

Energous Corporation

Second Quarter 2019 Earnings Conference
Call

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CORPORATE PARTICIPANTS

Mike Bishop - *Investor Relations*

Steve Rizzone - *Chief Executive Officer*

Brian Sereda - *Chief Financial Officer Corporate Finance and Development*

PRESENTATION

Operator

Good afternoon, and welcome to the Energous Corporation Second Quarter 2019 Financial Results Conference Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the * key followed by 0. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press *, then 1 on your touchtone phone. To withdraw your question, please press *, then 2. Please note this event is being recorded.

I would now like to turn the conference over to Mike Bishop with Investor Relations. Please go ahead.

Mike Bishop

Thank you, operator, and welcome everyone. Before we begin, I would like to remind participants that during today's call, the company will make forward-looking statements. These statements, whether in prepared remarks or during the Q&A session, are subject to inherent risks and uncertainties that are detailed in the company's filings with the Securities and Exchange Commission. Except as otherwise required by federal securities laws, Energous disclaims any obligation or undertaking to publicly release updates or revisions to the forward-looking statements contained herein or elsewhere, to reflect changes in expectations with regard to those events, conditions, and circumstances.

Also, please note that during this call, Energous will be discussing non-GAAP financial measures as defined by SEC Regulation G. Reconciliations of these non-GAAP financial measures to the most directly comparable GAAP measures are included in today's press release, which is posted on the company's web site.

Now, I would like to turn the call over to Steve Rizzone, CEO of Energous. Go ahead, Steve.

Steve Rizzone

Thank you, Mike. Good afternoon, and thank you for attending the Energous second quarter conference call. Brian Sereda, our Chief Financial Officer, is joining me today. As in past conference calls, I will begin with comments on the company's progress and provide a general business update before turning the call over to Brian for a financial update. We will then open the call to questions.

As many of you know, two days ago, our customer Delight in conjunction with SK Telesys announced that their Oasis-RC Personnel Sounds Amplification Product, or PSAP, is now available for sale on Amazon. The launch of the Oasis-RC on Amazon is a major milestone and validation point for our WattUp, wireless charging technology. We have always noted that a strong leadership position in an industry is traceable to a few key elements with first-to-market being one of these elements. We are looking forward to additional products from partners coming to Amazon over the coming months as the launch of WattUp Wireless Charging 2.0 accelerates.

We also saw the announcement this week from NewSound, a leading hearing-aid manufacturer based in China. NewSound will be launching a next-generation hearing-aid at EUAH in Germany in October, with expected availability in the U.S. and Europe by the end of this year. As we've noted on prior calls, we're seeing very strong interest for our RF-based charging

technology in the hearing aid and PSAP markets, as our technology removes the major pain point for these types of product, that being constant battery replacement.

In June, we announced the availability of a hearing aid and PSAP developer kit, which enables faster integration for manufacturers looking to finally remove the chore of endless battery swaps by their users. Delight was the first-to-market. NewSound will be the second, and we anticipate additional announcements between now and the end of the year for WattUp-enabled products, not only in the hearable market but also in the wearable, medical sensor, and smart glasses markets.

At the end of July, we announced receiving FCC certification for our GaN-based WattUp Near Field transmitter technology. We also noted the same system has now been approved for sale in the European Union. These are very important approvals for us as we continue to expand available options for our partners based on their product application needs. This GaN solution provides higher power with improved efficiency for devices such as earbuds, smart watches, and smart glasses. Whereas our CMOS based technology offers the lowest wireless power (INAUDIBLE) costs for smaller devices, such as hearing aids, fitness bands, and others. This newly certified GaN transmitter will also be the foundation for an upcoming hearable developer kit planned to launch this quarter. Much like the hearing aid developer kit we announced in June, the hearables developer kit allows us to support additional incoming partners and their applications without impacting our current engineering resources.

An additional comment on regulatory approvals. As we've noted in the past, Energous is driving a worldwide regulatory campaign for RF-based charging. For the most part, this goal has been achieved with the exception of Japan, Korea, and China. While it is difficult to predict timing when dealing with government agencies, indications are that we could expect to see positive movement later this year, potentially moving to the first half of next year for regulatory approvals in these important markets. That is, we are anticipating months, not years, in terms of the first regulatory certifications in Asia.

As all of the pieces are now coming together: strategic partnerships, technological maturity, customer shipments for revenue, and global regulatory approvals, we can look forward to answering the main questions surrounding Energous. How fast will the company ramp, and how quickly will it achieve profitability? With each passing month, the answers to these questions become clear, so let's move the commentary to the question of profitability.

I would like to begin by discussing product launches to consumers by our customers with the potential revenue ramp, focusing on what we can expect to see between now and the end of this year and what the initial picture for 2020 is starting to look like. As noted, Delight has launched their Oasis-RC for sale on Amazon for U.S. customers, and the NewSound is launching in the U.S. and European Union markets. The point being, while the Asian regulatory certifications have delayed launches from some of our top-tier customers requiring global certification capability before committing to launch, we have other top-tier opportunities that we have moved to a regional focus, and we believe there is a high probability that at least one top-tier consumer electronic, or IoT company, will commit to launch cycles and start buying free production quantities of chips before the end of this year.

Each top-tier product launch, even on a regional basis, represents a seven-figure sales opportunity, scaling over a 12-month period. At the same time, momentum is strong for regional launches from our second-tier of opportunities with the potentials for thousands to tens of thousands of chip sales from each customer, again scaling over a 12-month period. From a

revenue perspective, the product launches have a layering effect with typical product lifecycles measured in the two to three years or more. All of this points to a gradual ramp of revenues through the end of this year, scaling and accelerating each quarter of 2020.

To complete the picture, revenues are ramping while at the same time our expenses are declining, lowering the bar for profitability. Brian will provide more color on this trend in his remarks, but suffice it to say, despite the move from a developmental to a commercial stage company, we have been able to lower our expenses. This would appear to be counterintuitive as most models see expense acceleration at this stage.

That is not the case with Energous largely due to two factors. First, we have the benefit of the dialog partnership. As we stated in the past, dialogs customers are our customers, which is one of the principal drivers for the partnership. The commonality of customers allows us to effectively benefit from leveraging the dialog sales team and avoiding the costs associated with the dedicated sales force. Also, the relationship with dialog and their assumption of all backend operations substantially reduces the operational costs associated with qualifying, inventorying, and supporting just sales. The net result is several millions of dollars of annual cost savings over a standalone model.

Second, the company's biggest expenses are employees and chip development. Over the last three years, Energous has invested heavily in chip development to the point where the company now has a very complete, flexible, and powerful catalog of transmitter, receiver, and power amplification chips. The current portfolio of chips is strong enough and flexible enough to support both the company's near-term customer acquisition and revenue expectations, as well as the transition from contact- to distance-based charging.

While Energous will continue to invest in chip development to maintain and expand our leadership position in innovation and first-to-market commercial launches, the number of chip developments and their respective costs will be lower due to a more elongated roadmap. Further, with respect to our other major expense, we are currently at about 60 employees. We believe this number will remain relatively flat through next year, which highlights the leverage our development and deployment model brings to the table. We believe that we will not have to be 100-person company to generate \$100 million in revenue, thanks largely in part to the dialog relationship.

The Energous model is very scalable, sustainable, and economical, and now that it is starting to kick in, our shareholders will begin to benefit in value appreciation as revenues ramp, customer shipping products to consumers expand, and expenses stay flat. The net result of both of these efforts is a significant annual reduction in annual operating expenses, which the company believes it can maintain into 2020 without negatively impacting customer acquisition or technical leadership.

Moving on, I would like to put the positive trends in revenues and anticipated revenue acceleration in perspective relative to addressable market penetration. Current estimates of the total addressable market, or TAM, in our four target markets of hearables, wearables, smart glasses, and medical sensors is over 885 million devices sold in a year. At our current expense level, we estimate that Energous can be cash flow breakeven with as little as a 1% market penetration. This is a very realistic and achievable goal. Yes, it was expensive to get to this point, and it took longer than we anticipated. But the path to commercial market dominance and profitability is clear and accelerating.

A few final comments before I turn the call over to Brian. Discussions with our long-term strategic partners are continuing. So, there is nothing new to update on the relationship at this time.

A couple of comments on competition. As many of investors are aware there have been some recent technology and regulatory announcements, which have garnered interest in the press. In general, we believe product and regulatory announcements surrounding Wireless Charging 2.0 are positive. It is good for the market as they demonstrate momentum and generate consumer interest in the potential of 2.0 charging.

But it's important to keep in mind exactly what these announcements represent. They are, by and large, initial stage technologies focused on peripheral markets like RFID tags and active harvesting. These markets are interesting and show potential, but they are not the mainstream market energy is successfully attacking and establishing a sustainable market leadership position in. When we see Wireless Charging 2.0 competition with deliverable solutions that are ready for integration at the customers we are engaged with, we will then comment differently, but that has not happened yet. Clearly, Energous has a very significant first-to-market advantage in the deployment of wireless power 2.0 solution in mainstream, consumer electronics, and IOT devices.

Finally, I want to highlight that the numbers discussed earlier in terms of market penetration are for the four target markets and contact-based technology. The WattUp Near Field technology, given its first-to-market and technological advantages, is in a position to establish a dominant, sustainable leadership position in hearables, wearables, medical sensors, smart glasses, and more, leading to a very profitable business in and of itself. If you layer on the fact that in 2020 the company is targeting to expand into portable computing, gaming, industrial, IOT, and smartphone markets, which will add over 2.4 billion devices to the addressable market, the potential for Energous is staggering. The vision of building a very profitable, very significant, and sustainable model has always been possible. We are now turning possibilities into reality.

Brian, I will now turn the call over to you.

Brian Sereda

Thanks Steve. As you saw at the close of market today, we issued our Q2 earnings press release announcing operating and financial results for our second quarter fiscal 2019 ended June 30th. Summarizing the second quarter, we recognized \$48,000 in revenue compared to \$67,000 in the prior quarter and \$206,000 in the second quarter of last year. As Steve discussed, with two recent customer announcements, we expect additional customer releases and accompanying chip orders in the next two quarters as we complete final integration and production-related work.

Like all new ground-breaking technologies, the first customers require a significant amount of engineering support, and we expect this to decrease overtime as the technology matures and knowledge base of RF wireless power transfer expertise builds at customers and other partners. In addition, the introduction of reference design, such as the recent one we announced and expected future reference design releases for a variety of vertical markets will also help improve future integration and sales cycle timelines. Total GAAP expenses for the second quarter totaled \$10 million, the lowest in over three years and approximately \$1.2 million lower than \$11.2 million recorded for the prior quarter and \$2.5 million lower than the same period last year.

The decrease compared to the prior quarter and prior year is mainly a result of lower engineering cost and lower stock compensation expense. We expect this trend to continue through the balance of this fiscal year and potentially through 2020, with the bulk of the expensive ground up shift innovation behind us for the current generation of our core technology. However, we could see minor spikes due to chip take out costs, depending on production plan and direction from Dialog who will take up the operational aspects of order fulfillment.

Leveraging Dialog's global operations will allow us to keep our headcount in the range of 60 people plus or minus for the foreseeable future, and we ended Q2 with a total headcount of 58. Despite our expectations for increasing chip shipments and customer engineering engagements, we should continue to see the benefits of what we believe is a highly leverageable model, even as chip production volume, and revenues grow.

The net loss for the third quarter on a GAAP basis was approximately \$9.8 million, or \$0.32 per share on \$30.4 million weighted average shares outstanding. This compares to an \$11 million net loss in Q1 or \$0.39 per share and a \$12.3 million net loss or \$0.48 per share in Q2 of 2018.

Now, let me switch over to a non-GAAP year-over-year numbers for the quarter, as we believe adjusted or non-GAAP EBITDA provides a useful comparison for investors, especially for a company at our stage when used together with GAAP information. Excluding \$3 million of stock compensation and depreciation expense from our total 2Q GAAP expenses of just under \$10 million, net non-GAAP operating expenses total approximately \$7 million, down approximately \$0.8 million over Q1 and \$0.9 million lower than Q2 of last year.

Net of revenues, our adjusted EBITDA, or non-GAAP operating loss for Q1 was \$6.9 million, approximately \$0.8 million lower over the prior quarter and Q2 of last year. Non-GAAP engineering expenses decreased by approximately \$1 million to \$3.9 million versus the prior quarter and was also \$1 million lower than same period last year. This is mainly attributed to lower chip development, project-related, and headcount costs. Non-GAAP SG&A increased by approximately \$0.2 million over the prior quarter due to higher legal year-end proxy and other public company costs typically incurred in the second quarter. We were essentially flat to Q2 last year when comparing SG&A spending.

Lower cash spending translates to a lower cash burn rate. We used \$6.9 million of cash in the second quarter, ending with approximately \$29.2 million in cash and we continue to remain debt free.

To close, we expect our cash operating expense run rate to remain in our current range with the potential for minor quarterly increases for production of chip tape out costs. We continue to believe we are on track to see the launch of additional customers later this year, setting the stage for growth and chip royalties, supported by our partner Dialog. It goes without saying, but commercializing next generation technology on a global scale, while being a public company, has been no small task. But our confidence continues to be bolstered by the increasing depth of new interest in the technology and support from our customers and partners.

We thank our investors for their patience and continued support. And I'll turn the call back to Steve for additional commentary.

Steve Rizzone

Thank you, Brian. To this point, today's comments have centered around the fact that Energous is building a profitable business with its (INAUDIBLE) technology. There is more than enough opportunity and momentum for the WattUp Near Field technology, in and of itself, to drive a sustainable profit model for the company. It is important to keep in mind that distance opportunities are equally, if not more, compelling in terms of chip sales and potential revenue.

The same WattUp core technology that is driving the near field market will also power midfield and far field. Our investors can expect to see distant product launches begin to layer on top of Near Field in the latter part of next year. This is what makes Energous so unique and compelling. We are the only company, the only company with a mature technology and a viable roadmap to deliver Wireless Charging 2.0 to the consumer across a broad spectrum, spanning contact through distance. I am sure we will continue to have skeptics who will have doubts about the technology and our ability to (INAUDIBLE). But I am equally sure that with each passing quarter, we will demonstrate continuing and accelerating process to the end goal of being a wireless charging 2.0 ecosystem dominated by Energous.

Operator, I will now take questions.

Operator

We will now begin the question-and-answer session. To ask a question, you may press *, then 1 on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press *, then 2. At this time, we will pause momentarily to assemble our roster.

The first question comes from Ilya Grozovsky of National Securities.

Ilya Grozovsky

Steve, the Delight hearing aids have been available on Alibaba's website since the product launch, I believe, six months ago. Obviously, given the chip volumes that you are reporting, there really hasn't been much traction on the product from the Alibaba website, which is a very popular website. What gives you the confidence that them being available on Amazon's website is going to change some dynamic? Thanks.

Steve Rizzone

Well, I think that there has been some traction, and first of all, it's a PSAP product. It's not a hearing aid product, and this is a whole new category of product. I believe that the primary driver or benefit is, at least to Energous, is the fact that the product is now available in the U.S. for delivery to the consumer, and that is a major milestone that it's shifting to U.S. We're unsure of the revenue ramp as it relates to this, until we start to see how the sales play out here. I think they've issued a very conservative forecast as this is their first adventure not only into the PSAP but also into the U.S. market.

And so, I think the importance of Delight is the fact that we have a product now shipping and available to the consumer in the U.S. market. We expect that these revenues will ramp from this customer, and we also expect and I think it's important that we'll begin to layer on additional customers. That's the important element. Each one of these product launches, as I mentioned, has a two- to three-year product life associated with it. They start small, as you know, and then, may begin to build quarter-on-quarter depending on the success of the sales. But as we continue to layer in additional customers, you can expect to see the revenues we believe ramp, as I said, gradually to the end of this year and then accelerating into next year.

Ilya Grozovsky

Shifting gears a little bit to the mid-range. I think you had said that you anticipate a mid-range product roll-out by a partner in the latter half of 2020. What type of a (INAUDIBLE) do you think that would be married to? Thanks.

Steve Rizzone

I think that there are a number of possibilities. I think Smart Speaker is certainly one of them that we're seeing interest in. I think a standalone transmitter in conjunction with devices like hearables and the smart glasses might be another option. Again, there are a significant number, dual-digit number, of efforts currently underway with distance opportunities, and how these unfold in the coming months will really determine which will be the first. Again, the good news here is that it's the same core technology. The same chips that are driving the near field product are the ones that are going to be used in the initial launches of the distance technology. So, it's a matter of application and product decisions and product rollout as to how and which will come out or what will come out at the end of next year.

Operator

The next question will come from William Gibson of ROTH Capital.

William Gibson

Steve, do you think there's a chance of any non-recurring engineering revenue this year?

Steve Rizzone

I think there's a chance. I don't want to forecast it, certainly, because there are a number of variables that are coming into play here. Our focus quite frankly is on chip revenue because chip revenue translates directly to product launch, and our clear focus is on chip revenue. I would see engineering services revenue as possible. But I'm not prepared to make any kind of a commitment at this time as to if that will happen and, if so, what the magnitude or the level of this revenue might be.

William Gibson

And you mentioned potential IoT devices from a top-tier company. Is that a separate company from the two we talked about before, your strategic partner and then the second top-tier consumer products company whose products pushed out?

Steve Rizzone

We're actually quite excited about our portfolio of top-tier opportunity. It's expanded significantly, and it continues to expand. And this category of customer, of course, has a tremendous impact potentially on our revenue ramp. Initially, there was concerns because the product launches that we're focused or targeting were global in nature, and as you know, the Asian regulatory certifications have taken longer than we originally anticipated.

Fortunately, we now identified a number of applications and opportunities with top-tier companies, and they are realigning their launch focus on a regional basis, covering the U.S. and the EU, as the primary drivers for their product launch decisions, and so, we have a significant number of top-tier opportunities. And as I said, we think it is highly likely that at least one will commit to a formal product launch with initial product or chip sales hitting before the end of this year.

Operator

The next question will come from Jon Hickman of Ladenburg.

Jon Hickman

I was wondering if you could, maybe you don't want to answer this question, but is there any frustration building with the fact that the progress has been limited with your strategic partner?

Steve Rizzone

Well, I don't think it's a question of frustration. Anytime you're dealing with very, very large companies, there are always issues that crop up. There's changes that are made, so on and so forth. I don't think there's a level of frustration, because as I said the changes are not product or technology based, and the fact that we are seeing very significant interest and have a significant number, high single digits of top-tier companies that are interested and active in their engagements in the technology, again, I think is really what is cause for optimism internally.

Would we like things to happen quicker? Certainly. Have we been disappointed in some of the directions and the movement? Absolutely. And if this were involved or because of the viability of the core technology, we would certainly have concerns, but that is not the case. The core technology is solid. The applications are real. We're now shipping to consumers, and so any question of viability, hopefully, will have been answered.

And as I said, there are a number of top-tier consumer opportunities, both contact- and distance-based, that we're actively engaged in. They'll certainly take longer than our second-tier opportunities typically because of their product cycles and distance cycles, but as we begin to layer these things on, again, we are optimistic and confident in terms of the rollout of this technology, the momentum that's being built, and the fact that we can build a very, very profitable and sustainable business.

Jon Hickman

I have one more. As you mentioned, you expect some other product announcements later this year. Do you think you'll be able name names, like you've done with Delight?

Steve Rizzone

Yes, I think so. Yes, I think we'll be able to name names, and as I said, I think you'll see additional markets start to kick in. We see smart glasses as a very, very interesting market for us. Hearing aids and PSAPs, we are really establishing a very significant position in these markets. Wearables and medical sensors, all of these markets I think that we'll have announcements in the coming months in terms of actual customers participating in these markets.

Operator

And this concludes our question-and-answer session. I would now like to turn the conference back over to Steve Rizzone for any closing remarks.

Steve Rizzone

Thank you very much for your attention. As Brian said, we want to thank our investors for your patience as we continue to drive the company forward. Certainly, it has taken us longer than we thought, but I think that we've now reached an inflection point where we have customers that are shipping product to the consumer, which should eliminate any concern about viability of technology. And we are extremely confident that we are now on a path of continuing advancements in revenues and additional customer placements, and so, I believe that each follow-on quarterly call, we're going to be in a position to announce better results and aggressive movement as we continue to rollout wireless power 2.0.

So, thank you again, and we'll look forward to talking to you all in three months.

Operator

Thank you. The conference is now concluded. Thank you all for attending today's presentation. You may disconnect your lines.