

Lantronix, Inc.

Third Quarter Fiscal 2024 Earnings  
Conference Call

Monday, April 29, 2024, 5:00 PM Eastern

**CORPORATE PARTICIPANTS**

**Saleel Awsare** - *President, Chief Executive Officer*

**Jeremy Whitaker** - *Chief Financial Officer*

## **PRESENTATION**

### **Operator**

Good afternoon and welcome to the Lantronix Third Quarter Fiscal 2024 Earnings 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 telephone keypad, 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 Jeremy Whitaker, Chief Financial Officer. Please go ahead.

### **Jeremy Whitaker**

Good afternoon, everyone, and thank you for joining our quarterly earnings call. Joining me on the call today is our President and Chief Executive Officer, Saleel Awsare. A live and archived webcast of today's call will be available on the company's website.

In addition, you can find the call-in details for the phone replay in today's earnings release. During this call, management may make forward-looking statements, which involve risks and uncertainties that could cause our results to differ materially from management's current expectations. We encourage you to review the cautionary statements and risk factors contained in the earnings release, which was furnished to the SEC today and is available on our website and in the company's SEC filings such as its 10-K and 10-Qs.

Lantronix undertakes no obligation to revise or update publicly any forward-looking statements to reflect future events or circumstances. Please refer to the news release and the financial information in the investor relations section of our website for additional details that will supplement the management's commentary. Furthermore, during the call the company will discuss non-GAAP and financial measures. Today's earnings release, which is posted in the Investor Relations section of our website describes the differences between our non-GAAP and GAAP reporting and presents reconciliations for the non-GAAP financial measures that we use.

With that, I'll now turn the call over to Saleel.

### **Saleel Awsare**

Thanks, Jeremy, and thank you, everyone, for joining us on the call today. I'm pleased to report record revenue of \$41.2 million for the third quarter of fiscal year 2024, a year-over-year increase of 25% compared to the same period of 2023 and a sequential increase of 11% compared to the December quarter.

Non-GAAP EPS in fiscal year Q3 grew 88% compared to the same period last year demonstrating leverage in our operating model as revenue improves. Jeremy will provide you with more details and analysis on the third quarter financial results shortly.

As I have recently completed five months with Lantronix and having spent a lot of time with our key customers, strategic partners and most importantly the Lantronix team, I'm very optimistic about the future given our strong products and solutions, our growing customer engagement and an improving EBITDA and solid balance sheet.

We see both compute and connect technologies converging at the edge of the network and that's exactly where we play with our core capabilities and solutions. We have a deep understanding of edge compute requirements and provide our customers with complete solutions, including hardware, software, design services and our Perception IoT platform for device management and application integration.

Our focus going forward will be on three key vertical segments including Smart Cities, Automotive Infotainment and Enterprise. We estimate the serve available market the company is addressing in the three different verticals is \$8.5 billion and we expect compound annual growth rate over the next few years to be approximately 12%.

Let me give you an example in each of these verticals. In Smart Cities, we have the opportunity to drive revenue growth over a couple of key areas, namely, smart grid and critical infrastructure. We estimate the serviceable addressable market of the Smart Cities vertical to be approximately \$3.9 billion and the compound annual rate over the next few years to be approximately 12%.

In the smart grid sector, we see continued momentum with our lead smart grid customer, where we received our first follow-on order for the first half of fiscal year '25 as this customer is transitioning from design and initial production to a run rate business. Our relationship continues to deepen with our lead customer, and we are engaged at all levels of the organization.

We expect that as they expand their market beyond the current rollout and into broader applications and geographies with the QED device and its variants, we will continue to partner with them to address these needs. I expect this to be a long-term mutually beneficial engagement.

Now, moving to critical infrastructure. A great example of this sector is a recent design win with a tier 1 telecom customer who is using our FOX Telematics device coupled with our Perception SaaS solution for monitoring and managing cell site power generators. We are replicating this design win with multiple generator makers who have similar needs. Looking further out, the same solution can be extended to applications at construction sites, hospitals and other such locations.

In Automotive Infotainment, the trend is clearly towards pillar to pillar, large interactive displays with a digital cockpit becoming a highly valued part of the vehicle. We estimate the current SAM in the automotive infotainment to be approximately \$900 million and the annual growth rate to be about 21%.

Our IP resides in the automotive infotainment compute system. We developed Togg, the Turkish-based automotive OEM, and we are seeing strong interest from Tier 2 and Tier 3 automotive OEMs as well as manufacturers of commercial trucks, motorcycles and heavy machinery.

Let me also add an update on Togg. They recently unveiled their second vehicle, the T10F sedan and our embedded compute solution is designed into the vehicle's digital cockpit. Additionally, they have told us they plan to start shipping vehicles in Germany in the calendar year 2025. We continue to collaborate and innovate with them as they expand their business.

In the enterprise vertical, we are focused on out-of-band, videoconferencing and security and surveillance. We estimate the serve available market of our enterprise vertical opportunity to be approximately \$3.7 billion, growing at about 9% annually over the next few years.

Let me add some color on one of our products, addressing the growing need for out-of-band management. Out-of-band solutions provide alternative paths to access servers, networks and routers when the primary access is unavailable. Providing uptime in resilient networks is important for many sectors, including banks, government, health care and the retail sector. We provide not only hardware but also management software, ongoing support and warranty services.

In summary, we are focused on three growing attractive vertical markets with a combined serve available market of \$8.5 billion and growing. Our business teams are actively targeting new customer design wins across the three verticals and all our major geographic areas. I remain excited about the growth opportunity ahead for Lantronix, especially given our broad portfolio, IP and great customer base.

In summary, we have a great company, and we are building on strength. Moving forward, we will become an even stronger company given the technology and talent we have in place, driving profitable growth and shareholder value.

With that, I will now turn the call over to Jeremy, our Chief Financial Officer, for his comments on fiscal year Q3 and guidance for the next quarter. Jeremy...

### **Jeremy Whitaker**

Thank you, Saleel. Now, I will provide the financial results and some business highlights for our third quarter of fiscal year 2024 before commenting on our financial outlook for the fourth quarter of fiscal 2024.

For FQ3 2024, we reported revenue of \$41.2 million, an all-time record for Lantronix. Revenue was up 11% and 25% from the sequential and year ago periods respectively. IoT Systems Solutions revenue increased by 16% and 91% from the sequential and year ago periods, respectively. The increase was primarily driven by the continued ramp of production shipments for our lead smart grid customer.

In addition, the year-over-year increase was impacted by strong sales from our out-of-band management products. For the remainder of the fiscal year, we expect continued growth from our IoT Systems Solutions.

Sequentially, embedded IoT solutions revenue was up 6% with continued contribution from our lead automotive customer. As expected, we experienced a year-on-year decline in embedded IoT solutions as the year ago period included a large enterprise video customer design that ended in FQ4 2023.

In FQ3 2024, software and services revenues were down from the year ago period, primarily a function of the completion of two large design services projects that transitioned into production during the first half of fiscal 2024.

GAAP gross margin was 40.1% for FQ3 2024 compared to 40.6% in the prior quarter and 44.4% in the year ago quarter. Non-GAAP gross margin was 41% for FQ3 2024 compared to 41.6% in the prior quarter and 45.1% in the year-ago quarter. The decline in gross margin

percentage was primarily a function of a change in product mix driven by the product ramp with our smart grid customer. In FQ4 2024, we expect gross margins in a similar range.

GAAP SG&A expenses for FQ3 2024 were \$9.9 million compared with \$9.7 million in the year-ago quarter and \$10.2 million in the prior quarter. GAAP R&D expenses for FQ3 2024 were \$5.2 million compared with \$5.1 million in the year-old quarter and \$4.7 million in the prior quarter. In the upcoming quarter, we expect a sequential increase in OPEX related to variable compensation as revenue and earnings are expected to improve in FQ4 2024. GAAP net loss was \$423,000 or \$0.01 per share during FQ3 2024 compared to GAAP net loss of \$3.1 million or \$0.08 per share in the year ago quarter.

Non-GAAP net income doubled from the year ago quarter demonstrating leverage in our operating model and cost control. Non-GAAP net income was \$4.2 million or \$0.11 per share in FQ3 2024 compared to non-GAAP net income of \$2.1 million or \$0.06 per share in the year-ago quarter.

Now, turning to the balance sheet. We ended FQ3 2024 with cash and cash equivalents of \$24.6 million, an increase of \$2.5 million from the prior quarter. Working capital was \$54.3 million, an increase of \$2.4 million from the prior quarter. Net inventories were \$40.6 million at the end of FQ3 2024, a decrease of \$2.2 million from the prior quarter.

Now, turning to our outlook. For the fourth quarter of fiscal 2024, we expect revenue to be in the range of \$46.5 million to \$51.5 million and non-GAAP EPS in a range of \$0.12 to \$0.18 per share.

In summary, we are maintaining the annual guidance for fiscal 2024 that we provided during our February 2024 earnings call. At the midpoint of our FQ4 2024 outlook, we expect to deliver revenue and non-GAAP earnings for fiscal 2024 with 22% organic revenue growth and a 74% increase in non-GAAP EPS as compared to our fiscal year 2023 results.

With that, we complete our prepared remarks for today. So, I will now turn it over to the operator to conduct our Q&A session.

## **QUESTION AND ANSWER**

### **Operator**

We will now begin the question-and-answer session. To ask a question, you may press "\*" then "1" on your telephone keypad. 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 is from Jaeson Schmidt with Lake Street. Please go ahead.

### **Jaeson Schmidt**

Hey guys. Thanks for taking my questions. I just want to start with the Gridspertise. Curious if you could help us size this follow-on opportunity or how we should be thinking about this additional order? And relatedly, should we assume you're still sole source here?

### **Saleel Awsare**

Hey, Jaeson, it's Saleel. Thank you very much for the question. So let me take it on. As discussed in our prepared remarks, we have a steep product ramp with our smart grid customer

during fiscal Q3 and fiscal Q4 with around \$20 million of product expected to ship in the fourth quarter of the fiscal year. We expect them to remain a very important customer and the opportunity for further growth. While we don't expect \$20 million in the quarter to be the immediate run rate, we expect it will take some time for them to deploy the units we are currently shipping, and they demonstrate their success.

We expect the business will continue to grow over time. That said, I'm very pleased that we received our first follow-on order even though they are just at the beginning of the deployment, and the initial order is around \$11 million to be delivered in the first half, as they've also gone to a run rate sort of business. It shows the customer's commitment to the program and as they put in more supply for a successful rollout. To conclude, we expect the overall opportunity is much larger is what they have told us than what we shipped in fiscal 2024 and we really look forward to enabling their continued success in their rollout. Jaeson, what is the second half of your question?

**Jaeson Schmidt**

Just if we should assume you're still sole sourced.

**Saleel Awsare**

Yes. To my knowledge, we are the sole sourced.

**Jaeson Schmidt**

Perfect. And then just as a follow-up, curious if you could update us on what you're seeing from sort of a customer inventory or channel inventory standpoint?

**Saleel Awsare**

Yes. So great question, right? So if I think about our business, Jaeson, it's in two areas. We've got a broad-based channel business. And based on the quarter that we just completed and our current forecast, it appears that our broad-based channel business is normalizing and is poised for growth over the next several quarters. In addition, we looked at the inventory and it's come down from the prior quarter and is running at its historical average. So that's on the channel side.

On the embedded compute, we've said in the past that there were some delays in our embedded compute. One specific couple of designs that were done in fiscal 2023 they were supposed to ramp in 2024, but they're now going to ramp in 2025. And Jaeson, I had the great opportunity of visiting the CEO of one of the large companies that we're working with and they're on track to start ramping in fiscal 2025. So, as they're successful we'll be successful with them.

**Jaeson Schmidt**

Okay. That's really helpful. Thanks a lot, guys.

**Saleel Awsare**

Thanks.

**Operator**

The next question is from Mike Walkley with Canaccord Genuity. Please go ahead.

**Mike Walkley**

Great. Thanks for the question. I guess, Saleel, just on the three targeted segments that make a lot of sense given your product portfolio. As you went through the portfolio, are there some

areas maybe that you're pruning that could impact the fiscal 2025 growth on a run rate basis?

**Saleel Awsare**

Yes. So we did a review with the products...our whole products, our technology. I'm really happy to report, I really like where we are sitting at today. We've got a pretty broad, but also deep product portfolio for the three verticals that I spoke of. As I'm looking to the future, we are going to be putting a lot more focus on products that are really going to provide us some outsized growth, embedded compute being one of them, out-of-band being one of them. Some of the other ones I won't go into, but really, we'll get some outsized growth out of there. Also, the products that we are focusing on pull in our PercepXion IoT software for device management and application integration.

So, in summary, as I think about the company three verticals transitioning, not just selling point products but a solution that consists of our hardware, our cloud-based software and in some areas even our design services. So putting it all together, really bringing a holistic solution to our customers.

**Mike Walkley**

Okay. Thanks. And just a follow-up question, thanks for some of the color in the Q&A on Gridspertise, as they go through a digestion period. Maybe, I know you're only giving a quarter at a time guidance, but as you share the SAMs for the three different targeted areas, how should we think maybe about like a baseline run rate for modeling fiscal 2025, given Gridspertise is likely to have a decline from the strong initial shipments?

**Saleel Awsare**

Yes. As we mentioned in our last call, we are transitioning like most companies to providing a quarterly as opposed to an annual guidance. And I'm really looking forward to providing you with an outlook in our fiscal Q1 in the August call for our fiscal Q1 2025. But having said that, let me be very clear. The long-term growth prospects are tremendous here. We've got a big SAM. We're growing at 12%, \$8.5 billion over SAM. And with our product portfolio and a growing customer base, I expect, over the longer term, we can grow at or really faster than the market.

**Mike Walkley**

Okay. That's helpful. I'll pass the line. Thank you, Saleel.

**Operator**

The next question is from Scott Searle with ROTH MKM. Please go ahead.

**Scott Searle**

Hi, good afternoon. Thanks for taking the questions. Nice job on the March quarter and nice to see the continued growth into June. Saleel, maybe to follow-up on the Gridspertise outlook, it looks like they're starting to rapidly expand or create some other opportunities both within the Pan-European opportunity as well as in the US markets. I'm wondering if you could help us, kind of size and understand the opportunity set there and the timeline that might be associated with it? And then I have a couple of follow-ups.

**Saleel Awsare**

Yes. So, let's start with what they have told us specific to their largest customer, which is Enel. We've been told that the opportunity size there is in the hundreds of thousands of units. So,

we're just getting started, Scott, to that extent. They are putting in a big team in the United States to get started. They were at DISTRIBUTECH. And they're now going to be in the show in San Diego. And it's mainly public power companies that are going to be there. So, it's early days for them to get started in the US, but we are engaged with them on many areas and that's another area that we are really looking forward to. So, the Enel opportunity we understand, as they look at the US in the future we'll be working with them as they deploy. But it's early days for the United States for them right now.

**Scott Searle**

Great. And maybe to couple that into Mike's question, looking at the design pipeline it seems like there's a lot of opportunity going on within that right now. I think the blended CAGR was about 12% beyond the three different verticals that you talked about and growing faster than that. I'm wondering, if you could tell us how that design pipeline is looking up. And then, again, we should be thinking about 12% plus growth as a long-term growth rate, excluding any sort of I'll call it normalization in the near-term Gridspertise shipment rate.

**Saleel Awsare**

Yes. So the opportunity pipeline is really healthy. We've reviewed it. We reviewed it relatively often. So I'm happy to report, it's very healthy. We continue to target large customer deals with our compute and connect. So that will give us visibility as we look at the business longer term. We are focused on the three key verticals, Scott, that I talked about. And it's an \$8.5 billion SAM growing 12%. So, as I said, we expect to be growing at or better than in the longer-term.

**Scott Searle**

Great. And one last one, if I could. You certainly have expertise in terms of edge compute and connect. That together equals a lot of discussion around AI. So, I'm kind of wondering how that's filtering into the conversation with customers? And how you're specifically positioned for those types of opportunities? Is it driving a larger opportunity both in terms of hardware software and cloud? I mean, how is that shaping up? And when do we start to see I'll call it a more defined impact from that? Thanks.

**Saleel Awsare**

That's a great question, and thank you for bringing that up, Scott. So, Lantronix is really integrating edge compute devices with our PercepXion IoT software to simplify and streamline the edge AI applications, as I think about it as build, deploy and accelerate. It's going to start with our Compute SOM, which allows for rapid development. And as you know, we've got this MDU [ph] on that. So, it gives you a robust tool that streamlines optimization. So this results in a powerful scalable solution that accelerates the transition from prototype to production significantly boosting efficiency and product reliability. We gave an early look at this at the embedded show in Nuremberg as a matter of fact, our partner actually called it out and we showed it working. It's early days, but we feel really good about it. And that was one of the areas we are focusing on as I look into the future.

**Scott Searle**

Great. Thanks so much.

**Saleel Awsare**

Thank you.

**Operator**



Again, if you have a question, please press "\*" then "1." The next question is from Christian Schwab with Craig-Hallum. Please go ahead.

**Tyler**

Hey, guys. This is Tyler on for Christian. Thanks for letting ask a couple of questions. I guess, first maybe the three key areas you highlighted, and I think we can kind of do some math to understand what the smart city one kind of looks like...then you have Gridspertise. But could you maybe frame a little bit how much revenue you're doing? I understand you outlined the size of the markets, but how much revenue in those three areas are you currently doing?

**Saleel Awsare**

So right now...and the way we report our revenue right now, so I want to not change our reporting on the call today. We report it as embedded solutions, IoT and software and systems. So that's how we report it today, and that's how Jeremy and I'm going to talk about it specifically. Going into the specific verticals, I don't want to break out the revenue right now, because some of the products that we report like our embedded compute go into a couple of different verticals. They go into the automotive vertical. They go into the smart cities vertically and even in the enterprise side. So it kind of goes into different verticals. So, I don't have it specifically for those three verticals. We specifically give it out for what we have that we're talking about there. But the way I look at it right now, our enterprise is probably our largest. Our smart cities is our second largest and automotive is the third one, just to kind of put it in perspective for you.

**Tyler**

That's completely fair. And I appreciate the rank order color. I guess, maybe to be a little bit pointed, but I understand not trying to give guidance for next year, but with Gridspertise going to be you know sounds like down next year, with some digestion on this first order, which I think makes sense. Can you still grow your top line, your total top line next year? And if so, comparatively I guess where is that offset?

**Saleel Awsare**

Yes. So again, just going back to what we said, right, we've gone through a quarterly guidance. So, I'm really looking forward to spending a lot of time with you guys as I get into the August call, with you to give you a much better view into fiscal Q1 2025. Having said that, let's be clear, we had a big ramp with them, excited about that, but they gave us a follow-on order and they're deploying systems as we do forward. So as this goes to run rate and our follow-on order is only for the first half of the fiscal year, we are working with them for the future.

**Tyler**

Yes, fair enough. Alright. That's all for us. Thanks, guys.

**CONCLUSION****Operator**

This concludes the question-and-answer session and the conference has also now concluded. Thank you for attending today's presentation. You may now disconnect.