

# NASDAQ:NVEC Q2 2025 Earnings Call Transcript

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## Dan Baker | President and CEO:

Good afternoon and welcome to the NVE Corporation conference call for the quarter ended September 30th, 2024. I'm Dan Baker, NVE's President and CEO. I'm joined by Controller and Principal Financial Officer, Daniel Nelson. This call is being webcast live via YouTube and Amazon Chime, and it's being recorded. A replay will be available through our website, nve.com, and our YouTube channel, youtube.com slash nvecorporation. All participants are currently in a listen-only mode. After our presentation, there will be a question and answer session. You'll be able to ask a question by pressing star 7 from a phone or clicking raise my hand from the Chime website or app. After my opening comments, Daniel Nelson will present our financial results, I'll cover products and marketing, and we'll open the call to questions. We issued our press release with financial results and filed our quarterly report on Form 10-Q in the past hour following the close of market. Links to the press release and 10-Q are available through the SEC's website, our website, and on X, formerly known as Twitter. please refer to the Safe Harbor Statement on your screen. Comments we may make that relate to future plans, events, financial results, or performance are forward-looking statements that are subject to certain risks and uncertainties, including, among others, such factors as uncertainties related to the economic environments and the industries we serve, and risks and uncertainties related to future sales and revenue, as well as the risk factors listed from time to time in our filings with the SEC, including our annual report on Form 10-K for the year ended March 31, 2024. Actual results could differ materially from the information provided and we undertake no obligation to update forward-looking statements we may make. We're pleased to report strong earnings despite continuing challenges in the semiconductor industry. Daniel Nelson will cover the financials. Daniel?

## Daniel Nelson | Controller and Principal Financial Officer:

Thanks, Dan. Total revenue for the quarter ended September 30, 2024 decreased 5% due to a 14% decrease in product sales, partially offset by a 3,950% increase in contract R&D revenue. The decrease in product sales was primarily due to continued inventory gluts, particularly in the distributor channels, driven by weak chip demand and a slow recovery in global manufacturing. Although the semiconductor industry recovery has been slower than most of us in the industry had hoped, we have an optimistic outlook. Our end markets are improving, and we have growth markets in the industrial Internet of Things and electrification. Gross profit increased 5% from the prior year, and gross margin percentage increased to 86% from 78% in the prior year quarter. The increases were due to more profitable product mix and a larger proportion of direct rather than distributor sales. Total expenses increased 55% for the second quarter of fiscal 2025 compared to the second quarter of fiscal 2024, mostly due to a 24% increase in research and development expense and a 31% increase in selling, general, and administrative expense. The increase in research and development expense was due to increased new product development activities. The increase in selling general and administrative expense was primarily due to increased sales and marketing activities. We added sales personnel and increased marketing activities. Then we'll talk about those activities shortly. Interest income for the quarter decreased 9% due to lower interest rate. Our effective tax rate, which is the provision for income taxes as a percentage of income before taxes, increased to 17% for the second quarter of fiscal 2025 compared to 8% for the second quarter of fiscal 2024. The lower tax rate last year was due to a recovery of credit losses and changes in the timing and amounts of federal tax credits and deductions. The 15% decrease in net income in the second quarter of fiscal 2025 compared to the prior year quarter was primarily due to decreased revenue, increased R&D, increased SG&A, decreased interest income, and a higher tax rate partially offset by increased gross profit margin. With an unrealized gain from marketable securities, comprehensive income increased to \$4.71 million from \$4.67 million the prior year quarter. It was a profitable quarter with 86% gross

margin, 65% operating margin, 60% net margin, and earnings of \$0.83 per share. For the first six months of fiscal 2025, total revenue decreased 15% to \$13.5 million from \$16 million for the first six months of the prior year. The decrease was due to a 20% decrease in product sales, partially offset by a 457% increase in contract R&D revenue. Net income for the first six months was \$8.12 million, a \$1.68 per diluted share, from \$9.13 million, or \$1.89 per share, for the first half of fiscal 2024. Now I'll turn the call back over to Dan Baker to cover the business. Over to you, Dan.

## **Dan Baker | President and CEO:**

Thanks, Daniel. I'll cover new products, sales and marketing, and CapEx. As Daniel mentioned, we've increased our investment in R&D. We spent 13% of revenue in the past quarter on R&D expense, plus customer-sponsored R&D, which is included in cost of sales. As a result of the efforts of our R&D team, we introduced a significant new product earlier this month, the ALT521-10E Tunneling Magneto-Resistance Rotation Sensor. Its build is the world's most sensitive device of its type, which allows for wide mechanical tolerances. Rotation sensing is ubiquitous. Applications include detecting complex motion in factory automation and automotive systems. The technology is also applicable to medical device navigation. There's more information on our website, and our YouTube channel has a demonstration of the new sensor's extraordinary sensitivity and precision. NVE would like to congratulate NASA on its successful Europa Clipper launch last week. Our robust components are mission-critical parts of the spacecraft's sophisticated instruments that will search Jupiter's icy moon for signs of life. The craft is scheduled to reach Europa in April 2030. NASA rigorously qualified our parts, a great validation of our quality and reliability. As Daniel noted, we've also increased our investment in sales and marketing. We exhibited at the Medical Design and Manufacturing Trade Show last week in Minneapolis, part of the Advanced Manufacturing event. Minnesota's healthcare industry hub and medical devices are an important market for us. We have a convincing benefit proposition for medical devices with small size, low power, and superb reliability. Specifically, we demonstrated our new high-field tunneling magnetoresistance sensors, which have a unique omnidirectional capability and detect high fields so they can detect the high fields from MRI to enable MRI-tolerant medical devices. We also featured our medical device navigation technology and our best-in-class electrical isolators to ensure the safety of medical instruments. Turning to CapEx, we've previously discussed plans for \$4 to \$5 million in capital investments over the next two fiscal years, fiscal 2025 and 2026. We've already spent \$1.13 million in the first half of this fiscal year, fiscal 2025. The investments will increase our capacity and capabilities, including the capability to manufacture wafer-level chip-scale packages in-house. These parts will be smaller, higher performance, and allow us to be more self-sufficient and capture more value. We are developing several wafer-level chip scale part types, we have provided customers with prototypes, and there has been strong customer interest. We hope to begin some production late this fiscal year. We have looked at other buildings in the area as options for the expansion, or we could expand in our current buildings. Our current lease expires in March 2026, and we're exploring a lease extension with an allowance to help pay for an expansion in our current building. We held our annual shareholders meeting in August in person here at NVE. Proxy advisory firms recommend in-person annual meetings for good governance. All of our directors and officers attended, along with our auditors. We had a chance to meet shareholders and answer questions. In the formal meeting, each director was re-elected, including Kelly Way, who was elected for the first time. Named executive officer compensation was approved, and the selection of our independent registered public accounting firm was ratified. Shareholders had a chance to see and try out hands-on product demonstrations and tour our facility. Demonstrations included a hot dog cooker to demonstrate our power conversion products and a chessboard to demonstrate an array of position sensors. There's a replay of the meeting with slides and product demonstrations on our website and YouTube channel. We filed the final vote counts in a current report on Form 8K. Now we'd like to open the call for questions. To ask a question from a phone, press star 7 to unmute, or from a browser or Chime app, click the Raise My Hand icon under the meeting chat. That's at the bottom of the left column, and unmute yourself to speak. Please state your name and affiliation before your question. And to prevent background noise, please mute your line after asking your question.

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

Hi, Dan and Dan. It's Jeff Bernstein from Silverberg Bernstein Capital. How are you?

**Dan Baker | President and CEO:**

Good. How are you, Jeff?

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

Good. Good. I have a couple questions for you. One, you had a big uptick in the R&D, contract R&D. Can you just talk about what that completed project was about?

**Dan Baker | President and CEO:**

Yes. So most of our contract R&D is related to defense business and developing new systems, particularly anti-tamper systems. So that's usually the nature of the contract R&D, and our hope is that it will result in product sales, down the road defense product sales. So because of the nature of those types of contracts, we are generally not able to get too specific about them. But the other advantage of those types of contracts is they build our intellectual property portfolio, they expand our technology platform, and our R&D team did a great job on that project.

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

Gotcha. And so is that something that you think could be a product in the next 12 or 18 months?

**Dan Baker | President and CEO:**

it could be it's difficult to to predict time frames they depend on procurement cycles sometimes they take longer than that but uh that's that's the goal is uh that we we typically do r d with with a goal of developing either technology that we can uh turn into products or that it's for a customer that will buy a custom high value added product

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

I understand. Okay. And then the unclonable functions business has been volatile over time. Can you just give us an update there? Seems like we're sending a lot more sophisticated systems overseas these days and that at some point that ought to convert into some positive momentum.

**Dan Baker | President and CEO:**

It does, Jeff. As you say, defense systems that are sold to allies often need anti-tamper protection. They're especially susceptible to falling into unfriendly hands. So while we hate to see some of the conflicts and instabilities, So allied weapon sales and defense system sales do tend to help that business. And as you know, there was recent earlier this year, there was an appropriation for allies specifically for Taiwan, Ukraine, and Israel. So those types of systems tend to require anti-tamper.

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

Okay, and was it kind of a low quarter on unclonable functions this quarter, or has this business been strong?

**Dan Baker | President and CEO:**

They were strong in the past quarter, but as you know, the sales can be lumpy and vary from quarter to quarter based on procurement schedules. We're optimistic about the long-term defense sales based on what we see now, but it's hard to predict quarter to quarter.

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

Gotcha, yeah, and... You did make the comment in the queue and on the call about a mixed shift in revenue more towards direct and less distribution. That had a very nice positive impact on gross margin. And you mentioned that the product revenue weakness was more due to inventory hangover in the distribution channel. and with direct customers. Can you just dive into that a little bit further?

**Dan Baker | President and CEO:**

Yes. So the industry is in a slowdown. The semiconductor industry in general is in a slowdown. So when that happens, what tends the distributors tend to build up their inventories because then customers aren't buying them. And then we get what's sometimes called the bullwhip effect. The supply chain amplifies market changes since customers tend to cancel orders to manage inventories during downturns. But the positive was that our end customer sales remained strong, and because we don't have a distributor margin in there, that tends to help our margins. And so as Daniel pointed out in the prepared remarks, our gross profit actually increased in the quarter year over year, even though the revenue was down slightly.

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

And can you just give us kind of an order of magnitude, you know, range of sales as a percent to the distribution channel? You know, does it range from, you know, 40 to 50 percent or 10 to 20 percent or, you know, et cetera? And I would assume that so we're in a trough now and we're kind of at the lower end of whatever that range is.

**Dan Baker | President and CEO:**

You're exactly right. We certainly hope we're at the lower end and that the inventories in the channel appear to be being depleted, which is a good sign for us because that means that the distributors will tend to return to buying so that they're booked to bill, if you will, that the amount that they're buying is going to more closely correlate to what their customers are buying. We don't report a percentage or a number, but I think qualitatively, you're right. The distributor sales are low right now and user sales have not been as depressed because of the effects that I mentioned. And so we're hopeful that the distributor sales will pick up again and the percentage will increase.

**Jeff Bernstein | Analyst at Silverberg Bernstein Capital:**

Okay. And then I wanted to touch on, you had a piece out during the quarter and you touched on this in the call about precise navigation sensors for catheters. Um, and, uh, and we talked about, uh, you and I during the quarter, um, that that was potentially, um, uh, something that was applicable to the new pulse field ablation, uh, catheters out there and, and your biggest customer, uh, is offering one and, um, and it's expected to be a big growth area for them. Uh, looks like, uh, Medtronic where your new director. is also offering the same thing. And they describe theirs as, this is Medtronic, as having real-time local impedance reading to assess catheter proximity to tissue. So I'm assuming that we're kind of talking about the same thing in terms of the navigational capabilities that your parts bring, but can you just discuss that a little bit?

**Dan Baker | President and CEO:**

Yeah, so as you point out, that is an important area for us and an area where we have a convincing benefit proposition in that our sensors are smaller and more sensitive than other technologies. So the way our customers can use this is to detect an external magnetic field that's imparted on the catheter, and then they can infer from that the position of the catheter in the body. And that's very important so that they can get the catheter to the right place and deliver the therapy or make sure that it's in the right blood vessel in the case of things like coronary cancer. angioplasty catheters. So it's an area that's becoming more important and where precision and small size is becoming more important. So our sensors have unique advantages in that area. And that was one of the things that we were promoting at the recent MD&M conference that we talked about in the prepared remarks. Gotcha. I understand. Thank you. Thank you, Jeff.

**Mike Osterman | Investor:**

This is Mike Osterman. Can I ask a question?

**Dan Baker | President and CEO:**

Yes, go ahead, sir.

**Mike Osterman | Investor:**

Yeah, Dan, this is Mike Osterman. I met you a couple of years ago at the annual meeting. Oh, yes, of course. Yes, two questions. First of all, I know you finished up your trade show, all your trade shows. I was just wondering, What the outcome was anything real positive is going to come out of that, and then the second question is since you've increased your capital cap X expenditures is that affecting your cash flow or how is it affecting your cash flow in relation to the dividend.

**Dan Baker | President and CEO:**

All right, so with regard to the first question, trade shows, we were pleased with the response, the traffic, and the leads that we got at the trade shows. We recently did a wrap-up video. It's on YouTube if you're interested. But we had three major trade shows during the season. And the last one was MD&M, which was last week. And we have a lot of leads to follow up. So our sales and sales support staff are working on that. And we're working on with the customers and with our distributors to follow up on some of the leads that we got at shows and at trips that were associated with those shows. So, we're pleased with that. Sometimes there's obviously a lag there and it takes some time to develop these leads, but we're optimistic that these will turn into business and into sales. In terms of the capital expenditures and cash flow, so the cash flow tends to

lead the capital expenditure. We often make down payments, so much of the \$1.1 million that we mentioned that we've spent so far in CapEx this fiscal year, the first half of the fiscal year, is down payments on equipment, so the equipment will be delivered Subsequently, but in the meantime, we have to pay cash for it to get the equipment going because these are custom pieces of equipment that are being designed to our specifications. The hope, of course, is that they will be able to generate products and business and will have a good return on the investment. But in the meantime, we're spending money that we believe is an investment. We believe though that we have a strong balance sheet and that we can continue to have both an aggressive dividend to build our shareholder value and the investments in capital expenditures, sales and marketing, and R&D that will pay off in the future.

**Mike Osterman | Investor:**

Okay, because your balance sheet, the cash balance, has come down as you've been making these forward payments for equipment, correct? Correct.

**Dan Baker | President and CEO:**

It has, yes. But we still have, by most metrics, a very strong balance sheet. We can support a dividend, and we can continue to make the investments we need to make.

**Mike Osterman | Investor:**

Okay. And this equipment hopefully comes online. Did you just have a time frame? Did I may have missed the timing that you said?

**Dan Baker | President and CEO:**

This fiscal year and next fiscal year. So that's fiscal 2025 and 2026. However, we do hope to be in some production of some of the new products that are related to the investments this fiscal year, which would end March 31st, 2025. Okay. Okay.

**Mike Osterman | Investor:**

Thank you.

**Dan Baker | President and CEO:**

Are there any other questions? You can unmute your microphone. Well, if not, we were pleased to report strong earnings for the past quarter and increases in gross profit and comprehensive income as the industry continues to recover. We look forward to speaking with you again on our next earnings call in January. A replay of this call will be available on the investor events page of our website, NVE.com, and our YouTube channel. That's YouTube.com slash NVE Corporation. Thank you for participating in today's call.