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Transcript of Issuer Direct
Third Quarter 2018 Earnings Call
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Participants
Brian Balbirnie – Chief Executive Officer
Steve Knerr – Chief Financial Officer

Analysts
Mike Grondahl – Northland Capital Markets

Presentation

Operator
Ladies and gentlemen, thank you for standing by, and welcome to the Issuer Direct Corporation third quarter 2018 Earnings Conference Call. As a reminder, today's call is being broadcast live via Investor Network, a link of which can be found in today's earnings release. You can also view the full text of the Companies earnings release on their website in the investor relations section.

Today's call will be conducted by the Company's Chief Executive Officer, Brian Balbirnie and its Chief Financial Officer, Steve Knerr, I'll now turn the call over to Mr. Steve Knerr.

Steve Knerr – Chief Financial Officer
Thank you, and good afternoon everyone. Brian and I would like to thank you for taking the time to participate in our third quarter 2018 earnings call today. Before we begin, I need to read the following Safe Harbor statement. Statements or comments made on this conference call may be forward-looking statements that include financial projections or other statements of the company's plans, objectives, expectations or intentions. These matters involve certain risks and uncertainties. Our actual results may differ significantly from those projected or suggested in any forward-looking statement due to a variety of factors, which are discussed in detail in our recent SEC filings.

Further, we will discuss both GAAP and non-GAAP financial information on this call. We believe the presentation of non-GAAP information provides you with useful supplementary data concerning the company's ongoing operations and is an appropriate way for you to evaluate the company's performance. Non-GAAP results are, however, provided for informational purposes only. Please refer to the press release and related tables for GAAP information and a reconciliation of GAAP to non-GAAP information. We also posted to our website, in our Investors relations tab, a description as well as reconciliation of GAAP measures to which we will refer on this call.

With that complete, I'll begin by going over our results for the quarter and then turn it over to Brian who will provide his operational review and outlook, followed by a Q&A session.

The third quarter was another productive and progressive quarter for Issuer Direct as we finalized the acquisition of FSCwire in July, completed a secondary public offering in August and continued to make enhancements to Platform ID, resulting in the release of our conference management module last week.

Focusing on the results for the quarter, total revenue increased 11%, or $324,000, to $3,255,000 for the third quarter of 2018, as compared to $2,931,000 for the same period of the prior year. Revenue for the nine months ended September 30, 2018 increased 15%, or $1,355,000, to $10,584,000, as compared to $9,229,000 for the same period of the prior year. Revenue from customers obtained from our acquisitions of Interwest Transfer Company and FSCwire, totaled $526,000 and $1,325,000 for the three and nine months ended September 30, 2018, of which $46,000 and $142,000 came from additional subscriptions to Platform ID or services cross sold to these customers.

Platform and Technology revenue increased $309,000, or 17%, to $2,085,000 for the third quarter of 2018 and increased $1,077,000, or 20%, to $6,363,000 for the nine months ended September 30, 2018. Platform and Technology revenue increased to 64% of our total revenue for the third quarter of 2018 compared to 61% for the third quarter of 2017. The increase in revenue for the quarter is primarily the result of additional licenses of Platform ID, as we added an additional 33 subscriptions of Platform ID with an annual contract value of $343,000, bringing our total to 89 net new subscriptions for the year with an annual contract value of $907,000. We also achieved growth in Accesswire revenue, primarily due to the addition of customers acquired in the FSCwire acquisition as well as revenue from our transfer agent module due to the addition of customers acquired in the Interwest acquisition. These increases were offset by the continued decline in revenue of our shareholder outreach offering that are specifically tied to our annual report distribution services.

Services revenue of $1,170,000 for the third quarter of 2018 increased 1%, or $15,000 compared to the third quarter of 2017 and increased $278,000, or 7%, to $4,221,000 during the nine months ended September 30, 2018, compared to the same period of the prior year. The increases are primarily the result of an increase in transfer agent services, due in combination to the addition of Interwest customers as well as an increase in activity of our longer-term Issuer Direct transfer agent customers. The increase in transfer agent revenue was partially offset by the continued decline of revenue from our legacy annual report service, as well as, decline in revenue from our compliance services as we continue to face pricing pressure in the market or customers begin to take advantage of our platform offerings.

It is important to note, when comparing results to previously filed reports, $157,000 and $550,000 of revenue during the three and nine months ended September 30, 2017, respectively, which were previously reported as Services revenue, were reclassified to Platform and Technology revenue. This was the result of the adoption of a new accounting pronouncement as of January 1, 2018, that required us to separate the revenue in bundled contracts for our ARS, or shareholder outreach offering, which include both electronic and physical hardcopy delivery of our customer's annual reports. The reclassified amounts represent the allocation of contract value of electronic delivery of the annual reports. All results have been appropriately adjusted for comparison purposes.

Switching to gross margin, our overall gross margin percentage was 70% and 71% for the three and nine months ended September 30, 2018, respectively, compared to 72% and 73% for the same periods of the prior year. It is noted there was an increase in cost of revenues of $117,000 and $373,000 for the three and nine months ended September 30, 2018, respectively due to an in amortization of the capitalized software placed in service in 2017. Platform and Technology gross margin percentage was 77% and 79% for the three and nine months ended September 30, 2018, respectively, compared to 83% and 84% for the same periods of 2017. Again, there was an increase in cost of revenue due to the increase in amortization I noted earlier, as well as additional costs as we continue to expand our news distribution capabilities. Gross margin percentage from our Services revenue stream was 57% and 60% for the three and nine months ended September 30, 2018, respectively, compared to 55% and 58% for the same periods of the prior year.

Moving down the income statement, operating expenses increased $526,000, or 32%, and $1,358,000, or 26%, during the three and nine months ended September 30, 2018, as we continue to invest in our business for top-line growth. A majority of the increase is in Product development which has more than doubled over the prior year due to less capitalization and continued development of new products associated with Platform ID, as well as, modules placed into production during 2017. In a few minutes, Brian will talk further about our new conference management module and soon to come insight and analytics platform. General and administrative expenses increased 24% for the quarter and 15% YTD as a result of an increase in stock compensation, as well as, additional G&A expenses associated with both Interwest and FSCwire, some of which we hope to stream-line as integration has now been completed. Sales and marketing expenses increased 18% for both the quarter and YTD due to an increase in our sales and marketing teams and costs associated with expanding our distribution capabilities. Lastly, amortization expense increased due to additional amortization resulting from intangible assets acquired as part of both the Interwest and FSCwire acquisitions.

For tax purposes, we recognized income tax expense of $32,000 and $246,000 for the three and nine months ended September 30, 2018 as compared to $174,000 and $438,000 during the same periods of the prior year. Lower tax expense is the result of lower pre-tax income as well as a decrease in the statutory rate in 2018, offset by a benefit in 2017 related to the exercise of stock compensation.

For GAAP purposes, we recorded net income of $86,000, or $0.02 per diluted share, for the third quarter of 2018, as compared to net income of $308,000, or $0.10 per diluted share for the same period of 2017. For the nine-month period ended September 30, 2018, we recorded net income of $772,000, or $0.23 per diluted share, compared to net income of $1,126,000, or $0.37 per diluted share for the first nine months of 2017. The decrease in earnings per share was due in part to the additional shares outstanding as a result of our secondary offering that closed during the third quarter of 2018.

Looking at some Non-GAAP metrics, total EBITDA for the third quarter of 2018 was $473,000, or 15% of revenue, compared to $663,000, or 23% of revenue, during the same period of the prior year. On a YTD basis, EBITDA was $2,063,000, or 19% of revenue, compared to $2,093,000, or 23% of revenue, for the first nine months of 2017. Non-GAAP net income was $411,000, or $0.11 per diluted share for the third quarter of 2018 compared to $445,000 or $0.15 per diluted share for the third quarter of 2017 and $1,531,000, or $0.47 per diluted share for the nine months ended September 30, 2018, compared to $1,441,000 or $0.48 per diluted share during the same period of the prior year. Again, the decrease in non GAAP earnings per share despite similar, or in the case of the nine months ended September 30, 2018, an increase in Non GAAP net income was due in part to the additional shares outstanding as a result of our secondary offering that closed during the third quarter of 2018.

Changing to the cashflow statement, we continue to generate positive cash flows from operations as we generated an additional $564,000 during the third quarter of 2018 compared to $638,000 during the same period of the prior year, bringing total cashflow from operations to $2,153,000 for 2018 compared to $2,095,000 during the same period last year. Also, due to our focus on selling subscriptions of Platform ID, we've increased deferred revenue by 57% since year-end, bringing the total to $1,389,000.

As you may have seen in a recent press release, our Board of Directors has decided to discontinue the quarterly dividend in order to direct the funds on our balance sheet toward reinvestment in our business, specifically Platform id., our sales and marketing teams as well as acquiring complementary businesses, products, technologies and/or assets, which we are committed to focus on in the upcoming quarters.
With that, I will turn it over to Brian who will now talk further about our new products and outlook for the remainder of 2018 and beyond.

Brian Balbirnie

Thank you, Steve, and thanks to everyone for joining us today to discuss our third quarter 2018 results. As Steve just highlighted in his prepared remarks, our third quarter. Saw total revenues grow by 11% compared to Q3 last year. Sequentially, total revenues decreased 14% from Q2 this year. Platform and Technology growth continued, and on a year over year basis revenues were up 17% for the third quarter. As a percentage of total revenues, our platform business continued to expand, from 58% in Q1 this year and 59% in Q2 to 64% in the third quarter

As our subscription business continues to expand, so does our deferred revenues numbers and backlog. With one quarter remaining, our total of net new subscriptions for the first nine months totaled 89 with an annual contract value of $907,000.

More specifically we are seeing both new and existing customers subscribing to platform id. in Q1 for example of the 29 new subscriptions, 19 came from current customers as a result of cross selling from the Interwest. During Q2, we had 10 current customer or 37% subscribe to platform options and in Q3 of the 33 new annual subscriptions 12 or 36% of those were from current customers. We are laser focused on continuing to increase new subscriptions over the previous period, with a goal of ending the year with a min of 120. ARPU for the third quarter remained consistent with the first half of the year, averaging just over $10K per customer per year from these subscriptions.

As a result, deferred revenue for the third quarter grew 9% sequentially and 57% from end of last year, bringing the total to $1,389,000 to be recognized within the next year.
In summary, we saw sequential net new customers in both our Platform and services business. We had 2,143

Platform and Technology customers during Q3 2018, compared to 1,996 in Q2 and 1,582 in Q3 last year. This represents or 35% on a year over year basis and 7% on a sequential basis. The sequential growth is primarily due in part to our FSC acquisition in July of this year, the customers acquired in that transactions were approximately 300, of which 174 did work with us during the period.

We also had 679 Service customers during Q3 2018, compared to 567 in Q2 this year and 493 in Q3 last year, that 38% year over year gain came primarily from customers acquired as part of the Interwest acquisition in Q4 of last year.

Growth in pipeline is vital for us, and making the investments in our sales and marketing teams is also fundamental for this to happen. Reinvesting short term profits to help fuel long term sustained growth and market share is what were focused on, this is evident in the dividend being suspended and as we have messaged for several quarters something we feel is the right time for us to do.

Although our Platform business has expanded and customer counts continue to grow, we believe we could have done a better job this quarter in top line revenues, more specifically within our shareholder communications and newswire business, where we did not see the growth we expected. I think this holds true to part of our services business as well, being down due to pricing pressure. As we continue to transition our business to more of a subscription based engagement, we still are party to services types of engagements that are harder to predict and in some cases out of our control in as far as timing.

As part of that growth and commitment to invest in our business was the FSC wire transaction previously announced on July 3. We are happy to report the integration is has been completed. Our editorial teams are now located both in North Carolina and Calgary Canada, giving us 10 full-time editors, backed up by an entire compliance and operations team. As we said previously when we announced the transaction we were not focused on any cross selling until integration was completed and customers were well situated in our platform. We are now gearing up for this to occur late Q4 and into early 2019. Like Interwest success, we believe we will have similar success here with our FSC customers that are both TSX/CSE and OTC listed. Our communications subscription will be the biggest value driver for these customers in the long term.

The last couple of acquisitions of Interwest and FSCwire are the latest demonstrations of a solid track-record of integrating accretive acquisitions. We continue to believe our industry will further consolidate. As such, we are focused on additional accretive opportunities in the market. This is part of the reason why we raised the additional capital which I would like to touch on briefly.

During the third quarter we completed a secondary offering of 927,418 common shares for net proceeds of just over $13M after commissions and offering expenses. For those of you that know us, this was the first offering we have done in our 11 year public history. This offering now bolsters our balance sheet to almost $20M in cash and further invest in our business. Something we have been focused on over the last couple months and will continue to be here in the short term.

The end of the quarter marked the completion of our investor conference software module for Platform id. This module add-on has further expanded our platform subscription business to the Professional Conference Organizers (PCO). So in the coming quarters our platform business will become more refined and expanded, having specific platforms for Public Companies, Private Companies, PCO's and Investors. These four different platforms will make up our entire platform id subscription business.

More specifically, this new PCO subscription module allows conference organizers to market their events, schedule and manage the millions of 1-1 meetings held each year, at the same time adding the power of our webcasting technology and newswire distribution to an entire eco-system.

Since this product just was released in October of this year, we have seen a couple of deals already sign, but revenues will be minimal in fiscal 2018, as these conferences are for next year. We anticipate that in 2019 this module will be a driving force for expanding our Platform id. products to a broader audience than today. In some ways this product has opened up an adjacency to our current platform business. These types of innovations are critical to getting our platform fully commercialized.

Six months ago we talked about these planned modules and what they would do for us as a company in the future –

The next planned expansion is our insight and analytics module, this in limited roll out is planned for the end of this quarter and broadly available to our entire customer base as well as new subscribers in Q1 2019.
Insights are generated by investors and shareholders, as they are engaging with earnings events, IR website content from our network, investor conferences, alerts and requests from investor registrations and subscriptions. Having this data in one real-time platform will allow our customers to segment their investors in several different ways, so as to maximize and target their messaging more efficiently. This module gives us, expanded ARPU for our current customers and higher arpu's from new subscribers in the future.

These two new platform add-ons are investments in our business we have had planned for over a year. By investing in our technology we still have been able to keep R&D at about 10% of revenues for the quarter, something we believe will continue as we bring to market these and other platform advancements.

Absent of our core technology, we have also made investments and improvements in other parts of our organization. We recently promoted an 11 year veteran of the company to Director of Operations, and expanded our sales and marketing team by 3 additional headcount, bringing Sales & Marketing totals to 22 for the end of the quarter. Beginning this month we are happy to report that Dick Bromley has joined our team as the EVP of sales. Dick bring 17 years of sales management and industry leadership to Issuer Direct, with deep experience in communications and newswire. We are excited to have him and look forward to expanding our team as a result of his presense. Mr. James Michael whom previously served the company for 12 year in various capacities and most recently as VP of Sales, will move to VP of Business Development – focused on our exchange partners, and our new PCO business we recently announced.

I'd like to spend a minute on how were refining and improving our offerings for 2019 and beyond. With these planned upgrades to our platform id. you will see us begin to offer subscriptions to public, private, PCO's and investors. These visible subscriptions will be purchasable right from our platform and designed based on each of the four segments just mentioned. By doing this, we feel we can maximize our subscription modules best for our customers. I also think this is vital to be able to further provide the necessary metrics of our business to our shareholders. Costs to acquire these types of customers are drastically different, and conversely the spends from public to private are also different. 2 years ago we began segmenting customers whom purchased platforms and services, then this past year we have further detailed arpu spends on new platform id subscriptions, but this is not telling the full story, there are even more customers renewing individual modules each year, this is why it is necessary to further segment our customers spends by the public, private, pco and investors. In closing, although were behind in our internal goals, top line revenues are 15% higher for the first nine months of the year compared to last year and customer growth has continued during the same period. Fact is, even though we have messaged yoy growth, we expect a lot from ourselves and continue to work hard to push top line as we continue to invest in our business, which has had a short term effect on operating results.

We are encouraged by our continued client expansion, specifically the customers that are purchasing our platform, and the investments were making in the business, both in our new product development and our employee base, which will put us in a position to further grow and scale the business.

This concludes our prepared remarks, operator, can we please begin the question and answer session.

Operator
Thank you. We will now be conducting a question and answer session. [Operator instructions]. Our first question comes from the line of Mike Grondahl with Northland Capital Markets. Please proceed with your question.

Q: Thank you, guys. The first question is just I know you were working on some distribution wins with Accesswire and expanding that product; how are those distribution wins going and what's the timeline there?

Brian Balbirnie – Chief Executive Officer
Thanks for the question. We have got three major broker terminal distributions, as we've talked about in previous periods, those being predominantly the TD Ameritrade, the Schwab's, and the Bank of America/Merrill Lynch systems. Our feeds are live inside of their networks as of the end of Q3 and completing testing on their end for release by the end of this quarter or the first quarter of fiscal 2019.

We're optimistic that we'll see that happen. We're confident based on what we've done in the previous quarters with expansion to groups like the Bloomberg system more broadly in Canada and the United States, as well as E-Trade, so that will round out our broker terminal distribution.

Q: Brian, let me paraphrase, you're testing getting Accesswire to AMTD, Schwab, and Bank of America/Merrill Lynch, and you hope to have that rolled out at year-end or 1Q formally. Did I hear you right?

Brian Balbirnie – Chief Executive Officer
That's correct, yes.

Q: And then secondly, could you talk a little bit about your acquisition pipeline and how busy you are looking for acquisitions today and if you think you can close anything by year-end or the first quarter?

Brian Balbirnie – Chief Executive Officer
In reflection of the quarter, it's interesting you ask that question. Steve and I looked at some of the progress in the business, the investment that we're making, the acquisition announcement of FSC, the integration, completing the offering, launching a new product, expanding the team, absent of all that activity and still finding a way to get some year-over-year growth, although not maybe what we expected and wanted. But we still have been busy, exactly to your point, looking at opportunities, conducting preliminary due diligence, trying to find opportunities that fit our business that are very accretive to an adjacency and/or a current operation.

And we're really focused on our shareholder communications modules and components. If we think about the webcasting, the IR website businesses, the newswire business of course, and anything that enhances our analytics and insight opportunities for next year, those are the areas that we're looking at. I wish I could tell you that we've got something today that will close tomorrow. Obviously, it's something we can't talk about specifics, but we're optimistic that by the end of this year we're going to see some opportunities break loose for us that's going to further give us an opportunity to gain access to additional clients, to be able to be confident enough to walk in and sell them our platforms in the future.

So rest assured, we're hard at work on that. There's no doubt there.

Q: I'll maybe ask one more before jumping in the queue. In the press release, in the prepared remarks you noted you were disappointed a little bit in the September quarter revenue. Can you just be a little bit more specific? What area were you disappointed in? Where did that arise from?

Brian Balbirnie – Chief Executive Officer
As we said, we expect a lot. When we forecast and we look at our businesses from a year-over-year perspective and our client accounts and what we anticipate our [indiscernible] to be at our customers, our bigger growth drivers, I think everybody knows, is our shareholder communication segments, and it's heavily driven by our newswire business. There's a lot that's attributable to that. It's the distribution question you asked earlier, that plays a role in it. There's larger accounts that play a role in it that sometimes tend to do less work during certain periods that have variances on some of that.

Candidly, I think we expected more growth there. The folks that have examined our newswire business for the better part of the last four years now plus, since we've owned Accesswire, there's been tremendous year-over-year growth, and in most all cases great sequential growth too.

We've said as a company that's hard to sustain, right? As we continue to build distribution, we're trying to work ahead with anticipation of being able to continue to do that. Candidly, we just didn't get it. It just didn't happen for us in the quarter. We look back at the four-plus years and that shareholder communications business, is we've grown so fast sometimes there's going to be a period where you don't get what you thought out of those clients.

But that doesn't mean in reflection that the pipeline has slowed down. It doesn't mean that we're not seeing the opportunities in Q4 and next year. And we are seeing those. So we're optimistic that we're a good group of guys and gals that work hard and pick ourselves back up, and we'll get at it again. And I think we feel confident that we're going to be able to see that growth coming forward.

Q: Thank you.

Operator
There appear to be no further questions at this time. I'd like to turn the floor back over to Mr. Balbirnie for closing comments.

Brian Balbirnie – Chief Executive Officer
Thank you, operator. I'd like to thank everyone for taking the time to listen to Steve and I talk about our third quarter results today. If anybody has additional follow-up, we'd welcome an opportunity, as always, to speak with you again. I wish you all a great afternoon. Thank you.