've done that with many of our customers. We have shown them our buildup of inventory, our buildup of MEMS, our buildup of CMOS, the fact that we are a fabless company, and I think that's given them good, good opportunity to sort of not do too many pull-ins. So I think all in all, supply chain has done well for SiTime and, in fact, is one of our strengths as we go into the timing market. We actually think that some of the larger customers will see the difference between us and, for example, some of the producers of high-end OCXOs and TCXOs who are suffering significant shortages because of shutdowns in places like India or Europe or other parts of the world where they have factories and most of the factories are not working.

Operator

And your next question is from Blayne Curtis with Barclays.

Blayne Peter Curtis ***Barclays Bank PLC, Research Division - Director & Senior Research Analyst***

Kind of curious when you look at the comm segment and somewhat the industrial, auto as well, those segments are based upon ramping new products. And I'm kind of just curious in this environment whether any of those products, you have the wins, but whether the end products will get delayed in terms of the ramp. And I guess as part of that, if you can just address, like, Rajesh, you or Art -- you said a significant second half, I guess, based versus what you would have said 3 months ago for those segments. I'm just curious if it's still on track.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

Generally, they're still on track. There is -- there are 1 or 2 customers that we think have pulled back a little bit just because of the market condition. These are smaller customers. But generally, if you're looking at either RRUs or edge computing or backhaul or fronthaul or microwave, all of these small cell, all of these continue to be deployed. In fact, we think that they might even be deployed with a greater sense of urgency if you see what some of the big guys like Verizon and others are doing. The other thing that's happening is in the data center area, which has not been a huge, big area for us, we are seeing traction, particularly in China, where we see a resurgence of China, Chinese products for China manufacturer. For Chinese consumption, sorry. And we see this in the area of data center, but we also see this in the area of just high-end processing, with high-end processors coming out of China that would compete with processors in the United States, for example. So we see more strength in this market, not less, and we are pretty happy with our traction. And the breadth, as I pointed out in my prepared remarks, I was really happy to see that we have our 12 of our Elite and Emerald products are being put out into 10 different applications. And for example, I never would have expected radios and -- not radios, but test instruments as one. Very happy to see that. And of course, these are higher ASPs. So that's why we can connect that to increase in gross margins as we go forward in the year.

Operator

Your next question is from Tore Svanberg with Stifel.

Tore Egil Svanberg ***Stifel, Nicolaus & Company, Incorporated, Research Division - MD***

Yes. So I know you're not giving full year guidance. But if you look at historical, you tend to have sort of this 40, 60, first half versus second half ratio. Is that the way we should be thinking about 2020 as well?

Arthur D. Chadwick ***SiTime Corporation - Executive VP & CFO***

Yes. Again -- Tore, this is Art. I don't want to put hard numbers on it because we're not giving hard guidance for the year. But clearly, if you look at our 2018 and 2019 fiscal years, the back half substantially stronger than the first half. And we feel pretty confident that, that's how this year is going to look also. We just have a lot of growth drivers that will drive some pretty significant increases in revenue in the back half. So again, I don't want to put a number on it. But we're pretty bullish about Q3 and Q4 at this point.

Tore Egil Svanberg ***Stifel, Nicolaus & Company, Incorporated, Research Division - MD***

Very good. And when we listen to some of your larger cap peers, they're kind of entering June quarter with pretty high backlog levels and quite a bit of orders. But they're also kind of haircutting those given the environment. How did your backlog and how your bookings sort of performed here over the last few weeks?

Arthur D. Chadwick ***SiTime Corporation - Executive VP & CFO***

Yes. Given the global contraction, I kind of would expected some of our customers to hold off on orders, but that has not happened. Again, we don't want to get too specific about what percentage is booked. But I will say this. We are more booked where we are today going into Q2 than we were in either Q1 or Q4. So I would concur with those observations.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

And we looked at it, particularly in light of the comment -- or question earlier about how much of it are pull-ins. And we did shake that tree, and we don't think that these are significant pull-ins. We just think that people are just placing orders better, and I think it's working out much better for us.

Operator

Your next question is from Quinn Bolton with Needham.

Quinn Bolton ***Needham & Company, LLC, Research Division - Senior Analyst***

I apologize because I got dropped from the call during some of the prepared comments. But just wanted to come back to the gross margin. Art, I think you said margins up 2 to 4 points in the second half versus the first half. And is that still sort of the same drivers of better mix, better absorption, taking some business direct and just the ramp of new products?

Arthur D. Chadwick ***SiTime Corporation - Executive VP & CFO***

Yes. I think you listed it just quite well, Quinn. That's exactly correct. As we've always talked about, our newer products have higher ASPs and higher gross margins. As that becomes a larger percentage of our sales, that helps blended margins. As we take more sales direct, that cuts out the distributor for those particular sales, that leads to higher margins. Higher revenue helps our manufacturing overhead absorption, so that leads to higher margins. So all of the above is true. And I feel very confident that, that should be happening in the back half of the year. So we guided up 2 to 4 points. If things work in our favor, it could be at the high end of that range or even a little higher. Obviously, if we have a very, very strong consumer, mobile, IoT, that may obviously help the top line, but temper a little bit of the gross margin percentage improvement. But in either case, those are good news scenarios.

Quinn Bolton ***Needham & Company, LLC, Research Division - Senior Analyst***

Great. And then just a follow-up on Elite and Emerald. It sounds like those design wins are still largely on track to ramp in the second half. And Rajesh, I think you mentioned some of the applications like remote radio heads or 5G and data center servers. But just want to make sure that on the Elite and Emerald, that there's been no significant delay or pushout in some of the bigger design win you have with those.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

That's right. In fact, as I said, we might even be seeing a little bit of an acceleration in some of them. We're very happy with the success of that. We have -- we have this -- the strategy of taking a platform product like Elite and then doing multiple derivatives of it. And the derivatives of Elite in the last 4, 5, 6 -- 4, 5 months have grown remarkably because these derivatives are either MIL spec or they are automotive spec or they have features like a VCXO or differential or TCXO that are added to it. It cost us relatively lower to produce these derivative products, yet they have a significant impact on revenue, and we continue to push that strategy. And certainly, Elite has been very, very instrumental in that, and Emerald is just getting to that level right now.

Quinn Bolton ***Needham & Company, LLC, Research Division - Senior Analyst***

Great. And then just last question for me. In the automotive, industrial, MIL or aerospace bucket, wondering if you could give us some sense how much of that is automotive. I would think automotive and consumer are probably some of the harder hit segments of the business with the COVID outbreak. But I was specifically wondering how much of the -- that bucket is automotive today. Or is it more industrial or aero?

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

Automotive is probably -- automotive, Quinn, is probably the smallest. We think industrial, as I've always said, is one of the largest. And defense is slowly growing. Not very big, but of course, very profitable. And the aerospace business is doing very well for us. So we do very well because that's a good combination of volume, ASP performance and we have multiple design wins in many, many satellites and so on. So I think automotive, we -- it's holding its own. It's directionally up. It's not very large. It's directionally up. But in the long run, we are seeing that the automotive design wins we are getting or the ones we're being considered for are those, again, where we bring exceptional value. And that business continues to take SiTime and design with SiTime. And these are in the areas of UWB. These are in the areas of of SerDes for serializer, deserializers for -- in the working in the cars. These are in the area of 1588, in the area of cameras, radar, LiDAR. All of these are great examples of business for SiTime.

Operator

And there are no further questions at this time. I'll turn the call back over to Mr. Chadwick at this time.

Arthur D. Chadwick ***SiTime Corporation - Executive VP & CFO***

Great. Thanks, operator. Well, that concludes our call today. We want to thank everybody for spending the time and listening to what we had to say. We hope everybody is safe and healthy. And we look forward to having another conference call in a quarter, hopefully with good results by the end of Q2. Thank you, everybody. Have a great day.

Rajesh Vashist ***SiTime Corporation - Chairman, President & CEO***

Bye-bye.

Operator

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