Information Services(Q1 2019 Earnings)
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Corporate Speakers:
- Jonathan Hackshaw; Information Services Corporation; Director of IR & Capital Markets
- Jeff Stusek; Information Services Corporation; President & CEO
- Shawn Peters; Information Services Corporation; Executive VP & CFO

Participants:
- Stephanie Price; CIBC Capital Markets; Research Division, Director of Institutional Equity Research & Software and Business Services Research Analyst
- Steven Bain; GMP Securities L.P.; Research Division, Associate

PRESENTATION

Operator: Good day, ladies and gentlemen, and welcome to the ISC Q1 2019 Earnings Conference Call and Webcast.

(Operator Instructions)

As a reminder, this conference call is being recorded. At this time, I'd like to turn the call over to your host, to Jonathan Hackshaw, Director of Investor Relations and Capital Markets. Please go ahead, sir.

Jonathan Hackshaw: Thank you, Dylan, and good morning, ladies and gentlemen. Welcome to ISC's conference call for the quarter ended March 31, 2019.

With me today are Jeff Stusek, President and CEO, and Shawn Peters, Executive Vice President and Chief Financial Officer. Jeff will provide some opening comments, followed by a review of operational and financial results by Shawn. Jeff will then make some closing remarks before we open up the call for the question-and-answer session.

Before we begin, we would like to remind everyone that we will only be summarizing results today. ISC's unaudited condensed consolidated interim financial statements and management's discussion and analysis for the period ended March 31, 2019, have been filed on SEDAR and are also available in the Investor Relations section on our website under Financial Reports. We encourage you to review those reports in their entirety.

I would also like to remind you that any statements made today that are not historical facts are considered to be forward-looking statements within the meaning of applicable securities laws.

These statements may involve a number of risks and uncertainties that are described in detail in the company's SEDAR filings, in particular, in ISC's annual information form dated March 20, 2019, and ISC's unaudited, condensed, consolidated financial statements and notes and management's discussion and analysis for the 3 months ended March 31, 2019.

Those risks and uncertainties may cause actual results to differ materially from those stated. Today's comments are made as of today's date and will not be updated except as required under applicable securities legislation.

Today's conference call is being broadcast live over the Internet and will be archived for replay shortly after the call on the Investor Relations section of our website. With that, I'd now like to hand the call over to Jeff.

Jeff Stusek: Thank you, Jonathan, and good morning to everyone joining us for today's call. It's been a good start to 2019, and we performed as we expected to.

Consolidated revenue was up 6.5% year-over-year and we recognized revenue of $28.6 million for the quarter compared to $26.9 million in 2018.EBITDA was also up 2.1% year-over-year, coming in at $7.4 million for 2019 compared to $7.2 million in the prior period.

Our Registry Operations segment continues to be a strong free cash flow contributor, and I'm also really pleased with the year-over-year organic growth of our Services segment, both at the top and bottom lines.

The diversity of our revenue streams is offsetting the economic impact to Registry operations. During the quarter, we enhanced our Know-Your-Customer solutions in our Services line of business with ESC's acquisition of Securefact.

While not material financially in the quarter, it is the addition of value-add services like this, particularly in the KYC space, that are making us more competitive and able to offer our existing customers more of what they want.

The response from our customers to this news has and continues to be positive. With that, I'd now like to ask Shawn to summarize our financial and operating performance for the 3 months ended March 31, 2019.

Shawn Peters: Thank you, Jeff, and good morning, everyone. I'll provide you with some of the highlights of the first quarter on a consolidated basis and then provide some further commentary about each of our reporting segments and their performance for the reporting period.

Before I begin, I want to draw your attention to some changes in our reporting in the MD&A. Commencing this quarter, in addition to reporting revenue by segment, we introduced the reporting of expenses and EBITDA by segment to help provide a better understanding of each segment's performance.

With that in mind, on a consolidated basis, revenue for the 3 months ended March 31, 2019 was $28.6 million, an increase of $1.7 million or 6.5% compared to the first quarter of 2018 due to strong organic growth in our Services segment, offsetting the lower revenue in our Registry operations.

Net income for the period was $3 million or $0.17 per basic and per diluted share, an increase of $0.4 million compared to the first quarter of 2018.

EBITDA for the quarter was $7.4 million compared to $7.2 million in the same quarter last year, an increase of 2.1%, again due to increases in our Services segment partially offset by lower EBITDA in our Technology Solutions segment.

The EBITDA margin for the first quarter of 2019 was 25.7% compared to 26.8% in the same quarter in 2018, down as expected as a result of the continued growth in our lower-margin collateral management business.

Excluding stock-based compensation expense or income, stock option expense, transactional gains or losses on assets and acquisition and integration costs, adjusted EBITDA was $7.8 million for the quarter compared to $7.5 million in the same quarter last year, with an adjusted EBITDA margin of 27.3% for the quarter compared to 28% for the first quarter in 2018.

For the 3 months ended March 31, 2019, our consolidated expenses were $23.8 million, an increase of $1.3 million compared to the same period last year, due to increased cost of goods sold for the new Services revenue and increased staffing in Services and Technology Solutions. These increases were partially offset by decreased staffing in Registry Operations and decreased depreciation in Services.

Free cash flow for the 3 months ended March 31, 2019, was $5.3 million, a decrease of $1.1 million compared to the first quarter of 2018 due to higher income taxes and additions of intangible assets.

On February 19, 2019, we announced that our wholly-owned subsidiary, ESE Corporate Services Limited, acquired substantially all of the assets used in the business of Securefact Transaction Services, Inc. for $6.8 million by way of an asset purchase agreement.

Turning to our specific segments. Revenue for Registry operations was $16.3 million for the 3 months ended March 31, 2019, a decline of $0.6 million or 3.8% compared to the first quarter in 2018 due to decreased revenue from the Saskatchewan Land Registry. Most of the revenue generated from the Land Registry is from the Land Titles Registry and is derived from value-based fees.

Land Titles Registry revenue for the quarter ended March 31, 2019, was $10.2 million, a decline of $0.7 million or 6.1% compared to the same period in 2018 due to lower transaction volumes partially offset by increased high-value transactions.

Revenue from high-value transactions was $1.3 million for the first quarter of 2019, up from $1.2 million in the same period in 2018.

As a reminder, each high-value registration generates revenue of $10,000 or more. Overall transaction volumes for the Land Registry decreased by 9.1% for the first quarter of 2019 compared to the same period last year.

The volume of mortgage registrations and title searches declined by 11.7% and 8.5%, respectively, compared to the same quarter in 2018, while regular land transfers volumes increased by 2.8% compared to the first quarter of 2018.

Volumes appeared to continue to be impacted by federal policy changes, such as the mortgage stress test and increases in interest rates which have contributed to softness in the Saskatchewan real estate market.

The Saskatchewan Personal Property Registry and Saskatchewan Corporate Registry both performed well in the first quarter and were generally stable compared to last year.

While smaller in size compared to the Land Registry, these two registries continue to make solid contributions to our top line as well as our bottom line given that they are both highly automated. Nearly 100% and over 80% of all transactions for the Personal Property Registry and Corporate Registry, respectively, are completed online.

Expenses for Registry Operations were $9.5 million for the quarter, a decrease of $0.6 million from the same period in 2018 due to lower staffing costs and a decrease in Corporate and other allocated costs and related party expenses.

Registry Operations EBITDA for the first quarter of 2019 was $6.8 million, flat compared to the same period last year as the overall decrease in costs offset the lower revenue.

Turning to our Services segment. Revenue for Services was $11 million for the first 3 months ended March 31, 2019, an increase of $2.2 million or 24.3% compared to the first quarter of 2018.

This year-over-year increase was a result of a combination of organic growth within existing customers and the ramping up of new customers, particularly in the KYC, due diligence and collateral security registration space.

Financial Support Services revenue was $8.7 million, up $2.1 million or 31.8% compared to $6.6 million for the same period of 2018. The increase represents the strong growth in our collateral management business combined with additional expansion into KYC with our acquisition of Securefact in February of 2019.

We also saw a consistent year-over-year contribution from our Legal Support Services, with revenue in the first quarter of 2019 remaining fairly flat at $2.3 million compared to the first quarter in 2018.

For the quarter ended March 31, 2019, Services expenses were $9.6 million, an increase of $1.9 million compared to $7.7 million for the same period in 2018.

This was due to increased staffing levels required to support the growing business as well as addition -- the additional staff related to our Securefact acquisition, increased cost of goods sold consistent with the increase in the related collateral management revenue in the quarter and an offset from the decline in depreciation and amortization costs compared to the same period in 2018 due to the full amortization of certain assets.

EBITDA for our Services segment was $1.5 million for the 3 months ended March 31, 2019, an increase of $0.4 million compared to $1.1 million for the same period last year, up at a rate consistent with the margin profile for our collateral management business.

Finally, in our third line of business. Technology Solutions revenue was $4.9 million for the 3 months ended March 31, 2019, flat compared to the same period in 2018.

There were limited milestones scheduled during the first quarter, so while related party revenue will stay relatively flat or trend slightly lower, the revenue from external parties will continue to grow as the company achieves overall performance-related milestones for customers whose implementations are scheduled throughout 2019. In addition, projects will begin to move into the steady state or application maintenance after implementation.

Technology Solution expenses were $4.5 million for the quarter, an increase of $0.4 million compared to $4.1 million for the same period in 2018 as result of increased wages and salaries as we increased employee levels to service the contracted and growing business.

EBITDA for our Technology Solutions segment for the 3 months ended March 31, 2019, therefore, decreased by $0.4 million from the first quarter of 2018.

Capital expenditures for the 3 months ended March 31, 2019, were $0.9 million compared to $0.4 million for the same period in 2018. The increase was due to new enhancements to the system supporting our corporate area and system development work in our Services segment.

With respect our debt. As at March 31, 2019, the company had $19.5 million of total debt outstanding compared to $20 million at December 21, 2018. Further details on our debt and our credit facilities can be found in our MD&A financial statements.

From a liquidity perspective, as at March 31, 2019, we held $17.6 million in cash compared to $28.7 million as of December 31, 2018.

Working capital at the end of the quarter was $7.1 million compared to $13.2 million at December 31, 2018. The decrease in both cash and working capital is primarily the result of our acquisition of Securefact in February 2019.

Consolidated free cash flow for the 3 months ended March 31, 2019, was $5.3 million compared to $6.4 million for the same period in 2018. The decrease in the quarter was due to higher income taxes and the addition of intangible assets.

Finally, we also announced yesterday that our Board of Directors approved our quarterly cash dividend of $0.20 per share. The dividend will be payable on or before July 15, 2019, to shareholders of record as of June 30, 2019. I'll now turn the call back over to Jeff for some concluding remarks.

Jeff Stusek: Thanks, Shawn. Before we move to the Q&A session, I'd like to share a few thoughts with you. As I said at the start of the call, we've had a good start to the first quarter.

While our Registry Operations segment continues to feel the effects of the Saskatchewan economy, it again delivered good results, generating strong free cash flow and remaining well positioned to be a beneficiary of any upswing should the Saskatchewan economy begin trending upward again.

And while much of the focus on our business is directed at Registry Operations in Saskatchewan, the performance of our Services business is beginning to shift that.

The growth in our Services line is helping to offset economic effects in Saskatchewan, and Services now accounts for nearly 40% of consolidated revenue compared to only 16% in the first quarter of 2018, mainly through new customer acquisition.

We expect the primary driver of our growth to continue to come from Services, largely through the continued growth of our customer base and our collateral management services product line. We also expect to continue to compete effectively in the KYC space while increasing our overall market share over the course of 2019.

Our Technology Solutions segment continues to focus on executing on current implementations of the new contracts, and we expect to realize the additional revenue from this segment in 2019 and profitability in the short term.

While we'll always look to grow our Services and Technology Solutions businesses organically, we will continue to look for acquisition opportunities that will add value to our current offering and help our customers.

As always, we will only invest capital in the right opportunity at the right price. With that, I will now hand the call back over to Jonathan.

Jonathan Hackshaw: Thanks, Jeff. Dylan, we'd now like to begin the question-and-answer session, please.

QUESTIONS AND ANSWERS

Operator: (Operator Instructions)

Our first question comes from Stephanie Price from CIBC.

Stephanie Price: I was hoping you could talk a bit more about the growth you saw in the financial services vertical this quarter and how we should kind of think about the outlook for that division for the remainder of the year.

Shawn Peters: Stephanie, it's Shawn. Thanks for the question. Yes. That's one of the areas that we talked about where we expect to continue to see growth.

That's primarily through the combination of organic growth through existing customers but also winning new mandates from both existing and new customers. So that's the area that we expect to continue to grow over the course of 2019, and I think this quarter would be pretty typical for what we expect to see for growth.

Stephanie Price: Great. And then on the Technology division, both revenue and margins there came in a bit lower than we were expecting. Can you kind of walk through how we should think about kind of the cadence of these implementations ramping up?

Shawn Peters: Yes. The challenge with that line of business is the revenue is based on achieving the milestones, and so the milestones aren't equally scattered throughout the quarters. And so it's a little bit hard. I appreciate the question. It's little bit hard to predict that.

But as -- in Jeff's concluding comments there, we expect that over the course of 2019, we'll achieve the rest of those implementations and recognize that revenue on the books and achieve profitability in the short term. So that's little bit of a vague answer, I realize, but it's hard to predict just given where the milestones land in any particular quarter.

Stephanie Price: Okay. Great. And then just one final me -- one from me on Securefact. Could you give us a bit of a background on that acquisition and how you see it fitting in with the rest of the business?

Shawn Peters: Sure. So that's an acquisition that's largely in the KYC space, which is an area that we're continuing to expand on through our Services offerings.

It fits in really nice because it's complementary to the products that we already offer to our customers. It's just one more in a bucket of items that our customers are looking for from a service provider.

So it was a pretty small acquisition but a good acquisition of a known technology in the market. And as we talked about in the comments, we've gotten really positive response from our customers on that. So we're pretty excited about that.

Operator: (Operator Instructions)

I show our next question comes from Steven Bain from GMP Securities.

Steven Bain: Just a question on the Securefact revenue contribution during the quarter. Are you able to give us an idea of that? And just also an idea of the run rate for kind of going forward on an annual basis for Securefact.

Shawn Peters: Yes. Steven, it's Shawn. Thanks for the question. So the contribution during the quarter was pretty minimal. The product or the company was just finishing up some of the products and so their level -- one of the attractive things to us in the acquisition was an ability to partner it with our products and really ramp up the sales and amplify their sales effort.

So the amount in the quarter is very, very small, it was a couple of hundred thousand dollars on a revenue basis. Going forward, we haven't really disclosed the run rate on that, but it would -- we'll certainly be taking that into account when we issue guidance or confirm our guidance.

Steven Bain: Okay. And just with the IFRS 16 changes, are you able to quantify at all what the impact to EBITDA was during the quarter, Q1?

Shawn Peters: Yes. Yes, pretty -- it's pretty small. You can see that in our disclosure. I think it's about 18,000 on a net income basis. So I don't have the EBITDA number off the top of my head, but very, very small for IFRS.

Operator: I show no further questions in the queue at this time. I'd like to turn the call over to Jonathan Hackshaw, Director of Investor Relations and Capital Markets for closing remarks.

Jonathan Hackshaw: Thank you, Dylan. With no further questions, I'd like to thank everyone again for joining us on today's call and for your questions, and we look forward to speaking with you again when we report our next quarter. Have a good day.

Operator: Thank you, ladies and gentlemen, for attending today's conference. This concludes the program. You may all disconnect. Good day.