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AMRS - Q2 2015 Amyris Inc Earnings Call

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PRESENTATION

Operator

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As a reminder, today's call is being recorded. You may listen to a webcast replay of this call by going to the investor section of Amyris's website.

I would now like to turn the call over to Peter DeNardo, Director of Investor Relations and Corporate Communications.

Peter DeNardo - *Amyris, Inc. - IR Director*

Thank you, Eric. Good afternoon and thank you for joining us this afternoon. With me today are John Melo, our Chief Executive Officer, and Raffi Asadorian, our Chief Financial Officer.

Please note that on this call, you will hear discussions of non-GAAP financial measures. Reconciliation of these non-GAAP measures to the most comparable GAAP financial measures is contained the news release distributed today, which is available at investors.amyris.com. The current report on Form 8-K furnished with respect to our press release is also enveloped available on our website as well as on the SEC's website at sec.gov.com.

During this call, we will make forward-looking statements about events and circumstances that have not yet occurred, including projections of Amyris' operating activities and financial results for 2015 and beyond. These statements are based on management's current expectations and actual results and future events may differ materially due to risks and uncertainties, including those detailed in the Company's recent SEC filings and the risk factors section of its quarterly report on Form 10-Q, filed with the SEC on May 57, 2015.

Amyris disclaims any obligation to update information contained in these forward-looking statements, whether as the result of new information, future events, or otherwise. Please refer to the Amyris SEC filings for a detailed discussion of the relevant risks and uncertainties. Before we begin today, I'd like to note that included in our webcast is a slide presentation we will refer to in today's presentation.

I will now turn the call over to John Melo. John?

John Melo - *Amyris, Inc. - President and CEO*

Thank you, Peter. Good afternoon and thank you for joining us today. We've completed the first half of the year, delivering a 36% increase over 2014 product revenue and collaboration inflows or a 2% revenue increase on a GAAP basis. This is in line with our expectation of delivering over 60% of our collaboration inflows in the first half of the year and about 80% of our product revenue in the second half of the year.

The second quarter was much lighter than the first quarter for collaboration inflows. We expected this based on partner payments and contract timing. Product revenue was 60% higher in the second quarter versus the first quarter and is expected to be significantly higher in the second half of the year as we deliver on our fragrance agreements and continued growth of our personal care and performance material business.

If you will recall, our fragrance ingredient business is batch manufacturing, where we run batches during single points of the year for full-year products to our customers. I will cover our first-half and second-quarter business highlights, review our strategic progress, and then pass to Raffi for a detailed financial update. And then end with our outlook for the second half of 2015.

Now let's turn to our first-half and second-quarter highlights. We delivered a 36% increase of product revenue and collaboration inflows in the first half of 2015 versus 2014. Due to the heavy collaboration mix, this resulted in a 2% increase on a GAAP revenue basis.

We expect to increase the rate of improvement over last year in the second half, with the mix in the second half driven by product revenue. Our production costs are 20% lower on a like-for-like basis. This includes the successful restart of farnesene and the production of our fragrance molecule that successfully started in July.

We've improved our free cash flow by $14.2 million from a loss of $37.9 million in the first half of 2014 to a loss of $23.7 million in the first half of 2015. We've effectively reduced our debt by nearly 60% and accessed $25 million of new equity as we continue to improve our liquidity and invest in growing our product revenues. We appreciate the continued strong support of our leading shareholders, including Total and John Doerr, who participated in our recent funding.

We are the first company in our sector to have successfully transitioned from the development phase of a renewable hydrocarbon fuel to the commercialization phase. We are very pleased with our relationship with Total and are continuing to work closely with them on commercialization of fuels along with supply opportunities for our performance materials.

The transition from development to commercialization will result in lower operating costs for us going forward. This transition has also provided us full access to global renewable diesel rights and we are in active discussions for potential regional licenses for our fuel technology. These transactions conclude our transition from direct exposure to crude oil pricing to very low correlation business activity with options to access value through our joint venture structure and licensing to upside value from our fuel technology and higher oil price environments.

We signed a multiyear multimillion-dollar collaboration for a key food ingredient. We received initial funding in July and expect first product commercialization around 2017. First-year commercialization should result in about $7 million to $10 million of product revenue and steady-state performance of around $40 million to $50 million of annual product revenue from this collaboration.

Today, we also introduced the launch of our second product technology in our microPharm platform: bio-opioids, for large and fast-growing chronic pain market. Our microPharm activity is focused on solving supply issues in markets where we have a significant product cost and performance advantage.

Our mission in these markets is to supply ingredients to API manufacturers who are leaders at regulatory, packaging, and distribution of pharmaceutical products. This is where our Company first started and where we continue to see significant opportunity to be disruptive. We announced two MOUs in the first half of this year with Indian and Chinese pharmaceutical leaders with a focus on the malaria market and are in active discussions with several leaders in their chronic pain medicine market to supply low-cost, high-performance opioids.

We expect our first product revenue in this segment starting in late 2016 for the lead malaria treatment ingredient. We expect first-year product revenue of $3 million to $5 million and second year around $10 million to $15 million. Our potential in this segment over the next 3 to 5 years is about $50 million to $70 million of annual product revenue.

We successfully introduced two new brands that are receiving strong consumer acceptance. Biossance.com has received over 163,000 visitors and requests for 42,000 samples. 90% of consumers who sampled and responded to our survey claim this is the best skin moisturizer they've ever used.

Based on early consumer activity and expected conversion, we expect the current annual revenue run rate of about $1 million and are tracking to potentially end the year at an annual revenue run rate of about $3 million to $5 million in this segment of our business.

Let me now turn to our strategic focus. We are continuing to simplify our business and execute on our differentiated business model of collaborating with industry leaders to solve supply challenges by delivering lower-cost and higher-performance products into the personal care and performance material sectors. This activity has more than covered our direct R&D spend over the last four years and we already have agreements in place to continue delivering on this type of performance for the coming years.

In addition to helping us prioritize the right products to solve real market needs and reduce the market risk of our technology, these partnerships are also delivering strong renewable product revenue growth. This activity represented one-third of our product revenue last year and is expected to deliver about 40% of this year's product revenue, or around $20 million of product revenue this year from collaboration partners where the products are now commercial. We expect to continue adding two to three new partners thea year and to launch two to three new products a year for these partners in our portfolio for the coming three to five years.

The second key focus area of our strategy is around farnesene-derivative products into the personal care and performance chemical markets, where we are the key ingredient supplier to over 400 brands. We have the leading emollients into the skin and hair care markets and have successfully introduced a high-performance, low-cost replacement for limonene into the industrial cleaning market. We are continuing to experience strong market demand for these products, with over 100% increased sellthroughsell through from distributor inventory and an additional 50 brands adding our ingredients to their formulas during the second quarter of 2015.

We continue to believe in the long-term disruptive nature of industrial biotechnology for large commodity markets like fuel. Our focus in this area is to have no exposure to low oil price environments and maintain access to the upside value in high oil price environments through licensing relationships and our jet fuel JV with Total.

Now let me turn the call over to Raffi to discuss our second-quarter financial results before we provide our current business outlook for the remainder of 2015.

Raffi Asadorian - *Amyris, Inc. - CFO*

Thank you, John, and good afternoon, everyone. As we noted on our last call, we expected second-quarter revenues would be down from Q1 2015 and it would be our most difficult quarter of the year, as we did not plan any new collaborations or any significant new product sales, given the timing of expected revenues from new product launches and fragrance molecules in the second half of the year. This said, as John discussed earlier, we've made progress on our plan in a number of areas that we believe position the Company for improved market access.

There are three main topics that I will cover today. First, providing details around our capital structure from the previously announced debt conversion, restructuring, and $25 million private placement transactions. Second, explain our cash flows for the quarter; and finally, explain the operating results in more detail.

At the end of the second quarter, our gross debt balance before debt discount approximated $321 million. The majority of this debt was convertible debt, with approximately $180 million held by our two largest shareholders: Total and Temasek. The announced debt conversion and restructuring transactions effectively converts the entire $180 million plus accrued and unpaid interest into Amyris common equity, and in the case of Total, additional interest in our fuels joint venture.

Approximately $37 million of this amount will convert at the maturity of the respective notes with redemption rights removed. In summary, we will not repay these notes and at maturity, they will automatically convert into Amyris common stock.

The notes converted into Amyris common shares were converted at a price of $2.30 a share, with warrants provided in case an equity offering was done at a price below the $2.30 per share, plus other warrants granted to one shareholder to maintain its pro rata share of ownership related to the conversion transaction.

Following the transaction and excluding the $37 million of debt that will be converted at maturity, we have approximately $140 million of gross debt before debt discount and $115 million, including the remaining debt discount. The remaining $140 million of debt consists of a $25 million convertible note maturing in 2017; approximately $47 million of senior secured debt, with maturities ranging from 2017 through 2022; $55 million of 6.5% convertible notes maturing in 2019; and $12 million of convertible notes maturing in 2018 and 2019.

Concurrently with the closing of the conversion transaction, we successfully closed a $25 million private placement of new common stock led by existing shareholders John Doerr, Naxos Capital, and Total. Again, we are thankful to have such a strong and committed shareholder base, which allowed us to quickly close this transaction.

After closing these transactions, our current outstanding common shares approximate $157.5 million before the warrants mentioned above and 204.8 million, including the warrants related to the transactions. Following these transactions, Total and Temasek have invested approximately $370 million of equity in Amyris with an average cost per share of $2.83. And they remain highly supportive as evidenced by their current actions.

We are continuing to review our capital structure to provide us with the flexibility to meet our growth plans toward generating positive cash flow in the coming quarters. Separately, it important to remember that we have maintained our $50 million committed equity facility.

This takes me into the second main topic: explaining our cash flows for the quarter. Our total cash investments balance at the end of the quarter was $12.7 million compared with $45.5 million at the end of Q1. The higher cash burn in Q2 was driven by four factors.

First, the startup of our production operations early in the quarter, including the buildup of inventories, which, excluding the inventory provisions, approximated $4 million. Second, increased marketing spend for our two new consumer product launches -- the run rate of which is planned to be lower in the second half. Third, the expected lower-than-average collaboration inflows in the quarter. And finally, increased debt service as certain loans began to amortize in Q2.

We expect the run rate cash outflows to reduce in the second half of the year, driven by expected higher revenues, lower expenses as we continue to focus on improving efficiencies and implementing cost reductions. And finally, we plan to refinance existing loans to improve current terms focused on cash flow generation.

Our first-half free cash flow improved by $14 million over the same period last year and was positively impacted by collaboration funding timing, but also improved gross margins over 2014.

Now let me take you through our second-quarter results in more detail. GAAP revenues for Q2 2015 were $7.8 million compared to $9.3 million in Q2 2014. Revenues for the quarter consisted of $4.5 million in collaboration and grant revenues, plus an additional $3.3 million in product sales.

The decline in Q2 revenue is largely attributed to the completion of a couple government contracts accounting for about $1.6 million of the decline. Product sales were negatively affected by foreign currency movements of about $0.6 million as well as lower cosmetic product sales due to high distributor inventory levels, despite continued high end-user demand. We believe this will continue to impact revenues for the next quarter until distributor inventory levels are all aligned.

Revenues for the 6 months ended June 30, 2015, were $15.7 million, an increase of 2% over Q2 2014. The increase was negatively impacted by foreign currency fluctuations of $0.7 million, the timing of a large fragrance product shipment of around $1 million in the first quarter of 2014, as well as the completion of a government contracts of about $2 million in the first half of 2014.

Our cash revenue inflows represent GAAP product sales plus cash payments received from collaborations and is a non-GAAP measure. For the 6 months ended June 30, 2015, our cash revenue inflows were $35.5 million compared with $26.1 million for the same period last year.

Despite some delays, our collaborations pipeline continues to be realized, as we recently announced our first collaboration in the food ingredients sector, which is expected to generate GAAP revenues and non-GAAP cash revenue inflows in the remainder of 2015. We also expect other collaboration in our pipeline to be closed and realized in the second half of this year.

Product cost of sales are comprised of three main components. First, actual cost of production of our products. Second, certain plant overhead costs during periods when the plan is operating below normal capacity or charged directly to the P&L, which we call excess capacity. And finally, any charges or benefits related to inventory provisions.

For Q2, our cost of products sold was $11 million compared with $7.5 million for the second quarter of 2014. The increase was mainly attributed to higher inventory provisions in the quarter, principally related to the lower fuel sales prices, which impact the value at which our fuels inventory can be recorded.

As illustrated, excluding the inventory provision, cost of sales were comparable to last year. For normalization purposes and to analyze our product-level costing, we review adjusted gross profits. Adjusted gross profit excludes the inventory provisions, excess capacity charge and depreciation.

Our adjusted gross margin in Q2 compared to Q2 2014 declined to 37.7% compared to 51.4%. This decline is largely due to product mix as the contribution from fuels in total revenues was higher in the second quarter, which we do not expect to recur in the second half of the year.

Our underlying farnesene cash production costs per liter have continued to decline. For the second quarter of 2015, excluding excess capacity charges, our farnesene cash production cost is $2.36 per liter. This compared with an average $3.40 per liter for the fiscal year 2014.

We anticipate the downward trend in cash production cost to continue as we continually improve strains, operational efficiency, and increased volumes. This should also lead to a favorable reduction in excess capacity costs. We will start to realize the favorable impact from these lower farnesene production costs from 2015 mainly in 2016.

Moving down the P&L, our second-quarter combined R&D and SG&A expenses were $25.5 million, down from $26.1 million for the second quarter of 2014. Excluding stock-based compensation and depreciation and amortization, the combined operating expenses were $21.3 million for Q2 2015 and $20.2 million for Q2 2014, respectively. The year-over-year increase in SG&A was due to our scaling up headcount and infrastructure to support our overall commercial expansion and new product introductions for Biossance and Muck Daddy.

Turning now to our net loss for the quarter, there were a couple large nonrecurring and non-cash items impacting our net loss of $47.1 million in the second quarter, which includes a non-cash gain of $28.8 million related to a change in fair value of derivatives and a $36.6 million acceleration of amortization of debt discounts related to the closing of the debt conversion transaction previously discussed.

Our adjusted net loss, excluding stock-based compensation, gains and losses from changes in fair value of derivatives, losses on debt extinguishment, and the acceleration of the amortization of debt discounts was $37.3 million or $0.47 per share in Q2 2015 compared to $27.5 million or $0.35 per share in the same period last year.

In summary the lower second-quarter revenues were planned; however, the unfavorable product sales mix in the quarter negatively impacted our ASPs and gross margins as the contribution from fuel sales was higher than planned as a result of the Total joint venture restructuring. With the expected Q4 delivery of our three new fragrance molecules to partners, the ramp-up of new product launches, and continued realization of our collaboration pipeline, the second half of the year is expected to shape up to an overall solid year for Amyris.

Finally, we are pleased to have successfully executed on a convertible debt conversion and restructuring as well as the private placement. These were initial steps in our efforts to strengthen our balance sheet and help secure our operational flexibility and financial security, which complements our existing $50 million equity facility put in place earlier this year. We intend to take additional steps with regards to improving our financial position and we'll update you as we make further progress.

Let me turn to call back over to John now for a review of our outlook and then we will open up for your questions.

John Melo - *Amyris, Inc. - President and CEO*

Thanks, Raffi. Now I'd like to provide you with our current business outlook for 2015. We delivered over 67% of our collaboration inflows target of around $50 million in the first half and expect the remainder of the year to come from milestone payments related to current agreements, the expansion of agreements with current partners that are in negotiation, and the addition of one to two new multimillion-dollar multiyear collaborations. In other words, we feel very confident about the second half of the year around our collaboration inflows.

We delivered 11% of our annual product revenue target of about $40 million to $50 million. We have $22 million to $27 million under agreement for delivery to current customers or collaborators in the second half and are expecting $7 million to $12 million from new products or distribution discussions that we expect to close by year end.

We've reduced our target to reflect the transition of jet fuel into the Total joint venture. We believe this translates into an expected cash revenue inflow range between $82 million and $102 million for the year.

We are also now introducing GAAP revenue expectations for the first time, which we believe will be in the range of $63 million to $75 million for the year. The wide ranges are driven by the collaboration revenues, which can fluctuate in large ranges given their size, the revenue recognition accounting for such agreements, and the timing. This guidance remains in line with our prior expectations and is adjusted for the transition of jet fuel sales into the Total joint venture.

Our differentiated technology platform, stable, low-cost manufacturing, and our market-leading products are continuing to deliver strong year-on-year revenue growth and lower cash burn. I would like to thank the continued commitment of the Amyris team that is focused on delivering renewable products that perform better and are lower costs than what we are replacing.

Our team cares most about the impact we can have, whether it's providing healthier and more sustainable skincare products, higher performing industrial cleaners that don't do harm to our planet, or making more available at a lower cost the key ingredient to the millions of patients suffering from chronic pain or children dying from malaria. We are becoming one of the leading specialty ingredient providers and we are doing this by making each brand we supply and each product we improve more sustainable, one molecule at a time. Our visionmission is to make renewable products mainstream by delivering better products made from renewable sources.

Let me end with a quote from one of our newest Biossance customers: I am always skeptical about product claims that revitalize. I tried Biossance, the revitalizer, with the same skepticism, but was just blown away. I have an autoimmune disease that limits the ingredients I can use. I need to stay as natural as possible.

When I read the main ingredient in the revitalizer is nNeossance squalane, I was concerned, because it sounded like some kind of placenta material. I was relieved to learn that it is derived from plant sugars and occurs naturally in the body.

Absolutely love this product. I get rough dry patches around my eyes and along my jaw line due to my disease and one application of the revitalizer greatly smoothes those areas. I tend to be really sensitive to new products, too, but there have been no allergic issues with this one. I will be purchasing the revitalizer on a long-term basis. Thank you.

This is the kind of impact we like to have: changing people's lives, delivering better products, doing it in a way that provides access to a better planet.

I'd like now to turn over to questions you may have. Eric?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Jeff Osborne, Cowen and Company.

Jeff Osborne - *Cowen and Company - Analyst*

Great. Thanks, John and Raffi, for all the detail on the call. Very helpful to get a sense of where you are at and also where you're headed. Thanks again for the non-GAAP and GAAP guidance -- that's certainly helpful from a modeling perspective.

I just wanted to get a sense of how do we think about the cadence of both revenue and expenses between the third and the fourth quarter? You obviously gave guidance for the full year. It sounded like there's quite a few things happening in the fourth quarter.

If I heard you right, you had some channel inventory on the cosmetic side that would hinder the third quarter, as it did in the second. And then also, you had three new molecules on the fragrance side in the fourth quarter. So what would be the sequential growth in the third quarter? Is that largely Muck Daddy and Biossance or how should we be thinking about Q3 versus Q4?

John Melo - *Amyris, Inc. - President and CEO*

Jeff, this is John. I'm sure Raffi will have some thoughts on this also. Thanks for making the call. What I would say is we have one of the first fragrance molecule batches being shipped in the third quarter. So you will see a sequential increase in the third quarter for product revenue.

I'd almost say that you saw a pretty significant increase first quarter to second quarter and you'll see another pretty good step up in product revenue second to third quarter. And then obviously, a significant move up in the fourth quarter because it is where the majority of our fragrance shipment occurs.

So you got to think of the branded products being a small slice third and fourth quarter; the fragrance shipments and personal care current products being a large slice of third and fourth quarter.

Jeff Osborne - *Cowen and Company - Analyst*

Okay. That's helpful. And then any moving pieces as it relates to OpEx? Are we going to trend at the existing rates here?

John Melo - *Amyris, Inc. - President and CEO*

I would say trend at existing rate third and then a step down in the fourth.

Jeff Osborne - *Cowen and Company - Analyst*

Just out of curiosity, what's the rationale for the step down?

John Melo - *Amyris, Inc. - President and CEO*

It's really related to the activity in fuels going down significantly and us adjusting our cost as that activity moves to the joint venture company.

Jeff Osborne - *Cowen and Company - Analyst*

Okay. And then the $2.36, I believe it was, cost per liter in the quarter. Are there any introductions of any new strains in the third or fourth quarter that you would see in Brazil and Brotas? Or is it just kind of greater volume should drive down cost and yields improving to get to that $2 number?

John Melo - *Amyris, Inc. - President and CEO*

You have two things occurring -- the current strength performance has continued to improve. Even the June number versus the May number was already significantly better. And my guess is the combination of either the existing strain improving or we do have the better strain in the pipeline will give us around get us around $2 if not slightly below $2 before year end on farnesene.

Jeff Osborne - *Cowen and Company - Analyst*

Okay. That is helpful. The last question, just going back to the cosmetics, is there a way that you going forward might have a better pulse on channel inventory? Or is that something that's kind of par for the course for the industry that you are selling into, that visibility is a little bit more challenging? Or had you seen this coming?

John Melo - *Amyris, Inc. - President and CEO*

We have pretty good visibility on it. It's not a surprise to us. It's more -- I would say we're probably a quarter behind, and really from the end of last year to this year, in the sales uptake that we expected. It is now coming through, so we expect that by the fourth quarter, that will all be worked out and we have some pretty good visibility on that.

Jeff Osborne - *Cowen and Company - Analyst*

Great to hear. I appreciate the detail. Thanks again.

Operator

(Operator Instructions)

Pavel Molchanov, Raymond James.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

Thanks for taking the question and congrats on the debt restructuring. Your business mix is obviously undergoing a lot of change: a lot of products and some older ones that seem to be less emphasized now. What's kind of a steady state gross margin target based on the latest iteration of your revenue mix?

John Melo - *Amyris, Inc. - President and CEO*

Pavel, welcome to the call, by the way. Thank you for making it. I'd say the big shift is really around fuels. When we think about deemphasizing fuels in the short to medium term, what that gets us is a pretty sustainable 50% to 60% in the cash gross margin.

And as Raffi highlighted on his part of the call, we are still working through and will really through the end of this year older inventory that will dilute that a bit. But from a cash respective, if I think about our actual manufacturing costs and our cash margin, we expect to be in the 50% range with the product mix.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

Okay. So is that a realistic target, for example, exiting 2015?

John Melo - *Amyris, Inc. - President and CEO*

It is.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

Okay. Okay, good. And then kind of looking at, again, your business mix broadly, you talked about reducing exposure to the commodity price. But as we're here sitting at $50 oil, what percentage of your $63 million to $75 million of GAAP revenue is tied in some way to petroleum?

John Melo - *Amyris, Inc. - President and CEO*

6.5% as of the end of the second quarter.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

And is that all renewable diesel?

John Melo - *Amyris, Inc. - President and CEO*

It is.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

And jet fuel?

John Melo - *Amyris, Inc. - President and CEO*

No, just renewable diesel in Brazil. Jet fuel has moved over to the Total joint venture.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

Got it. And none of your kind of specialty chemicals have any significant linkage to crude?

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John Melo - *Amyris, Inc. - President and CEO*

That is correct. There's some upside in it because in our current pricing and margins assumptions, we are using current market price. So there are some markets, specifically in the polymer side, that there is some correlation. But the way we have built our model and our current pricing is based on current crude pricing for those products.

Pavel Molchanov - *Raymond James & Associates, Inc. - Analyst*

All right. Very good. Appreciate it, guys.

Operator

(Operator Instructions)

And I'm showing no further questions. I'd like to turn it back to CEO John Melo for closing remarks.

John Melo - *Amyris, Inc. - President and CEO*

Thanks, Eric. Appreciate your help and thanks, everyone, for joining us today and for your continued support of Amyris. We are very pleased with the progress the Company is making.

It's obviously never as fast and as low cost as we like, but I think now with the restructuring that we've achieved with the new products and with our product focus on really specialty ingredients in the markets that we know well and the partners we know well, we are really looking to sustain growth going forward. Again, really appreciative of everybody's support. I'd like to wish everybody a good day and thank you for making the call with us today.

Operator

Ladies and gentlemen, this does conclude today's conference. Thank you for your attendance. You may now disconnect. Everyone, have a great day.
