REFINITIV STREETEVENTS

EDITED TRANSCRIPT

SITM.OQ - SiTime Corp at Barclays Global Technology Conference

EVENT DATE/TIME: DECEMBER 07, 2023 / 7:35PM GMT

CORPORATE PARTICIPANTS

Rajesh Vashist *SiTime Corp - Chief Executive Officer, Board Member*

CONFERENCE CALL PARTICIPANTS

Tom O'Malley *Barclays - Analyst*

PRESENTATION

Tom O'Malley - *Barclays - Analyst*

All right, welcome back to the Barclays Tech Conference. I'm Tom O'Malley, Semi and Semi-Cap Analyst here at Barclays. Lucky enough to have SiTime CEO Rajesh Vashist with us. Thank you so much for being here.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

It's a pleasure.

Tom O'Malley - *Barclays - Analyst*

I think you want to kick off with some disclosures, and then we can hop into some chat.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

That's right. Last time I did one of these, I was going to try to read this. But I'm not going to put you through that pain. But the usual disclaimers on this. That's it, right?

QUESTIONS AND ANSWERS

Tom O'Malley - *Barclays - Analyst*

All right. Perfect. All right. So again, great having you here today. It's been a busy couple of weeks for you.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Yes.

Tom O'Malley - *Barclays - Analyst*

So I want to start out with the Aura clock business that closed last week. Could you talk about why you did that deal from a strategic perspective? And why was this such a must-have asset for you?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Right. So SiTime, as you know, is focused on timing. And timing has two or three components to it. One is the oscillators, which is most of our business. The resonators, which is business we're going to grow into. We know how to do that natively. But the clocking business is one that we have talked about since the IPO, and one we wanted to get into significantly. It is because the oscillators we sell and the clocks that we now will sell sit at the same motherboard, the same systems that customers consume. So it fulfills our promise of being a single-stop purveyor of all timing-based products. And we found one of the best companies with the best technology. We found it at a fabulous price. So the rest of it was just the hard work of doing it.

Tom O'Malley - *Barclays - Analyst*

Yeah. So does this take you into another realm in terms of the competitive environment? When you're moving into more of a full solution, does the competition change? And does your go-to-market need to change at all?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Absolutely. So as you recall, we've been competing against quartz crystal vendors, people like Epson, Kyocera, TXC, et cetera, mostly Asian. The quartz business is a 60-, 70-year-old technology. So there's a general slowness of innovation in this business.

We now move into clocking, which is a companion chip to oscillators. And in clocking, our competitors are Renesas, TI, Skyworks. And competitors like that are clearly a little bit more semiconductors. They're more aggressive. But at the same time, they're not very focused on timing. Most of them are $10 billion-plus revenue companies. And the timing piece of it is about $100 million, $200 million business. So this is not something of investment for them.

So it gives us the edge in going to our customers in the networking telecommunications market, whether it's a Google or it's an Infinera or it's a Nokia, and giving them a full solution, fully integrated. It's a game changer for the customer.

Tom O'Malley - *Barclays - Analyst*

When you look at the model and how that changes when you're moving to this full solution, both from a spend perspective and from a margin perspective, can you help just give us a feel how your business changes? Your go-to market seems like it has to change slightly because there's new competition. But it's easier for you, right? You bring more to the table. But how does it impact your P&L?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

So at the top level is where the biggest contribution is. It's a little bit slower to get to revenue because it needs some momentum. It needs a design momentum. And we're not getting any revenue. So we're going to get the momentum and revenue as we go. So we'll probably call it '25, '26.

The gross margin is actually favorable. Most of Clocks sell around 70% gross margin. So it's a more favorable business. And on the OpEx side, because we're getting fully formed business or fully formed, excuse me, products from Aura, 50 products by the early part of '25, it's going to be relatively low impact on the OpEx. So that sounds like a pretty good deal, something that grows your top line. The gross margins are equal to or greater. And the OpEx impact is relatively light. So that's another reason why I like this business.

Tom O'Malley - *Barclays - Analyst*

Very helpful. So from a broader perspective, zooming out of it, you talked about the model. You've talked about the strategy and the customers. You've done a very good job historically about talking about your TAM and SAM, both of which have kind of grown. What does this do to both of those? Does it expand your market? And do you think that your served addressable market is a bigger increase than your TAM, meaning you could go into a lot more areas than you couldn't have previously?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Absolutely. So there are the numbers. And then there's the actual customers we go with. So the best part of this thing is that we go to the same customers. We go to the customers that we're already talking to. And they've been underserved by some of our competitors, because this is not an area of investment for them. So many of them are relieved to find us owning this part of the business, particularly in the area of networking, telecommunications, data center, which is a big, important piece of business for us, but also in automotive, also in aerospace, and that portion of the market.

Now, as far as when we look at the impact on the business, I think all of that gives us a very strong impact on the business. It just takes a little bit longer. When we did the deal, we had to do sort of a creative deal. We couldn't do a full acquisition, because Aura had revenue coming out of entity-banned China companies. So we basically took the rest of the world for this business.

Tom O'Malley - *Barclays - Analyst*

Helpful. Do you feel like this is the last acquisition that you need to complete the portfolio? If you look at just the three moving pieces that are in your industry, you've covered them all now. In this year, yeah.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Yes, in this area. In this year.

Tom O'Malley - *Barclays - Analyst*

In this year. Oh, excuse me. So do you think that there is an additional asset that is a must-have, or do you think that there is a direction that you see the business going where you need something that's inorganic?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

So the fact is that you're absolutely right. We did fill in a gap with 50 products to come in our business that was the clocking piece. The other part of it is that we didn't get any revenue with it, so it's a slower ramp to revenue. So if by chance we could get a clocking business that was already had revenue, that would be a pretty good deal to get. In the area of MEMS technology, we don't see anybody. But we do see that timing is becoming more important. People continue to buy timing as IP. There are people who sell timing-based software. There are people who sell timing modules. There's people who sell timing-based systems. Some of these systems, for example, sell for $100,000, $200,000.

So I'm not saying that SiTime is going into those tomorrow, or even day after tomorrow. What I am saying is SiTime is focused on timing. SiTime is focused on delivering the world's most innovative timing products. And so that's what keeps my eye looking for companies to buy, or not buy, or partner with.

Tom O'Malley - *Barclays - Analyst*

Super helpful. So yeah, I think we've covered the M&A portion early. I want to move to a topic that I think I've started most conversations with this week, which is just the cycle. So you've clearly seen this exacerbated cycle. You guys experienced it, as everyone else did. But I think you're talking about a first recovery here in December, which is a good sign. How are things tracking sense earnings? In what areas of your business are you seeing that are turning on, that are leading to you being so confident about a recovery from here?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Right. So the general message for anybody, ourselves included internally, is that when a downturn happens, there's no place to hide. We, as management teams of companies, look for places to hide, but there isn't any. So we embrace that early on. Last year, we said we saw the downturn coming consumer. Then we started poking at all the businesses. And we saw that there was no running from that. So we embraced that. We called a down on network telecommunications, on data center, on automotive. The only one which hasn't turned that much is aerospace and defense. But even that has not gone down, but that's flattened out.

On the other hand, we called the up, which happened for us in Q3. So consumer was, as you would expect, the up. And it's leading to some increases in data centers. It's leading to some increases next year in electric vehicles, particularly in China. So we see all of this coming around the fact that our customers, and specifically their CMs, are digesting all the inventory. We think that that is done by the middle of the year, coming year '24, and that we start to get normalized in Q3, Q4. And we're looking for 2025 onwards, for the next few years, to be significantly growth years for SiTime.

Tom O'Malley - *Barclays - Analyst*

Do you think there's a difference in inventory levels between the CMs and your end customers? Is there worse behavior in a certain end market versus another? I know that you had called out the consumer downtick prior to some of your other core end markets. But I thought what was very beneficial to you is that the areas in which you said that you were originally going to win back from the IPO started to recover, too.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

That's right.

Tom O'Malley - *Barclays - Analyst*

So can you just talk to what strengths are you seeing in those core markets? And are those the big customers coming back? Or is that across the board?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

So the consumer business is coming back. We see our biggest customer come back. We see some pick up in some of the other consumer products and the light industrial. But in general, I would say sometimes that those companies are, because they deliver slimmer margins, they pay greater attention to operational issues such as inventory. Sometimes companies that are consuming $5,000 chips and $20,000 chips or $40,000 chips, they are less focused on a $5, $10 chip. And we know what kind of companies those are.

So our job now has begun not only to pay attention to the OEMs, but also to the CMs. Our top 50 OEMs represent 150. Our 150 CMs represent the top 50 OEMs. So we're trying to get as high a level of clarity on an ongoing basis and trying to build reporting structures. Nothing fancy, just salespeople pushing hard and trying to figure out where CMs are. And we think that that's going to be very valuable.

Tom O'Malley - *Barclays - Analyst*

One unique feature of this cycle, other than the rapid build of inventory at the end, was just the pricing dynamics. And I think companies, both because of wafer cost increases as well as the ability to pass through cost end customers without demand deteriorating, saw a massive increase in both their gross margins as well as their ability to kind of hold price. Where is pricing today for you guys versus where you started at the beginning of the cycle? And do you think that these levels of pricing are sustainable?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

So as far, shortly as Q3, we said that we have seen a steady growth in ASPs. And even in the results on Q3, we talked about ASPs either holding or not declining or increasing. So one of the features of SiTime is that we're accessing a $10 billion market. And we have, as of now, a $2.5 billion SAM. And as of now, analysts, such as you, have us at $200 million for the coming year. At that level, it allows us to have a huge playing field for us to pick and choose the differentiated business that needs our differentiated product.

And the buy side of the aspect of that is that's high-priced product. So we have started to lead with premium pricing since the pandemic. We've found that not only do customers buy us because of performance reasons, and there's about 15 different reasons to buy us on performance reasons, but they also buy us on supply chain.

And there's about six reasons, which have to do with programmability, capacity, quality, reliability, and focus on that. So we're finding that 80% of our business is single source. You can imagine that gives us significant pricing ability. And we're not gouging on price. We think our price premiums are fair price premiums for what we deliver.

Tom O'Malley - *Barclays - Analyst*

And I think that's something that's been unique is the resilience of your gross margin profile. You guys are talking about a recovery back to that mid-60s range by even the end of the year. How do you get confidence in that? Is it just because you can go out and lead with price? Or are there any other factors that help build that confidence?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Well, some of it comes mechanically. As we get back on revenue, we get to claw back a few percentage points, about 5 percentage points with the overhead. If you go back to $60 million a quarter, all of that takes care. We get back five points just through that.

But then we do have the pricing. The other thing is the pricing mix has shifted. So we are shipping more and more higher-performance products, which tend to be higher price.

But we've also taken this opportunity to focus on cost. And even though we still have high-cost wafers, particularly in the MEMS area, we are paying attention more to yield. We're paying attention more to spending minor CapEx for better enhancement of product cost.

Tom O'Malley - *Barclays - Analyst*

And then at the same time, you also are introducing new products, which I would imagine it's very easy to lead with price on new products as well. So can you talk about, or at least refresh the audience of a couple of new products that you've announced? And then can you give us the timeline for when you're going to announce your first integrated product? I think you gave some timeline on that when you did the deal.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Right. So first of all, today we introduced the Endura Epoch product line. So Endura is our mill aerospace, especially hardened product lines. And in that, we introduced our highest-price oscillator for the commercial market. In the commercial market, the Epoch product goes for $30. So it wouldn't be hard to imagine that in the military aerospace defense, that would be 5x to 10x higher price. So that's an example right there of higher price.

Another product that we introduced some time back was the Cascade product line, which was our first, actually, Aura product, in a sense. We didn't share it openly. But we OEMed the Aura clock. We integrated it with our oscillator. And we won about 10 design wins -- sorry, excuse me, 100 design wins. And we hope to have solid revenue around the $10 million range for that in the coming year.

So that, in fact, answers the second question about integration. Integration is not that hard to do. It's not that easy, but it's not that hard. And we're already selling those integrated products. So we have the one plus one equals three between the clocks and the oscillators already demonstrated.

Tom O'Malley - *Barclays - Analyst*

I want to pivot to the competitive environment. So you've talked about the new competition that you're getting into with the acquisition. But historically, the quartz competitors had capacity issues during this period of time, right? And so if someone comes to you and says, hey, I think that most of those customers would actually go back to the cheaper option, at least in the lower-end markets, how would you respond to that? And two, in your higher end markets that you've always outlined as core to your business and the differentiation from a technology perspective, why do you keep them using your product versus moving to a cheaper solution?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

So the quartz issue of quartz supply becoming easier already happened in the first half of '22. So we've now been for more than a year in the regime of having easy supply of quartz crystal.

Now, a side point on quartz crystal is that there's no such thing as easy supply. They still have 22-week lead times. In some cases, they have 35-week lead times. And the so-called ordinary lead times are just 14 weeks to just pick on something. So it's never a great supply situation in the world of quartz.

But the point is that we've already experienced that. And in my opinion, we hardly lost any revenue as a consequence of that, primarily because those who came to us at that time all appreciate the quality, reliability, the supply chain aspects of it, even if they didn't want the performance aspects of it.

Now, switching to the people who want the performance aspects, it's our job. It's our engineering job. It's our marketing job to deliver products of such exceptional value that, quote, customers just got to have it. So that's what we lead with. And if it takes us six years to develop, like it took us to develop the Epoch product, took us six years to develop it, to get it to a level where on nine metrics with quartz crystal, we beat them on eight, that's the kind of product we want to win. I like to join battle where the battle is already won before the battle is joined. So we do that by defining the products early for winning.

Tom O'Malley - *Barclays - Analyst*

So you talked about that $200 million mark, and you also talked about being selective in where you went with your product, because you have that ability and can lead with price. When you have that capability, you oftentimes can steer some of where your revenue goes into markets you want it to go, because you have that luxury. When you look at your end markets into '24, could you just walk through, either rank order or just give some comments on each, about where you see the most growth in getting to that $200-million range?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

So I think that data centers continue to do well for us. I think that even in the radio access networks, there are certain markets, India, Turkey, the Balkans. So these are small markets with small revenue, but they look like positive places for us. We see industrial, and in industrial, there's robotics. There are farm equipment that we see doing well for us. Consumer continues to do well. And automotive, in particular, automotive out of China continues to do well -- not continues, starts to do well, to be more accurate. And also, finally, the aerospace business, whether it's a Viasat or a Cooper satellite or a SpaceX, we're in -- we think that that's a good business to be had.

So we see, in the second half of the year in particular, we see a nice steady growth of pretty much every piece of business. And that's why we think we get to exit Q4 at, quote unquote, normalized run rate, maybe not at the levels of '22, but still very healthy, setting us up for '25. Because my eyes are on the '25 price. We want to do well in '24, but we want to do exceptionally in '25.

Tom O'Malley - *Barclays - Analyst*

And is it just the rolling on of new products from the acquisitions you just did that add to that '25?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

And the fact that we would have had two years with our own native developed products, products like Epoch, products like Elite RF, products like Elite X, they will have greater time to get the design wins. And by the time, they'll be in full flight.

Tom O'Malley - *Barclays - Analyst*

So I just want to dive a little more into the consumer and market, just because that market moved the most. And that market would also be subject to some of the customers that were most at risk to switch from quartz and then switch back, right? What do you think the right run rate is for that business? And then with the largest customer that you have in that business, you guys have gone through a variety of different content changes there. What are your expectations there?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Well, we think that our largest customer continues in their consumer products, where we add value in the watch, in some of the audible products, in the computing products. I think we reach a base level of keeping us around the 25-percentage mark. So I think that's a good number for us for next year. Consumer gets us to, what, 30, 35, depending on how things go. Yeah.

Tom O'Malley - *Barclays - Analyst*

And then in terms of the enterprise, mil-aero, auto, et cetera, could you point out one particular area that you think as an end market is going to offer the most growth for you? Because you've talked about content at those customers being very strong and the desire to have a higher end of technology. But if you were to pick one area into the '25 time period, which you're the most excited about, you're bringing these new products to the table. What end market are you marrying that with? Is that across the board, or can you pick a couple?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

I would pick the data center market. Because whether it is in the rack or on top of the rack, whether it's an optical, whether it's in switching, whether it is in computing, whether it's in acceleration, I think SiTime, particularly with the Aura products, is in an exceptional position for getting revenue out of those markets. So I think it'll do well. I think it'll do really well for us.

Tom O'Malley - *Barclays - Analyst*

Generally, with timing, you scale with the market as a whole, just because you have so much exposure to almost every digital device. When you look at a theme that we're talking about with all our companies here, which is AI, when you assess what could that do for your company, do you have some specifics in what you think that could add to growth? Or do you just think broadly, hey, more servers, more GPUs, more success for us?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Yeah, so that is in fact the right answer for now. More servers, more GPUs, more performance-based products from SiTime. But what we haven't quite understood fully is what does AGI do? What is the level of synchronization? What does latency do in that business? And it's such early days that we've given ourselves about a couple of quarters to figure it out. But I just have a hunch that that's a big growth market for us, we just have to identify in what way, in what time, with which customers.

Tom O'Malley - *Barclays - Analyst*

One thing that is more of a CFO question, but I'll give it to you because you're well-versed. Inventory levels on your own balance sheet ticked up during this period of time. And I think two of the questions on the call, you said most of that was wafer stock. You wanted to make sure that you had supply. Could you talk about, one, where is the target for inventory for your business? Or where should, from a day's perspective, or even dollars, if that's helpful, where should that go? And then, other than that wafer stock, are you holding any other product there that is a problem? Or is it really just safety?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

It's almost all wafer stock. And in that, I would say 70% of that is particularly MEMS wafers, which have a eight- to nine-month lead time. And given that we are 80% single-sourced with some very critical customers, we think it's prudent to have inventory.

Now, the other factor, because even based on that, I think it's a little bit higher for what I would like, but there are two other reasons for having done this. One is we have a very reliable supply chain and it pays to keep it running smoothly. It pays to keep Bosch and TSMC and all our backend guys running smoothly, keep our testers up. So, to some extent, we overbuilt just to keep the supply chain lubricated, as it were.

The second reason is more me, which is that I think that if we didn't understand what speed the market would go down at, I think we're not going to understand what speed the market will go up at. And therefore, that's an opportunity for us because we'll have the product, we'll be able to satisfy demand, and I see that as a prudent use of resources. Having said that, I think where we are is pretty much the height of absolute dollars. We should probably be about $10 million or so less on a running basis.

Tom O'Malley - *Barclays - Analyst*

Okay. We have a couple minutes left, I wanted to open it to the crowd if there was anything here, and I have a couple more if there's none. Something that's also coming up in terms of companies that saw pricing increases is just wafer costs, right? So you clearly saw the ability for TSMC and others to raise pricing, that led to companies raising pricing, and oftentimes that has stuck. If you see, and I think there's been a resilience from the foundries to keep pricing high despite falling utilizations, I think that many think the next step is some leniency on pricing such that they get utilizations back higher. If you see your foundry partners being more lenient on pricing, do you feel like you're in a position where you need to give that cost break to your customers?

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

You know, when the cost of goods went up, when the cost specifically of TSMC wafers went up or Bosch wafers went up, we didn't pass it all on. We passed some of it on and some of it we ate. Therefore, when it goes away, it's unlikely that we're going to go back and offer anything substantial in price reductions as a consequence of that.

The other part is that, as you rightly point out, some of these guys are sticking, these guys, the wafer foundries, are sticking with their prices, because why not? They like that and they can sort of get away with it. And foundry business is now the new oil business, right? So I think we're here to stay with those price increases. I don't see them going away.

Tom O'Malley - *Barclays - Analyst*

Helpful. I had one more on the acquisition. When you look at the earnouts, could you give us a little color of what those are based on? Is it just standard revenue hurdles or is it product hurdles? Any color there.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Yeah, so we have two kinds of -- we call only one of them an earnout, but the other one, $148 million plus a $2 million SLA, $150 million, is also in a way not quite an earnout, but it's based on performance. So it's based on delivery of products as they go. So that $150 million, for example, we paid $36 million because we got 20 products right away at the close on Friday. As the year progresses, we're going to pay something at max, something like $70 million to $75 million if we get all the products that we're supposed to get in the remaining, the first quarter of '25. So that's also in a sense of kind of an earnout.

But the earnout earnout is based on revenue that SiTime produces with those products. And based on the goodness of those products, based on the goodness of the performance of the products, we think that'll be accepted. And if that's accepted fast, we give them revenue. We give them the earnout. And it's over five years and it has a cap of $120 million. Most of it, because it's based on revenue, is probably skewed to the last two years, so '28 and '29. So probably almost nothing gets paid in '24 and some smaller amounts get paid in '25 and then increasingly onwards.

Tom O'Malley - *Barclays - Analyst*

Very helpful. It sounds like exciting times ahead. Thank you very much for being with us.

Rajesh Vashist - *SiTime Corp - Chief Executive Officer, Board Member*

Thank you and welcome to your new job.

Tom O'Malley - *Barclays - Analyst*

Yes, thank you very much. I appreciate it.
