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IMI - Q2 2017 Intermolecular Inc Earnings Call

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## CORPORATE PARTICIPANTS

**Bill Roeschlein** *Intermolecular, Inc. - CFO & Principal Accounting Officer*

**Christian F. Kramer** *Intermolecular, Inc. - CEO, President & Director*

## CONFERENCE CALL PARTICIPANTS

**Arthur Su** *Needham & Company - Analyst*

## PRESENTATION

### Operator

Good day, ladies and gentlemen, and thank you for standing by. Welcome to the Intermolecular, Incorporated second quarter fiscal year 2017 earnings conference call. (Operator Instructions). I would now like to introduce your host for today's presentation, Mr. Bill Roeschlein. Sir, please begin.

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### Bill Roeschlein - Intermolecular, Inc. - CFO & Principal Accounting Officer

Thank you, Howard. Good afternoon. And welcome to Intermolecular's second quarter 2017 earnings conference call. We announced our results after the market closed today, and you'll find a copy of the press release on our website at [www.intermolecular.com](http://www.intermolecular.com). On the call with me today is Chris Kramer, President and Chief Executive Officer.

Today's conference call contains forward-looking statements. Any statement that refers to expectations, projections or other characterizations of future events, including financial projections or future market conditions, is a forward-looking statement. Actual results may differ materially from those expressed in these forward-looking statements. Intermolecular assumes no obligation to update these forward-looking statements, which speak only as of today.

For more information about factors that may cause actual results to differ materially from forward-looking statements, please refer to the press release we issued today as well as the risks described in our Form 10-K for fiscal year 2016 as filed with the SEC, particularly in the section titled Risk Factors.

Before we begin, please note that during this call we will discuss non-GAAP financial measures as defined by the SEC and Regulation G. We believe non-GAAP financial measures provide useful supplemental information to both management and investors but note that these measurements are not a substitute for GAAP and should only be used to evaluate the company's results of operations in conjunction with corresponding GAAP measures. All non-GAAP measures are reconciled to the most directly comparable GAAP financial measures in our press release issued today.

Now I would like to turn the call over to Chris. Chris?

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### Christian F. Kramer - Intermolecular, Inc. - CEO, President & Director

Thank you, Bill. Good afternoon, everyone, and thank you for joining us on today's call.

We continue to stabilize our business and drive for growth and profitability. I believe that the second quarter 2017 results mark a key milestone in turning around our business. Building a broader and higher-velocity pipeline remains my top priority. It is a key element to build a successful business.

Our pipeline of programs continues to grow not only in numbers but in diversity of customers and work performed. This quarter, we signed three new deals during the quarter and have started out the third quarter on solid footing with the signing of a significant returning customer.



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New deals provide the basis for our positive revenue outlook for the remainder of the year. The signed deals are in line with our strategy to strengthen our position in the semiconductor ecosystem and focus on the advance memory market. Returning customers are proof of our strong value proposition and our ability to execute customer programs successfully.

Establishing a solid and diverse pipeline also allows us to have better visibility [of] future revenue. You will have seen in today's press release that we are now providing an outlook for the second half of 2017 financials. Our growing bookings and expanded number of customers enable us to better manage the inherent choppiness of materials in the nation's services. Programs have a defined timeline. And as they end, we are focusing on securing additional bookings to ensure continuity of work for our organization as well as establishing a steady flow of revenue. This model only works with a large and diverse customer base.

From a technology point of view, we continue to strengthen our position in advance memory. At the 2017 Flash Memory Summit, we announced our high-throughput experimentation platform for the discovery and development of new materials for next-generation nonvolatile memories like 3D XPoint.

Selector elements are key to improving performance, density and reliability. Along with our industry partners, we've demonstrated that chalcogenide materials are excellent candidates for MDM selectors. But without Intermolecular, MDM selector development would be more expensive, more time consuming and more difficult.

We've configured our platform to enable memory makers to perform rapid and numerous experiments to find the right chalcogenide combinations for their next-generation nonvolatile memories. We expect more interest and additional traction from potential customers in the months to come.

Our internal R&D efforts are limited but focus on select areas supporting our main strategy to strengthen our materials innovation business. We are making excellent technological progress with positive results that will lead to additional revenue within 2 years.

As we engage more customers, we are conscious of controlling our costs and keeping our investments in line with our plan to establish sustained profitability. The cost reductions we've implemented in the last quarter are bearing fruit, and the organization has embraced a leaner and more efficient way of operating.

In summary -- we are making solid progress along the plan we've outlined previously: number one, sign two to three new deals per quarter to drive revenue growth; number two, establish a cost-effective, efficient and customer-centric organization; number three, build a broader and higher-velocity pipeline; number four, keep our costs under control while managing our growth. I believe we've gained excellent ground as we continue to advance towards building a scalable and profitable advance materials innovation company.

Now I'd like to return the call to Bill to go over our financials.

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**Bill Roeschlein** - *Intermolecular, Inc. - CFO & Principal Accounting Officer*

Thank you, Chris.

Let me review some selectives financials for the second quarter of 2017. IMI revenue for the second quarter was \$8.1 million, down 18% sequentially compared with the previous quarter and down 31% from Q2 the prior year. Program revenues of \$6.5 million represented approximately 80% of total revenue in the quarter, with licensing and royalty revenue of \$1.6 million, representing approximately 20% for the quarter. As a reminder, the previous quarter's results were positively impacted by the one-time sale of certain patents following the conclusion of a customer engagement.

In the second quarter, we had two customers which were each greater than 10% of total revenue. These two customers represented approximately 82% of total revenue in the second quarter of 2017. For the second half of 2017, we expect revenues in the range of \$18 million to \$18.5 million.

I would like to remind you to please review today's earnings press release for both GAAP and non-GAAP measures and reconciliation between those results. The key difference from GAAP to non-GAAP measures is the exclusion of stock-based compensation expense. On this basis, GAAP



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and non-GAAP gross margins in the second quarter were 68.5% and 69% respectively, compared with 70% and 70.6% in the previous quarter respectively and 64.8% and 65.6% in the second quarter of 2016 respectively.

For the second half of 2017, we expect non-GAAP gross margins of approximately 65% plus or minus 1%. GAAP and non-GAAP operating expenses for the quarter were \$8.5 million and \$8.3 million respectively, compared to \$12.9 million and \$12.4 million respectively in the prior quarter and \$11.7 million and \$10.9 million in the same period a year ago. Excluding the impact of \$1.3 million of restructuring expenses in the prior quarter, operating expenses declined by \$2.8 million quarter-over-quarter on a non-GAAP basis.

For the second half of 2017, we expect non-GAAP operating expenses to remain flat with current quarter results in the third quarter of 2017 and down \$500,000 in the fourth quarter of 2017 as we hit the payroll tax caps for many of our employees.

GAAP net loss in the quarter was \$2.9 million or a loss of \$0.06 per basic share, and non-GAAP net loss was \$2.5 million or a loss of \$0.05 per basic share. This compares to a GAAP net loss of \$5.8 million or a loss of \$0.12 per basic share, a non-GAAP net loss of \$5.2 million or a loss of \$0.10 in the previous quarter, and a GAAP net loss of \$4 million or a loss of \$0.08 per basic share and a non-GAAP net loss of \$3.1 million or a loss of \$0.06 per basic share in the same period a year ago.

For the second quarter of 2017, our adjusted EBITDA loss improved to \$1 million compared to an EBITDA loss of \$1.9 million in the previous quarter and an adjusted EBITDA loss of \$1.2 million in Q2 of 2016. For the second quarter, we had \$1.6 million of depreciation, amortization and accretion and \$0.3 million of stock-based compensation that were the noncash charges we netted against our GAAP net loss.

At the end of Q2 '17, our balance sheet included cash and investments of \$27 million, compared with \$28 million in the previous quarter. For the remainder of the year, we expect an adjusted EBITDA breakeven point of around \$9.5 million in revenue.

Now I would like to return this call to the operators for any questions.

## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Our first question or comment comes from the line of Edwin Mok from Needham & Company. Your line is open.

### Arthur Su - Needham & Company - Analyst

This is actually Arthur on for Edwin. Thanks for taking our questions, and congrats on some of the accomplishments you made during the quarter. So the first one is just on the three new customer contracts that you mentioned you signed during the quarter. Can you provide a little bit more color on these wins, whether they were for applications in memory or logic; and also when we can expect some revenue contribution?

### Christian F. Kramer - Intermolecular, Inc. - CEO, President & Director

There's a mix. Of the three, they're in the semi ecosystem, which means it's a combination of tool suppliers and material makers. And the revenue contribution will start, it takes about a quarter. So that will show up in Q3, the ones that we sign in Q2.

### Arthur Su - Needham & Company - Analyst

Got it. So moving on to outside of semi -- can you kind of share some progress that you made on that front? I know in the past you've talked about efforts to diversify the business. Just any sort of like data points you can share with us on what IMI has done?



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**Christian F. Kramer** - *Intermolecular, Inc. - CEO, President & Director*

Well, the last earnings call, we talked about concentrating more in semiconductor and the semiconductor ecosystem. Not fully abandoning our diversification, but [our] core competency keeps coming back to semi. And where, I believe, we can continue to grow the business is in that area, semi and the semi ecosystem. But having said that, we have programs that involve optical coatings, and we're pursuing businesses there. But vast majority of our progress is in semi.

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**Arthur Su** - *Needham & Company - Analyst*

Got it. Okay. And then, on the operating expenses -- so OpEx was down \$3 million this quarter, which is better than your \$1.8 million for core savings [you] had talked about last quarter. Obviously, it sounds like you guys have seen better savings from your cost-cutting initiatives. How should we think about the breakeven point going forward? Is it below \$10 million, as you had previously stated?

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**Bill Roeschlein** - *Intermolecular, Inc. - CFO & Principal Accounting Officer*

Yes. We're expecting flat, close to the \$8.25 million in OpEx for this quarter. And in Q4, we historically get about a \$500,000 benefit from payroll tax maximizing out. And so overall, that's about a \$16 million OpEx for the second half. And that puts us more like in the \$9.5 million revenue range for an adjusted EBITDA breakeven.

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**Arthur Su** - *Needham & Company - Analyst*

Great. Thanks for that, guys. That's all I had.

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**Christian F. Kramer** - *Intermolecular, Inc. - CEO, President & Director*

Thank you.

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**Operator**

(Operator Instructions).

I'm showing no additional audio questions at this time. I'd like to return the conference back over to management for any closing remarks.

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**Christian F. Kramer** - *Intermolecular, Inc. - CEO, President & Director*

Thank you. And I look forward to speaking to you all next quarter.

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**Operator**

Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may now disconnect.

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