rakon

Market Release

23 November 2023

Rakon continues to focus on efficiency initiatives and investment for future growth

Global high technology company Rakon (NZX: RAK) has today released its financial results for the six months ended 30 September 2023.

All numbers are stated in New Zealand dollars (NZ$) and relate to the six months ended 30 September 2023 (HY24), with comparisons to the six months ended 30 September 2022 (HY23) unless stated otherwise.

Financial Highlights

- Revenue of $61.3 million (HY23: $87.2 million) reflects industry-wide challenges and the completion of one-off chip shortage contracts
- Telecommunications revenue down $13.4 million to $34.2 million and Positioning revenue down $9.2 million to $7.2 million, reflecting anticipated normalisation of customer inventory levels. Space and Defence recorded its highest revenue to date of $15.3 million, up 24% from HY23
- Gross margin of 42.7% (HY23: 49.9%) reflects non-recurring costs associated with workforce restructuring and lower production due to the move to the new India facility
- Operating expenses were relatively flat at $28.8 million (HY23: $28.4 million) reflecting both increased investment for future growth and inflationary pressures, and the offsetting effect of Rakon's focus on efficiency initiatives to improve long-term competitiveness
- Underlying EBITDA[1] of $5.3 million (HY23: $28.1 million) reflects the fall in revenue, non-recurring costs and sustained investment for growth
- Reflecting the deferment of 5G infrastructure deployment by mobile network operators as they adjust to current macroeconomic pressures, and longer than anticipated inventory normalisation by Rakon's Telecommunications and Positioning customers, Rakon now expects FY24 Underlying EBITDA[1] of between $13-$19 million.

Strategic Highlights

- Continued market share gains and an all-time high design win rate, which has increased 33% YoY with a conversion rate of over 90%
- Planned production of select New Zealand and France product lines at the new India facility is progressing on an accelerated schedule – delivering margin improvement from FY25
- Now established in the fast-growing NewSpace and Low Earth Orbit (LEO) satellite ecosystem; highest order book for Space over 12-month period and expecting this growth to continue
- Launched the latest Rakon semiconductor chip, the first of its AI computing hardware portfolio, and working with leading players in AI computing hardware on next generation platforms
- Continued delivery of three-year growth strategy and on track to deliver all FY24 milestones.

Chief Executive Officer, Sinan Altug says "There is no doubt that we continue to deal with a tough short-term macroeconomic environment. Our customers continue to work through their inventory levels, after stockpiling through the global supply chain disruptions, and mobile network operators are deferring some planned 5G capex. As evidenced by recent announcements, we are now seeing these conditions lasting for longer than previously anticipated. However, we share the confidence of our tier 1 customers,

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who are seeing these adjustments as temporary pauses on the path to growth, and unequivocally expecting the deployment of this deferred investment to return."

"We are focused on diversifying and growing in new markets. A great example of this is our Space and Defence segment, which is going from strength to strength, delivering highest revenue to-date in HY24, and has become another strong vertical alongside Telecommunications. We have also taken the first steps towards AI computing hardware becoming a core market. The launch of our next generation semiconductor chip, Niku, lays the foundation for our AI computing hardware portfolio and we will add more next-generation products to this portfolio in the coming year."

"We are also leaving no stone unturned as we focus on optimising and running our business as efficiently as possible. The steps we have taken to date are already providing tangible benefits, but we continue to look for more efficiencies across our global operations. This will put us in the best position to navigate the current macroeconomic conditions, offset inflationary impacts and improve our resilience and competitiveness into the future.

"The medium to longer-term growth fundamentals for Rakon's core markets remain strong. We continue to deliver and execute on our three-year growth plan, which will ensure we're well positioned to capture and maximise significant opportunities. The strategic and focused investments we are making today will enable us to grow market share, revenue and margins", says Mr Altug.

Financial Result

Total revenue was $61.3 million, compared with $87.2 million for HY23. This reflects a $10 million impact from the completion of one-off chip shortage contracts as well as the normalisation of inventory levels – impacting both the Telecommunications and Positioning segments.

Telecommunications, Rakon's largest market, fell to $34.2 million (HY23: $47.5 million) on the back of anticipated industry-wide normalisation of inventory levels among customers. Positioning fell $9.2 million to $7.2 million (HY23: $16.4 million), reflecting the completion of one-off chip revenue of $4 million in HY23 and normalisation of customer inventory levels. Increased activity in Space and Defence resulted in a 24% revenue increase to $15.3 million (HY23: $12.3 million). Rakon's 'Other' segment revenue fell from $11 million to $4.6 million, also reflecting the completion of one-off chip shortage contracts.

Gross profit was lower at $26.1 million and margin percentage was 43% (HY23: 50%), impacted by one-off costs associated with workforce restructuring, lower production due to the move to the new India facility, and lower order volumes impacting economies of scale.

Operating expenses were relatively flat at $28.8 million (HY23: $28.3 million) even with continued growth strategy investment (R&D up to $8.9 million) and incurred inflationary pressures. Rakon's focus remains on investing for growth while proactively carrying out efficiency and cost control measures.

Underlying EBITDA[1] of $5.3 million reflects the fall in revenue along with non-recurring expenses and investment for future growth. Net Profit After Tax (NPAT) was $0.5 million, reflecting Underlying EBITDA[1], as well as a share of a loss made by an associate.

Net cash was $13.4 million, down from the prior year after investment of $6.1 million in capital expenditure, including the completion of the India manufacturing facility, and payment of $2.9 million dividend in August.

Balance Sheet

Rakon's balance sheet remains robust, with net assets of $154.22 million. The company had $13.4 million in net cash at balance date, $5 million lower than a year ago as it continues to self-fund key growth-focused projects and paid its first dividend in August 2023.

Since 31 March 2023, inventory levels have reduced from $62.6 million to $60 million and are down $12 million YoY as Rakon used up safety stocks that were accumulated to mitigate supply chain risks and support the transfer of Rakon India's manufacturing operation to the newly built facility. The company will continue to focus on lean and agile inventory management going forward.

Rakon is committed to managing its balance sheet to support the company's long-term sustainability and growth strategy, including maintaining capacity to execute ongoing growth opportunities over time.

Efficiency initiatives

As Rakon continues to invest for growth while navigating the challenging market environment, it is also taking a multifaceted approach to driving efficiency across the business. By streamlining the business without compromising core capabilities Rakon can ensure resilience and maintain market leadership and competitiveness in the years ahead.

In HY24 Rakon reduced its global workforce by over 10% compared to its business plan, optimising production efficiencies while ensuring retention of the right capabilities for continued execution of its growth plan. General and Administrative costs were flat at $14.1 million (HY23: $14.2 million), a positive reflection of the effectiveness of ongoing efficiency actions to offset inflationary pressures. Rakon continues to proactively look at all expense categories, and associations with revenue and future growth objectives.

Growth strategy

Rakon's three-year growth strategy, as outlined to shareholders at the 2022 and 2023 annual meetings, sets a path for building long-term shareholder value by diversifying revenue with focused investment to grow Rakon's market share, revenue and margins over time. The growth strategy investments made to-date have allowed Rakon to successfully diversify into higher margin products and are estimated to have increased the serviceable addressable market by 10% in just one year to almost $3.7 billion.

Rakon is on-track to deliver all FY24 milestones for the growth strategy, including the planned production of select product lines from France and New Zealand at the new India facility. This is progressing well on an accelerated schedule and once completed will bring margin improvement from the second half of FY24 and gain increasing efficiencies from FY25.

Rakon launched its latest semiconductor chip, Niku™, the first of its AI computing hardware portfolio and continues to work with leading players in AI computing hardware on next generation platforms – projecting tangible substantial benefits within the next 12-18 months. The next product in Rakon's AI computing hardware portfolio, MercuryX™, is scheduled for launch before the end of 2023 and has been released to selected customers for testing.

The Space and Defence segment continues to outperform for Rakon. The company has its highest order book to-date over the 12-month period and is now established in the fast-growing NewSpace and Low

Earth Orbit (LEO) satellite ecosystem. This growth is expected to continue as Rakon focuses on expanding into new geographies and moving up the value chain for this market.

Rakon continues to evaluate and consider acquisition opportunities to expand into the US market. This would provide access to top-tier US customers through local manufacturing, strengthen existing customer relationships and significantly increase Rakon's Total Addressable Market. Rakon is taking the necessary time to ensure any acquisition can be funded, integrated and is value accretive. Rakon is also working on organic expansion into the US, focusing on getting the appropriate market certifications underway.

Outlook

Overall, HY24 Underlying EBITDA[1] performed in line with the July market update. However, market dynamics continue to evolve and following further dialogue with customers, and a number of recent peer and customer announcements, Rakon now believes the risk to FY24 guidance is higher than the $10 million (implied FY24 Underlying EBITDA[1] of $16 million to $24 million) indicated to the market in July. In the Telecommunications market, mobile network operators are continuing to defer some capex investments for the roll-out of 5G infrastructure as they navigate current macroeconomic pressures. Additionally, both the Telecommunications and the Positioning segments continue to be impacted by inventory corrections. This is partly offset by the outlook for the Space and Defence segment, which continues its strong performance and is set to benefit from seasonal delivery orders driving H2 revenue.

The fundamental growth drivers supporting Rakon's core markets remain resilient, reflecting robust medium to long-term prospects. Tier 1 Telecommunications customers remain confident in the deployment of delayed investment for the next stage of the 5G network build-out and forecasts show 5G accounting for half of all mobile subscriptions by 2030. Positioning is now showing early signs of recovery and key customer inventory normalisation, and the order book for Space and Defence remains strong, extending beyond FY25.

Opportunities are significant and growing with the ongoing evolution of 5G, Cloud and Edge Computing, AI, autonomous machines and vehicles, aerospace and the entire NewSpace ecosystem. Building on the strong foundations of its products, innovation and customer service, Rakon's programme of investment for growth and efficiency initiatives will ensure it is well placed to capture and maximise future opportunities.

Ends

Authorised for release to the NZX by Rakon's Board of Directors.

Conference call details

Sinan Altug (Chief Executive Officer) and Drew Davies (Chief Financial Officer) will present the HY24 Financial Results and Business Update at 11.00am NZDT. All shareholders are invited to listen and view the presentation broadcast. To join the live broadcast online please pre-register using this **link.**

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About Rakon

Rakon is a global high technology company and a world leader in its field. The company designs and manufactures advanced frequency control and timing solutions. Its three core markets are Telecommunications, Positioning and Space and Defence. Rakon's products are found at the forefront of communications where speed and reliability are paramount. Its products create extremely accurate electric signals which are used to generate radio waves and synchronise time in the most demanding communication applications.

Rakon has three manufacturing plants, six research and development centres, and sixteen customer support offices worldwide. Founded in Auckland in 1967, Rakon is proud of its New Zealand heritage. It is a public company listed on the New Zealand stock exchange, NZX, ticker code RAK.

[1]Non-GAAP disclosures

Refer to note 4 of the FY2023 consolidated financial statements for an explanation of how 'Non-GAAP Financial Information' is used, including a definition of Underlying EBITDA and reconciliation to net profit after tax (NPAT)