PCTEL Q2 2016 FINANCIAL RESULTS CONFERENCE CALL

August 2, 2016

OPERATOR:

Ladies and Gentlemen, thank you for standing by, and welcome to the PCTEL second quarter 2016 conference call. At this time, all participants are in a listen-only mode. Later, we will open up the call for your questions. Instructions for queuing up will be provided at that time. As a reminder, this conference call is being recorded for replay purposes.

I will now turn the call over to John Schoen, Chief Financial Officer.

John Schoen:

Thank you for joining us today for the PCTEL financial results conference call for the second quarter 2016. On today's call will be Marty Singer, Chairman and CEO, and I am John Schoen, Chief Financial Officer.

Our remarks contain forward-looking statements and projections of future results. Please review the forward-looking statement section at the end of today's earnings release for various factors that could cause actual results to differ materially from projections.

PCTEL reports its financial results in accordance with U.S. generally accepted accounting principles. Today's call will contain various operating results on an adjusted Non-GAAP basis, which excludes items that affect the comparability of reported results. Descriptions of these non-GAAP financial measures and reconciliations are included in today's earnings release, which is available on our website.

Now I'll turn the call over to Marty.

MARTY SINGER:

Thank you, John, and good evening.

For those of you who have not had the opportunity to review our press release, let me recap some of the Non-GAAP highlights from the quarter:

- We achieved revenue of $24.2 million, an increase of approximately $3.2 million over the first quarter.
- Gross Profit Margin was 39 percent.
- Operating Margin was six percent.
- Net income was $1.3 million; or $0.08 per diluted share.
- Cash and investments were $29.3 million, an increase of $1.4 million from last quarter.
- We generated approximately $2.4 million in free cash flow.
- We paid $853,000 in dividends.

At this point, I will turn the call over to John Schoen, who will discuss our financial performance in some detail. After John completes his remarks, I will discuss our new products, markets, and strategic direction.

JOHN SCHOEN:

Revenue

Revenues were $24.2 million in the quarter, down 12 percent from the same period last year. I will speak to the changes by reporting segment.

RF Solutions revenue was $8.5 million in the quarter, down $1.1 million, or 11 percent, from the same period last year. Services revenue declined, largely associated with Samsung, which was partially offset by growth in product revenue. The Samsung contract ended after the second quarter last year.

Connected Solutions revenue was $15.8 million in the quarter, down $2.3 million, or 13 percent from the same period last year. The second quarter last year included a $3 million discrete project for Cisco and $350,000 in mobile tower revenue.

Gross Profit Margin

Non-GAAP gross profit margin as a percent of sales was 39 percent in the quarter compared to 35 percent in the same period last year. I will speak to the changes by segment.

RF Solutions gross profit margin as a percent of sales was 53 percent in the quarter compared to 44 percent in the same period last year. The major contributor to the improvement was the increased mix of product revenue with its higher margins compared to services.

Connected Solutions gross profit margin as a percent of sales was 31 percent in the quarter, up three percent of revenue from the same period last year. The change is attributed to manufacturing cost reductions implemented in the fourth quarter last year.

Operating Expenses

Now let's turn to Non-GAAP operating expenses. Operating expenses were $8.0 million in the quarter. This is a $1.4 million decrease from the same period last year. The decline is attributed to the restructuring cost reductions implemented in the second half of 2015.

Non-GAAP Income Taxes

The Non-GAAP income tax rate in the quarter and the year was 18 percent, unchanged from the prior year.

Non-GAAP Earnings

Non-GAAP net income per share was $0.08 compared to Non-GAAP net income of $0.02 in the same period last year. The increase was driven by cost reductions implemented in both manufacturing and operations during the second half of 2015.

Our GAAP earnings in the quarter were a loss of $11.1 million, or $0.69 per share. There were two non-cash charges that aggregated to $12.4 million pre-tax, or $0.66 of the loss net of tax. The first was a $4.7 million dollar non-cash impairment of acquired intangible assets related to engineering services. The Company experienced a decline in services revenue primarily related the ending of the Samsung contract after the second quarter of 2015 and a slow-down in DAS spending by the carriers. The Company is replacing that revenue with other types of work, but is not experiencing the same margins it had when the assets were originally capitalized. The result is an impairment of the intangible assets by $4.7 million.

The second item is a $7.6 million charge for the establishment of a valuation reserve on the deferred tax assets in the U.S. tax jurisdiction. For U.S. tax purposes, the Company deducts the intangible assets and goodwill from its acquisitions over a 15 year period but they are amortized over a much shorter period for book, creating a deferred tax asset. The Company’s growing success in small cell sales to large wireless infrastructure OEMs has caused more of the Company’s anticipated future worldwide taxable income to be outside the U.S. tax jurisdiction than previously forecast. The result is the Company believes some of its future U.S. tax benefits will not be realized as they will not be recoverable within the maximum carry forward period.

Balance Sheet & Cash Flow

Now let us turn to the balance sheet.

Cash and investments ended the quarter at approximately $29.3 million, about $1.4 million higher than the previous quarter.

In the quarter, the Company generated free cash flow of approximately $2.4 million, comprised of cash flow from operations of $3.1 million and capital spending of $700,000. The Company was able to reduce working capital approximately $1 million in the quarter on higher sequential revenue as a result of its ongoing inventory reduction program.

Depreciation in the quarter was $799,000.

During the quarter the Company paid a cash dividend of $853,000.

Income Statement Guidance Q3 2016

Now I would like to discuss guidance for the third quarter 2016.

We anticipate third quarter revenue, gross margin and operating costs to be in line with the quarter just ended.

The Non-GAAP effective income tax rate is expected to remain unchanged going forward at 18 percent.

The fully diluted share count in the quarter is expected to be about 16.0 million shares.

That concludes the financial review. I would like to turn the call over to Marty for his summary comments.

MARTY SINGER:

Thank you, John.

We were pleased with the sequential quarterly rebound in all of our core business activities. As we suggested in our last earnings call, we anticipated that our business development activities with major OEMs such as Huawei would result in stronger antenna revenues for the second quarter and for the second half of the year. We also thought that our in-building engineering services and our staffing business would show renewed growth. We now expect that by the end of the year, the run-rate for our services operation will be nearly double what it was in the first quarter. Finally, we thought that carrier spending – in the U.S.

and in China – would strengthen and that it would favorably impact our scanning receiver sales. That happened as well.

As you may recall, we also committed to reducing our operating costs to 2014 levels. We exceeded that goal and are currently running at an annual operating expense level of $32 million, $1 million below 2014 OPEX run rates. We also did a much better job of controlling inventory and other COGS related expenses. John already reviewed the impact of these efforts on earnings and free-cash flow. By the end of the year, we will have eliminated over $4 million in inventory and greatly reduced our third-party storage costs.

We do anticipate some cost increases – primarily in sales, business development, and expenses associated with the introduction of new products. As we have previously announced, we have launched Engage, our subscriber-based test and measurement tool, a variety of cloud-based SeeHawk Analytic capabilities, new engineering services, and a vastly expanded in-building and mobile antenna product line. We expect OPEX to increase modestly in the fourth quarter as we focus on the execution of our product development roadmap, expansion of our engineering services business, and sales growth.

Let me now turn to specific events in our Connected Solutions and RF Solutions segments. Connected Solutions had a very strong quarter with respect to major customer development. In addition to Huawei, we had our first significant sale into an LTE-based public safety agency, shipped over 3000 antennas for a coach voice communications system used in professional football and very strong GNSS sales into the aviation market. Small cells continue to emerge as an important, multi-year opportunity for PCTEL. By the end of the year, we anticipate GNSS, LTE, and WiFi sales into the three largest cellular infrastructure vendors.

In-building opportunities are now served by our VenU sector antennas by major North American radio manufacturers and we have also applied our VenU PIM160 products to outdoor DAS applications.

RF Solutions experienced sequential quarter revenue growth across the board, some of it directly related to in-building. Engineering services nearly doubled and overall services increased approximately 60 percent. In addition to a 100,000 mile drive test project, we secured preparatory engineering services work from a national sports league to support their playoff games and projects with SouthernLinc, Ericsson, Mobilitie, and Sprint-Kelly.

Our IBflex enjoyed strong sales in North American markets and we saw continued growth in APAC. We had a strong quarter with a major U.S. carrier, our first IBflex order with Google, and we secured our first orders after launching our subscriber-based Engage product at the DAS and Small Cells World Congress. Engage is now fully integrated with our scanning receivers and analytic tools. Our cloud-based SeeHawk Analytics post-processing tool now supports all of PCTEL's test and measurement products, and provides real-time support and reporting for our Network Engineering Services group.

The recent announcements regarding the allocation of spectrum for 5G will accelerate the development of new networks and the transformation of existing networks. This type of sea change in wireless technology creates new opportunities for PCTEL. The deployment of 5G and the transition of public safety networks to LTE will require test and measurement equipment, engineering services, and our performance critical antennas. Moreover, the aggregation of WiFi and LTE requires the type of expertise that PCTEL has developed over years of RF experience. Of course, the underlying impetus for 5G and more efficient use of spectrum is what drives our core business: the planet's unquenchable thirst for wireless data.

We were active in a variety of industry events, including the B. Riley Investment Conference and the IDEA conference in Boston. We attended and presented at Cisco Live, NEDAS Boston, CommunicAsia, the LTE LATAM, CIBET, the North Eastern DAS conference, Mobile World Congress in Shanghai, and Interop Japan with our value-added distributor, Marubun. We also attended the invitation-only Sports Entertainment Alliance in Technology (SEAT) Conference. We attended RSSI (Railway Systems Suppliers, Inc.) in Grapevine, Texas where we featured PCTEL's innovative custom antenna farm designs for the rail industry.

We will be presenting our products at Wireless Connect at the University of Maryland on August 10-11. Finally, we will present at the IDEAS Conference in Chicago on August 30-31. We look forward to meeting with investors, customers, and others at these events.

We have set aside 30 minutes for your questions.

Operator?