NASDAQ:CSPI Q2 2026 Earnings Call Transcript

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Operator | Conference Operator:

day, everyone. Welcome to CSPI's second quarter fiscal year 2026 conference call. At this time, all participants have been placed on a listen-only mode, and the floor will be open for questions and comments after the presentation. It is now my pleasure to turn the floor over to your host, Michael Polyview. The floor is yours.

Michael Polyview | Host:

Hello, everyone, and Kelly, thank you for joining us to review CSPI's financial results for the fiscal 2026 second quarter, which ended on March 31, 2026, as well as recent operating developments. Today with me on the call is Victor DeLobo, CSPI's Chief Executive Officer, and Gary Levine, CSPI's Chief Financial Officer. After Victor and Gary conclude their opening remarks, we'll then open the call for questions. During the Q&A session, we asked participants to limit themselves to one question and one follow-up question, then please re-key if you have additional questions. And in advance, thank you for your cooperation with this process. Statements made by CSPI's management on today's call regarding the company's business that are not historical facts may be follow-up statements as those identified in Federal Securities Law. Or it may, you'll expect, believe, anticipate, project, plan, intend, estimate, and continue, as well as similar expressions or intended to identify follow-up statements. A look at statements should not be meant as a guarantee of future performance or results. The company cautions that these statements reflect the current expectations about the company's future performance or events and are subject to several uncertainties, risks, and other influences, many of which are beyond the company's control that may influence the accuracy of the statements and the projections upon which the segment and the statements are based. Factors that may affect the company's results include, but are not limited to the risks and uncertainties discussed in the risk factor section of the annual report in Form 10-K and quarterly report in Form 10-Q filed with the Securities and Exchange Commission. Follow-up and statements are based on the information available at the time those statements are made and management's good faith believe as of the time with respect to future events. All follow-up and statements are qualified in entirety by this cautionary statement and CSPI undertakes no obligation to publicly revise or update They need any forward-looking statements, whether as a result of new information, future events, or otherwise, after the date they're up. With that, I'll turn the call over to Mr. DeLobo, Chief Executive Officer. Victor, please go ahead.

Victor DeLobo | Chief Executive Officer:

Thank you, Michael, and good morning, everyone. CSPI returned to growth during our fiscal second quarter as our product sales grew 30% and our service business grew 7% over the prior fiscal year quarter. Our top-line growth and bottom-line improvement was driven by our U.S. technology solution business and some large customer purchase orders. We did see an increased pickup in the AZT Protect orders during the quarter with more than 10 of what we call land and expand orders with new customers. This was double the amount of AZT Protect orders we signed in Q2 2025. Typically, these orders are used as a test at a single site by a customer to make sure AZT Protect meets our claims. It works within the customer's existing cybersecurity infrastructure, which I am happy to report has been the case every time. Then our team goes to work to expand our relationship with the customer through deployment at other sites. This phase of the process has taken longer than anticipated, largely due to evolving stakeholders alignment, and internal review requirements. For example, change within customer teams often require us to re-engage and re-establish

momentum, while some organizations seek additional validation from initial deployment sites. In other cases, IT teams initially assesses the existing infrastructure, addresses OT security needs, creating an opportunity for us to provide further education on distinct requirements of the OT environments. We view these dynamics as a natural part of the sales cycle in a complex and evolving market, and they continue to present opportunities for deeper engagement in long-term value creation. We are, however, making progress within the land and expand strategy. For example, AZP Protect is now deployed at the fourth plant in a major raw material manufacturer. to approach each plant separately, but with AZT Protect's track record is taking less and less time to add each site. We are seeing similar expansion at other customers where we deployed at a single site in 2025 and now slowly expanding to additional sites within the organizations. Our most exciting AZT Protect land and expand relationship to date was signed in April. It is a three-year agreement for more than two dozen US sites of a global cement manufacturer. The six-figure annual revenue value of this contract will be recorded in the fiscal third quarter. This agreement took approximately 13 months to get across the finish line, but now puts us in a position to pursue the manufacturer's other sites, which number more than 100 around the world. In late March, we entered into an agreement with a leader in the cloud-based commercial content automation service to deploy AZT in our ARIA ADR across the company's production infrastructure. And in early March, we deployed AZT Protect at a leading pet food producer. These are examples of how we are consistently evolving our approach to the OT market to shrink time between the initial land and expand. What's helped our effort in the growing awareness by the market of the increasingly threats generated by AI and the so-called friendly fire attacks generated by internal sources. Cybersecurity solutions tend to use patches to address cybersecurity threats. but continuous patches are largely ineffective in the OT operating realm. In a friendly fire attack, IT mistakenly sends a faulty update to manufacturing, which can be even more devastating than the attack's impact to OT production. With AZT Protect, no patches are needed, and to date, no breaches have occurred. At the same time, we continue to pursue strategic OEM relationships, most notably with Acronis. as they work to embed AZT Protect into their platform. While these integrations require time to mature, they represent highly scalable opportunities with substantial long-term potential, and we are hoping to begin generating revenue from the Acronis relationship by the end of the current fiscal year. AZT Protect continues to have little in the way of effective competition. However, the unique procurement process and development criteria for each customer and even and even each site within the customer has resulted in various timing delays. Our team is relentless when it comes to realizing the AZT Protect opportunity, and we continue to work through each challenge as it occurs. And we are definitely moving the needle. After a month into their fiscal third quarter, we are encouraged by the progress we are making with the AZT Protect deployments. During the second quarter, Once again, the technology solution business was the primary generator of our top-line growth. Our offerings increased the efficiency and effectiveness of our customers' IT investment in network, wireless and mobility, unified communication and collaboration, data center and advanced technology security. A managed cloud and managed service practice continued to perform well and grew 11% over last year's comparable period. We continue to benefit from the ever-expanding business and organizational migration to the cloud and the increasing trends for enterprises of all sizes to acquire operation support required once the migration is complete. A primary factor behind this market driver is the growing complexity of the cloud and the unique and specific needs of each enterprise. In Q1, we signed a new MSP customer that was generating nearly six figures in monthly revenue that commenced during the second quarter. And as we mentioned in the press release a week ago, one of the top 15 landscaping companies in the U.S. is engaging us to provide comprehensive managed services. As we look out over the remainder of the year, we believe our service segment momentum can continue. Meanwhile, based on our best-in-class services, our customer retention rate remains extremely high, contributing to our expanding gross margins in the service segment. During the quarter, service gross margins increased more than 100 basis points over the last year's comparable period. Overall, our fiscal second quarter results reinforce our confidence in the fiscal 2026 is shaping up to be a growth year for CSPI. After being in the market with AZT Protect for just a short amount of time, We have gained more than 60 unique customers, some of whom, as I noted earlier, have multi-site installations underway and additional expansion opportunities. These customers span a broad range of verticals, including steel, energy, manufacturing, water utilities, pharmaceuticals, food, and telecommunications. At the same time, we are dedicated to maintain momentum in our service business, and we are pleased with the margin expansion

realized from these operations during the quarter, as well as the profitability we achieved during the quarter. Overall, we are hopeful of sustained top and bottom line growth during the second half of the year and generating full fiscal year growth over the last year. With that, I will turn the call over to Gary to discuss our recent financial results in more detail. Gary.

Gary Levine | Chief Financial Officer:

Thanks, Victor. For the fiscal second quarter ended March 31, 2026, we generated $6 million in revenue compared to $13.1 million for the second quarter ended March 31, 2025. Product revenue grew 30% over last year's quarter to $11.1 million, with the growth primarily attributed to a large one-time purchase order completed for a customer. Service revenue for the period grew 6.6% to $4.9 million. Gross profit for the quarter increased to $4.5 million compared to $4.2 million for the same prior year period. Gross margin for the fiscal second quarter was 28%, of sales compared to the year-ago fiscal second quarter gross margin of 32% of sales. Gross margin realized from product revenue for the quarter was 15% versus 18% for the second quarter of fiscal 2025, while gross margin realized for the service revenue was 57% as compared to 55% for the year-ago quarter. Research and development expenses increased 7% to $818,000 compared to $763,000 for the same period year quarter as we supported the customization of AZT Protect deployments and OEM embedded developments. Selling general and administrative expenses for the fiscal second quarter increased 2% to $4.5 million from $4.4 million for the year-ago fiscal second quarter. The company grew interest income during the quarter by 27.9% due to the increase in financing transactions with customers. We recorded a tax benefit of $568,000, primarily from excess tax benefit from restricted stock awards vested during the second quarter, enabling the company to report net income of $264,000, or 3 cents per share, for the fiscal second quarter, compared to a net loss of 108,000, or 1 cent per share, common share for the prior fiscal second quarter. Our strong balance sheet offered us the opportunity to finance customer purchase orders, and as of March 31, 2026, we extended terms on over 30 transactions. We finished the quarter with cash and cash equivalents of $23.1 million. And the balance sheet continues to provide us the necessary resources to execute our growth strategies for the managed service and the ACT Protect product, offering us as well as paying a dividend of $0.03 per share on June 15, 2026 to shareholders of record on May 21, 2026. and we purchased 15,510 shares of common stock. Turning to our results for the first six months of fiscal 2026, revenue was $28 million compared to revenue of $28.8 million for the same prior year period. Gross profit for fiscal six-month period ended March 31, 2026, was $9.2 million, or 33% of sales, compared to $8.8 million, or 30% of sales. Benefiting from the fiscal seventh quarter tax benefit, the company reported net income of $355,004 per share of common in fiscal six months ended March 31, 2026, compared with the net income of $364,000 or 4 cents per share for the six-month period ended March 31, 2025. With that, I will turn it over to the operator for your questions.

Operator | Conference Operator:

Certainly. The floor is now open for questions. If you have any questions or comments, please press star 1 on your phone at this time. We ask that while posing your question, you please pick up your handset if listening on a speakerphone to provide optimum sound quality. Please hold for just a few moments while we pull for any questions. Your first question is coming from Mike Price. Please pose your question. Your line is live.

Mike Price | Analyst:

Good morning. Thanks for taking the question. I know you just awarded shares, Victor, 35,000 shares, but nothing shows more confidence, especially with the growth prospects that you have, when you actually buy shares. And I know the dividend isn't payable until June 15th. but there's plenty of cash. It seems like Joe Nurgis is the only one that has confidence in the company to continue to buy shares.

Unknown Participant | Participant:

Any thoughts? Yeah, no, not really.

Victor DeLobo | Chief Executive Officer:

You know, if I think at one time I would like to purchase it, I will. I definitely have confidence in what we're doing. I have not sold anything in many, many years. So I think that shows the confidence level that I have with the organization and where we're going.

Unknown Participant | Participant:

We will send a message, though, if you actually buy shares. So consider it.

Operator | Conference Operator:

Your next question is coming from Joseph Nurgis with Segrin Investments. Please close your question. Your line is live.

Joseph Nurgis | Analyst, Segrin Investments:

Good morning, guys. How are you today? Good, Joe. Let's elaborate a little bit on the cement company. You said in the press release that we've installed AZT in over two dozen plants currently in the U.S. Yeah. And I think you also mentioned on the call that worldwide, what is the opportunity? Over 100 plants? If it expands... Beyond the U.S.? Now, is the U.S. fully deployed with the plants, or do they have more plants to deploy here, too?

Victor DeLobo | Chief Executive Officer:

No, that was just the first phase. So there's potential for growth in the U.S., but the big growth is a sister company of theirs that has plants outside the U.S. that we're in talks with right now, and there is over 100 plants.

Joseph Nurgis | Analyst, Segrin Investments:

Okay, so I just wanted to clarify. And... As a follow-up, let me just get into the press release you guys did on the cement company. I think it was pretty – the bullet points you made were great. And a couple of points that we didn't know in the past that we talked about, and especially is the savings that the customers are accruing because they've installed AZT. You mentioned $1,000 per plant savings. And can you elaborate on where the savings are coming from?

Victor DeLobo | Chief Executive Officer:

It's just from talking to some of these companies that they're just saying that they're reducing the patching spend and preserving the life of their assets. So they're just estimating that extending these assets for a period of time, a year or two or three, would be... just on the average would be saving close to $1,000 per plant per month. So it's pretty significant when you look at if they can extend it for another 12 to 24 months of these units and there's less downtime because taking out a whole system and putting a new one is not

something you do 24 to 48 hours. It takes a lot of time, effort, and planning time. and that means that machine is down, and when those machines shut off, they're not making money for the organization. So those are just some cost numbers that came from some of the talks we had with different companies that we're talking to, and I'm guessing every company might have a different number, but based on the one that we were just talking to, that's what they're estimating.

Joseph Nurgis | Analyst, Segrin Investments:

And also in the press release, you mentioned requirements. Are these industry requirements or government requirements? You call them CISA, CPG-20, and IEC-62443. Are they requirements? Where are these requirements being deployed? I mean, who's coming up with these requirements?

Victor DeLobo | Chief Executive Officer:

Yeah, sometimes they're industry requirements. Sometimes they're government requirements. It just depends.

Joseph Nurgis | Analyst, Segrin Investments:

Okay, and the question basically is that you said some of the competitors cannot meet these requirements. And it looks like it's coming from the fact that their software is too comprehensive to meet some of these endpoints or to – protect the end point?

Victor DeLobo | Chief Executive Officer:

They're not investing some of the older versions of the software that are out there to meet those requirements. The new stuff, of course, they're moving forward with, but some of the stuff that Windows 7, Windows 10, they're choosing not to continue supporting that.

Joseph Nurgis | Analyst, Segrin Investments:

Okay. I guess this ties into it. You mentioned the lightweight, the fact that we take less memory and less core And I guess some of the competitors take much more, you know, for cybersecurity software. And in this case, they can't meet requirements because the software is too comprehensive, the competitor's software, to solve the problem.

Victor DeLobo | Chief Executive Officer:

Yeah, the older versions of software, you know, once you start putting, like the Windows XP, you start loading, you know... you know, just the way, you know, we're lightweight, right? Because there's not a lot of CPU being used with that. And when you have an old XP system, there's not a lot of extra memory or CPU that's just sitting there and not being used. And as a new software for some of these other organizations, you know, it's CPU intensive. And, you know, we were able to keep it 1% to 2% utilization on the CPU, and the memory is like 16 meg. It's very, very small. I haven't mentioned that in the last, I think, three or four conference calls.

Joseph Nurgis | Analyst, Segrin Investments:

So basically, a lot of competition is excluded because they really can't, with their current software, not be able to... It's just they're choosing to...

Victor DeLobo | Chief Executive Officer:

That's their go-to-market strategy, what they're choosing to support and not to support. Every organization, I guess they're looking at the overall market and what makes sense to them. And a lot of the software that they're doing is, you know, it's on the network side, not so much on the endpoint side. You know, we're very focused on the OT only, right, where some of the big players that are out there are focused on the IT side of it.

Joseph Nurgis | Analyst, Segrin Investments:

All right. Well, thanks a lot.

Victor DeLobo | Chief Executive Officer:

Appreciate it. Thanks, Joe.

Operator | Conference Operator:

Your next question is coming from Will Lauber with Visionary Wealth Advisors. Please pose your question. Your line is live.

Will Lauber | Analyst, Visionary Wealth Advisors:

Yes. Victor, I noticed you guys have a number of new board members. I know it's early on, but can you give kind of a quick review of what they're bringing to the table? Is it some new ideas or just kind of what they're adding to the board?

Victor DeLobo | Chief Executive Officer:

Sure. Jim has been in the OT world his whole life. We worked with him at the Lodge Pharmaceutical that evaluated our products, saw the value in it. He has a lot of contacts. He's very well known in the industry with a lot of the manufacturers of the world, the Emerson, the Siemens, the Honeywells. He has a lot of contacts there. And, you know, his reputation being in the OT industry is second to none. So he's very, very familiar with the AZT product, the development, the testing, where the value is. He's done a webinar with us, if some of you guys had attended that probably a year ago or so. I'm not sure exactly of the date. So, yeah, he's definitely, he knows the OT space. You know, we're consulting with him on where we should go. the market strategy, and then just a testimonial on how much he believes in the product that he was able to join our board.

Will Lauber | Analyst, Visionary Wealth Advisors:

Okay. And then on the land and expand, is it like budget issues by plan or is it contract issues that they might have a contract that goes on for another year or two or what's kind of,

Victor DeLobo | Chief Executive Officer:

No, it's just getting inside. And, you know, the way we do things is quite different with no patching. People, you know, they want to see it work, right? It's definitely a different methodology compared to everyone else. You know, it's kind of, as they say, it sounds like magic. So we definitely have to go through the testing process inside the organization and if we could get one individual to basically back us up, go through the testing, get it into their lab, get all the applications loaded, go through the whole process with the big steel plant. That's kind of the way we did it. The same thing with the big cement. You get someone who definitely believes in the product and it's easier to position it throughout the organization. And as I mentioned, I think on the last call, IT is definitely getting more and more involved. So being able to support, you know, our vision on how we can help them has helped us, you know, convince the IT folks that we can work side by side with some of the other big endpoint protection products that you're familiar with, like of the CrowdStrikes of the world or whatever that it's, you know, focused on. mainly on the IT side of the house that, you know, we compliment them. We don't really compete with them.

Will Lauber | Analyst, Visionary Wealth Advisors:

Okay. Um, so out of all these, uh, places where you've landed, um, if you were able to get, say 50% of all those different sites, does that make, uh, ARIA profitable or break even at that point?

Victor DeLobo | Chief Executive Officer:

Um, it, it, It'd be in the right direction. It'd be in the right direction, yeah.

Will Lauber | Analyst, Visionary Wealth Advisors:

Okay. And then on the cement producer deal, if I've identified it correctly, and if you've done two dozen sites, you've probably gone over the number of their cement producing sites, so I assume you guys are probably doing some of their aggregate sites as well. Is that correct?

Victor DeLobo | Chief Executive Officer:

Yeah, the ones that were under a particular budget, those are the ones we targeted. So instead of going one by one like what we have to do with the steel plant because its budgets are separated, we were able to consolidate and do kind of like a master's agreement to service those plants on one particular budget. So anything else that falls. There's expansion in that too. Those were the immediate expansion. um, systems that had older, older software on it that we targeted, but there's expansion inside the 20 sites, um, 20 some odd sites that we have in the U S. And then, like I said, the real big potential is if we can get outside the U S to those on a hundred plus, um, where there's a lot of systems out there that could be significant and we're working with them. Um, the good part of it is the it folks have already seen the product. So, um, I'm confident one way or the other, it's not going to take another 13 months to get over the finish line one way or the other. Whether they go with us or they don't, I think we can get that sales process shrunk into, you know, much shorter period of time.

Will Lauber | Analyst, Visionary Wealth Advisors:

Okay. And would that be the kind of an all or nothing kind of deal or quite a bit that you're not going to have to go one by one?

Victor DeLobo | Chief Executive Officer:

No, I think it would be all or nothing. I could be wrong, but I think the way they seem to want to work, it would be all or nothing. To be honest with you, it's a little too early to really give you 100% one way or the other, but my goal is to get the whole thing.

Will Lauber | Analyst, Visionary Wealth Advisors:

Yeah, I was kind of surprised. Usually you guys play things pretty close to the vest, and I have to assume that the talks are pretty advanced for you guys to put that up there publicly. So.

Victor DeLobo | Chief Executive Officer:

Yeah. Like I said, I kind of try to fill you in on as much as I can. You know, like I said, there's no guarantee on the other sites, but we are in talks, but at least we got the first, the first us based ones under our belt already.

Will Lauber | Analyst, Visionary Wealth Advisors:

Okay. All right. That's all I have. Thank you. Thank you.

Operator | Conference Operator:

Your next question is coming from Brett Davidson. Please pose your question. Your line is live.

Brett Davidson | Analyst:

All right. Good morning. I'm going to use you guys as a conduit here and correct me if I'm wrong, but the AZT products are less resource intensive than some of the competitors, more robust products targeting current hardware. Whereas the older hardware has less resources available, so making AZT an option because it's less resource intensive. Is that accurate?

Victor DeLobo | Chief Executive Officer:

That's accurate.

Brett Davidson | Analyst:

All right. The question I have is regarding a statement in the release that says, we continue to work with our strategic partners and distributors on additional multi-site deployments across key markets. Just looking for clarification on what exactly that means. Is that that the company is attempting to obtain commitments, or is this actively working on deployments or a mix of both?

Victor DeLobo | Chief Executive Officer:

It's a mixture of both, right? We're working with the distributors that I have mentioned prior that there are press releases out there, the CEDs, the RECCELs, the Sonar Powers of the World, with their end-user customers where we have sold maybe one particular site and we're trying to expand. There's a lot of water districts that we've sold into where there's expansion opportunities. probability in each and every one so it's you know we continue to expand with the distribution side of it to get more and more of their end user customers talking to us and then there's also expansion inside the customers that we've already closed small land and expand deals with so some of these are contracts where we're actively working to deploy on multi-site Yeah, they're all, you know, our goal is to get in there, get it tested, get it one site, two sites, working in purchase orders, right? A lot of the things that we're trying to do now is not just do a POC where we're giving it away. We're attempting to do more paid POCs where the customer is actually buying a starter kit where you get one trust center and say five or ten licenses. And so there's a commitment on both sides now, you know, that will help them get it up and running. But they're committed to really that it's not just kicking the tires. It's, you know, they're committed to a true PLC. And then we get in there and they, you know, purchase it, we install it. Hopefully they're happy and they evangelize us either at corporate where we try to do an enterprise agreement. or where in some cases we have to go to each and every site because of the way the budgets are distributed across the organization.

Brett Davidson | Analyst:

And what would you say is the current split of these deals coming through internal sources and through these third-party relationships, these distributors and what not?

Victor DeLobo | Chief Executive Officer:

We're leaning on the channel significantly right now. We're trying not to take anything direct any longer. There's always an exception, but the channel that we built over the last 18 months, we're trying to build that relationship, whether we walk them into something or the majority is, to be honest with you, they're walking us into their customers because they have long-term relationships with them.

Brett Davidson | Analyst:

And how many of these types of relationships do we have currently?

Victor DeLobo | Chief Executive Officer:

Well, there's three major ones that we have, but there's probably another half a dozen or so smaller resellers or integrators that we have. So, you know, I would say collectively probably 10.

Brett Davidson | Analyst:

And are all of them feeding – deals through or it's there's the, some of the larger ones are, you know, the majority of this or is this distributed?

Victor DeLobo | Chief Executive Officer:

Yeah, it's distributed all over the place. Some of the, some of the bigger resellers, uh, integrators that we're, we're talking with, you know, we're talking to 75 reps, some better than others, some more aggressive than others. Some have, uh, you know, better relationships than others. But those are the relationships that we've been trying to build over the last year plus is getting, you know, who is CSPI inside the, their organization that, you know, what our value is and how easy our product is to position. And there is a value to separate them from the rest of the world. That's the messaging we're trying to work with these folks going on to small little shows and, in different areas of the country where they bring in five or ten different customers, and we just do a little hour presentation to the customer and then try to build rapport.

Brett Davidson | Analyst:

So at this point, we've got a whole bunch of folks outside the organization that are evangelizing for this product at this point. That's correct. Oh, perfect. Thank you so much. Yep.

Operator | Conference Operator:

Once again, if you do have any remaining questions or comments, please press star 1 at this time. There are no further questions in queue at this time. I would now like to turn the floor back over to Victor DeLovo for closing remarks.

Victor DeLobo | Chief Executive Officer:

Thank you, everyone, for joining us today. We've made solid progress during the second quarter and are aggressively pursuing our opportunities for the remainder of fiscal 2026 both on the service side of our business as well as AZT Protect, and we look forward to reporting our progress with you in August. In the meantime, thank you to our shareholders for your support, to our team for the dedication and effort, and we wish everyone a good remainder of the day. Goodbye for now.

Operator | Conference Operator:

Thank you, everyone. This does conclude today's conference call. You may disconnect your phone lines at this time and have a wonderful day. Thank you for your participation.