Ocean Power Technologies Inc. Fiscal Fourth Quarter 2018 Call Script

Operator Comments

Good morning, ladies and gentlemen, and welcome to the Fourth Quarter Fiscal Year 2018 Ocean Power Technologies Conference Call. My name is Sabrina, and I'll be your coordinator for today. As a reminder, this conference is being recorded for replay purposes. I would like to turn the presentation over to your host for today's call, Mr. Stephen Calk, Investor Relations for Ocean Power Technologies.

Introduction

Good morning, and thank you for joining us for Ocean Power Technologies Conference Call and Webcast. On the call with me today are George Kirby, President and Chief Executive Officer; and Matthew Shafer, Chief Financial Officer and Treasurer. George will provide an update on the company's operating highlights, and then Matt will review the fourth quarter and full fiscal year 2018 financial results. Following our prepared remarks, we'll open the call to questions. This call is being webcast on the company's website at oceanpowertechnologies.com. It will also be available for replay after this call.

On July 17, 2018, Ocean Power Technologies issued its earnings press release and filed its full year report on Form 10-K for fiscal year 2018 with the Securities and Exchange Commission. All our public filings can be viewed on the SEC website at sec.gov or you may go to the OPT website, oceanpowertechnologies.com.

Now let me reference to the safe harbor provisions of the U.S. securities laws for forward-looking statements. This conference call may contain forward-looking statements that are subject to significant risks and uncertainties, including the future operating and financial performance of Ocean Power Technologies or OPT. Although OPT believes that the expectations reflected in its forward-looking statements are reasonable, it can give no assurance that such expectations will prove to be correct. Important risk factors that could cause actual results to differ materially

from those reflected in the forward-looking statements are included in OPT's filings with the SEC. The information contained in this call is accurate only as of the date discussed. Investors should not assume that these statements will remain operative at a later time, and OPT undertakes no obligation to update any information discussed in this call. Now I'm pleased to introduce Mr. George Kirby, President and CEO of Ocean Power Technologies to begin the discussion. George?

George H. Kirby – President and Chief Executive Officer

Thanks, Steve, and good morning, everyone. I'd like to open the call with some comments on the industry outlook and offshore development activity where we see the opportunities for Ocean Power Technologies and what we are working on now. Then I'll pass the call to Matt Shafer, our Chief Financial Officer, for a review of our financials, and then we'll open the call for questions.

We're seeing what we believe to be signs of building demand for our PowerBuoy solutions compared to just 6 months ago. In particular, we're addressing many more new requests for proposals and information, predominantly within the offshore oil and gas market, which would use our PowerBuoys in their operations. Despite what appears to be signs of stabilizing oil prices, the offshore oil and gas market continues to aggressively cut costs in offshore operations to competitively meet demand along with onshore oil and gas, while also addressing alternative forms of energy. New technologies, such as unmanned stations and subsea drones, enable safer, cleaner and less-expensive remote land-based operations over traditional methods, which use more expensive offshore vessels and crew. Likewise, the security and defense markets are constantly searching for new technologies to augment their operations. Our business development team received significant interest from a number of military and defense contractor participants at recent conferences like the Offshore Technology Conference in Houston and the Sea, Air and Space Exhibition in Washington, DC over these past few months. While the team is busy tracking down these opportunities, we're also excited to progress our work with the Office of Naval Research upon receipt of next phase funding.

Interestingly, the Department of Energy is turning its focus to autonomous ocean wave power. Recently, the DOE solicited input to a draft maritime market report, where wave energy devices may be used to provide power into 12 markets. These markets include some of the same areas that our company has already been addressing, such as science and research, unmanned systems and autonomous underwater vehicle charging, shoreline protection, disaster relief and recovery and others. This DOE report could allow decision makers to prioritize new funding opportunities for technologies like ours.

Additionally, the DOE announced up to $23 million in funding to support marine energy technology projects that aim to reduce capital costs and shorten deployment time lines. Earlier this year, the House released their version of the fiscal year '19 Energy and Water Appropriations Bill and included $59 million for marine energy R&D, which is the highest funding level that DOE may have ever received. Though we are laser-focused on further commercializing our products and services, we would be remiss if we didn't consider funding opportunities where we might exploit much of the great work that our team has already accomplished, while simultaneously maintaining our competitive and intellectually property positions.

The past year marked several critical milestones as our company continues its positive trajectory. Just a few weeks ago, we announced a contract with Premier Oil to deploy a PowerBuoy in the Central North Sea. Previously, we announced our contract with Eni to a deploy a PowerBuoy in the Adriatic Sea. These combined contract values are worth potentially over $3.1 million, and they reflect our ability to provide a cost-effective solution and be a critical partner to some of the largest offshore oil and gas companies in the world. We believe that through these contracts, we have passed an important inflection point in ourbusiness by achieving fourth quarter revenues as a result of our BD efforts in a totally new market with 2 totally new PowerBuoy applications. We also believe these 2 important new contracts could be just the beginning of building a robust backlog towards sustainable revenues.

As we continue our vision of transforming the world through innovative ocean energy solutions, the strength of our team is more important than ever. In the past year, we added several new employees around the world, including Matthew May, OPT's Vice President of Global Business Development; and Chris Phebus, our Vice President of Engineering. Both Matthew and Chris are highly focused on growing our company and will be strong contributors to our ongoing success.

We're fortunate to have them be part of our leadership team, and we're already seeing the fruits of their labors. For instance, in their short tenure, both Matt and Chris have individually traveled to Europe to help close the Eni and Premier Oil contracts and identified potential new customers and opportunities and to identify and work with potential new partners that could help us to sell and deliver our ocean energy solutions in the future.

As we look forward, our objectives are clear and our focus is razor-sharp: Sell, build, ship. Our new facility in Monroe Township, New Jersey, allows us to own the entire life cycle of our business, from business and product development to delivery and ongoing customer support. We passed the critical and necessary inflection point by transitioning from research to commercialization, and we believe we have the infrastructure to capture diverse end markets with unique applications across multiple sectors, geographies and customer types.

We're confident that Ocean Power Technologies offers a unique and innovative solution. That technology plus our unique expertise are giving us clear access to very large addressable markets, where utilizing new technologies for operational cost savings is paramount. We're building our pipeline of new and existing customer relationships and actively pursuing a range of projects. Our 2 recent announcements are just the beginning, and we look forward to adding more customers and projects in the coming quarters. Now let me turn the call over to Matt to take us through the numbers. Matt?

Matthew Shafer - Chief Financial Officer

Thank you, George, and good morning, everyone. First the quarter. We recorded $222,000 in revenue during the fourth quarter ended April 30, 2018, while revenue in the fourth quarter of fiscal 2017 was $250,000. The decrease over the prior year was due to the timing of our start date on the Eni contract versus the timing of our work with Mitsui Engineering & Shipbuilding and Department of Defense Office of Naval Research.

The net loss for the fourth quarter of fiscal 2018 was $3.3 million as compared to a net loss of $2.6 million for the fourth quarter of fiscal 2017. The uptick in the net loss was mainly attributable to additional hiring of needed personnel, costs associated with our new headquarters in Monroe, the decrease in gains from the change in the fair value of the warrant liabilities and impacts from foreign currency exchange rates. These were slightly offset by increased interest income.

Now for the full year. Revenue for the full year -- full fiscal year 2018 was $511,000 as compared to revenue of $843,000 for the 2017 full fiscal year. The net loss for the full fiscal year 2018 was $10.2 million as compared to a net loss of $9.5 million for the full fiscal year 2017. The increase in net loss was primarily driven by the decrease in gains from the change in the fair value of warrant liabilities and gross margins and also partially offset by the increase in the income tax benefit, interest income and foreign currency exchange impacts.

Turning now to the balance sheet. As of April 30, 2018, total cash, cash equivalents and marketable securities were $12.3 million, up from $8.9 million on April 30, 2017. As of both April 30, 2018, restricted cash was $726,000. Net cash used in operating activities was $10.7 million during the 12 months ended April 30, 2018, as compared to $10 million for the prior year. During fiscal 2018, our net cash burn rate was approximately $900,000 per month.

With that, I'll turn it back now to George.

George H. Kirby – President and Chief Executive Officer

Thanks, Matt. Before we move on to Q&A, I must say that I'm both proud and humbled by the strong team we've built over the past year at Ocean Power Technologies. The depth of our engineering talent is unrivaled. Over the past year, we've strengthened our cutting edge technology by implementing reliability enhancements, such as next generation controls logic and enhanced power take-off capabilities. We also developed and integrated a power and communications umbilical system for customer subsea equipment, such as for Eni. Our sales and marketing team continues to find new opportunities for our innovative solutions around the world. We're ushering in new sales and marketing processes, and we're pursuing new channel strategies, all of which will accelerate commercialization and transform our business toward a culture of commercial excellence, while maintaining OPT as the market leader in offshore wave power. Likewise, our support services have built what we believe are world-class policies and procedures to both enable growth, while maintaining strict compliance. In short, we are executing on our communicated strategy, and we believe we've turned the corner towards sustainable revenues. As always, thank you for your time and support as we continue to build Ocean Power Technologies to deliver to our customers. Operator, we're now ready to take questions.

Question-and-Answer Session

Operator:

[Operator Instructions] And our first question will come from the line of Peter Ruggiere with Dawson James.

Peter G. Ruggiere:

I got a question for you because when we -- there's been a lot of conference calls we've been talkative on. How close do you feel like

actually signing a meaningful maybe 3- to 4- or 5-buoy, 10-buoy contract?

George H. Kirby:

Well, we believe that the Eni and Premier Oil contracts are extremely meaningful to us. They're meaningful to those companies and they are meaningful to us in terms of having commercial contracts in a brand new market segment that we didn't have before, and we're deploying for these customers in different parts of the world. In terms of a multi-buoy order, we're addressing RFPs on a daily basis. I can tell you that they're not all for 1 buoy or 2 buoys. I think that what we're going to see, Peter, is an acceleration here. Now that we have a couple of buoys that are going in the water, we anticipate later this year, at least that's the plan, other companies are going to see the value in this. It's a race to be second, which is typical with new technologies being deployed, and we're going to start seeing more and more companies, we believe, come to the table to ask to use our buoys to help offset their operational costs. So we believe that's coming. We believe it's in the near future.

Peter G. Ruggiere:

You guys have been around a long, long time, and that's -- and I don't hear anything negative about you. But the stock start price is one thing because, I mean, thank God, you don't want any debt but I mean, that's the only negative, is we're all down in the shares.

George H. Kirby:

Right. It wouldn't make sense for us to necessarily have debt right now until we have revenues to offset the debt coverage. And I will tell you that if you look back over the last 3 years, we have built a product, which the company has never had before. We have developed markets around that product, which the company never had. And now, we have launch customers that are at the table that want our product, they want our expertise, and we feel that we have really turned that corner.

Peter G. Ruggiere:

That's a good thing. I have a client of mine that knows people at Premier, and he is surprised that your stock didn't move when you actually went forward with it actually. The Premier -- What's Premier, like a multibillion-dollar company, right?

George H. Kirby:

Yes, I don't exactly know off the top of my head what they're worth, but they're definitely a player in offshore oil and gas.

Peter G. Ruggiere:

I have a question on something. I read this through your 10-K. There was something on with this Tiderunner Marine on June 13. What's the story with that?

George H. Kirby:

Tiderunner Marine is a New Jersey marine operations company out of Atlantic City that we had used in the past for deployments for research and development purposes. And very plain and simple, we have a dispute over payments. So we're going to work it out with them through the courts. Really not much more that I can say about that.

Peter G. Ruggiere:

I understand. I like to see -- and on -- as far as the Navy goes, what are the deadlines for that or maybe advancing to another phase? I forgot off the top of my head.

George H. Kirby:

We're waiting for funding right now. The Navy has been vocal with us that they like what we have done. We've achieved all necessary objectives in prior phases, and it's really just a matter of rolling out funding. We are ready to move forward.

Peter G. Ruggiere:

Any idea when that might take place or...

George H. Kirby:

Your guess is as good as mine right now. We are in constant communication with them to understand what are the drivers and what are the triggers and really no insights that anybody else might have.

Peter G. Ruggiere:

Hey, the stock prices just trade -- your cash balance is right now is trading as if you have nothing, which is kind of ridiculous to me, anyway.

George H. Kirby:

It really is. I mean, we believe that we're undervalued. We've got great intellectual property. We've got burgeoning markets. We've got customers that we're working with and that are asking to potentially work with us. So we are extremely optimistic here. We're excited. There's a buzz of energy here. We're building buoys. It's a really exciting time for us, because we're doing something that this company has never done before. And the entire organization has their hands in building this company, and it's just a really exciting time right now.

Peter G. Ruggiere:

That's cool. How many buoys do you have built so far?

George H. Kirby:

We have 4 built. We've got 2 more that are being built.

Operator:

And the next question comes from the line of Robert Littlehale with JPMorgan.

Robert Littlehale:

Could you -- George, can you give us a sense of the time line when you described sell, build, ship? How long that potentially takes?

George H. Kirby:

Excellent, Bob, good to talk to you. I hope you're doing well. Sell, build, ship is a -- has become a mantra within our company. It's really become a battle cry internally. If you think about -- before I address your question, if you think about the cultural change that a small established company like ours has to go through, in terms of switching our mindset from a totally R&D mentality to one of product focused and most importantly, customer focused. That battle cry, sell, build, ship, is all about what we want to focus on. And if you look at our internal processes, we've got a sales process that we're looking to refine, and the more that we refine that, both internally as well as understanding our customers' buying process, we're able to condense the time to get to a sale. Likewise, with build, when I say build, it's not just physically building a buoy, but it's all the engineering that has to happen with individual customers in customizing that buoy for that customer's need. So for instance, with Eni, we had to design an umbilical that goes to the seafloor. An umbilical is nothing more than an extension cord that provides power and communications to the seafloor for their purposes. But we had to design and integrate this into the PowerBuoy, and then we have to physically build it, right? And then ship naturally is what it is.

But the timing for that, we believe, is going to accelerate. Right now, we are selling, building and shipping. And when I say sell, it could be either renting a buoy or it could be physically selling. And we are looking at selling as well as continuing to rent PowerBuoys. So that time line is going to condense more and more. Right now, sales processes vary depending on the market that we're looking at. So for instance, it took a lot longer to close the Eni project than we had originally expected. We were really working on that well before April of last year, that's April of 2017. And this is not to say that any of the parties drug their feet. There's a lot of work that goes into this. There is supply chain qualification on our part that we're really not going to publicize when we become qualified or certified by a major entity like Premier Oil. But it is abig deal internally, and we high five on something like that because there is a lot of work that goes into that, and there's a lot of engineering -- mutual engineering between both parties that has to happen. There is risk assessments in our operations. There are approvals that need to be obtained up and down the customer's organization. So these things take time, but as our BD team learns about their customers and learns about the buying process, we're able to ask the right questions upfront and condense this cycle in order to, hopefully, get to a sale more quickly. Likewise, we're looking at accelerating our buoy builds more quickly, and we're working on our engineering processes in order to consolidate the way that we approach new engineering tasks. So we're looking to consolidate or condense this entire process to get from initial inquiry all the way to shipping a buoy more quickly. And that just simply means revenues come to our company more quickly. We recognize revenues as work is accomplished, right? So it's based on work milestones with the customer. Our job right now is to build our backlog of revenues. We want to get contracts in the door, so that we can start working on them and recognizing revenues. Does that help?

Robert Littlehale:

It does. The Eni and Premier Oil are both leases. And have you announced what the lease terms are in terms of the length of the lease?

George H. Kirby:

Yes, we have. But I'll reiterate it. So for Eni, the initial project is 2 years. It's 6 months of upfront engineering, buoy build, ship, prepare for deployment and then deploy and install, and then the actual deployment is for 1.5 years. And that's not to say that Eni doesn't capture the information that they need earlier than 1.5 years, but the project is scheduled for 1.5-year deployment, at which time, it could be either continued for another 1.5 years. They may decide to buy the buoy. I mean, as time marches on in these deployments, it makes more economic sense for our customers to actually buy the buoy outright than to continue to lease it. But it also depends on what their operational objectives are as well. And likewise, with Premier Oil, what we have ultimately is an initial 9-month lease. We have an upfront 3-month trial period where Eni is looking very hard at, does the buoy do what we say it will do. We're all confident on both sides, both Premier and us, we're confident it will. But we're putting the buoy in the North Sea. It's designed to operate in that type of a harsh environment. It's going in the water in the mid to late fall in through the winter time. We feel confident that it's going to operate very well. In fact, it's those types of conditions where power generation is at its optimum, right? So during that first 3 months, we'll work with Premier, at which point, once we prove that the buoy does what it says it will do, it will continue on for another 6 months. And then there's an option to extend and also to buy the buoy after that. There are -- with both parties, we're also looking at other opportunities to use PowerBuoys within their operations. So this naturally opens up discussions for other opportunities.

Robert Littlehale:

The uses of the 2 leased contracts are different between Eni and Premier. Can you just quickly review that for us?

George H. Kirby:

Sure. In our commercialization presentation that we gave a few months ago, I laid out 3 discrete areas or applications that we're looking to address. One is subsea charging. So delivering power to the seafloor for operations that are happening on the seafloor, equipment that needs to be powered, data that needs to be collected, et cetera. And that's what

the Eni project is doing, subsea charging. Ultimately, they would like to use our PowerBuoy with subsea charging of autonomous underwater vehicles. So essentially, creating charging cages that these AUVs can go into, charge their batteries, upload data back to our buoy, which we can then send to land, and then download new mission profiles for the autonomous underwater vehicles. That way, you're not sending ships out to recover the AUVs, charge their batteries and deal with data. Everything is happening real-time. With Premier Oil -- and the second area of applications is surveillance and monitoring, and that's really what Premier Oil is all about. They have these platforms that need to be decommissioned. After a certain amount of time of use, just like any kind of capital equipment, it needs to be decommissioned. And this actually becomes a construction project, if you will, that's offshore. And they need to create safe zones around these construction projects, where they're taking down these platforms. They can't have any vessels coming within any near proximity of the platform as well as the subsea equipment. So historically, offshore oil and gas has used vessels. They'll actually put vessels out there 24/7 for weeks, sometimes months at a time, switching them on and off with crew in order to protect these zones. Well, the value play that we bring to the table is a unmanned platform. That's what our PowerBuoy is. We have power, we have communications, we essentially have everything that's needed that a vessel could do. We can even have cameras where we're monitoring live. We can have 2-way communication systems, really anything. So that's what this project with Premier Oil is all about, is to put our buoy on station as an unmanned station in order to protect that zone. Once we provethat out, the next step could potentially be to simultaneously provide subsea charging. Now we can do 2 missions, if you will. We can protect the surface and we can also power and monitor what's happening subsea. So there's really a lot of opportunities here with this one application. And just to fill it out, the third application is telecom. We're talking to some very big telecommunications companies right now around the prospect of bringing 4G on to the water, right? 4G, just like we all use on our cellphones, on to the water where they can't get it today. The only way that you can have 4G on the water is to have a cell tower on a physical platform. Well, what if you're looking to develop further out to sea where there are no platforms? You lose that 4G coverage. You can drop a PowerBuoy with 4G gear right on the PowerBuoy, either directly on the PowerBuoy or build a mast on top of

the PowerBuoy where you raise the gear very high up. And now, you've extended your network, either through a repeater system or through a base station application. So that's really exciting. And I'm going to point out, Matthew May, who joined our company, came from Tampnet, who is one of our partners. It's a group that we're working with and talking with about North Sea and Gulf of Mexico applications. Their gear is going to be on the Premier Oil buoy. And Matt clearly understands the needs of the telecom industry. So there's a real strategic advantage there as well.

Operator:

As there are no additional questions, I would like to turn the call back to Mr. George Kirby.

George H. Kirby:

Thank you, operator. And again, I want to thank everybody for joining the call. I want to thank everyone for your support. Please follow us, all the great things that we're doing. And we look forward to talking to you next quarter.

Operator:

Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may all disconnect. Everyone, have a great day.