

Usio, Inc.

Second Quarter 2023 Financial Results  
Conference Call

Monday, August 14, 2023, 4:30 PM Eastern

**CORPORATE PARTICIPANTS**

**Louis Hoch** - *Chairman and Chief Executive Officer*

**Tom Jewell** - *Senior Vice President and Chief Financial Officer*

**Greg Carter** - *Executive Vice President of Payment Acceptance*

**Houston Frost** - *Senior Vice President of Prepaid Services*

**Paul Manley** - *Senior Vice President, Investor Relations*

## **PRESENTATION**

### **Operator**

Good afternoon, everyone, and welcome to the Usio Earnings Conference Call for the Second Quarter of Fiscal 2023. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the "\*" key followed by "0." After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press "\*" then "1" on a touchtone phone, to withdraw your question, please press "\*" then "2." All participants on this call are advised that the audio of the conference call is being broadcast live over the internet and is also being recorded for playback purposes. A replay will be available shortly after the call through August 28, 2023.

I would now like to turn the conference over to Paul Manley, Senior Vice President, Investor Relations. Please go ahead.

### **Paul Manley**

Thank you, and thank you, everyone, for joining our call today. Welcome to Usio's second quarter fiscal 2023 conference call. The earnings release, which we issued today after the market closed, is available on our website at usio.com under the investor relations tab.

On this call today are Louis Hoch, our Chairman and CEO, Tom Jewell, Senior Vice President and Chief Financial Officer, Greg Carter, Executive Vice President of Payment Acceptance, and Houston Frost, Senior Vice President of Prepaid Services.

Let me remind our listeners that certain statements made during the call today constitute forward-looking statements made pursuant to the safe harbor provisions of the Private Securities and Litigation Act of 1995, as amended. Such forward-looking statements are subject to both known and unknown risks and uncertainties that could cause actual results to differ materially from such statements. These risks and uncertainties are described in our earnings press release and in our filings with the SEC. The forward-looking statements made today are as of the date of this call, and we do not undertake any obligation to update these forward-looking statements.

During today's call we will refer to Non-GAAP Financial Measures, such as adjusted EBITDA. Our earnings release includes a reconciliation of adjusted EBITDA to GAAP operating income. Management will provide prepared remarks, then we'll have a question and answer session. So let me start with some highlights from this afternoon's release.

I am pleased to report another quarter of record results, with second quarter revenue up 31%, accelerating significantly from the 18% growth rate reported in the first quarter and our 12th consecutive quarter of revenue growth. And for the third consecutive quarter, we reported over \$1 million of positive adjusted EBITDA, which was once again up dramatically from the year ago quarter. These results solidly exceeded expectations from the analysts and have us well on our way to meeting our fiscal 2023 financial guidance. In addition, we continue to be in excellent financial condition, with cash up again this quarter, which we believe is more than sufficient to support our growth objectives for the year.

So, another record quarter along with strong bottom line results and positive cash flow. What you will further hear on this call from our team are the many opportunities in our pipeline that illustrate how our strategy is working and why we are extremely excited about the future here in Usio. Lastly, I would like to announce that Usio has initiated a comprehensive ESG process,

with the goal to issue our Inaugural ESG report sometime early next year, reporting on the progress that we will be making in this important area.

Now, I will turn the call over to Louis.

### **Louis Hoch**

Thank you, Paul, and welcome, everyone. I want to begin by reiterating Paul's key points, that not only was this a record quarter in terms of current financial performance, but it was also another quarter of significant progress in expanding our franchise and planting the seeds for even a better future performance. For those reasons, we today are reiterating our guidance for revenue growth in the 18% to 20% range this year.

Results once again reflect our diversified business strategy, diversified in the markets we serve and the payment channels that we offer. This quarter, results were led by performance at prepaid, where revenues were up 276%, and Output Solutions, which had another 20% growth quarter.

Prepaid continues to benefit from growth of the underlying business aided by a growing stream of residual revenues from expiring card programs. As Houston will discuss, we are bringing on numerous new accounts with both diverse needs and diverse end markets as our reputation and technology within these markets continue to grow. While, in this era of high tech, we are very proud of our advanced technology not only in prepaid, but across Usio, we are equally, if not prouder, of our high touch customer service strategy. In all of our businesses, paying attention to the customer is a corporate imperative.

Output had another great quarter, with revenue up 20% and bottom-line profitability significantly improving. Keep in mind that unlike the first quarter where we have some unique programs, such as printing tax documents, the second quarter did not have similar programs, putting that 20% year-over-year growth in better perspective. The Output growth strategy is also customer relationship focused. For instance, a new relationship with FundView, a Cloud ERP system that is provided to local governments, resulted in the addition of 30 new cities as customers over the past year and seven in just the last quarter.

The relationship we have built with L.A County has resulted in an expansion of that relationship, and we are now handling their check disbursements needs for fees and fines overpayments, where we recently mailed 9,000 checks in one day. And, because of our strong relationship in these industries, we added another three energy providers and three electric utilities in the quarter. We will continue to invest in Output as we believe there is potential to grow the business. Consequently, we recently hired a 30-year, seasoned print and mail sales executive to complement our existing sales efforts.

Let me add a few more developments at Output that are representative of the transformation and integration transpiring across the organization. Output recently signed a toll road customer for disbursement of toll bills. The bills have a QR code that the recipient scans, which takes them into a payment portal built and operated by Usio, and there's more automation coming.

For instance, our last two new accounts are completely electronic with no print or mail service. We will create e-bills that are emailed to customers who like the toll road business are directed to a Usio managed payment portal. This should push the proportion of Output's revenues from electronic payments to approximately 40% and climbing. This is much more profitable work, and as a result, expanding Output's gross margins.

The story is the same for card, where we're focusing on building relationships that has enabled us to continue to add new ISVs. I would point specifically to an ISV with strong government ties. We're penetrating many of their accounts such as toll roads, including the Massachusetts Department of Transportation, Florida Turnpike, Delaware Tolls and other government organizations such as the City of Miami for fees and fines.

Why do ISVs keep on giving us more business? Because of our long tenure in the business, pioneering PayFac technology and our great customer service. And in ACH, we had a growth quarter despite ongoing tough comparables on the large year ago Voyager volumes. While we will face another tough quarter of comparables in the third quarter when Voyager was still running off, we expect to see performance in the ACH starting in the fourth quarter when there was virtually no Voyager volume to speak of.

Our strong growth is also leading to better margins as we leverage our fixed direct costs. In addition, overhead for the second quarter was virtually unchanged from a year ago as we kept a tight lid on costs and continue to focus on improving efficiency and productivity.

So far this year, revenues were up 24% on the top line with only about 1% added overhead, which includes the absorption of significant inflationary pressures. The result is another quarter of more than \$1 million in adjusted EBITDA, which is now up \$3 million compared to the adjusted EBITDA generated over the first half of fiscal 2022.

In addition, we delivered positive GAAP net income and earnings per share for the second consecutive quarter, which has been an important objective. Consequently, as previously noted, we are reiterating our guidance for the year, although we believe that the second half will be comprised of somewhat slower third quarter followed by a stronger fourth quarter.

As a result of the first half of the year is the best in the company's history, and we expect this to be a record year. Our pipeline is extremely strong and many of our existing relationships are with fast-growing organizations with whom we are growing. We're in great financial condition, and we can't wait to get back to work every day.

And now, I'd like to turn the call over to Houston Frost.

### **Houston Frost**

Thank you, Louis, and thank you to everyone participating on our call this afternoon. As Louis noted, prepaid had an exceptional quarter, nearly tripling revenue while growing load volume by 48% and purchase volume by 51%.

While revenues benefited from the breakage earned on inactive New York City incentive cards, load and purchase volume trends reflect the strong growth of new and existing client card programs. June was our best month ever for both prefunded card loads and transaction volume and early figures show continued growth in July.

Importantly, this load and transaction volume is largely coming from longer-term programs with recurring and/or larger card loads. These include guaranteed income and other multiple load cash assistance programs as well as corporate expense and other specialty card programs. As Usio's card issuing business matures, we believe it's important to build a base of programs that will generate longer-term recurring payment volume.

Admittedly, there's a trade-off here. Single-load card programs, especially with loads of \$100 or less, generate higher revenue as a percentage of load volume than do recurring and larger load program. And typically, single load program revenue is higher gross margin, although from a net profit perspective, the additional gross margin is partially consumed by higher customer service and operational expense as a percentage of loads.

That said, we're confident that continuing to focus on and shift toward longer-term recurring load programs is the right long-term decision. These programs and clients are less price-sensitive and have higher switching costs. Building a business that is more defensible and more stable will ultimately be more valuable. That said, we certainly don't plan to turn away any single-load card programs. We see our success is being driven by our operational execution, our proprietary processing platform with the flexibility and capabilities it offers and our relentless focus on the client relationship.

This bolsters our confidence in our strategy, focus on clients and programs where these strengths provide true value. Class Wallet is a great example of this strategy in action. They operate a service that assists academic and government organizations with managing their purchasing and reimbursement process.

We first began issuing their cards more than three years ago in 2020. The company's products had a unique need requiring them to be involved in transaction authorization decisions, and we had a solution, what we call external authorization. Today, Class Wallet has grown to be one of our top clients by load and transaction volume.

MoviePass is a similar example, a long-term relationship also using our novel external authorization solution. And of course, we also continue to build relationships at the local government and nonprofit space. Among our many newer engagements is a program with the California Department of Social Services, which will be using a Usio card to disburse nearly \$100 million to eligible individuals who experienced hardship as a result of storms in that state. These programs often take advantage of our transaction restrictions and controls, virtual cards and/or consumer choice offerings. But what customers tell us they appreciate most is our partnership. Our willingness to jump on a call and troubleshoot an issue, facilitate an improvement or simply be honest about a mistake and work toward an acceptable resolution.

In total, we continue to be on pace to add approximately 80 to 100 new clients this year. While we do expect to see card issuing revenue and gross margin decline somewhat over the next few quarters, as income generation from the New York City and City of Houston and other vaccine incentive programs wind down, we are thrilled with the programs we manage today and the business we are building. Our June record loaded transaction volume indicates Usio's card issuing business is poised for continued growth over the long-term.

With that, I'd like to turn the call over to Greg Carter.

**Greg Carter**

Thank you, Houston, and good afternoon, everyone. Card revenues were up once again in the second quarter, led by a 26% growth in our PayFac business, where virtually all of our efforts and resources are being concentrated.

For the quarter, dollars processed were up 2% and transactions processed were up 15% from a year ago. Louis noticed some nice recent wins with governmental entities, all of which are from

a very strong ISV relationship. We also added a fitness exercise practice management ISV whose software is being rapidly adopted by gyms and fitness centers.

To illustrate the dynamics affecting our implementation process, and to use one of my dad's analogies, this was way more than the carpenter's old rule, measure twice and cut once. It was closer to measure 14 times. That's okay. While competitors may have balked and walked away, this is what makes us different, and we fully expect this to be a long and mutually beneficial relationship.

There was an equally exciting new implementation with an agricultural and rent supply company. They're already set up with ACH and they're now switching all of their e-commerce transactions onto our card platform. Our expectation is that eventually, they will move the remainder of their payment needs, primarily on-premises to Usio, which could be quite significant. In addition to our strong relationship with this firm, they like the flexibility that Usio provides and of course, we remain price competitive.

On the product side, we've made a significant upgrade in our card-present transaction device which we believe will drive incremental revenues. And I think now we have the strongest prospect pipeline we've ever had, including opportunities arising primarily from trade show attendance with organizations in the veterinarian, fundraising and waste industries.

As with all of the Usio business development efforts, our success is primarily a function of the variety of payment channels and the strong relationships we are building in the market. For many of our new accounts, we may be their first payments platform. In addition, there's a lot of cross-selling taking place. For instance, as a result of their relationship with Output Solutions, we are talking to a large player in the printing market about how to provide an electronic payment solution to complement their existing business.

And in May, we added Stephanie Gonzales to speed up our marketing efforts and amplify our various initiatives. As previously noted, in the short-term, results can be impacted by the pace of new ISV implementations as well as the rate at which they ramp. Fortunately, as we grow our pipeline and engage with an ever greater number of ISVs, the rate of implementation continues to improve, so we are optimistic about the second half of the year with revenue growth returning to the strong trajectory for the last several years.

With that, I'd like to conclude my remarks and turn the call over to Tom Jewell, our Senior Vice President and Chief Financial Officer, to discuss our financial results.

### **Tom Jewell**

Thanks, Greg, and welcome, everyone. Thanks again for joining our call today and for your interest in Usio. Let me quickly provide some color around this quarter's results before opening the call to questions. Revenues were up 31% to a record \$21.3 million, driven by strong growth in prepaid and Output Solutions. Credit card revenues were up 3%, ACH and complementary services were up 5% this quarter after being down the last few quarters.

Gross profits of \$5 million were a quarterly record for the third consecutive quarter and margins expanded 340 basis points from a year ago. The gross margin improvement reflects a higher contribution from breakage and spoilage, which significantly improved margins in the prepaid segment growth in our high-margin ACH revenues as well as strong margins at Output Solutions.

Selling, general and administrative costs were basically flat with the year ago period and are up just slightly more than 1% for the first half of the year. For the third consecutive quarter, we generated over \$1 million in adjusted EBITDA.

For the quarter, we reported \$0.01 per share of GAAP EPS, while also reporting \$0.01 per share of GAAP EPS for the first six months of the year. Non-GAAP-adjusted operating cash flows as described in our 10Q and earnings release was \$1.5 million for the six months ended June 30, 2023.

Our cash position at the end of the quarter was \$6.6 million, up approximately \$900,000 over the first half of 2023. For the first half of the year, revenues were up 24.4%, gross margin has expanded 350 basis points, SG&A is up 1% and adjusted EBITDA was \$2.2 million compared to a loss of \$875,000 for the first half of last year.

I do want to call out our efforts to drive interest income where we had employed investment sweeps to generate over \$300,000 of interest income over the first half of the year. In July, 2023, alone, interest income was a \$160,000. As Louis noted, we expect to meet our revenue guidance for the year, but expect to see a slight slowdown in revenue growth and gross profits due to declining breakage and other items.

With that, I will turn the call back to the operator to conduct our question and answer session.

## **QUESTION AND ANSWER**

### **Operator**

We will now begin the question and answer session. To ask a question you may press "\*" then "1" on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw your question, please press "\*" then "2." At this time, we will pause momentarily to assemble our roster.

The first question today comes from Scott Buck with H.C. Wainwright. Please go ahead.

### **Scott Buck**

Hi, good afternoon, guys. Thanks for taking my questions. First of all, I was hoping you could give us a little bit color around what you're seeing with MoviePass and maybe how that business has performed versus expectations, granted it's early.

### **Houston Frost**

Yes, hi Scott. This is Houston Frost. I think generally speaking, MoviePass has performed in line with our expectations. They have...we have continually seen their volumes ramp up. Ultimately, they are going to be a fairly significant client of ours. It's hard for me to say I mean on being number one, number two, number three, number four, number five, but will be in the top 10 and I think last quarter, just by payment volume, they are already in our top 10 clients. So, it's a long-term recurring revenue type client. It's not New York City where you're going to...we're going to...they are going to turn up revenue one quarter and then maybe watch it roll off or wait for breakage at the end of that. It's going to provide consistent revenue month-over-month and that revenue should continue to grow from here.

**Scott Buck**

Thank you, that's helpful. Second one I want to ask about gross margin. I know it's mix dependent, but curious given the progress you've made so far, where can we expect to see gross margin go over next 12 months or so?

**Houston Frost**

Are you referring to prepaid specifically are you referring to companywide?

**Scott Buck**

Companywide. Sorry, companywide.

**Louis Hoch**

I'll take that question. So there's obviously the big component is the mix and the last few quarters have been very positive in terms of prepaid breakage. Output Solutions has been pretty consistent. It might drop a little bit depending really on the pickup in the ACH business.

**Scott Buck**

All right. That's helpful. And then last one I just want to ask quickly about the acquisition environment. Is there anything else there that could potentially be interesting for you guys or is...or are you strictly focused on the organic business?

**Louis Hoch**

We look at the overall return, we don't have anything in the hopper, but we're open to acquiring more companies. We have very strict criteria and nobody lately has been able to meet that criteria.

**Scott Buck**

Right. That's helpful. I appreciate the time guys and congrats on the quarter.

**Louis Hoch**

Thanks.

**Houston Frost**

Thanks Scott.

**Operator**

The next question comes from Michael Diana with Maxim Group. Please go ahead.

**Michael Diana**

Thank you. My first question is on expenses. So, I think Greg mentioned that you hired a senior marketing person in PayFac. You're obviously spending more money for growth and yet the G&A expenses are very flat which is great. What...there must be a...well, there are pluses, there's got to be a minus to offset it somewhere. So what are some of the things maybe you are doing to keep that G&A number low?

**Greg Carter**

Well, the first thing is we hired a new head of marketing for the company, and that was a replacement. So that doesn't increase SG&A. And then we hired new senior sales people. We are always looking for experienced sales people across the organization. So you will see us continue to add sales positions. But we are continuing to scale where we need to scale, but we



are definitely at the point where we have operating leverage, where we are leveraging our fixed costs and our volumes are going up. So that's really helping out with OPEX in general.

**Michael Diana**

Okay. Great. And Tom mentioned you are generating interest income, which I noticed went way up from sweeps. Could you just tell us a little how that works though?

**Louis Hoch**

It has a lot to do with inflation and the Fed, and it may be somewhat temporary, but Tom and his team have been really doing well, investing our deposits in a safe manner that are yielding good interest. And we think that interest amount will even go up this quarter.

**Michael Diana**

Alright. So it's not necessarily the sweeps being more efficient, it's the interest rates going up or some combination of both...

**Tom Jewell**

It's definitely a combination of both. You know we have multiple banks and we basically went through all the banks and are sweeping the money, and then you also have the compounding effect of the higher interest rates. And just talks about his loan increases, everything we do as we grow business as business changes, all of that factors into the incremental interest income.

**Michael Diana**

Okay. Great. And then Houston, you mentioned again, I you've mentioned it for guaranteed income programs. Can you give us an update on whether that's something that's growing as far as number of programs or individual programs?

**Houston Frost**

Yes. You know, I think broadly speaking, absolutely, it's growing. In fact, I guess, it was early June. We were at a conference in Chicago, of the basic conference...Basic Income Guarantee. And it's always surprising to me to know that that conference has been going on for almost 20 years, I believe, but they were just now discussing private a scale, full-fledged guaranteed income programs. So for...it was just an interesting context to hear about how they have been talking about these in kind of a theoretical or academic kind of way for well over a decade and we have participated in the very first real pilot program [indiscernible] a couple of years ago. So what we are seeing are pilot programs turn into larger programs and also being extended and even just saying that there is no end to those programs. And we continue to add to both through direct sales as well as by partnering with service providers that are kind of servicing the non-profit and local government space that covers them.

So very positive trends there, and we absolutely expect it to continue. I think if there's anything on our mind it's that the continued growth will likely lead to increasing competition in the space. But no, I don't think guaranteed income programs are going away. I think direct cash assistance is only going to continue to go up from here, just broadly speaking.

**Michael Diana**

Okay, great. Thank you.

**Louis Hoch**

Thanks, Michael.

**Operator**

The next question comes from Jon Hickman with Ladenburg. Please go ahead.

**Jon Hickman**

Hello. Can you hear me okay?

**Louis Hoch**

Hi, Jon.

**Jon Hickman**

Hi, Louis, would you elaborate on your comments about headwinds for ACH in a couple...in the coming quarters?

**Louis Hoch**

So, ACH absent Voyager continues to grow. So if we take Voyager out in the mix, we are continuing to add new accounts. And those accounts were actually producing more than they did last year without Voyager. So ACH is doing well in that aspect. It's...you know, the comparables year-over-year right now are tough, and they will be for Q3 because we still do a lot of work for Voyager in Q3, but Q4, you will see the comparables even out and we should do well from there. We do have initiatives. We're implementing the Clearing House network. We're implementing the FedNow.

We do believe that some ACH traffic will go to those real-time methods. We're early entrant in those two payment channels. So because we're early, we'll create some new business out of it. And all that goes into the ACH and complementary services bucket. So you're going to see some growth there.

**Jon Hickman**

Okay. And then on the PayFac side, you mentioned then ag. Supply, was that an ISV or is that a retail chain?

**Louis Hoch**

It is actually more of an enterprise account, not a pure-play ISV but given the size and the and the requirements that they had, it was a good fit for Usio, but to be clear, it's not an ISV.

**Jon Hickman**

Okay. And then let's see, I had one more brilliant question. What was it? That's it from me. Thanks for taking my question.

**Louis Hoch**

Thanks, John. Thank you.

**Houston Frost**

Thanks ,John.

**Operator**

As a reminder, if you would like to ask a question, please press "\*" then "1" to enter the question queue.

The next question comes from Gary Prestopino with Barrington Research. Please go ahead.

**Gary Prestopino**

Hey, good afternoon. Well, Louis my questions were all around this FedNow. Is this going to be a positive for you or does this take away from your ACH business?

**Louis Hoch**

It's going to pull away some ACH traffic, not much. ACH is still the cheapest method to send a payment. ACH, you can still do same day. So it fits for a lot of different applications. Nobody is going to pay their mortgage real time or their life insurance real time. It's that same day or next day. So ACH is always going to be around. In fact, ACH globally, the volume continues to increase. And now FedNow, anything with real-time payments is definitely going to grow and we're there. And we have a strategy being diverse in the payment channels that we offer.

So we're going to be implementing FedNow. FedNow is opt-in program for banks, even though every bank has access to a Fed terminal it doesn't mean that they can accept FedNow payments. So it's going to be a limited rollout just like the Clearing House has been a limited Fed rollout. So the Clearinghouse is the network that Zelle runs on. And I'm sure if you've used that before, you realize that you can't send payments to everybody.

The Clearing House today is primarily just credits and segment FedNow and for it to be effective payment mechanism it needs to be credit and debit. And, so we'll see that the debit, once a debit portion rolls out, then it will have more applications available to it. But we're implementing both and we don't care which one wins. We think the margins are going to be similar to ACH. And we think our ACH business in itself is going to continue to grow.

**Gary Prestopino**

Well, that's what I'm asking You danced around it here. I mean with your ACH business, as I understand it, that is two or three days payment like we said on a mortgage, FedNow is instantaneous. So you are...will be capable of doing both ACH and FedNow once you hook up to, now I realize FedNow has not proliferated. It's just recently come out. But if there's a business that's going to be pulled away, what would it be pulled away? What are you doing right now that has had same-day settlement?

**Louis Hoch**

So, ACH is, we can do same day ACH. We do next day ACH, that technology exists, and we do that every day. We do a lot in real-time payments today. We call that PINless debit, that's the same technology that you would use if you're making a Venmo payment with somebody, that's PINless debit. It goes across the debit rails. So, it doesn't really matter. When you're looking at Usio as a company, it doesn't really matter what payment method is going to win. We're involved in every one of them.

And FedNow and the Clearing House, once they implement debits will become, have more applications. Right now, the Clearing House is good for spending money and it's not good for somebody receiving a payment, a merchant receiving payment. So Clearing House or Zelle is pretty much person-to-person payments. So you can see they've limited themselves in the way they're rolling out.

But when they get debits, it's going to be important, and it will shift. The payment world shifts all the time. We had a big shift in COVID, where we went from people willing to insert their card or swipe their card to contactless. Houston's team before COVID would issue more plastic cards, after COVID, we issued more virtual cards. People really want to touch their card. So it didn't matter that, that shift occurred within prepaid because we were in both channels. And that's

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important to understand about our company is that we believe that we need to have all channels. And it's very unlike our competitors.

**Gary Prestopino**

Okay. Thank you, thank you, Louis.

**CONCLUSION**

**Operator**

This concludes our question and answer session and concludes the conference call. Thank you for attending today's presentation. You may now disconnect.