



CPS Technologies Corporation

October 31, 2024

9:00am ET

Operator

Good day, everyone, and welcome to the CPS Technologies Third Quarter Earnings Call. At this time, all participants have been placed on a listen-only mode. If you have any questions or comments during the presentation, you may press STAR ONE on your phone to enter the questions que at any time. and we will open the floor for your questions and comments after the presentation.

It is now my pleasure to turn the floor over to your host, Chuck Griffith, Chief Financial Officer of CPS Technologies. Sir, the floor is yours.

Charles Griffith

Thank you, Matthew, and good morning, everyone. Today, I'm joined by Brian Mackey, our President and CEO. We look forward to discussing our third quarter results with you. But first, Chris Witty, our Investor Relations Advisor will provide a brief safe harbor statement. Chris?

Chris Witty

Thanks, Chuck, and good morning, everyone. Before we begin the business portion of today's call, I would like to point out that statements in this conference call that are not strictly historical are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, and should be considered as subject to the many uncertainties that exist in CPS' operations and environment.

These uncertainties include, but are not limited to, the wars in Ukraine and Israel, other geopolitical events, economic conditions, market demands and competitive factors. Such factors could cause actual results to differ materially from those in any forward-looking statements. Additional information can be found in our filings with the SEC.

I will now turn the call over to Brian to offer his perspective on the third quarter highlights, after which Chuck will review the financial results in greater detail. Brian?

Brian Mackey

Thank you, Chris. Good morning. Third quarter revenue was \$4.2 million with an operating loss of approximately \$1.5 million. Revenue declined year-over-year primarily due to the end of our U.S. Navy Armor contract with Kinetic Protection, as we previously discussed while another major customer also purchased significantly less year-over-year as it worked through some excess inventory. Chuck will review this further in a moment.

While the quarter's results were negatively impacted by such factors, as well as third shift start-up costs and supply chain issues, we have recently improved product throughput and with recent wins under our belts, are much more optimistic about our fourth quarter and beyond.

I'll now turn the call over to Chuck to provide further details about our financial results, after which I'll provide some additional perspective. Chuck?

Charles Griffith

Thanks, Brian. As was just mentioned, the company's revenue totaled \$4.2 million in the third quarter compared with \$6.3 million last year. Most of the year-over-year change was due to the end of our contract with Kinetic Protection as expected, related to the Armor shipments for the U.S. Navy fleet of aircraft carriers.

We previously announced that the completion of this program would negatively impact results by approximately \$2 million in revenue per quarter. Kinetic Protection does remain cautiously optimistic about landing additional work for other naval ship classes in the coming year and is focused on bringing advanced ballistic shielding to the remainder of the surface fleet.

We reported a gross loss in the third quarter of \$1.5 million or approximately negative 12% of sales compared with a gross profit of \$1.2 million or 20% of sales last year. This decrease was due to lower overall revenue and reduced manufacturing efficiencies, along with costs associated with hiring and training the third shift that began operating the last week of August, as I just mentioned.

During the quarter, this new staff worked alongside other workers for training, impacting overall cost of goods sold with virtually no corresponding top line revenue component in the quarter. We anticipate that gross margins will improve as volumes climb in the fourth quarter in fiscal 2025.

As previously discussed, we did incur the expenses of hiring and training our third shift, but saw only a very limited impact on the revenue in Q3. However, our first four weeks of Q4 are off to a solid start, especially relative to the first four weeks of Q3. This is attributable both to the addition of a third shift as well as abnormally low shipments early in Q3.

Given our expanding manufacturing capability and recent new contracts, we're optimistic about further growth in fiscal 2025, along with the operating leverage and improved margins that, that should bring. While we'll continue to work to stabilize and support our increased manufacturing operations, many of the initiatives necessary to increase output are showing results.

Selling, general and administrative expenses, SG&A totaled \$1 million in the third quarter versus \$1.1 million in the prior year period as we did remain focused on controlling costs, even while investing in new business development initiatives aimed to accelerate long-term growth. The company posted an operating loss of \$1.5 million in the third quarter compared with operating income of approximately \$0.1 million last year, and we reported a net loss of \$1.0 million or \$0.07 per share versus net income of \$0.2 million or \$0.01 per diluted share in Q3 of fiscal 2023.

Turning to the balance sheet. We ended the quarter with \$4.7 million of cash and \$1 million in marketable securities versus \$8.8 million in cash and no marketable securities at the end or -- sorry, at the start of 2024. Trade accounts receivable as of September 28 totaled \$3.7 million versus \$4.4 million at the end of December of 2023. Inventories also totaled \$4.4 million at the end of the third quarter compared with \$4.6 million at the start of the fiscal year.

Turning to the liability side. Payables and accruals totaled \$3.3 million at the end of the third quarter versus \$3.6 million as of December 31, 2023.

Now I'll turn the call back over to Brian, and he will provide more in-depth discussion of the period.

Brian Mackey

Thanks, Chuck. While the third quarter saw lower revenue both year-over-year and sequentially versus Q2, we're now optimistic about the outlook for CPS. Obviously, the completion of the Armor contract with Kinetic Protection will continue to be a headwind while we continue to pursue a follow-on order from the United States Navy.

However, there were certain challenges that are now largely behind us. First, as previously mentioned, one customer was holding off on additional purchases as it worked through existing inventory. Orders have not resumed, and we anticipate growth in the coming months and quarters.

At the same time, we've successfully trained a third shift of operators and are now able to successfully turn orders into shipments at an increased rate, something that has constrained us in the past few quarters. While our manufacturing operations remain lean and efficient, we have a greater ability to improve our capacity utilization and at the same time, have recently won several orders that position us well for the remainder of this year and beyond.

Specifically, I'm referring to the Phase 2 SBIR Award with the Department of Energy, which we've discussed in the past. The new \$12 million contract with our existing semiconductor customers and a new development contract with the Navy that was secured very recently. The DOE Phase 2 award provides funding of \$1.1 million over 24 months for CPS to continue its development effort for Modular Radiation Shielding for transportation and use of micro reactors.

This is the second Phase 2 award, since June and a great recognition for our team, as it acknowledges our ability to develop and deliver novel yet practical solutions in response to well-defined requirements.

We're committed to addressing critical customer needs. In this case, lightweight shielding for nuclear radiation for a host of agencies and their mission-critical programs.

With regard to the semiconductor customer, the new contract represents a larger agreement than we've had in recent years, and it is expected to significantly boost revenue in fiscal 2025. As we announced concurrently with earnings, the contractor power module components is cancelable by either party in light of the ongoing negotiations and the manufacturing ramp-up that is required.

Today, the signed contract enables us to continue these discussions about future volume and pricing requirements even as we meet the near-term production requirements of our long-term customers. Under the contract, deliveries are scheduled to take place over a 12-month period starting now with components to be utilized primarily in a high speed rail, wind turbines, and EV or HEV applications. This is a very positive development for CPS Technologies as we work out final details on pricing and delivery to ensure the best outcome for us and our shareholders as well as our customers.

Recently, we've also received a new contract from the U.S. Navy for further application of our metal matrix composite solutions. This contract valued at \$200,000, provides funding for development work at CPS over the next 12 months. Our research will focus on addressing the requirements of the Naval Air Systems Command, or NAVAIR, specifically by providing lightweight, high strength materials. CPS' MMC solutions, in this case, fibrous materials infiltrated with aluminum provide higher strength than neat aluminum without the increased weight of steel.

We also remain cautiously optimistic about the likelihood of Kinetic Protection winning new armor orders for additional classes of naval vessels in fiscal 2025 as our holistic solutions address a large market across various types of ships as well as other military applications. We continue to be actively involved in seeking out other SBIR opportunities as well as bidding on new applications with an expanding array of customers, and we are awaiting word on proposals submitted to U.S. agencies, including several within the DoD as well as with NASA.

We're also optimistic about our expanded product line that now includes fiber reinforced aluminum or FRA composites. Manufacturing trials have been going well, and we're continuing to speak with customers in the aerospace and defense industry about FRA capabilities for stronger, more durable, and lighter-weight applications comprised of high strength aluminum alloys. This continuously reinforced with short ceramic fibers. We expect to begin the commercialization of FRA in fiscal 2025.

In addition to the SBIR Phase 2 on radiation shielding, we've been in discussions with other potential customers regarding our capabilities in this area. These discussions could lead to a generation of additional revenue in 2025 over and above our SBIR funding for this part of the portfolio.

Finally, with our new 5 axis CNC machine up and running, we're ready for higher production of hermetic packaging and other products in Q4 and beyond. Overall, given our expanded manufacturing capabilities, third shift being up and running and with several significant contract wins under our belt, the company is better positioned for growth and improved results than at any time within the past 12 months.

We're moving into a new era of expansion and are optimistic about the quarters to come. We appreciate our investors' patience and passion as we've navigated this year and the many challenges that entail, many of which have now largely been addressed. We look forward to the future and the many opportunities that 2025 will bring.

We can now open the call up for questions. Matthew?

Operator

Certainly. Everyone at this time, we'll be conducting a question-and-answer session. [Operator Instructions]. Thank you. That concludes our Q&A session. I will now hand the conference back to Brian Mackey for closing remarks. Please go ahead.

Brian Mackey

Thank you for joining us today for your ongoing interest in CPS Technologies. We look forward to speaking with you again after the end of our fourth quarter. If you have any questions in the interim, please reach out to our Investor Relations adviser. Thank you.

Operator

Thank you, everyone. This concludes today's event. You may disconnect at this time, and have a wonderful day. Thank you for your participation.