

Redline Communications Group Inc.

First Quarter 2021 Results

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CORPORATE PARTICIPANTS

Stephen J. Sorocky

Redline Communications Group Inc. — Chief Executive Officer

Philip Jones

Redline Communications Group Inc. — Chief Financial Officer

PRESENTATION

Operator

Good day and thank you for standing by. Welcome to the Redline Communications Group Incorporated First Quarter 2021 Results Conference Call.

I would now like to hand the conference over to your speaker today, Stephen Sorocky, Chief Executive Officer. Please go ahead.

Stephen Sorocky — Chief Executive Officer, Redline Communications Group Inc.

Thank you very much, Megan, and good morning, everyone. Thank you for joining us today.

I wish to remind everyone that some statements made on today's call are forward-looking in nature and therefore subject to certain risks and uncertainties which are all outlined in detail in Redline's regulatory files, which may found—may be found on [sedar.com](https://www.sedar.com).

On this call, I'd like to give a perspective on the quarter, how we see 2021 shaping up, and describe some of the positive accomplishments and ongoing challenges in this current pandemic environment, but first I'd like to give a brief description of who we are.

Businesses and governments globally rely on Redline to secure—deliver secure and reliable wireless data infrastructure for their industrial operations in challenging environments. Our private wireless networks have become the data backbone for some of the most remote and harsh locations on Earth, including the deserts of the Middle East, the rainforests of South America, offshore platforms in the North Sea, and on the frozen Alaskan slopes.

We are proud that most of our customers have relied on our networks for decades through the evolution from basic communications to advanced IoT, surveillance and security requirements that form the basis of modern, mission-critical industrial requirements.

Redline's vision is to become the global leader in private wireless data infrastructure for mission-critical industrial data applications. As more devices become IT enabled and network ready, the demand grows for wireless networks optimized for multiple mission-critical data applications, asset mobility, and worker safety. Redline is well-positioned to exploit opportunities emerging from these new requirements.

Our sales pipeline indicates an increase in demand from our current installed customers and from new prospects that made reliable data infrastructure to gather, manage, and effectively communicate information from remote sites and with minimum cost or downside. Redline has cultivated a reputation for delivering on wireless technology, professional services, and end-to-end

network solutions by offering the connectivity required to support the significant upgrade cycle for industrial data.

As I mentioned in our last earnings call, in many ways 2020 could be summarized as a year of advancing our product innovation strategy while riding out COVID. We remain excited about sales of our LTE solution to multiple clients in mining, remote learning applications, capitalizing in part on demand enabled by the increased spectrum availability from the CBRS band in the United States, and so the trend that began in 2019 was delayed by COVID and resumed in the second half of 2020 and has continued into 2021.

As we have said before, Redline has made a product development a cornerstone of our strategy. While our ruggedized mission-critical products lead the market in many ways, development and innovation remain critical to maintaining this position.

This brings me to one of our more significant recent accomplishments. On March 31, 2021, Redline announced that the Canadian Government had approved an investment into Redline via the Strategic Innovation Fund. This investment brings up to CA\$14 million into the Company, earmarked for the development of innovative industrial 5G network solutions.

The fund will reimburse 41.52 percent of eligible R&D costs incurred by Redline. The first investment submission of approximately \$460,000 was a period between August 2020 and March 31, 2021, and was submitted to the fund just after the close of Q1. This first payment is expected to be delivered to Redline in Q2, and going forward, payments to Redline from the fund will be made

quarterly. Amounts received are repayable starting in 2028 and continuing for up to 15 years based on revenue growth.

Without a doubt, the COVID-19 pandemic continues to present many challenges for our Company. We have been challenged by the uncertainty of customer orders—orders caused by reduced site access, delays in product delivery, temporary site closures, and restricted global travel. As a result, product deliveries were made difficult and occasionally impossible, and revenues in the quarter were lower than in Q1 2020.

Specifically, Q1 revenue was negatively impacted by the delayed shipments of a large order of over \$1.6 million for the second half of 2021 due to COVID protocols delaying a customer project. Site access and other restrictions are widespread across our customer base, and also prevent Redline from doing the site surveys which are needed to properly scope and price new opportunities. The situation has contributed to lower overall bookings in the quarter.

The Company expects that while these restrictions may start to ease in coming months, especially in the United States, COVID will continue to impact the business to some degree for the remainder of 2021, but we are seeing some green shoots. Redline's new 3200 product has received its first order valued at over \$100,000 from a city government in the Middle East which will be using the product to expand connectivity to its schools. This order was received shortly after the end of the quarter.

Also, the Canadian Government is expected to approve the use of TV white space spectrum, which will create opportunities and a new market for our TV white space product and inventory in the

Canadian market. We are also sensing new optimism among some customers that previously delayed orders which can now be bought (inaudible) online.

I'd like to now turn to our revenue mix.

The Company continues to evolve its sales efforts towards complete solution selling, which includes extended support and maintenance components in each sales transaction, in addition to equipment and software sales. Maintenance and support revenues also earn the highest gross profit margin amongst all of the revenue streams.

Q1 2021 marks the ninth consecutive quarter of growth on a quarter-over-quarter basis of maintenance revenue, which is both recurring and very profitable. Notably, the proportion of total revenue represented by recurring revenue hit a record 17 percent in Q1 2021. This clear focus in our sales growth efforts is delivering steady results. Percentage of revenues from core markets remain steady over Q1 as compared to the same period in 2020 as customers in oil and gas, mining and utilities continue to purchase our industrial products, and the Company continues to focus its sales and marketing efforts into these core markets.

The Company continues to realize revenues from countries around the globe, providing a balance against the possible impact of changes in any one country. Geographic distribution of revenues is consistent for Q1 2021 as compared to Q1 2020.

On the product side, markets with access to newly available CBRS spectrum, where Redline's LTE product delivers significant value, are now showing growth. In December, we signed four contracts for

our LTE products. All of these are initial orders and have the potential to grow beyond the initial first order size, and one such order has already been received. While LTE remains a small portion of our business still, we anticipate that CBRS will continue to drive additional revenues from our LTE products.

We are also seeing opportunity in worldwide efforts to improve connectivity for remote communications, distance learning, and telemedicine as a result of the changes from work from home and the pandemic environment. Our reliable solutions are well-suited to this market.

In addition to the LTE product line, we have also invested in the next generation of our cornerstone RDL-3000 product line. This version, the RDL-3200, is a next generation virtual fibre platform that incorporates all of our internal and external learning and customer feedback over the last years. As I mentioned in the last earnings call, in addition to the first order we have received and discussed above, testing has exceeded our expectations, and we have now moved to a customer beta with a Tier 1 oil and gas company. We are incorporating their continued feedback into a final development phase, with an expected product release this summer.

Due to the higher proportion of service revenues this quarter, gross margins reached a record high 69 percent, clearly a testament to our focus on building the recurring revenue component of our revenue base while we wait for extensive pipeline to be translated into firm orders.

Careful cost and cash management remains a key area of attention for the Management team. While lower revenues contributed to an EBITDA loss of \$1.1 million, thanks to strong working capital and cash management, including an ongoing deferral of certain capital expenses, cash balance net of borrowings was \$4.3 million reduced our 1 million in Q1.

We continue to deliver steady revenue reductions—steady inventory reductions, and our accounts receivable management achievements have now become ingrained in our operations. Redline ended Q1 2021 with a strong backlog of orders to be shipped within the next 12 months. All in all, as we approach the midpoint of our fiscal year, we are optimistic about the coming relaxation of COVID restrictions on the horizon, with ongoing strong financial controls and discipline, with CBRS poised to drive the LTE market product—market demand and next generation products on the horizon.

In closing, I wish to make one thing very clear about our prospects. The product lines and services we offer remain mission-critical to both our longstanding customers and new customers alike. We strongly believe that the pipeline of orders we currently have has a high degree of certainty to be converted into firm orders. The challenge our customers face is with COVID-related access restrictions. They need our product, but why purchase it when it cannot be installed? This will change in due course. That really is the core of our optimism.

With that, I'd like to hand over to Philip Jones, our CFO, for his remarks. Phil?

Philip Jones — Chief Financial Officer, Redline Communications Group Inc.

Thank you, Stephen, and welcome, everyone.

The earnings press release for Redline Communications was issued May 12, 2021 before market opening. The press release accompanied our filings on SEDAR of the Q1 2021 interim financial

statements and the Management Discussion and Analysis. My comments will focus on key highlights of our financial results, followed by a Q&A at the end of the session.

Revenue in Q1 was \$3.7 million, a decrease of \$0.7 million, or 17 percent, over the same period in 2020, and a decrease of \$0.9 million, or 20 percent, from 2020 Q4 due to a \$1.6 million project in the Middle East being rescheduled by the customer to a date later this year as a result of impacts caused by the COVID-19 pandemic.

Sales of hardware and software products continue to drive the majority of the Company's revenue. Revenue from professional services and third-party equipment is largely tied to network deployments, as the Company continues to focus on selling overall product solutions versus an equipment-only focus.

For Q1, the percentage of revenues from maintenance and support continues to increase as the Company has been focusing for the last two years on securing additional recurring revenue from maintenance and support contracts. The revenue from these contracts increased from \$0.57 million in Q1 2020 to \$0.64 million in Q1 2021.

Order bookings representing all accepted customer contracts and purchase orders received in a quarter decreased by \$2.6 million, or 44 percent, in Q1 2021 compared to the same period in 2020, and decreased by \$2.2 million, or 40 percent, from the prior quarter. This overall softness in order bookings can be attributed largely to COVID-19-related restrictions, impacting the timing of customer purchases and projects, along with preventing our employees from accessing the customer locations to

do the site surveys that are necessary for scoping and pricing our solutions, combined with the challenges of relying on remote sales activities when in-person visits are presently not possible.

The Q1 2021 order backlog, consisting of all open orders to be fulfilled at a future date as requested by our customers, is at \$11.3 million, up \$1.4 million, or 14 percent when compared to the same period in 2020, and down \$0.5 million since last quarter. Included within the backlog is \$3 million of support and warranty contracts. Approximately 67 percent of the backlog is represented by orders from customers in the core vertical markets oil and gas, mining, and utilities.

Overall gross margin for Q1 was 69 percent, an increase of 6 percentage points from the same period in 2020, largely due to an increase in revenues from higher margin, professional services, maintenance and support agreements compared to the same quarter in the prior year.

Hardware and software product margins for Q1 decreased by 3 percentage points over the same period in 2020, mainly as a result of product mix changes year-over-year. Professional services and third-party equipment margins for Q1 increased by 14 percentage points over the same period in 2020 as a result of a revenue mix containing higher margin network design and technical training services compared to lower margins earned on third-party equipment sales.

Maintenance and support margins for Q1 were unchanged over the same period in 2020.

Overall operating expenses for Q1 were \$3.9 million, down 5 percent from the \$4.1 million reported for the same period in 2020, and down \$0.4 million, or 9 percent, from Q4 2020. The overall reduction in operating expenses are primarily a result of reduced general and administrative

expenses, partially offset by increases in costs and headcount in the research and development and operations functions as the Company continues to enhance its existing products and to develop and roll out the next generation of virtual fibre and industrial LTE products.

The overall offering expense reduction was achieved in spite of an approximate 1.2 percent strengthening of the Canadian dollar compared to the U.S. dollar, as the Company incurs approximately 65 percent of its operating expenses in Canadian dollars.

Adjusted EBITDA loss, a non-IFRS measure, for Q1 was \$1.1 million as compared to an Adjusted EBITDA loss of \$1 million for the same period in 2020 due to lower revenue, partially offset by higher gross margin percentage and reduced operating expenses. Q1 2021 net loss was \$1.2 million, or \$0.07 per share, compared to a net loss of \$1.0 million, or \$0.07 per share, in Q1 2020.

Now turning to the balance sheet.

As of March 31, 2021, the Company had \$4.3 million of cash, a decrease of \$1.0 million from the balance as at December 31, 2020. Throughout all of 2020, and continuing in 2021, the Company has been focusing on cash preservation through a combination of controlling expenditures and continuously striving to improve working capital management. The lower cash balance is mainly the result of the loss from operations incurred in the quarter, as overall non-cash working capital was lower compared to the prior quarter.

Inventory was higher compared to the prior quarter due to the additional inventory on hand related to the large order mentioned earlier for which delivery was deferred by the customer to later in the year.

In March 2020, the Canadian Federal Government announced the Canadian Emergency Wage Subsidy, or CEWS program, as a response to the COVID-19 pandemic. In Q1, the Company recognized a benefit of \$0.3 million which is recorded as other income in the financial statements. The amount has increased compared to the prior quarter due to changes in the program and the relative change in revenue compared to the prior reporting periods. Please note that this benefit has been excluded from our Adjusted EBITDA calculations. The Federal Government's recent budget program announced—recent budget announced this program, under amended rules, will continue through at least September 2021.

Now I would like to turn the call back over to Megan for the question and answer period.

Q & A

Operator

We have no questions today. I'll turn the call back to presenters for closing remarks.

Philip Jones — Chief Financial Officer, Redline Communications Group Inc.

Thanks very much, Megan.

Thank you, everyone, for joining us this morning. I wish you a safe and happy day. Thanks very much.

Operator

This concludes today's conference. You may now disconnect.