NASDAQ:OSS Q3 2025 Earnings Call Transcript

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Operator | Conference Call Operator:

Good day and welcome to the One Stop Systems Inc. 3rd Quarter 2025 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, you will have the opportunity to ask questions during the question and answer session. As a reminder, this call is being recorded. As part of the discussion today, the representatives from OSS will be making certain forward-looking statements regarding the company's future financial and operating results. including those relating to revenue growth, as well as business plans, bookings, the company's multi-year strategy, business objectives, and expectations. These statements are based on the company's current beliefs and expectations and should not be regarded as a representation by OSS that any of its plans or expectations will be achieved. Please be advised that these forward-looking statements are covered under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. and that OSS desires to avail itself of the protections of the safe harbor for these statements. Also, please be advised that the actual results could differ materially from those stated or implied by the forward-looking statements due to certain risks and uncertainties, including those described in the company's most recent annual report on Form 10-K, subsequent quarterly reports on Form 10-Q, and recent press releases. Please read these reports and other future filings that OSS will make with the SEC. OSS disclaims any duty to update or revise its forward-looking statements, except as required by applicable law. It is now my pleasure to turn the conference over to OSS's President and CEO, Mr. Mike Knowles. Please go ahead, sir.

Andrew | Investor Relations:

Thank you, Andrew.

Mike Knowles | President and CEO:

Good morning, everyone, and thank you for joining today's call. OSS delivered a strong third quarter with significant consolidated revenue growth, higher gross margin, and positive EBITDA net income. Our third quarter and year-to-date performance underscored the solid foundation we have built as we capitalized on increasing demand from both defense and commercial customers for our rugged enterprise class compute solutions. Since implementing several strategic actions in 2023 and 2024 to reposition OSS for growth, we have seen continual improvements in our financial and operating results. These actions included strengthening our leadership team of proven defense industry executives, launching a multi-year strategic plan, rebuilding our go-to-market approach, expanding our sales pipeline, and driving higher gross margins. As a result, we have experienced positive booking momentum over the past 12 months, translating into increased sales and positive operating leverage. I'm extremely proud of what our teams have accomplished and believe we're well positioned for continued growth and strong profitability in the remainder of 2025 and into 2026. We continue to pursue strategic growth opportunities that leverage our high-performance edge compute solution to meet the growing demands of AI, machine learning, autonomy, and sensor fusion at the edge. Our pipeline is expanding across leading defense organizations and advanced commercial enterprises that seek trusted, proven partners like OSS. On a trailing 12-month basis, our OSS segment had a book-to-fill ratio of 1.4. After a historic level of bookings in the second quarter, third quarter trends reflected expected quarter-to-quarter variability. Our growing pipeline and customer engagement activities remain strong across both defense and commercial markets. Our second quarter performance also reflects our continued focus on fulfilling recent awards, investing in next-generation product development, and advancing new program opportunities that are expected to contribute to positive booking growth in 2026 and 2027. Overall, we are tracking ahead of our plan and product development milestones, which gives us confidence in our long-term growth trajectory. During the third quarter, we continue to support and increase our exposure on the P-8 Poseidon Recreation Aircraft. To date, we have recognized lifetime contracted revenue over $50 million on the PA platform. In addition, we had previously announced a five-year sole source supply agreement and a five-year extension support, which involves equipping the PA aircraft and ground-based stations with high-capacity flash storage systems, spare flash storage canisters, and related support services. We expect continued orders from both the U.S. Navy and our Defense Prime customer into 2026. Another highlight is our growing relationship with the leading medical imaging OEM, underscoring the growing relevance of our compute and storage solutions in healthcare. We believe there are opportunities to expand our presence with this customer beyond the current five-year expected program value of over $25 million. Additional booking highlights include the September announcement of an initial $500,000 contract with Saffron Federal Systems, with additional orders expected totaling over $3 million. While smaller in size, this award establishes a new relationship with one of the world's leading high-technology defense contractors, and we see meaningful opportunity to expand this partnership over time. In October, we announced an initial $1.5 million order from a Canadian-based integrator of passenger cabin systems for the commercial aerospace industry. We expect this platform to contribute approximately $6 million in total revenue over the next three years. This award highlights the growing demand for high-performance compute in the commercial aerospace sector an increasingly important component of our commercial market strategy. Across our pipeline, demand remains strong, supported by growing interest for our enterprise-class compute solutions. While the ongoing government shutdown may impact the timing of near-term bookings, we view this as a timing issue, not a demand issue, since OSS remains the sole source provider on affected platforms. As a result, we expect defense-related bookings to improve as conditions normalize, though timing may remain uncertain. We also continue to see signs of stabilization in our European markets that are served by our Bresner operating unit. Recent bookings and revenue within our Bresner segment have been in line with our targets, and Bresner remains on track to achieve higher sales and profitability for 2025 as compared to last year's results. Looking ahead, we believe OSS is uniquely positioned to capitalize on multi-year growth opportunities driven by accelerating adoption of artificial intelligence, machine learning, autonomy, and sensor fusion at the edge. As these requirements become increasingly central to defense and commercial innovation, customers are turning to trusted partners like OSS with proven expertise in rugged enterprise class compute solutions. In support of this, we increased R&D investments in 2025 to capitalize on emerging opportunities we see developing within our markets. Our high wattage, high density expansion products, such as Ponto, are currently under evaluation with several potential commercial customers, as we focus on delivering high-density, high-wattage GPU and AI accelerator solutions that address the growing need for performance-intensive compute in data-rich environments. We're also encouraged by recent traction in commercial aerospace, highlighted by our recent award, which underscores how OSS technology is extending into new regulated markets where reliability and compute performance are critical. Looking ahead, we expect to further broaden our commercial product lineup with the planned launch of two new Gen 6 systems in November, designed to bring even greater processing capability and efficiency to our customers. Together, these initiatives demonstrate how we are executing on our strategy to leverage our rugged, enterprise-class engineering heritage into fast-growing commercial segments driven by AI and data-centric workloads. We continue to execute against a growing pipeline in both commercial and defense markets. We recently attended the Association of the U.S. Army, or AUSA, conference in Washington, D.C., and introduced a newly developed portfolio of products that leverage the advanced compute and low-latency advantages of commercial data centers. In addition, we showcased our wide array of scalable AI-ML sensor fusion and autonomy compute solutions, delivering leading compute and latency capability and advantaged size, weight, power, and cost, or SWAP-Cs. These solutions generated strong interest and multiple new engagements across Army and OEM programs. We also recently attended the NVIDIA GTC conference in Washington, D.C., where we highlighted OSS's expanding capabilities in high-performance GPU and AI accelerator expansion systems. Our participation at GTC reinforced OSS's growing presence within the AI compute ecosystem, where our technology complements leading platforms from NVIDIA, Broadcom, and Stereolabs. The conference provided valuable engagement with commercial and government customers exploring next-generation architectures for AI, machine learning, and data analytics at the edge, and further validated the role OSS can play in enabling high bandwidth, low latency compute for commercial applications. The visibility and relationships we're developing through these engagements are creating meaningful opportunities to expand our role on next-generation platforms. For example, our delivery of a rugged compute solution for combat vehicles for the U.S. Army remains under test and evaluation, which is expected to continue for the remainder of the year. We are encouraged by the growing number of multi-year platforms we now support, adding to our portfolio that includes the likes of the P-8 for the U.S. Navy, the medical imaging platform, and the autonomous maritime program for leading defense prime in Asia. Pursuing these types of recurring programmatic opportunities remains central to our long-term strategy. To accelerate our growth initiatives, we strengthened our balance sheet after quarter end through a registered direct offering, raising approximately $12.5 million in gross proceeds. This enhanced financial position combined with improving fundamentals provides the flexibility to fund operations, pursue strategic opportunity, and capitalize on expanding global demand. Looking ahead, our solid execution and year-to-date performance give us the confidence to raise our full year 2025 consolidated revenue guidance range. from $59 million to $61 million to $63 million to $65 million, while reaffirming our expectation to achieve positive annual EBITDA. I'm pleased with how 2025 is shaping up. Our turnaround strategies are progressing faster than expected, reflecting strong demand and operational execution. As we look ahead, we remain focused on accelerating growth, expanding profitability, and creating long-term value for our shareholders. Finally, I want to thank our entire team for their dedication, innovation, and relentless focus on delivering results for our customers and shareholders. So with this overview, I'd like to now turn the call over to Dan. Dan?

Dan | Chief Financial Officer:

Thank you, Mike, and good morning to everyone on today's call. Our Q3 results reflect a number of important financial milestones. One, we achieved robust top line growth, increasing revenue year over year by 36.9% at a consolidated level, and by 43.4% for the OSS segment. This growth reflects strong demand for our product, as well as our ability to execute on that demand to meet our customers' needs. Two, we achieved positive quarterly EBITDA in both of our operating segments and positive GAAP net income at a consolidated level. These results were supported by strong gross margins, reflecting the value that customers place on our differentiated technology. After the quarter closed, we also strengthened our balance sheet by securing $12.5 million of gross proceeds through a registered direct offering of common stock. This offering strengthens our balance sheet, provides flexibility around working capital to support our growth, and positions us to pursue a disciplined M&A strategy in 2026 and beyond. We believe the company is in a strong position, and with a solid backlog of orders, we are on track to achieve our increased full-year guidance and to execute on our robust growth and profitability objectives. Now for a quick overview of Q3 2025 financial performance. For the third quarter, we reported consolidated revenue of $18.8 million compared to $13.7 million last year and $14.1 million for the 2025 second quarter. The 36.9% year-over-year increase in consolidated revenue was a result of approximately $2.8 million of higher OSS segment revenue and $2.3 million of higher Bresner segment revenue. Third quarter sales were above our expectations, and we expect continued strength in both revenue and profitability in the fourth quarter of 2025. Consolidated gross margin in the third quarter was 35.7%. As a reminder, gross margin in the prior year quarter included a $6.1 million inventory charge in our OSS segments. Excluding the inventory charge, gross margin for the 2024 third quarter was 32%. On a segment basis, gross margin for the company's OSS segment improved to 45.6% compared to gross margin adjusted for the inventory charge of 43.2% for the same period a year ago. The 2.4 percentage point increase was primarily due to a more profitable mix of products shipped this year. Year-to-date, OSS segment gross margin has benefited from both operational efficiency and a favorable product mix. We continue to expect some level of variability in gross margins quarter-to-quarter based on absorption, product mix, and program lifecycle. On a sustained basis, we continue to target OSS segment margins in the mid-30s to low to mid-40s. In the fourth quarter of 2025, we anticipate OSS segment margins in the upper end of that range. The company's Bresner segment had gross margin percentage of 26% in the third quarter. The 400 basis point increase from the same period last year was primarily due to a more profitable mix of products shipped in the quarter. Total third quarter operating expenses increased 22% to $6.1 million. This increase was predominantly attributable to higher R&D expenditures, reflecting targeted investment in new product developments. For the third quarter, the company reported gap net income of $0.3 million, or $0.01 per diluted share, compared to a net loss of $6.8 million, or $0.32 per share in the prior year quarter. The company reported non-gap net income of $0.7 million, or $0.03 per share, compared to a non-gap net loss of $6.4 million, or $0.30 per share in the prior year quarter. Adjusted EBITDA. A non-GAAP metric was $1.2 million compared to an adjusted EBITDA loss of $6 million in the prior year third quarter. Turning to the balance sheet. As of September 30, 2025, OSS had total cash and short-term investments of $6.5 million, $1 million of borrowings outstanding on our $2 million revolving line of credit, and a consolidated balance outstanding on our term loans of $1.2 million. After the third quarter ended on October 1, 2025, OSS completed a registered direct offering with participation from certain new and existing institutional investors, resulting in gross proceeds of approximately $12.5 million before deducting placement agents, commissions, and other offering expenses. For the nine months ended September 30, 2025, OSS used $4.9 million in cash from operating activities compared to operating cash flow of $2.1 million for the nine-month ended September 30, 2024. The change from prior year period was primarily due to the timing of working capital, particularly receivables associated with our revenue ramp, partially offset by higher net income. As Mike mentioned, the company has increased its 2025 full-year financial guidance due to stronger-than-expected bookings over the trailing 12 months. We now anticipate consolidated revenue of 63 million to 65 million for the full year 2025, compared to prior guidance of 59 to 61 million. We expect OSS segment revenue in the range of 30 million to 32 million, representing a 22% to 30% increase in annual OSS segment revenue. And we expect the company to achieve positive EBITDA at a consolidated level. As we move through the final quarter of the year, we remain focused on disciplined execution, including managing our supply chain and achieving our planned production rank. We also remain focused on continuing to drive growth by investing in our technology and securing new platform opportunities that can provide sustained multi-year revenue streams. I look forward to updating you on our success. This completes our prepared remarks. Operator, please open the call to questions.

Operator | Conference Call Operator:

Thank you. Ladies and gentlemen, we will now begin the question and answer session. Should you have a question, please press the star followed by the number one on your touch-tone phone. You will hear a prompt that your hand has been raised. Should you wish to decline from the polling process, please press the star followed by the number two. If you are using a speakerphone, please lift the handset before pressing any keys.

Operator | Conference Call Operator:

One moment please for your first question. Your first question is from Brian Kinslinger from Alliance Global Partners. Please go ahead.

Brian Kinslinger | Analyst, Alliance Global Partners:

Great. Thanks so much and solid results. As we think about the uptick of revenue in the second half of the year, how should investors think about the seasonality going forward for core OSS in light of the strong bookings execution, but also as we think about the government shutdown?

Dan | Chief Financial Officer:

Yeah, I'll start with the seasonality, and then Mike can talk a little bit more about the government shutdown. So in general, we've seen this consistent pattern where we tend to see higher revenues in the second half of the year, just based on timing of bookings. As the government goes into the holiday period, you tend to see a bit of a slowdown in bookings, and so just the timing of that tends to drive second quarter revenues. or second half revenue higher than first half. We'd expect that to continue as we go into 2026. Probably, you know, a somewhat moderated ramp compared to what we saw in 2025, but still somewhat of a ramp as we go through the year.

Mike Knowles | President and CEO:

Yeah, Brian, and, you know, we're with kind of the strong bookings we've had this year, and as we close out the year, we'll expect to be starting next year with a little bit more backlog. So we think while we had a fairly decent-sized ramp this year, as Brian mentioned, or as Dan mentioned, hopefully that backlog and the way we'll prosecute will soften that. A bunch of that will be dependent on the government shutdown here. As we may have noted prior, we have everything in backlog we need to achieve our guidance for 2025, and the bookings that we are making now will further support that and or build into backlog for next year and the Main bookings that are affected for us by the government shutdown are anticipated sole source awards. So we won't be losing opportunity. We'll be affected by time.

Brian Kinslinger | Analyst, Alliance Global Partners:

Got it. And then maybe you can update us on the data center market opportunity and the advancements you're making. I mean, that market has seen unprecedented demand in the last few months. And then maybe also at a high level, touch on the situational awareness technology procurement evaluation by the Army. I don't know if that's been able to progress given the government shutdown, but that was something obviously of importance to the company.

Mike Knowles | President and CEO:

Yeah, great, Brian. Thanks. Yeah, on the data center side, as we had noted prior and in the remarks here, you know, we launched Ponto, which is a bigger version of our standard 4U program. GPU expansion solution. And so that product's under evaluation by a couple customers, specifically in these kind of data center markets where they're looking for this opportunity for big GPU and compute expansion. So we've got product in that market. We've got outreach. We've got interest. We have people testing. So we'll look through the end of this year and into the first half of next year to likely and hopefully see that transition into awards and backlog. And then as we noted in this call, we will be augmenting that with bringing forward some of the new PCI Gen 6 and some of the other new technologies that will be launching into those data center architectures. So we'll be well positioned with multiple products across that to leverage into that market. On the Army situation awareness side, That testing continues on. As you noted, yes, anything that had been going on now has stalled as a result of the government shutdown. So we'll be losing time on their evaluation as they went through. Things have been progressing and tracking well. The Army has also seen how they could use our distributed compute system for that solution in multiple other ways. So it's created other opportunities that we will look to prosecute coming into 2026 and beyond to leverage our position in the technology across those. So we'll look for hopefully more news on that in the coming year and where that could progress to.

Brian Kinslinger | Analyst, Alliance Global Partners:

Great. I got some more questions, but I'll get back in the queue and ask some more after.

Andrew | Investor Relations:

All right. Thank you, Brian. Thanks, Brian.

Operator | Conference Call Operator:

Your next question is from Eric Martinuzzi from Lake Street.

Operator | Conference Call Operator:

Please go ahead.

Eric Martinuzzi | Analyst, Lake Street:

Yeah, it was good to see the EOSS segment come back so strong there. That was a terrific recovery. Obviously, that was something that you guys have been, or investors have been patiently waiting for. But actually, I wanted to ask about Bresner. That was outperformance, at least versus what I was estimating for the third quarter. Can you tell us what was behind that? And then were there any pull forwards out of Q4 or maybe point us in a direction for where we expect the final quarter of the year for Bresner?

Dan | Chief Financial Officer:

Yeah, Bresner's been performing strong. We've seen some nice recovery in their industrial end markets and expect continued strength as we go through the year. FX has been a tailwind to Bresner's segment revenue. In the third quarter, they grew by about $2.3 million, about $600K if that was due to FX. The other $1.7 million was growth on constant currency basis, just really based on strength in their end markets and some of the larger projects that they've been executing on. And so we continue to see Bresner performing well and see strength as we close out the year and go into 26.

Mike Knowles | President and CEO:

Yeah, Eric, I just add, right, the economy hasn't fully recovered across the EU and Germany to the growth expectations they had at the start of the year. But Bresner has been able to find some strength in its markets to keep them on our targets and on our plans for the year. And they've seen some pockets of people generating some bigger orders, which has helped keep them on plan through the year.

Eric Martinuzzi | Analyst, Lake Street:

Okay, well, just sequentially then, is your expectation that we're in line to better with the final quarter of the year?

Dan | Chief Financial Officer:

Yeah, I would model, so there's a few shipments in Bresner that are going to be right on the cusp between this year and next year. So where those fall will kind of impact Q4, but I would model Q4 as being basically flat to Q3 for Bresner.

Eric Martinuzzi | Analyst, Lake Street:

Gotcha. Okay. And then you talked about the registered direct offering that closed on October 1st and the $12.5 million of gross cash raised. Just curious to know how are we, at least here in the near term, how are we deploying the cash? Are you sitting on it? Are you investing in an inventory, sales channel investments? What can you tell us?

Dan | Chief Financial Officer:

Yeah, absolutely. So the cash raise did a couple of things for us. One, it supported our working capital ramp as we're going through this growth phase. So you can see that in our results this quarter, particularly in AR. So we have, I think, good visibility towards collecting that AR this year. I expect that as we go into Q4, we'll see positive cash flow. We'll have a number of shipments that'll be going out between the end of November and the beginning of December. So where those shipments fall within that range will somewhat impact where our cash flow is for Q4, but I do expect that it will be positive. And then in terms of the cash rate, so as we support the working capital ramp, we're using it for that, but then companies generating positive EBITDA will be generating positive cash flow, so then we'd look to redeploy that cash rate towards a disciplined M&A strategy as we go into 2026.

Andrew | Investor Relations:

Thanks for taking my questions. Thanks, Eric.

Operator | Conference Call Operator:

The next question is from Scott Searle from Roth Capital.

Operator | Conference Call Operator:

Please go ahead.

Scott Searle | Analyst, Roth Capital:

Hey, good morning. Thanks for taking my questions. Congrats on the quarter, guys. Hey, Mike, maybe just to get some clarifications on the government shutdown. I want to understand a little bit better about what's still operating and what isn't. It sounds like some larger sole source opportunities might just be delayed from a timing standpoint. But I'm just kind of wondering, you know, what you're able to do in concert with government entities at the current time. And I think given the backlog you've talked about in the past, you felt pretty good for the next six months or so. I'm wondering if that still holds and when the shutdown becomes a little bit more concerning for you as you start to look into 26.

Mike Knowles | President and CEO:

Yes, thanks, Scott, for your question. So what we're seeing today generally is major organizations are shut down and really not responding. So any contract awards or deliveries we need to make, if the government is using a third-party services independent company, we're still able to operate with them. And so we still have some of that ongoing. We still can make deliveries to the customers, and the government is set up to pay for delivery on stuff that's under contract. So deliveries we have planned for this quarter through defense primes and or directly to the end services, we will be able to ship and deliver those, and we should be able to get payment for those under understanding standard payment timings. So the biggest effect for us really at the end of this year is just planned awards we were intended to get. So we'll have some backlog to start in the first half of next year. So that number will be fairly higher if we can get the government bookings in when the government reopens. But as long as realistically, as long as those bookings get in here before the end of Q2 next year. We still have plenty of time and runway to convert that to revenue. So we've got some runway to watch and plan where that goes.

Scott Searle | Analyst, Roth Capital:

Great. That great clarification really helps to see that we got visibility then through the first half. Looking to the fourth quarter and the guidance, It really implies, though, that core OSS is either flat to up $2 million. So you're starting to get to new highs in terms of the business, which I guess brings sustained EBITDA profitability with it. So I guess as we're looking into 2026 now, is that sustainable? And are you thinking about the core OSS business now being EBITDA positive for the year, which is, you know, I think well ahead of prior expectations? Just want some clarification on the early thoughts there.

Mike Knowles | President and CEO:

Yeah, I'll let Dan follow up on it, too. But yeah, in general, as we've kind of highlighted, we believe, based on our pipeline and everything we've been looking at, that the core OSS segment has this opportunity to grow at 20% to 30% a year. And so the bookings this year, the pipeline for next year, how we've been performing still gives us confidence that we should see growth into 2026 for the OSS segment in that range. Clearly, that opportunity would give us an opportunity to get OSS into the positive EBITDA range next year. That actually would be accelerating our plans a little bit. But given where we are, how we're performing the opportunity, I think it would be our intent that if bookings can play through and the timing can work out correctly, would be to try to accelerate that plan further. and work into that, because we are now kind of at that, we are kind of at that nexus point where the revenue inside of OSS segment would support that kind of outcome. Dan, anything?

Dan | Chief Financial Officer:

Yeah, no, the only thing I'd add, you know, just kind of reiterating that, high-level parameters for 26, revenue growth, that 20 to 30% that we've been targeting, gross margins for the OSS segment, we continue to see it in that mid-30s to low to mid-40s range. for the segment. Off-X we would see as being roughly flattish, but we did make some one-time investments to accelerate our R&D in 25, so I think you'll see some moderation or normalization of R&D expenditures as we go into 2026. And then Bresner segment, you know, we model growth in the range of 5% a year and stable gross margin.

Scott Searle | Analyst, Roth Capital:

Gotcha. And lastly, if I could, Mike, just, you know, kind of looking at the opportunity pipeline, certainly been a lot of government and military opportunities But commercial as well now, kind of given the slowdown with the current government infrastructure, are some more of those commercial opportunities kind of accelerating to the forefront? I think you referenced some, you know, in-flight entertainment opportunities and commercial aviation. But are there some bigger things that we should be thinking about in the 2026 timeframe on the commercial side? Thanks.

Mike Knowles | President and CEO:

Yeah, I think consistent with what we said in the earnings call here was we're seeing that movement. We've got some product placement. That was all about trying to continue to advance the commercial side of the strategy. We're probably a little bit slow to where we thought some commercial opportunity would have showed up. And so we're thinking that hopefully we'll start to see that coming to fruition in 2026, where we thought we might have seen it closer to the back end of 2025. But we're positioned well, I think, now with the products. We've got contacts, engagements across a number of fronts, as we mentioned, not only around data centers, but around medical imaging and some of the work we were doing with commercial aerospace. So we're starting to see some of that expansion. As long as the economy and the investments in those markets continue to go, I think we'll continue to see us be able to operate in those markets.

Andrew | Investor Relations:

Great. Thanks so much. All right. Thank you, Scott. Thank you.

Operator | Conference Call Operator:

Ladies and gentlemen, as a reminder, should you have any questions, please press the star key followed by the number one.

Andrew | Investor Relations:

We will pause a moment for further questions. There are no further questions at this time. Please proceed with closing remarks.

Mike Knowles | President and CEO:

Andrew, that completes our remarks for today. We appreciate everybody's support of the company and the questions. You can end the conference call.

Operator | Conference Call Operator:

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines.