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Presentation

Operator

Good afternoon. My name is Audra, and I will be your conference operator today. At this time, I would like to welcome everyone to the SkyWater Technology Third Quarter 2023 Financial Results Conference Call. Today's conference is being recorded. [Operator Instructions]

At this time, I'd like to turn the conference over to Claire McAdams, Investor Relations for SkyWater. Please go ahead.

Claire E. McAdams
Headgate Partners LLC

Thank you, operator. Good afternoon, and welcome to SkyWater's Third Quarter Fiscal 2023 Conference Call. With me on the call today from SkyWater are Thomas Sonderman, Chief Executive Officer; and Steve Manko, Chief Financial Officer.

I'd like to remind you that our call is being webcast live on SkyWater's Investor Relations website at ir.skywatertechnology.com. The webcast will be available for replay shortly after the call concludes. On our IR website, we have also posted an investor slide presentation as well as a new financial supplement to accompany today's call.

During the call, any statements made about our future financial results and business are forward-looking statements. These forward-looking statements are subject to risks and uncertainties that could cause our actual results to differ materially. For a discussion of these risks and uncertainties, please refer to our filings with the Securities and Exchange Commission, including our earnings release filed on Form 8-K today and our fiscal 2022 10-K. All forward-looking statements are made as of today, and we assume no obligation to update any such statements.

During this call, we will discuss non-GAAP financial measures. You can find a reconciliation of these non-GAAP financial measures to GAAP financial measures in our earnings release, our financial supplement and in our Q3 earnings presentation, all three of which are posted on our Investor Relations website.

And with that, I'll turn the call over to Tom.

Thomas J. Sonderman
CEO & Director

Thank you, Claire, and good afternoon to everyone on the call. Today, we are pleased to report strong third quarter financial results as SkyWater set another record for quarterly revenues at nearly $72 million. Q3 revenues exceeded our expectations going into the quarter and marked an unprecedented fifth straight quarter of sequential growth.

Revenues were 3% higher than the previous record set in Q2 and grew 37% from Q3 of last year. We believe the sequential growth in our ATS business demonstrates that our customers' innovation investments remain strong despite the incremental softening in end market demand since our last call. Not surprisingly, the strong growth achieved in our ATS business this year has been partially offset by a lower level of Wafer Services revenue, which has seen a greater impact from the overall macroeconomic weakness and slowing consumer demand environment.

For SkyWater, 2023 has continued to see a robust R&D environment in the face of the current inventory correction facing the broader semiconductor industry and, most recently, the automotive and industrial markets. We expect this will result in a significant increase in ATS revenue mix this year from the 2/3-1/3 split seen in 2022 to an expected 80-20 split for fiscal 2023.

Year-to-date, total revenues of $208 million are up 40% year-over-year, clearly exceeding our expectations entering 2023. While the outperformance we have achieved this year has been primarily driven by the increased demand and improved operational execution, we are also entering a new stage of

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expected amplified tool revenues within the ATS business. Not only is this a trend we expect to continue but anticipate a significant increase in tool investments over the next several quarters. We believe this is a strong indicator of our customers' desire to make increased investments in SkyWater to enable the production ramp of multiple products and platforms being developed here at our fab in Bloomington as well as in Florida.

The largest contributor to our ATS growth this year, up over 50%, has been multiple strategic aerospace and defense programs. These have been ramping in scale and scope throughout 2023 and include important progress with phase 2 of our RadHard 90-nanometer platform. Other A&D programs are also moving forward aggressively, which we believe signifies the Department of Defense's increased trust and commitment to SkyWater to provide critical national security technologies.

The government's increased commitment to SkyWater is enabling us to achieve several important milestones this year. We are on track to exceed our long-term revenue growth target of 25% annually in a year that is otherwise down for the semiconductor industry and where the overall foundry market has seen about a 10% decline from 2022. Our continued progress towards the maturation of our A&D technologies is accelerating our engagement with new customers and partners.

It is SkyWater's intent to develop some of the most advanced RadHard and imaging platforms in existence. Both platforms serve a similar customer ecosystem. By leveraging our unique technology enablement and product realization model within this community, we continue to see design capture momentum as these technologies are ready for our production ramp in 2025.

We expect to be able to leverage the A&D investments happening today at SkyWater to support numerous commercial use cases that require reliable CMOS performance in nontraditional applications like extreme environment computation, edge-based AI and focal plane array thermal imaging. These capabilities are needed in a range of use cases, including low-Earth orbit satellites, industrial MCUs, IoT devices and autonomous systems.

The ability to execute well on multiple government programs is a key attribute of our CHIPS application framework as we pursue funding to expand our 2 existing fabs and establish a greenfield facility in partnership with Purdue. While this funding is not essential to our long-term growth plans, we do expect it to be an accelerant to our advancement in the second half of this decade.

Beyond strategic A&D, there are several important commercial programs underway with our bio health and advanced computing customers, each of which are generating multi-million dollar revenues for us this year. In bio health, we are seeing continued strength in the areas of rapid diagnostics, genetic sequencing and health wearable devices, all high-potential products that are demonstrating a strong demand for innovation services.

And SkyWater's differentiated leadership capabilities in superconducting and photonics offer an important value proposition for customers pursuing innovations in the rapidly accelerating artificial intelligence and quantum computing industries.

While the very nature of our business as a technology foundry is to work with emerging companies and entirely new product categories, fewer than half of these engagements are with early-stage or start-up companies. As our Technology-as-a-Service business model has matured and developed over the last few years, we have become increasingly selective with our customer engagements. As a result, our commercial business pipeline has never been stronger. All these programs are pursuing emerging and large market opportunities which, while relatively small today, have a path towards high-volume production within the next couple of years.

Fundamental to SkyWater's ability to continue to ramp and scale our business are the transformative investments we are making today in our fab and enterprise operations. These investments are focused on rapidly improving the operational efficiencies needed to achieve even higher outputs from our Bloomington fab, enhance the monetization of our unique value proposition and optimize the utilization of our workforce.

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This approach is already starting to pay dividends. In Q3, we increased wafer velocity, achieved record levels of ATS activities and realized more linear Wafer Services production. These continuous improvements are enabling us to realize a higher concentration of ATS activities, improving the service level we provide to our customers. We expect the transformation to be completed by mid-2024 as these proprietary business processes and systems are integrated across the company.

Turning to our recent announcement regarding Cadence Design Systems. The world's leading systems design company is now offering a SKY130 PDK to their user base, encouraging and facilitating design work and subsequent tape-outs on one of SkyWater's key CMOS technology platforms. Cadence's incorporation of the SKY130 PDK is an important validation of the key role we are playing in the future of open source design. By leveraging Cadence's substantial global user base, SkyWater's reach continues to expand to new customers, markets and applications. This is a significant milestone for us and the open source community as we continue to enable this capability for the global semiconductor ecosystem.

Now turning to our outlook for Q4 and the year ahead. We expect to achieve a similar level of core ATS activities in Q4 after well exceeding our forecast in Q3. At the same time, we anticipate a further increase in our Q4 tool revenue. We expect that offsetting this ATS growth will be another sequential decline in Wafer Services revenue, which is materializing due to the inventory corrections taking place in the automotive and industrial sectors. Altogether, we expect Q4 revenue in the mid-$70 million range.

As we look ahead to 2024, SkyWater's core ATS activities are anticipated to show solid growth after the 50% growth forecasted for 2023. We believe our continued momentum in ATS, coupled with a strong year of customer tool investment, will result in continued outperformance in SkyWater's revenue growth in 2024 compared to the overall industry even with the expected decline in Wafer Services. Steve will provide further details on 2024 during his remarks.

In summary, we believe that the distinction of our business model, the highly differentiated, innovative technologies we are bringing to market and the strong customer pipeline we continue to build position SkyWater for several years of above-industry growth and continued strong operating leverage.

I'll now turn the call over to Steve.

Steve Manko
Chief Financial Officer

Thank you, Tom. Before I begin my review of our third quarter results, I will direct you to a new financial supplement available on our IR website, which summarizes our quarterly financial results for the last 3 years. Starting in Q3, we have changed our policy regarding a couple of our non-GAAP financial metrics, namely tool revenues and margins are no longer excluded from our non-GAAP results, while the consulting fees incurred year-to-date are now excluded from our non-GAAP results. These helpful supplements on our IR website is where you can find the current non-GAAP treatment applied to prior periods.

The reasons for the non-GAAP changes are as follows. First, tool sales have historically been infrequent and viewed by management as secondary to ATS development revenue, which is why they previously were excluded from our non-GAAP results. Recently, our ATS customers have stepped up their commitment to fund tool purchases, and we expect this trend to continue going forward. As tool sales are expected to be a material and frequent component of our financials for the foreseeable future, we are no longer excluding their impact in the calculation of our non-GAAP financial measures.

That being said, the supplement on our IR website does provide the gross margin impact of tool sales every quarter and year since fiscal 2021, and we will continue to provide the detail regarding the impact of tool sales on our financial results.

Next, in the second quarter of 2023, we have incurred project-based management consulting fees related to the long-term transformation activities focused on improvement in automation and operational efficiency. Similarly, we have also incurred project-based specialist fees associated with our CHIPS Act application. Neither of these types of fees are required to run our business and, therefore, are incremental to ongoing operations and are not a normal operating expense. Beginning in Q3 2023, we began excluding these fees in the calculation of our non-GAAP earnings, non-GAAP earnings per share and adjusted

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EBITDA. The supplement on our website likewise shows a resulting retroactive non-GAAP earnings and adjusted EBITDA for prior quarters after excluding these fees. We hope you find this supplement a helpful guide as we compare results to future periods.

Now turning to our Q3 results. Third quarter revenues reached another record for us, exceeding our expectations to total $71.6 million, which was up 3% from Q2 and up 37% from the third quarter of last year. Record ATS revenue of $57.1 million was up 8% from Q2 and up 62% compared to Q3 of last year and included $3.2 million of tool sales. The sequential growth in ATS revenues exceeded our earlier expectations, especially considering the $3.6 million revenue pull-in recorded in Q2. Offsetting the strong sequential growth was a 14% decline in Wafer Services revenue as a result of the softening demand environment in the automotive and industrial markets.

The decline in Wafer Services volumes, along with the increased tool sales, resulted in a sequential decline in non-GAAP gross margin, which was 20.4% for the quarter.

Tool gross profit was $0.4 million, which negatively impacted gross margin by 40 basis points.

Non-GAAP operating expenses declined $13.4 million, reflecting the normalized quarterly run rate of our ongoing business cost structure.

Management consulting fees were within the range of our earlier expectations at $3.5 million in Q3.

Non-GAAP operating income was $1.2 million, and adjusted EBITDA was $8.3 million.

Interest expense was $2.5 million. And with nominal tax, the GAAP net loss was $0.16 per share, and the non-GAAP net loss was $0.05 per share.

Now turning to the balance sheet. We ended the quarter with $17.3 million in cash and cash equivalents, a net increase of about $1 million from Q2. As a reminder, we have been generating positive cash flow from the P&L for the last 4 straight quarters. And in Q3, this amount was about $4.5 million, essentially equal to adjusted EBITDA less interest and CapEx.

We added an additional $8 million in proceeds from our ATM early in the quarter at an average price of just under $10 a share. We reduced total debt by nearly $4 million, and the remaining use of cash was about $8 million of changes in working capital.

Turning to our outlook for Q4 and our expectations for various financial metrics as we enter 2024. As Tom mentioned, with our current visibility, we expect Q4 revenue levels in the mid-$70 million range. This reflects our assumption of a 15% to 20% sequential decline in Wafer Services revenue, a similar level of core ATS revenues and a significant increase in tool sales, which could grow to as much as $10 million.

Given the changes in the Wafer Services outlook and the expected revenue profile for Q4, we expect non-GAAP gross margin will decline sequentially between 14% and 15%. With our outlook for Wafer Services revenue in the range of $10 million to $12 million for the next several quarters, we expect Q4 gross margin will be impacted by factory under absorption before returning to the 20% range in Q1. We also expect the higher level of low-margin tool sales will impact gross margin by approximately 100 basis points. We expect to continue to manage non-GAAP operating expenses within the range of $13 million to $14 million per quarter.

As we look ahead to fiscal 2024, as Tom mentioned, we expect another year of strong revenue growth outperforming the overall industry driven by a significant customer-funded tool investments and continued solid growth in core ATS activities, which we expect will partially offset by a lower level of Wafer Services business.

While we expect tool sales will decline sequentially in Q1 '24, we believe customer-funded tool investments could increase significantly in Q2 2024 and beyond. This strong level of customer-funded CapEx would drive an increased mix of tool revenues and modulate our typical ATS margin flow-through performance, which has well exceeded 50% since last year.

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At the same time, after Q1 of 2024, approximately $3.7 million of quarterly depreciation from purchase accounting will phase out of our cost of revenue, reducing our total depreciation expense by about half. This will be a significant tailwind to our gross margin performance, which will help to offset the headwind of a greater mix of tool sales in 2024. We also expect to turn the corner to positive non-GAAP EPS in 2024 and look forward to discussing our success on this key milestone in future calls.

There is no doubt that our CapEx-light model is unique and brings some complexity to modeling our forward-looking financial performance. However, it's important to come away from today's call with an understanding of all the significant benefits of customer-funded tool investment. For example, we anticipate over 80% of our planned capacity expansion in 2024 will be funded by our customers. This means that we expect our quarterly depreciation will remain at these very low, approximately $3.5 million levels as revenues grow. Compared to typical semiconductor foundry depreciation levels of around 15% to 20% of revenues, for us, we expect to see depreciation shrink to less than 5% of our revenues, which is one of the reasons we believe we can be so confident in our long-term margin target of 40%.
With that, we can transition the call to Q&A.

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Question and Answer

Operator

[Operator Instructions] We'll go first to Krish Sankar at TD Cowen.

Kinney Chin
TD Cowen, Research Division

This is Steven calling on behalf of Krish. Just a first question on certain picture on the ATS business, Thomas, if you could. I guess just given the commentary about 2024, along with the customer tool revenues, just wondering like in terms of the underlying ATS revenue growth, I understand that you guys expected to potentially outperform the broader market, but should we be expecting a moderation in that growth because customers are potentially focusing more on moving their R&D design activities towards commercial production in 2025? Or is there additional layering on of new ATS programs? And also in terms of tool revenues, is that driven more by commercial customers? Or is it primarily or largely government-related type projects?

Thomas J. Sonderman
CEO & Director

Yes. Thanks for the questions, and I appreciate you joining the call. So just to start with ATS, we still feel like there's a lot of opportunity with our ATS business. We talked about solid growth going into next year. That's after 50% growth this past year. That will be a combination of continued program expansion as well as new programs. If you recall our funnel, we have new programs always entering the business and then we have other programs that are moving through the business as they move into volume production. So what we're seeing is all of those factors combined to create, again, an opportunity for us to continue to grow ATS and then when combined with the tool investment, significant tool investment, really position us to continue to have industry growth while, at the same time, putting new capabilities, new capacity into the fab that we believe will continue to pay dividends not just for the customers.

And the majority of the tools that we're talking about are coming through DoD and aerospace and defense programs, but they can be used for other commercial customers as well. So they're not exclusive. And when we put them in the fab. Many of them are with the expectation that they will serve the broader business.

Kinney Chin
TD Cowen, Research Division

That's very helpful, Tom. As a follow-up, I just wanted to ask about the Wafer Services business. So I know you guys mentioned industrial and automotive exposure being primary drivers of trends there. Just for clarification, for the top 2 or 3 customers in Wafer Services, the products that you manufacture with them, are they typically like dual-sourced products where there will be 1, 2 or 3 suppliers where they single source products from you?

Thomas J. Sonderman
CEO & Director

Yes. So it's a little bit of a combination. So if you look at our, we call them, legacy products from the old Cypress business that now Infineon has, there's kind of a combination of single-source products and dual and even multiple-source products within that customer. And then we have another customer, Parade, who is also legacy. This is all using our S130 technology on what we call a PSoC platform, a programmable system on a chip. So these are legacy products. We do have other products that go into both the A&D space and the bio space that complements those legacy products. The largest volumes are definitely the industrial and automotive, which are the legacy Cypress products.

Operator

We'll move next to Quinn Bolton at Needham & Company.

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Nicolas Emilio Doyle
Needham & Company, LLC, Research Division

This is Nick Doyle on for Quinn. Can you just talk again about the Wafer Services, and I guess, inventory burning related decline? I guess how long do you expect the inventory digestion to last? You talked about, I think, that it would be weak in the first quarter also. And is that you need demand to come back? Or is that really an inventory problem?

Thomas J. Sonderman
CEO & Director

Yes. I mean, if you look at the end customers, the automotive and industrial sectors are now beginning to feel the effects of the correction that's been going on for multiple quarters. And of course, given our concentration in that space, we are now seeing those effects as well. How and when those particular programs will come back is going to be dependent on the macro environment that we're in. Obviously, there's been inventory burn going on. There's been inventory build going on, we believe, as well. Our goal is really to transition away from these legacy products, move programs out of ATS into Wafer Services, prepare for the ramps that are coming in 2025 and really leverage the significant tool investment that's going to occur next year to position us for the second half of the decade and do this in a way where we can supplement some of the weakness that is happening across the industry and is affecting our Wafer Services business.

Steve Manko
Chief Financial Officer

But again, like as we would rather have that revenue coming through, keep in mind, we're talking only about 20% of our business and a slight decline only in a certain segment of 20% of our business revenue.

Thomas J. Sonderman
CEO & Director

Yes, that's an important point. Right now, we're looking at Wafer Services modeling about 20% of 2023 revenue. So it's a relatively small effect when you look at the overall business that we're running.

Nicolas Emilio Doyle
Needham & Company, LLC, Research Division

Okay. That makes sense. Yes. We're seeing that across the semi landscape, the auto and industrial inventory burning. Could you talk more about the tool revenue? What are you seeing from customers that's driving this change in how you're defining tool revenue? It seems like you're expecting a pretty big ramp next quarter and into '24. I guess, if you could just talk about the drivers where customers are kind of changing their decision to buy more tool revenue.

Thomas J. Sonderman
CEO & Director

Yes. So it's a great question, and I'm glad you're asking it because it's important to understand the CapEx-light model, and it's really a paradigm shift in the foundry business. Traditionally, the semiconductor manufacturer always had to go buy the equipment, and then they would recoup that investment when volumes materialize. But they were taking all the risk. The SkyWater model is to get our customers to basically take that risk to not only secure -- the fact that they're buying these tools, obviously, secures their supply chain, but it also moves the risk away from the manufacturer to the companies developing the products. And that's really an important part of the SkyWater model.

Our customers are investing in these tools. That's showing that they're committed to the tools and the products that will be developed on those tools. And as a result of that, we're able to bring in new capital equipment without having to fund it and also not having to depreciate it, as Steve talked about, once it actually goes into production. So it's a different model. It's one where we pushed the burden of investment, of equipment as well as the R&D engineering that goes on to prepare a given technology to go to market, we push that on the product development companies because they're the ones that are

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essentially trying to get something new and differentiated to the market. We work with them to provide that environment, but they have to absorb that risk of funding that capability. And that really is the difference between, say, us and a traditional foundry.

Nicolas Emilio Doyle
Needham & Company, LLC, Research Division

Can I just follow up on that? I see the benefit from the SkyWater perspective. I guess I'm more curious on what customers are seeing, where they're stepping up their investment. I guess it goes back to the value of working with you guys and understanding the different steps and getting some IP and how to develop their own chip. Is that the answer?

Thomas J. Sonderman
CEO & Director

Yes. It allows them to not only customize their product for our processes as opposed to having a standard process. But the other thing to keep in mind is we are in a very weak macro environment, so tool sales that maybe were committed as we entered 2023 have now been released. And we have certain customers that want to move faster, and that's allowing us to go secure equipment to put in our fab at a faster pace than maybe we thought as we entered the year. And this is all because customers want to secure capacity. And the difference is, instead of a customer coming to me and saying, "Hey, I want you to go buy a tool because I need to be prepared to ramp," we say, "No, you're going to buy that tool, and we're going to work with you to develop a customized process, and then you will have the secure supply on the other side." So that's really what we mean by CapEx-light. We don't invest our dollars in the tool. We expect our customers to do it. And as Steve alluded to, we're talking about 80% of the investment for the next tranche of tools will be coming from our customers as investments.

Operator

We'll move next to Richard Shannon at Craig-Hallum Capital.

Richard Cutts Shannon
Craig-Hallum Capital Group LLC, Research Division

I missed part of the call, I'm bouncing between a few calls here going on, so if I'm repeating stuff on the call, my apologies here. But I did get a sense of some sizable tool sales coming up here in the next number of quarters. Maybe if you could just help us understand the scope of the amount here. As I look back in your history here, like in 2021, you did like $19 million tool sales, one big quarter in there. How would you scale the next year or 2024 or however else you want to look at it relative to that year? And then kind of the follow-on to that question is, how do we look at ATS sales, excluding tool sales, going forward in the next few quarters? Is that something you can see flat to sequential growth? Or could we see some lumpiness in that pattern?

Steve Manko
Chief Financial Officer

Richard, this is Steve. I'll take the first part on the tool question, then I'll hand it over to Tom for the ATS. Like we talked about in the call today, we saw some tool revenue through in this quarter, which we told was very possible. We see additional tool revenue coming through in Q4, which we said it would be up to the $10 million. Now we still have a forecast where we would expect a certain level of tool revenue in Q1 of 2024. I don't expect it to be as high as the $10 million that we expect in Q4, but we still do see some sizable tool revenues coming in the first quarter. From there, that's about the best we have on the visibility.

Now what I'll say is we do have potential for 2024 to have more tool revenue in 2024 than we ever had before. So the largest tool revenue year was 2021 previously. We do have opportunity for larger tool revenue in 2024 than even of what we saw in 2021. We don't have perfect clarity on that. We wanted to give the information that we did have. I want to expect, in the third, fourth and first quarter of next year, as we get more clarity, we'll definitely share that with the market.

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Thomas J. Sonderman
CEO & Director

Yes. As it relates to ATS, again, we see solid growth going into next year. We're continuing to drive efficiencies. As we talked in the past, Richard, our goal is to extract more ATS activities out of our total activities bucket, and we're doing that. That's where a lot of these efficiencies gains are coming from. And at the same time we recognize that we have been growing very fast over the last 12-plus months. And it's important to realize, these are development programs. And so programs that are in development move at different stages based on where they are in our funnel. And so we're remaining, we'll call it, conservative but optimistic that the growth that we have been seeing in ATS can continue. And we believe that, that growth, coupled with the investment our customers are making in tools, are going to allow us to achieve above-industry growth as we get into '24 as we've demonstrated this past year with again above-industry growth.

Richard Cutts Shannon
Craig-Hallum Capital Group LLC, Research Division

Okay. That's fair enough. Maybe just a quick follow-on on this general topic here. What kind of time frame for return on the investment in these tool sales do your customers expect or is kind of implicit in their program progress?

Thomas J. Sonderman
CEO & Director

Yes. So as you kind of started out your question, you were referring to tools that came in, in '21, the $19 million. So think of a lot of the gains we're seeing now are resulting from the tools that were coming in, in '21. We had relatively low amounts in 2022. And then this year, it's beginning to pick up as we exit '23. So the tools come in. Obviously, they get installed, they get qualified, and then they start being used for development and ultimately prepared to go into production.

So think of it as a tool installed in '24 will begin to provide benefit in '25 and beyond. We have gotten very efficient with this process. And I think part of what we're doing is installing new tools to enable capabilities, and we have a very strong development team. And a lot of the work that we've talked about in the past of integrating ATS and Wafer Services holistically within a fab gives us great confidence that bringing these tools in next year will prepare us for the ramps that we're expecting in '25 and beyond. So tool investments in '24 should begin to pay dividends in '25.

Richard Cutts Shannon
Craig-Hallum Capital Group LLC, Research Division

Just kind of thinking about your profile of revenues here, and I'm probably interested mostly in ATS, but if you want to talk about on the whole business excluding tool sales. But I think about your kind of your revenues in 2 buckets, your government and A&D programs versus commercial on the other side, I think from your comments today and past calls that the government and A&D side has been particularly strong. As you're looking forward to the next few quarters, how do you see that mix changing? Is it still going to be dominated in growth or mix going towards government A&D? Or is it going to be more balanced?

Thomas J. Sonderman
CEO & Director

Well, I think we've always talked about our long-term model is kind of 30% to 40% for A&D. Obviously, it's running much stronger than that. And we're taking advantage of that given where the industry is. It's become a great lever for us to use to not only bring in new capabilities but to address some of the softness in the commercial side of the business, and not just for us but for everyone. So I think that over time, getting it to that 40% level is the objective. But I think you're going to see it continue to run hot through next year. And of course, in '25, we do have our RadHard platform coming online, our Read Open IC, the focal plane array thermal imaging platforms. So these are initially tied to DoD programs.

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So we believe that our goal is to maintain healthy levels of revenue coming from that customer base while growing the commercial base so that in the end, you get to that kind of 60-40 split between commercial and A&D. But it will take a couple more years to get that balanced.

Richard Cutts Shannon
Craig-Hallum Capital Group LLC, Research Division

Okay. Fair enough. Appreciate that. And my last question, I'll jump on the line here. Just following up on the topic from last quarter, I think I had a lot of questions from investors regarding the consulting fees and what they're for. When do we start to see the benefit of that? And I think there were some comments you've made in the past, even today, about velocity through the fab as well as efficiencies. So maybe if you can tell us, to date, whether we've seen any real benefits from that and over what time period we should expect to see that? And then maybe if you can just quantify the future consulting fees you're expecting to incur here.

Thomas J. Sonderman
CEO & Director

Yes. So I'll start and Steve can talk about the fees. So I think you are seeing the benefit of a lot of these transformation investments that we're making. And I said this on the last call that instead of having to invest in new equipment, we're investing in business transformation because we believe the opportunities we have are really dictated by us perfecting this unique model that we're putting in place. And so not only higher ATS activities than we've ever had, faster wafer velocity, better balance of our Wafer Services business to allow us to consistently meet customer commitments, these are all attributes that are coming together as a result of the transformation activities.

And then with John Sakamoto coming onboard as our COO, he and his team are really institutionalizing these processes so that we believe, as we get end of the second half of this coming year, as I said in my comments, that we will no longer need the third-party support. So in aggregate, you're looking around a 5-quarter program to prepare us for what we believe will be continued growth as this decade unfolds but also recognizing that we are doing something very unique in the industry. We believe it's proprietary, and we want to take the softness in the industry at a macro level and use it as an opportunity to prepare for the upswing that we all know is coming and do it in a way where we can scale effectively and efficiently as we continue to grow this business model that we put in place.

Steve, do you want to add?

Steve Manko
Chief Financial Officer

Yes. And Richard, you may have missed this in the opening remarks of the call, but Tom mentioned the program could go through the first half of 2024. So with that, I would expect a similar level of fees in the fourth quarter of this year as what we saw in the third quarter. I would then expect those fees to start tapering off as soon as the first quarter of 2024.

Operator

[Operator Instructions] And at this time, we have no further questions in the queue. I would like to turn the conference over to Thomas Sonderman for closing remarks.

Thomas J. Sonderman
CEO & Director

Thank you, operator. I want to close today's call by conveying the strong confidence all of us at SkyWater have in our ability to execute successfully towards our long-term growth and profitability objectives. Our amazing employees have now delivered consistent execution for several quarters. We intend to continue to build your confidence in our ability to execute on our future growth and profitability objectives as well.

We look forward to talking to you again on our Q4 call in February. And with that, I'll conclude today's earnings call. Thank you very much.

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Operator
And again, that does conclude today's conference call. Thank you for your participation. You may now disconnect.

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