



GSI Technology, Inc.

Third Quarter Fiscal 2022 Results Conference Call

January 27, 2022

CORPORATE PARTICIPANTS

Lee-Lean Shu, *Chairman, President and Chief Executive Officer*

Didier Lasserre, *Vice President, Sales*,

Douglas Schirle, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Jeffrey Bernstein, *Cowen*

PRESENTATION

Operator

Welcome to GSI Technology's Third Quarter Fiscal 2022 Results Conference Call.

At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session. At that time, we will provide instructions for those interested in entering the queue for the Q&A.

Before we begin today's call, the Company has requested that I read the following Safe Harbor statement. The matters discussed in this conference call may include forward-looking statements regarding future events and the future performance of GSI Technology that involved risks and uncertainties that could cause actual results to differ materially from those anticipated. These risks and uncertainties are described in the Company's Form 10-K filed with the Securities and Exchange Commission.

Additionally, I have also been asked to advise you that this conference call is being recorded today, January 27, 2022, at the request of GSI Technology.

Hosting the call today is Lee-Lean Shu, the Company's Chairman, President, and Chief Executive Officer. With him are Douglas Schirle, Chief Financial Officer, and Didier Lasserre, Vice President of Sales.

I would now like to turn the conference over to Mr. Shu. Please go ahead, sir.

Lee-Lean Shu

Good afternoon and thank you for joining us to review our fiscal third quarter 2022 financial results.

Our third quarter revenue grew year-over-year by 19% due to increased orders from our SRAM customer base, including network and telecom, military and defense, as well as automotive, medical, and test and measurement sectors. The increase in orders from other customers offset the lower orders from Nokia in the quarter. Gross margin improved by 800 basis points year-over-year, reflecting our ability to manage

our near-term supply chain challenges and increased costs. Our net loss narrowed year-over-year by 12%, and we ended the quarter with \$48.1 million cash, cash equivalents, and short-term investments

We continue to prioritize the allocation of our capital on R&D for the APU, which includes the software and API development for Gemini-I and the tape out for Gemini-II. The software development team continues to expand our library of algorithms and APIs for our targeted applications in Search. In February, we plan to release a compiler stack, and Didier will provide an overview of this in his section.

At the end of calendar 2021, we announced that GSI was among the leaders in the Billion-Scale Approximate Nearest Neighbor Search (ANNS) Challenge. We were encouraged by this outcome. The results showed that the APU technology and software performed on par with prominent industry leaders in AI, all with much broader resources than GSI. Contests teach us a lot about what we need to further develop and build, and how we can improve our performance.

Contests like Big ANN and the MAFAT Challenge are also effective ways to raise GSI's profile in our industry and with potential customers. These contests spotlight our team's capabilities and increase awareness of our APU unique value proposition. Last year, our first-place win in the MAFAT challenge resulted in our introduction to IAI/Elta, who engaged with GSI to develop a SAR image processing acceleration system using the APU and our software. Elta is funding the R&D to build a SAR system based on APU technology. Elta will grant an exclusive, perpetual license of the fast SAR algorithm to GSI to allow GSI to sell a SAR system including the algorithm to other customers. Assuming that the POC is successful, Elta will deploy the system in volume.

The GSI team continues to build a pipeline of customer engagement and increase our POC activity for the APU. In addition to the Elta SAR project, we are in discussions with several organizations to engage in POCs for a variety of use-cases for search applications we are targeting. Our current POC engagements include indexing medical images and text, encrypted communications, and natural language processing (NLP). A prime contractor is interested in testing a board for military and defense applications and we have a government agency considering the APU for object detection and facial recognition. We anticipate that a portion of these POCs will move to design-wins and eventually to production.

A few years back, once we had the Gemini-I chip available for testing, we made a strategic decision to pursue Search instead of the training and inference markets, where there were already large, well-funded competitors. The APU performed significantly better in search applications, and we decided to target our resources to develop that market. This has proven to be a good decision, as we are now seeing that Search may ultimately be a larger end-market. We recognized that the APU could work very efficiently with a trained database to rapidly search and deliver results, with low latency, low power consumption, and a scalable configuration. Accuracy, a smaller footprint, lowering the total cost of ownership, having "space-ready" chips, and reducing power consumption are key differentiators for the APU. We remain committed to our strategy and dedicating our capital to deliver the best technology for the rapidly growing search market.

Supply chain constraints continue to impact our order fulfillment. While there has been some improvement, the situation remains fluid. We have passed on some of the price increases and have factored in the extended lead times, but we do not expect significant relief from these constraints before the end of calendar year 2022. We have increased our operational focus on managing the supply chain to fulfill orders that we have in hand for the upcoming quarters. Doug will provide our outlook for the fourth quarter in his prepared comments.

This year will be a crucial year to proving out the feasibility of our groundbreaking APU technology. Our next important milestone is the release of the compiler stack in February. This release should accelerate customer adoption of our ground-breaking technology that can both lower enterprise AI capacity and

bring that capability to stand-alone servers at the edge. We are in the early stages engaging with customers who recognize the APU's potential for their applications. The compiler stack should help us grow our pipeline. It is an exciting time for GSI, and our team is focused on achieving our goals for current customer engagements, while continuing to build our pipeline new opportunities.

Now I'll hand the call over to Didier, who will discuss our business performance further.

Please go ahead, Didier.

Didier Lasserre

As Lee-Lean stated, we have new customer engagements in multiple applications ranging from e-commerce to military and defense for various use-cases. In our approach to the search market, we are pursuing opportunities that align with the applications we feel the APU is best suited. Right now, our team is seeding the field, and we fully expect that some will bear fruit. Our approach to supporting these customer engagements depends on the end users' needs. For some, we loan them a board to demo, some of them access our Sunnyvale data center to run their models, and some have purchased boards. Each of these engagements target unique market applications, and the ultimate size of each opportunity may vary. Since many are in the early stages of development, it is challenging to measure. That said, they are all of sufficient size to merit allocating our resources.

Today, we are working with universities with unique applications with broad market opportunities, a prime contractor that could eventually turn into a large order, and a government agency evaluating the APU for border security. There's also an e-commerce company looking at the APU for natural language processing. You can see why we are excited about these engagements, as they could potentially develop into customers and growth markets. Our objectives are to make the POCs as successful as possible for each entity, expecting a portion to move to design-wins and eventually to production.

As part of GSI developing its strategy for the AI and HPC, or high-performance computing, acceleration markets, we will soon be releasing an APU Compiler Stack. This release will deliver the environment for software and AI developers to write full applications using C for our Leda-E and Leda-S PCIe boards. The release will include example applications and training materials. Customers that need a specific use-case algorithm can edit our large collection of vector library functions or write their own APU fragments in Python using our low-level Belex stack product.

Achieving the APU Compiler Stack milestone should accelerate customer adoption and is one of the most important steps in front of us to move the APU to the next level. As I said earlier, the GSI team has been busy creating APIs for search workloads like image indexing, object recognition, natural language processing, as well as HPC workloads in the enterprise, and real-time SAR, ATR, and signal classification at the edge. We have documented that the APU technology can offer enterprise AI capacity in an edge stand-alone server, in support of that migration. The APU compiler stack is a powerful tool for researchers and developers that promises to significantly expand the market application of our non-Von-Neumann processor.

To help build a pipeline, GSI will introduce a series of training seminars to support the customization of our APIs for specific applications. The APU technology is available in a PCIe board for enterprise and edge server applications, capable of searching tens of millions of vectors per board. The platform is highly scalable, allowing us to connect unlimited boards installed in servers. The hardware capability can also function as a cloud-based Software-as-a-Service, for OpenSearch and Elasticsearch acceleration.

Once we launch the compiler stack, we plan to provide more detail in a press release. Let me switch now to the customer and product breakdown for the third quarter.

In the third quarter of fiscal 2022, sales to Nokia were \$1.9 million, or 24.0% of net revenues compared to \$2.8 million, or 42.0% of net revenues, in the same period a year ago and \$1.9 million, or 23.8% of net revenues in the prior quarter. Military/defense sales were 27.1% of third quarter shipments compared to 26.0% of shipments in the comparable period a year ago and 27.4% of shipments in the prior quarter. SigmaQuad sales were 40.5% of third quarter shipments compared to 62.0% in the third quarter of fiscal 2021 and 52.4% in the prior quarter.

In closing, as Lee-Lean mentioned, we have ongoing challenges with supply chain constraints with substrate lead times out more than a year. Overall, the impact of increased wafer prices, assembly labor costs, rising substrate prices and expediting charges led us to raise prices to all our customers in December.

I'd now like to hand the call over to Doug...please go-ahead, Doug.

Douglas Schirle

Thank you, Didier.

We reported a net loss of \$(4.6 million), or \$(0.19) per diluted share, on net revenues of \$8.1 million for the third quarter of fiscal 2022, compared to a net loss of \$(5.2 million), or \$(0.22) per diluted share, on net revenues of \$6.8 million for the third quarter of fiscal 2021 and a net loss of \$(4.6 million), or \$(0.19) per diluted share, on net revenues of \$7.8 million for the second quarter of fiscal 2022.

Gross margin was 55.3% compared to 47.3% in the prior year period and 53.6% in the preceding second quarter. The changes in gross margin were primarily due to changes in product mix sold in the three periods.

Total operating expenses in the third quarter of fiscal 2022 were \$9.0 million, compared to \$8.3 million in the third quarter of fiscal 2021 and \$8.7 million in the prior quarter. Research and development expenses were \$6.2 million, compared to \$5.7 million in the prior year period and \$5.9 million in the prior quarter. Selling, general and administrative expenses were \$2.8 million in the quarter ended December 31, 2021, compared to \$2.6 million in the prior year quarter, and \$2.8 million in the previous quarter.

Third quarter fiscal 2022 operating loss was \$(4.5 million) compared to \$(5.2 million) in the prior year period and \$(4.5 million) in the prior quarter.

Third quarter fiscal 2022 net loss included net interest income and other expense of \$15,000 and a tax provision of \$64,000, compared to \$25,000 in net interest and other income and a tax provision of \$90,000 for the same period a year ago. In the preceding second quarter, net loss included net interest and other expense of \$(8,000) and a tax provision of \$42,000.

Total third quarter pre-tax stock-based compensation expense was \$740,000 compared to \$693,000 in the comparable quarter a year ago and \$716,000 in the prior quarter.

At December 31, 2021, we had \$48.1 million in cash, cash equivalents and short-term investments and \$3.4 million in long-term investments, compared to \$54.0 million in cash, cash equivalents, and short-term investments and \$5.8 million in long-term investments at March 31, 2021. With no debt, working capital was \$49.9 million as of December 31, 2021, versus \$56.0 million at March 31, 2021. As of December 31, 2021, stockholders' equity was \$66.8 million compared to \$75.6 million as of the fiscal year ended March 31, 2021.

Supply chain constraints have impacted our ability to fulfill all of our orders. While there has been some improvement, the situation remains fluid, and we do not expect significant relief from these constraints before the end of calendar year 2022. Given these constraints, current expectations for the upcoming fiscal fourth quarter are net revenues in a range of \$7.5 million to \$8.5 million, with gross margin of approximately 54% to 56%.

Operator at this point we will open the call to Q&A.

Operator

Thank you.

Our first question comes from the line of Jeff Bernstein with Cowen. You may proceed with your questions.

Jeffrey Bernstein

Hi, guys. In terms of the orders that you have not been able to fulfill, are those gone? Do those go to someone else, or is that a backlog that's building up?

Didier Lasserre

The majority of it is backlog that's built up. I mean, certainly, some of them where we have multiple sources may have gone. With that said, it's a very small percentage of our business. The majority of it is sitting there and will be fulfilled later.

Jeffrey Bernstein

Got you. Okay, and then can you just give us a quick update on the Rad-Tolerant efforts?

Didier Lasserre

Sure. The Rad-Tolerant, we spoke in the past, we've had some shipments out, in fact, on some Rad-Hard as well. And so some of those we are in the prototype stages. We're waiting for them to do their testing. It takes some amount of time. What we didn't discuss is, in this quarter we actually booked another prototype for actually a Rad-Hard device. So we have a Rad-Hard on the books now that will ship hopefully this quarter. And again, it's for prototyping for a satellite that will go into production in a couple of years. So we're starting to still see some prototyping. As we mentioned in the past, the Rad-Hard still is a bit of a challenge, because some of the meetings we still can't have. But the Rad-Tolerant we're still seeing, certainly, traction there.

Jeffrey Bernstein

Okay. And then, there was the issue of actually getting some of these parts into space before some people would look at using them. Where are we on getting a ride?

Didier Lasserre

Right. Exactly. That's called heritage. So once you get heritage, which is proving that your parts work in space, it certainly makes our job with most customers very easy. In fact, we've had several customers that have said that they're going to wait for heritage before they move forward. Some of the parts that we shipped in I want to say summer of last year, it was late summer, maybe calendar third quarter, those were going to be our first parts that can get into space. Those are being put on the satellites being assembled now. So we're hoping it's launched sometime this year, and we certainly don't have control of when that happens. We are following up with that customer often, and right now it's sometime in Calendar 2022 they will be in space. If you recall, that was a demo system for a possible constellation in the future, but that would give us our first heritage, and we're hoping that's this year.

Jeffrey Bernstein

All right, thanks.

Operator

Okay, at this time, not seeing any more questions. I'd like to pass it back over to Mr. Shu for closing remarks.

Lee-Lean Shu

Thank you all for joining us. We look forward to speaking with you again when we report our Fourth Quarter and Full Year Fiscal 2022 results. Thank you.

Operator

This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation, and have a great day.