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CAMT.TA - Q4 2019 Camtek Ltd Earnings Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Camtek's Fourth Quarter and Full Year 2019 Results Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

You should have all received by now the company's press release. If you have not received it, please contact Camtek's Investor Relations team at GK Investor & Public Relations at 1 (646) 688-3559 or view it in the News section of the company's website, www.camtek.com.

I would now like to hand over the call to Mr. Ehud Helft of GK Investor Relations. Mr. Helft, would you like to begin, please?

Ehud Helft - *CCG Investor Relations Inc. - Managing Partner - Israel*

Yes. Thank you, operator. Good day to all of you. I would like to welcome all of you to Camtek's Fourth Quarter and Full Year 2019 Results Conference Call. And I would like also to thank Camtek's management for hosting this call. With us on the line today are Mr. Rafi Amit, Camtek's CEO; Mr. Moshe Eisenberg, Camtek's CFO; and Mr. Ramy Langer, Camtek's COO. Rafi will provide an overview of Camtek's results and discuss market trends in the fourth quarter of 2019. Moshe will then summarize the financial results of the fourth quarter and the full year. We will then open the call to take your questions.

Before we begin, I would like to remind our listeners that certain information provided on this call are internal company estimates unless otherwise specified. This call may contain forward-looking statements. These statements are only predictions and may change as time passes. Statements on this call are made as of today, and the company undertakes no obligation to update any of the forward-looking statements contained whether as a result of new information, future events, changes in expectation or otherwise. Investors are reminded that actual events or results may differ materially from those projected, including as a result of changing industry and market trends, reduced demand for services and products, the timing and development of new services and products and their adoption by the market, increased competition in the industry and price reductions as well as due to other risks identified in the company's filings with the SEC. Please note that the safe harbor statement in today's press release also covers the content of this conference call.

In addition, during this call, certain non-GAAP financial measures will be discussed. These are used by management to make strategic decisions, forecast future results and evaluate the company's current performance. Management believes that the presentation of non-GAAP financial measures is useful to investors' understanding and assessment of the company's ongoing core operation and prospects for the future. A full reconciliation of non-GAAP to GAAP financial measures is included in today's earnings release.

I would now like to hand over the call to Rafi Amit, Camtek's CEO. Rafi, go ahead, please.

Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

Okay. Good morning, and thank you for joining our call today. Camtek closed 2019 with record revenue and profit. I'm very proud of our achievements considering the weakness of the semiconductor market in 2019. Q4 ended with sales of \$33.2 million, and total sales in 2019 were \$134 million, which represents 9% growth year-over-year, while the semi market as a whole dropped by over 10%. We also demonstrated improvement in our profitability with \$25 million operating profit, which account to 18.7% of our revenue versus 18% in 2018.

As we discussed in our last call, market drivers supporting demand for our equipment have not changed. I would like to briefly summarize our activities in the various segments we serve. The CMOS Image Sensor continues to be significant to our business. As recently announced, we received order for 34 machines for CMOS Image Sensor application, mostly from customers outside of China. Our customers in this segment are expected to continue increasing their capacity due to the growing number of cameras in smartphone and especially in high-end phones supporting 5G. In addition, the higher-resolution sensor and cameras result in longer inspection time and more advanced capabilities, which require new and up-to-date inspection tools. Advanced interconnect packaging remains key to the expansion of many applications and continues to be a fast-growing segment. Especially in the memory space, we expect the DRAM transition into advanced packaging to resume in the second half of 2020 driven by the technical requirements for higher bandwidth and lower power consumption. In addition, the RF segment is expected to benefit from the production of 5G, and we expect to see growing demand in 2020.

In the front-end space, we continue to expand our presence to new applications and additional customers in China and other territories. During the fourth quarter, we received and installed additional machines at an existing major customer. During 2019, we launched several new exciting products, the EagleT+ for 2D inspection and EagleT+ AP for 3D metrology. This new product significantly improved our competitive position in terms of throughput and detection capabilities.

The market trends I just discussed, along with complex technology advantages and market position, are the reason for our expectations to maintain our ongoing growth and performance. We started 2020 with a strong backlog for the first half of the year. As we announced a few weeks ago, we received order for 34 machines for the CMOS Image Sensor market and additional multiple machines for other applications from 2 of the top 3 OSATs.

More than 70% of the orders we have received for the first half of 2020 came from outside China. The Chinese market continues to be significant to our business and represent important growth driver. We continue to receive orders from this territory. And even in recent days, we received several orders for major Chinese customers. Based on orders in hand, we expected revenues of between \$33 million and \$34 million for the first quarter. However, despite the current demand for complex product by Chinese customer, certain governmental restriction aiming to control the spread of the coronavirus may cause delays in installation in China and may therefore impact Camtek's revenue in the first quarter. At this stage, we assume that the situation is getting better, and we will be close to meet our revenue targets. Any delay in installation in Q1 will be shifted to Q2.

We have good visibility into our second quarter revenues, which are expected to be strong. Assuming the coronavirus situation resolved not too far into the second quarter, we expect that the first half of 2020, we would recognize revenues at the record level of approximately \$70 million. Regarding the supply chain for building our machines, at this stage, we don't expect delays in meeting the demand. However, we have no way to predict how the coronavirus situation will affect the supply chain in the long run.

I would like to take the opportunity to thank Camtek's employees and management team for the contribution to the company's record performance. Regarding our Chinese employees, all of them are well. Our heart goes out to them, and we hope their lives return to normal soon.

I would like to hand over to Moshe for a more detailed financial discussion of the financial results. Moshe?



Moshe Eisenberg - *Camtek Ltd. - VP & CFO*

Thanks, Rafi. We had good results in the fourth quarter with revenues within our guidance and improved profitability versus the previous quarter. In my financial summary ahead, I will provide the results on a non-GAAP basis. The reconciliation between the GAAP results and the non-GAAP results appear in the tables at the end of the press release issued earlier today.

Fourth quarter revenues came at \$33.2 million, similar to those of the fourth quarter of 2018. Full year revenues were a record \$134 million, up 9% year-over-year. The results were driven by demand across all our segments and applications. The geographic revenue split for the quarter was as follows: Asia was 92%; and rest of the world, 8%.

Gross profit for the quarter was \$15.9 million. The gross margin for the quarter was 48% versus 50.6% in the fourth quarter of last year, with product and sales mix affecting the margin. Gross profit for the year was \$65.1 million, representing a gross margin of 48.6%. This is compared with a gross margin of 49.7% last year.

Operating expenses in the quarter were \$10.5 million. This is compared with \$9.9 million in the fourth quarter of last year and to the \$10.1 million reported in the previous quarter. We know that while we have continued to strengthen the sales organization and increase our investment in R&D, we have kept the G&A at the same level.

Operating profit in the quarter was \$5.4 million compared to \$6.9 million reported in the fourth quarter of last year. Operating margin was 16.3% compared to 20.7% mainly as a result of a lower gross margin. Operating profit for the year was \$25 million or 18.7% of revenues. This is compared to operating profit of \$22.2 million in 2018 or 18% of revenues.

A few words about our profitability in general. Our gross margin depends on several parameters. The main parameter will be sales volume and product mix. Our gross margin is higher when we sell more machines to Tier 1 customers, to front-end customers and to customers who need machines that combine 2D and 3D. In the first half of 2020, we are strengthening our position as a leading 2D inspection supplier for the back-end segment. A large portion of our new customers are those who ordered 2D inspection machines for simple applications, such as post-dicing with relatively lower ASP and therefore slightly lower gross margin of about 46% to 48%. Our strategy is to expand our installed base worldwide so in the future, the same new customers will purchase machines for more complex applications with higher ASP.

Overall, we expect operating margin in the first half to be at the level of 16% to 18%. We expect our average selling price and gross margin to improve in the second half of 2020 as a result of several developments we are conducting with major Tier 1 customers.

Net income for the fourth quarter of 2019 was \$5.4 million or \$0.14 per diluted share. This is compared to a net income of \$6.4 million or \$0.17 per share in the fourth quarter of last year. Net income for the year was \$23.9 million or \$0.62 per diluted share. This is compared to a net income of \$20.9 million or \$0.57 in 2018.

Turning to some high-level balance sheet and cash flow metrics. We generated \$7.5 million in cash from operations in the quarter. Net cash and cash equivalents and short-term deposits as of December 31, 2019, increased to \$89.5 million compared with \$83 million at the end of the third quarter of 2019. During 2019, we generated close to \$25 million in cash from operations.

As Rafi mentioned earlier, we have a very strong backlog for the first half of the year, and we expect record revenues of approximately \$70 million for this period. Given the situation in China, although we have orders in hand and working plan for \$33 million to \$34 million, there may be a shift in revenues in recognition between Q1 and Q2.

And with that, Rafi, Ramy and myself will be open to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question is from Quinn Bolton of Needham & Company.

Quinn Bolton - *Needham & Company, LLC, Research Division - Senior Analyst*

Congratulations on the nice fourth quarter results and a strong backlog for the first half. I understand that the coronavirus is making near-term visibility and the split between first and second quarter a little bit difficult, but I was hoping you might be able to help us size what the risk is. First, I wanted to confirm, you said in your backlog, 70% or more of the orders are for deliveries outside of China. Is that correct?

Moshe Eisenberg - *Camtek Ltd. - VP & CFO*

Yes, we said that 70% of our -- of the orders we have received are from customers outside of China.

Quinn Bolton - *Needham & Company, LLC, Research Division - Senior Analyst*

So can I assume that roughly 30-ish percent of orders would be scheduled for customers in China in the first quarter? So you've got roughly about \$10 million or so of revenue that is scheduled to be delivered in China, and that amount of revenue was going to be subject to travel disruptions and potentially some portion of that shifts from Q1 to Q2?

Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

No, I don't think so. I don't think so because first of all, part of them, we already installed and the situation in China now getting better. I would say the only issue right now is related to engineer that -- our engineer that are supposed to install machine. Today, the new instruction that if our engineer needs to install machine, he should go to this city where the machine should be installed a week prior to the installation before we enter the new site. So this is right now the -- I would say the main issue, how to manage it and how to control it. Assuming things going better, we can manage it.

So this is why we believe that we are very close to meet this target. But that's what we know today. We still have about 1.5 months, and many things can happen. Could be more positive, could be the other way, we don't know yet.

Quinn Bolton - *Needham & Company, LLC, Research Division - Senior Analyst*

Okay. Understood. And then wanted to sort of ask, your margin commentary suggests that margins strengthen in the second half of the year, I think, you said because of activity with Tier 1 customers. Wondering if there's also a volume component to the better margins in the second half. So I guess as you look at the business, do you have any comments you can make about first half, second half seasonality? Do you see sort of a flat first half, second half? Do you think second half revenue could actually grow based on that Tier 1 activity in -- sorry, yes, in the second half?

Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

Moshe?



Ramy Langer - *Camtek Ltd. - VP & COO*

First of all, I think it is much too early at this stage to talk about the second half from the focus point of view. So what we can talk at this stage, and I think Moshe covered it, is the mix of the product that we are expecting in the second half. Whether it will be better, I think it is too early at this stage to talk about the volume, level of the revenues of the second half.

Quinn Bolton - *Needham & Company, LLC, Research Division - Senior Analyst*

Great. And then last one for me. You mentioned the EagleT+ platform with better throughput and detection capabilities. Wondering if you could just compare that to the existing EagleT platforms. Is it a 10%, 20% better throughput or any metrics you could share with us on the improved performance?

Ramy Langer - *Camtek Ltd. - VP & COO*

It depends on the application, but it varies from 20% to 30% up to 50% faster.

Operator

The next question is from Craig Ellis of B. Riley FBR.

Peter Peng - *B. Riley FBR, Inc., Research Division - Associate Analyst*

This is actually Peter Peng calling in for Craig Ellis. First off is just on the March quarter, if you can just kind of talk about some of the end market dynamics. Is it kind of flattish across the end segments? Or do you see some stronger than the other?

Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

Ramy?

Ramy Langer - *Camtek Ltd. - VP & COO*

When we talk about the segments, and I think Rafi discussed it in details, first of all, if we look at the CMOS Image Sensors, no doubt that this specific segment is growing and growing very fast. We thought already last year, we had a pretty good year for this segment. This year is going much bigger. And then we've talked about the orders that we already have on hand. So this is one specific segment. The segment, segment is advanced packaging that continues to grow. We see the heterogeneous integration and several other applications. And we also believe that the DRAM transition to advanced packaging will start -- will resume in the second half of this year. No doubt the advanced packaging is going to be significant in the second half of this year.

And last but not least, of course, is the 5G. And the 5G is driving other businesses like the RF. For example, the number of filters in a mobile phone that contains 5G component will be 2 to 3x compared with 4G. Obviously, this is driving a lot of capacity, and also, the inspection time for the new filters is much higher. It requires -- a lot of those filters require much more inspection and smaller dimensions. So I would say these are the 3 major segments or the major applications that we see at this stage that are going to dominate 2020.

Peter Peng - *B. Riley FBR, Inc., Research Division - Associate Analyst*

Got it. And then for just the second quarter, the implicit Q-on-Q dollar growth is about \$3 million just based on the orders range from CMOS Image Sensors. Could we kind of assume that this is -- that's what's driving the incremental \$3 million Q-on-Q?



Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

You want to comment on it, Moshe?

Moshe Eisenberg - *Camtek Ltd. - VP & CFO*

Not necessarily. I mean there is -- indeed, if you take the Q1 and then the overall first half, there is some \$3 million to \$4 million increase in the second quarter. But I can't really say that it's -- the incremental piece is related only to the CMOS but to other applications as well.

Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

Yes. I would like to add one more comment on that here to realize, at this point, all our customers, including China, insist of installation on time. They need the machine. They push us to install the machine. We do not see any delay or any request to delay. This is the current situation right now.

Peter Peng - *B. Riley FBR, Inc., Research Division - Associate Analyst*

Got it. And then can you provide, I guess, the 2D versus 3D mix?

Ramy Langer - *Camtek Ltd. - VP & COO*

It's -- I don't think that we can really go here into the details. What I can say that we are -- the 2D is larger than the 3D. I mean the market size of the 2D is significantly larger. And therefore, our business today after gaining a lot of market share in the last few years, obviously, it is bigger than the 3D. And we expect it to continue this way.

Peter Peng - *B. Riley FBR, Inc., Research Division - Associate Analyst*

Got it. And one final question for me. Just on the operating margin, as mentioned, 16% to 18% in the first half. So should we kind of just think about OpEx kind of being flattish from the 4Q levels and then margin, potentially a slight increase? How should we kind of think about that profile, the 16% to 18% operating margin?

Moshe Eisenberg - *Camtek Ltd. - VP & CFO*

Yes. So what we have said earlier is that the gross margin in the first half of the year will vary between 46% to 48%, slightly lower than our normal rates of 48% to 50% from last year. Operating expenses in the first half are actually expected to be slightly lower than the current level, although later in the year, we plan to increase the OpEx level mainly on the R&D front.

Operator

The next question is from Gus Richard of Northland Securities.

Auguste Philip Richard - *Northland Capital Markets, Research Division - MD & Senior Research Analyst*

In terms of the RF demand, can you just give us a little color on what region that's coming from? Is it China, Japan or North America or Taiwan?



Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

Ramy?

Ramy Langer - *Camtek Ltd. - VP & COO*

Well, this comes from all over. I mean it comes from Europe. It comes from Asia. There is also the U.S. So I think it is global. I can't limit it to one specific region. It's less in China, though. It's more Asia, U.S. and Europe.

Auguste Philip Richard - *Northland Capital Markets, Research Division - MD & Senior Research Analyst*

Okay. Got it. And this is -- you may not know the answer to this one. Is this more sub-6 gigahertz applications? Or is it millimeter wave?

Ramy Langer - *Camtek Ltd. - VP & COO*

So if you look at it, the sub-6, the number of capacitors will be about double. And when you talk to the full 5G, then it's close to 3x. It's close. And so -- but it's also moving to different -- it's different filters. It's basically -- some are sub, some are already above. So it's a little bit more complex. But overall, you can take the numbers that are multiplied. If you double is the sub-6 gigahertz in full 5G is about 3x.

Auguste Philip Richard - *Northland Capital Markets, Research Division - MD & Senior Research Analyst*

Okay. I understand. And then I think you talked a little bit about new front-end applications and new applications in general. Is there any more color you can provide?

Ramy Langer - *Camtek Ltd. - VP & COO*

I don't think we talked about new application. In general, I think what we said in the script, and this is what we are doing, we are doing in the front end -- I would say, the primary application is macro inspection, which is the back end of the line. I think we've been very successful in this area. And this is, I would say, the bulk of the business in the front end.

Operator

(Operator Instructions) There is a follow-up question from Quinn Bolton of Needham.

Quinn Bolton - *Needham & Company, LLC, Research Division - Senior Analyst*

Just a quick follow-up for Moshe. Moshe, it looks like -- and maybe I missed it, but it doesn't look like you gave a share count in the press release for the fourth quarter and the full year. Should you have that number for Q4 and 2019?

Moshe Eisenberg - *Camtek Ltd. - VP & CFO*

I don't have the exact share count in front of me. I can send it over right after the call if you don't mind.



Quinn Bolton - *Needham & Company, LLC, Research Division - Senior Analyst*

Okay.

Operator

There are no further questions at this time. Before I ask Mr. Amit to go ahead with his closing statement, I would like to remind participants that a replay of this call will be available on Camtek's website, www.camtek.co.il, beginning tomorrow.

Mr. Amit, would you like to make your concluding statement?

Rafi Amit - *Camtek Ltd. - Chairman of the Board & CEO*

Okay. I would like to thank you all for your continued interest in our business. Again, I would like to thank all of you, all our employees and my management team for the tremendous performance in 2019 so far, and we look forward to continuing. To our investors, I thank your long-term support. I look forward to looking (sic) [talking] with you again next quarter. Thank you, and goodbye.

Operator

Thank you. This concludes the Camtek's Fourth Quarter and Full Year 2019 Results Conference Call. Thank you for your participation. You may go ahead and disconnect.

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