Impinj Third-Quarter 2022 Earnings Conference Call
Wednesday, October 26, 2022
5:00 p.m. ET / 2:00 p.m. PT

Andy Cobb, Impinj VP Strategic Finance

Thank you, MJ.

Good afternoon and thank you all for joining us to discuss Impinj's third-quarter 2022 results. On today's call, Chris Diorio, Impinj's co-founder and CEO, will provide a brief overview of our market opportunity and performance. Cary Baker, Impinj's CFO, will follow with a detailed review of our third-quarter 2022 financial results and fourth-quarter 2022 outlook. We will then open the call for questions. Jeff Dossett, Impinj's CRO, will join us for the Q&A. You can find management's prepared remarks, plus trended financial data, on the investor-relations section of the company's website.

We will make statements in this call about financial performance and future expectations that are based on our outlook as of today. Any such statements are forward-looking under the Private Securities Litigation Reform Act of 1995. While we believe we have a reasonable basis for making these forward-looking statements, our actual results could differ materially because any such statements are subject to risks and uncertainties. We describe these risks and uncertainties in the annual and quarterly reports we file with the SEC. We do not undertake, and expressly disclaim, any obligation to update or alter our forward-looking statements except as required by law.

On today's call, all financial metrics except for revenue, or where we explicitly state otherwise, are non-GAAP. Balance-sheet and cash-flow metrics are GAAP. Please refer to our earnings release for a reconciliation of non-GAAP financial metrics to the most comparable GAAP metrics.

Before turning to our results and outlook, note that we will participate in the Baird 2022 Global Industrial Conference on November 10th in Chicago, and we will virtually attend the Susquehanna Semiconductor Showcase on December 13th. We look forward to connecting with many of you at those events.

I will now turn the call over to Chris.

Chris Diorio, Impinj Co-Founder and Chief Executive Officer

Thank you, Andy. And thank you all for joining the call.

Our third-quarter results were strong. Revenue and adjusted EBITDA exceeded our guidance, with both setting new quarterly records. Against the backdrop of broader macro crosscurrents, these record results highlight our growth potential as product supply improves. Last quarter I said that, based on my conversations with Impinj's leading end users and go-to-market partners, I expected demand to remain strong at least through second-half 2022. Recent conversations with those end users and partners suggest that that strength extends well into 2023, driven by new deployments and expansion at existing deployments. Highlighting that strong demand, we entered the fourth quarter with record backlog.

Starting with endpoint IC supply, the pace and lead times of wafer upsides from our foundry partner continue to gradually improve. Despite that improvement, third-quarter demand still exceeded supply by more than 50%, for the sixth consecutive quarter, and we expect demand to exceed supply well into 2023. At Impinj's yearly Executive Forum, a partner event which we just held, our leading inlay partners highlighted they are adding significant inlay-manufacturing capacity and reiterated they would layer on additional endpoint IC bookings if we had more wafers. We look forward to the day when our improving supply situation positions us to take those additional bookings.

Third-quarter endpoint IC revenue exceeded our expectations, and for the fourth-consecutive quarter set a new quarterly record. Our current supply visibility supports continued endpoint IC unit-volume growth in both fourth-quarter 2022 and 2023. Looking further out, we continue to see multi-year growth tailwinds for our endpoint ICs.

Turning to systems supply, component shortfalls again constrained our reader shipments, like they have for the past four quarters. For reader ICs, although third-quarter supply mostly caught up to demand, we see strong orders heading into fourth quarter, particularly for our E-family products. In aggregate, we entered fourth quarter with significant systems backlog, yet with product supply still constraining systems revenue growth into 2023. Like for endpoint ICs, we look forward to the day when we have enough systems supply to satisfy market needs.

Third-quarter systems revenue exceeded our expectations. Reader ICs were a bright spot, setting a new quarterly record. Reader and gateway revenue met our expectations, led again by shipments to the visionary European retailer's expanded loss-prevention deployment. Looking into 2023, we see solid systems demand, led by rapid unit-volume growth in our E-family reader ICs.

On the product front, I am thrilled by our September launch of the Impinj Authenticity solution engine. More than a decade in the making, Impinj Authenticity is an end-to-end platform offering for cryptographically authenticating everyday items as genuine. Comprising a new endpoint IC, the

Impinj M775, which pairs an ISO standardized cryptographic engine with a unique key in each IC; new firmware in our reader ICs and readers that enables a challenge-response dialog with those endpoint ICs; a new cloud-based Impinj Authentication Service that can verify an IC's authenticity in milliseconds; and easy-to-use APIs that enable partner or end-user product databases that pair each item with its authenticated endpoint IC; Impinj Authenticity will inhibit counterfeits, improve product safety and secure the supply chain. With Impinj Authenticity, we hope to make a substantial dent in global counterfeiting, which costs legitimate enterprises hundreds of billions of dollars annually. Only available from the Impinj platform, Impinj Authenticity is also our first product offering focused on expanding our recurring revenue opportunity from endpoint ICs to include cloud services.

Impinj Authenticity represents another key element of Impinj's mission of connecting every item in our everyday world and, while doing so, protecting those items, the privacy of people who benefit from those connected items, and the world we live in. Impinj Authenticity for protecting items. Protected Mode for protecting privacy. And looking forward, using the Impinj platform to improve the sustainability of those connected items.

On the project front, we see continued strong retail momentum. The visionary European retailer, pleased with our RAIN-based loss-prevention offering, continues deploying as planned. We expect that deployment to continue generating meaningful revenue for at least the next two quarters. The Asia-based global retailer's continued expansion of their self-checkout deployment into new geographies generated meaningful reader revenue again in the third quarter. And in supply chain and logistics, we continue to expect the second large North American customer to drive large endpoint IC volumes in 2023 and beyond.

In closing, I'd like to thank every member of the Impinj team for your tremendous effort this quarter. You delivered record revenue and adjusted EBITDA; introduced a new, first-of-its kind platform offering to inhibit global counterfeiting; strengthened our bond with partners and end users and positioned us for growth, all while navigating ongoing supply challenges. With a strong team and a growing opportunity, I remain confident in our market position and energized by our strong demand.

I will now turn the call over to Cary for our financial review and fourth-quarter outlook. Cary.

Cary Baker, Impinj Chief Financial Officer

Thank you Chris, and good afternoon everyone. On today's call, I will review our third-quarter financial results and fourth-quarter financial outlook.

Third-quarter revenue was $68.3 million, up 14% sequentially compared with $59.8 million in second-quarter 2022 and up 51% year-over-year from $45.2 million in third-quarter 2021.

Third-quarter endpoint IC revenue was $51.2 million, up 19% sequentially compared with $42.9 million in second-quarter 2022 and up 60% year-over-year from $32.0 million in third-quarter 2021. Accelerated demand timing for specialty and industrial ICs drove third-quarter revenue above our expectations. And although that specialty and industrial mix will normalize in fourth quarter, we still expect sequential endpoint IC revenue growth with our improving wafer supply.

Third-quarter systems revenue was $17.1 million, up 1% sequentially compared with $16.9 million in second-quarter 2022 and up 29% year-over-year from $13.2 million in third-quarter 2021. Third-quarter systems revenue exceeded our expectations, driven by strong reader IC shipments. On a sequential basis, reader IC revenue increased, reader revenue was flat and gateway revenue declined. On a year-over-year basis, reader IC and gateway revenue increased while reader revenue declined. Despite strong demand, we expect similar fourth-quarter systems revenue as we continue navigating reader component shortfalls.

Third-quarter gross margin was 56.9%, compared with 54.7% in second-quarter 2022 and 53.3% in third-quarter 2021. The sequential increase was driven by endpoint IC product margins, specifically the richer mix of specialty and industrial ICs. The year-over-year increase was driven by higher endpoint IC product margins, from both the specialty and industrial IC mix and a larger Impinj M700 mix, partially offset by decreased sales of fully reserved inventory.

Total third-quarter operating expense was $29.0 million, compared with $28.8 million in second-quarter 2022 and $24.4 million in third-quarter 2021. Research and development expense was $14.0 million. Sales and marketing expense was $7.4 million. General and administrative expense was $7.7 million. We expect similar total operating expense in the fourth quarter.

Third quarter adjusted EBITDA was $9.8 million, compared with $3.8 million in second-quarter 2022 and a loss of $400 thousand in third-quarter 2021. Third quarter adjusted EBITDA margin was 14.3%.

Third-quarter GAAP net loss was $2.2 million. Third-quarter non-GAAP net income was $9.3 million, or 34¢ per share on a fully diluted basis.

Turning to the balance sheet, we ended third quarter with cash, cash equivalents and investments of $201.1 million, compared with $183.7 million in second-quarter 2022 and $113.3 million in third-quarter 2021. Inventory totaled $31.9 million, down slightly from the prior quarter.

Third-quarter net cash provided by operating activities was $14.5 million. Property and equipment purchases totaled $2.3 million. Free cash flow was $12.2 million.

Before turning to our fourth-quarter guidance, I want to highlight a few items unique to our results and outlook.

First, third-quarter gross margins exceeded expectations, due primarily to the favorable shipment timing of specialty and industrial endpoint ICs. Looking forward, we anticipate gross margins to stabilize in the 53% to 54% range as endpoint IC mix normalizes, at least until further 300mm innovations create opportunities for gross-margin accretion.

Second, we currently anticipate receiving a meaningful quantity of wafers late in the fourth quarter that are scheduled for early first-quarter customer shipment. That balance-sheet timing will mask the fact that our shippable supply remains extraordinarily lean.

Third, equipment-delivery timing has resulted in lower-than-expected capital expenditures year-to-date. And despite some catch-up in fourth quarter, we now anticipate our 2022 CapEx will fall below 2021. Regardless, we have sufficient endpoint IC post-processing capacity that the equipment delays will not impact our ability to grow 2023 endpoint IC shipments.

Finally, as wafer upsides from our foundry partner continue layering in, we foresee increasing endpoint IC shipments driving mid-to-high single-digit sequential endpoint IC revenue growth in fourth-quarter 2022 and again in first-quarter 2023.

Turning to our outlook, we expect fourth-quarter revenue between $71.5 and $73.5 million, compared with $52.6 million in fourth-quarter 2021, a 38% year-over-year increase at the midpoint. We expect adjusted EBITDA between $9.8 and $11.3 million. On the bottom line, we expect non-GAAP net income between $9.0 and $10.5 million, reflecting non-GAAP fully diluted earnings-per-share between 32¢ and 37¢.

In closing, I want to thank the Impinj team for your outstanding execution this quarter, particularly in driving operating leverage, one of our key financial objectives. Back in 2020, we committed to returning to adjusted EBITDA breakeven. We have now delivered four consecutive quarters of positive adjusted EBITDA, with third-quarter 2022 setting a new record. And looking ahead, I see opportunities for continued operating-leverage improvement. Even as we continue investing in our business, we now turn our focus to our next goal, generating consistent free cash flow. I look forward to ongoing progress towards that goal. I will now turn the call to the operator to open the question-and-answer session. MJ.