Impinj Second Quarter 2017 Earnings Conference Call
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MARIA RILEY, INVESTOR RELATIONS FOR IMPINJ

Thank you, Operator. Thank you all for joining us to discuss Impinj's second quarter 2017 results. On today's call, Chris Diorio, Impinj's Co-Founder and Chief Executive Officer, will provide a brief overview of our performance and market. Evan Fein, Impinj's Chief Financial Officer, will follow with a detailed review of our second quarter 2017 financial results and third quarter 2017 outlook. We will then open the call for questions. Impinj's President and COO, Eric Brodersen, is also on the call and will join Chris and Evan in the Q&A session. Please note that management's prepared remarks, along with quarterly financial data for the last eight quarters, are available on the company's website. Also, we will consider questions received via email prior to the call and will address some of these questions in the Q&A session on this call.

Before we start, note that we will make certain statements during this call that are not historical facts, including those regarding our plans, objectives and expected performance. To the extent we make such statements, they are forward-looking within the meaning of the Private Securities Litigation Reform Act from 1995. Any such forward-looking statements represent our outlook only as of the date of this conference call.

While we believe any forward-looking statements we make are reasonable, our actual results could differ materially because any statements based on current expectations are subject to risks and uncertainties. Please see the risk-factors sections in the annual and quarterly reports we file with the SEC for additional information about these risks. We do not undertake, and expressly disclaim, any obligation to update or alter our forward-looking statements, whether as a result of new information, future events, or otherwise except as required by applicable law.

Also, during today's call, all statement of operations results, with the exception of revenue, or where we explicitly state otherwise, are non-GAAP financial measures. Balance sheet metrics and cash flow metrics are on a GAAP basis.

Before moving to the financial results, I'd like to announce that Impinj management will attend the Canaccord Genuity Growth Conference on August 9th in Boston. We hope to have the opportunity to see many of you there.

I will now turn the call to Chris Diorio, Impinj Co-Founder and Chief Executive Officer. Chris.

Chris Diorio, Impinj Co-Founder and Chief Executive Officer

Thank you, Maria. Thank you all for joining the call. I'm delighted to be here with you today.

We delivered a strong second quarter, with revenue growing 31% year-over-year to $34.1 million dollars, just above the top end of our guidance. Consistent with the market dynamics I described on our last earnings call, our second-quarter momentum remained strong, and my long-term view of the RAIN market remains "strong growth with enormous potential".

In the second quarter we saw significant wins and expanded deployments in retail, logistics and healthcare. We and our partner SLS enabled a major U.S. apparel retailer to automate logistics operations in their new 500,000 square-foot distribution center. Faurecia, the large European automotive supply company we discussed on our last call, has now deployed the Impinj platform at four of its logistics centers. With our partner Argo Wireless we expanded our platform deployment at a large Texas hospital, tracking 60,000 durable medical assets. And McDonalds Europe continues their roll out, with the Impinj platform now operational in 148 restaurants. Our fixed-reader business also continued its strong growth, with second-quarter reader and gateway unit volumes together up 53% year-over-year, driven in part by improved sales and channel execution behind updated partner programs.

We have previously disclosed the large size of some of our end-customer opportunities and how their rollout timing can be unpredictable. In 2016 we benefitted from several large end-customer rollouts that helped drive our endpoint IC volumes up approximately 70% over 2015. As we enter the third quarter we see a different situation, with several large end customers delaying planned expansions. I visited two of these customers, overseas, in the last 30 days. According to them, their deployment plans and goals remain unchanged, but their rollouts are delayed by internal schedule slips. Consequently, we are reducing our full-year 2017 endpoint IC guidance from between 7.8 and 8.0 billion units to between 7.0 and 7.2 billion units, representing 18% growth over 2016 at the midpoint.

Let me put our revised guidance in perspective. Our endpoint IC growth for 2010 through 2017 remains at roughly a 30% CAGR. The 2017 midpoint, 7.1 billion units, is a huge number. But it is still a miniscule fraction of the total number of connectable items per year. Some end users already consume more than 500 million ICs per year; future potential end users, such as the five

Japanese convenience-store chains we discussed on our last call, together anticipate using 100 billion ICs per year. We are, as I said on our last call, landing whales. Sometimes a few quicken their pace, like we saw in 2016. And sometimes a few go slower than we expected them to, like we see now. For these large opportunities, a rollout speedup or delay can represent several hundred million ICs to us. We are learning in real time the dynamics of leading a nascent but gigantic opportunity, engaging large end users who can set the adoption pace for their industry and help grow our opportunity to its long-term potential. And our focus remains that gigantic opportunity, that macro trend of connecting businesses and people to everyday items. So expect us to continue driving hard to accelerate and win every opportunity in every vertical we pursue, competing relentlessly with and at every layer of our platform, and investing in the people, platform and solutions that drive scale and long-term value.

Turning now to that platform and those solutions, we have previously emphasized the importance of fixed readers to our future. Unlike handheld readers, fixed readers deliver RAIN data in real-time, enable use cases that handheld readers cannot deliver and do not have ongoing labor costs. In the second quarter we introduced the Speedway R120 enterprise-class fixed reader, optimized for smart fitting rooms, inventory management and interactive product displays. With our introduction of the R120 we now sell a fully developed enterprise-class fixed-reader family with coverage from one to thirty-two read zones, allowing end customers to right-size their readzone coverage to their business needs. Our gateway family complements those fixed readers by locating items and tracking item transitions. Together, our industry-leading fixed readers and gateways allow end users to optimize their hands-free deployments in retail, healthcare, logistics, manufacturing and many other verticals. We also introduced a new reader module, the Indy RS1000, optimized for embedded reader integrations such as at point of sale.

We introduced four joint solutions in the second quarter, two in laundry, one in retail and one in fast food. We haven't previously discussed laundry on our calls, and although not as well-known as other opportunities we have discussed, our laundry opportunities span Asia, North America and Europe. Our partners use our platform to lease, source, clean, and maintain connected linens and uniforms in healthcare, hotels, restaurants and cleanrooms. These deployments, which already connect tens of millions of laundry items, employ specialized tags, embedded within the linen or garment, that survive repeated washings and pressings. Fixed readers identify, sort and track the connected laundry items. The result: faster processing, improved efficiencies and reduced loss. As one example, Berendsen, a large UK textile-service solution provider, uses our platform to process 15,000 laundry items per day at a single facility.

In retail, our joint solution with Capgemini uses our platform to identify and locate individual retail-store items by combining order and product information from SAP with data about an item's identity and location in IBM Bluemix, delivering real-time store inventory and eliminating manual stock counting. And our joint solution with Retail Reload allows French lingerie retailer Undiz to improve the consumer shopping experience by having up-to-date inventory available online, allowing shoppers to use their smartphones to select items before they get to the store. Upon arriving at the store, beacons detect the product from a smartphone app. Ninety seconds later, capsules shoot the items via pneumatic tubes from the store's stockroom to a kiosk. Shoppers can then pay on the spot without having to wait in line for a cashier.

In my talk at the RAIN Alliance meeting two weeks ago, I painted a picture of Impinj's vision of digital life for everyday items – a picture of what I believe is an inexorable trend in which every physical item has a digital life, a digital twin. The physical item has identity, location and authenticity. The digital twin has history, services and ownership. If you missed the meeting then I'd encourage you to look at that presentation, posted on the RAIN Alliance website. I'm energized by this vision, and my presentation is part of my effort to engage the community to drive it together. Other meeting presentations on the website, especially those from healthcare professionals, describe automated inventory replenishment, operating-room asset management and improved efficiencies and labor savings in hospitals. To me, their assessment of the value that RAIN solutions bring to the healthcare market is compelling.

In summary, I am proud of the Impinj team's execution this quarter and our continued progress toward our vision of digital life for everyday items. We grew to 283 employees and exited the quarter with 216 issued and allowed patents, an increase of six over last quarter. Although we see rollout delays, we understand those delays and remain confident and excited about our market leadership and our opportunity. Consequently, we intend to hold a steady course and continue investing in our people, platform and solutions. I will now turn the call over to Evan to give you a detailed look at our second quarter financial results and our outlook for the third quarter. Evan.

Evan Fein, Impinj Chief Financial Officer

Thanks, Chris. Before I review our second quarter 2017 financial results I want to remind you that with the exception of revenue, or unless explicitly stated otherwise, today's statement of operations is on a non-GAAP basis. All balance-sheet and cash-flow metrics are on a GAAP basis. A reconciliation between our non-GAAP and GAAP measures, as well as how we define our non-GAAP measures, is included in our earnings release available on our website.

As Chris mentioned, we delivered a strong second quarter, with revenue of $34.1 million dollars, representing 31% growth over second quarter 2016. Gross margin was 54.7%, compared with 53.4% in the second quarter of 2016. The 130 basis-point year-over-year improvement reflects continued adoption of our Monza R6 endpoint IC family.

Total operating expense in the quarter was $17.2 million, or 50.5% of revenue, compared with $17.0 million, or 53.4% of revenue in the prior quarter. R&D expense was $6.4 million, or 18.7% of revenue. Sales and marketing expense was $6.3 million, or 18.6% of revenue. G&A expense was $4.5 million, or 13.2% of revenue. We ended the quarter with 283 employees and 31 open positions, compared with 261 employees at the end of last quarter.

We delivered $1.4 million in adjusted EBITDA in the quarter, or 4.1% of revenue, compared with $246 thousand, or 0.8% of revenue in the prior quarter.

GAAP net loss for the quarter was $977 thousand. On a non-GAAP basis, we achieved second quarter net income of $1.3 million, or earnings of 6¢ per share, using a weighted-average diluted share count of 21.9 million shares.

Turning to the balance sheet, we ended the quarter with cash and cash equivalents and short-term investments of $74.5 million. Accounts receivable balance was $25.5 million, up $4.5 million from last quarter.

We increased inventory by $4.2 million over the prior quarter, bringing our inventory balance to $43.4 million. We will continue investing in inventory to build 1 billion units of endpoint IC buffer by year end, but at a slower pace going forward because we have already purchased most of that inventory buffer.

Turning now to our outlook, we expect third quarter 2017 revenue to be in the range of $31.75 to $33.25 million, up 4.6% year over year. We expect adjusted EBITDA to be a loss between $1.65 million and $150 thousand. We intend to maintain our current level of investment in the business, so on the bottom-line we expect non-GAAP earnings to be a loss between $1.7 million and $200 thousand or a loss between 8¢ and 1¢ on a per share basis using a weighted-average basic and diluted share count in the range of 20.8 million to 21.3 million shares.

As Chris already noted, we expect our full-year 2017 endpoint IC volume to be between 7.0 and 7.2 billion units, representing 18% growth over 2016 at the midpoint. We are confident in the long-term adoption trend, our market leadership and our progress towards our vision of digital life for everyday items.

I will now turn the call over to the operator to open the question-and-answer session.