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Q4, Inc. (QFOR.CA)

Q2 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Sara Pearson

Director-Investor Relations, Q4, Inc.

Good morning, everyone, and welcome to Q4's Second Quarter 2022 Earnings Call. My name is Sara Pearson and I'm Q4's Director of Investor Relations. I'm joined this morning with Darrell Heaps, our CEO; and Donna de Winter, our current CFO and COO, to review our first quarter results. Please note, a copy of today's presentation will be available on our website. Please be aware that today's prepared remarks have been posted live.

Following the prepared remarks, we will be looking forward to welcoming our research analysts onto the call for a live video Q&A session. To those in our virtual audience, you can use the webcast Q&A button to submit questions in real-time.

We need to remind participants that certain information discussed on today's call may be forward-looking in nature. Such information reflects the company's views with respect to the future events. Any such information is subject to risks, uncertainties and assumptions that could cause actual results to differ materially from those projected in the forward-looking statements. For more information on the assumptions related to the forward-looking statements, please refer to Q4's public filings available on SEDAR.

During the call, we will be referencing certain non-IFRS financial measures. Although we believe these measures provide useful supplemental information about our financial performance, they're not recognized measures and do not have standardized use under IFRS. Please see our MD&A for additional information regarding our financial measures including for reconciliations to the nearest IFRS measure. Please note that unless otherwise stated, all figures are in US dollars.

And with that out of the way, I'll pass it over to our CEO, Darrell Heaps. Darrell?

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

Wonderful. Thanks, Sara. And good morning, everyone. It's my pleasure to welcome you all to our second quarter's earnings call. And to be joined here with our newly appointed CFO, Donna de Winter. Welcome, Donna?

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

Thanks, Darrell.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

Today, we're going to be walking through the progress that we've been making in the second quarter and along with the macro environment comments in terms of what we've been kind of working through during the quarter and the progress that we've been making.

We could bring up the slides, we'll get into some of the prepared remarks. I want to kick off today's call a little bit – talking a little bit about our business and the market. When I set out to create Q4, the idea was always that if we could create web-based software that exists at the intersection between public companies and investors that would be a business that could last forever. Fast forward 15 years and this is what we have built and are continuing to build. Today, this platform is serving millions of investors each day as they access our websites, events and apps across the web to research companies and engage with management.

Today, I'm going to spend some time talking about our platform and some of the exciting things that we are doing here. However, before getting to that, a brief comment on the macro-environment. In terms of the macro-environment and the public markets, what's clear is that during the second quarter, we saw dramatic re-pricing evaluations across the board. The impact of this macro environment on our business is twofold. The first and positive is that current customers more than 2,685 of them lean into us more using more of our products, analytics and advisory services to help them navigate a challenging market. As Donna will cover in more detail, this can be seen in our continued growth in multiple product adoption, seen with our 65% plus of our ARR coming from our clients using two or more product categories. Average revenue per account growth, continued high controllable renewal rates of over 96% and more than 40% plus growth in our capital markets platform services segment.

On the flip side of this, with valuations at record lows, it causes potentially new customers to slow purchase decisions when switching vendors and causes companies to delay or cancel going public, making it more challenging for us to add new customers at the rate that we were adding during previous quarters.

The thing that I want to focus on is that the business that we have built, which sits at the intersection between companies and investors, is incredibly durable. Even in a market such as this, which is arguably the most challenging we have seen since 2008, we are still able to deliver solid double-digit recurring revenue growth and increased platform adoption across our large and diversified client base, with more than 100 customers upgrading their subscriptions with us this quarter. My point here is that as the market improves, our ability to deliver value to our customers, expand their spend with us and attract new customers to the platform, will continue to strengthen and enable us to continue driving impressive growth similar to what we've achieved over the last few years.

This quarter, we made significant progress in building out our platform ecosystem that all sides of capital markets will utilize to connect with one another. We launched Capital Connect along with a unified data layer across all

products. This new platform gives us the ability to now bring forward new apps and partnerships designed to expand our engagement with our customers. The launch of Engagement Analytics app is a great example. It's been very exciting that we have begun to realize our vision of being able to analyze the behavior of investors across our platform. What is really amazing is the sheer scale of our platform and the number of active companies and investors using it. Over 4 million daily users accessing more than 2,600 investor sites and thousands of events. We are analyzing hundreds of millions of data points each day, but what makes Engagement Analytics very unique is that we're also able to understand investors' actions in the market, both through standard data sets like 13-F filings, but also our own market surveillance services.

This gives us deep insight into what they are buying and selling. This combination gives us a unique view into the patterns of the market and helps us make better recommendations to our clients on who they should be targeting and engaging with. This is just the start of where we're going with this ability. In future quarters, you'll see us expand the insights and recommendations that we provide, along with releasing expanded functionality to help companies and investors engage with one another. In June, we also launched the website management app onto the platform, allowing customers a faster and easier way to make changes to their investor websites. This critical feature is now being used by more than 1,500 customers on a daily basis. We are committed to delivering the best customer experience in the industry, [ph] bar none (00:06:40) as we scaled quickly during the pandemic, our response times started to grow. But through the launch of this app and the maniacal focus on fast turnaround times during trading hours, I'm absolutely thrilled to see the consistent flow of customer five star ratings across all of our service teams.

Finally, around the middle of the quarter, we started to roll out a new product called the Q4 Login. You may have actually seen this as you registered for this call. Simply, it allows an investor to choose to create a Q4 account and then be automatically logged into any quarterly earnings call hosted by Q4 in the future. Our vision is to connect the capital markets across our platform, and this is a big step in that direction. This is the first of many investor and issuer focus features that will be rolling out onto the platform over the coming quarters. As of today, we've had more than 85,000 investors create an account just this quarter. And we're excited to see this database grow and help augment our larger database of 350,000 investor profiles. This is really an important step as we begin to unify all of the capital markets experiences across our platform.

On the partnership front, we continue to sign partnerships focused on bringing our customers access to the best quality products and services. This quarter, we are pleased with the addition of Diligent who provides governance solutions and extend – eSSENTIAL Accessibility. Who offers digital accessibility expertise to better serve our client needs. Working with the expanded NYSE program has begun to show new business opportunities, with the addition of Q4 virtual events services. Our expanded role within the provides program is promising as it allows NYSE corporate issuers the flexibility to leverage the investor relations products and services that are right for them. On an M&A front this continues to be one of our strategic priorities. And we have been making really good progress on a number of fronts. This year time has been on our side as we have seen the environment improve for buyers over the second quarter, along with private company valuations continuing to come down, although still at a slower pace than in the public market.

Having said that, we remain absolutely committed to bringing forward, highly accretive and strategic assets that will help to accelerate our vision and path to profitability. More to come on this front. This quarter, I'm also happy to report that we have completed our planned OpEx investments for the year and I would describe this quarter as being the peak investment quarter. These investments have enabled us to build out our platform, unify our data across our products, and bring differentiated, high value insights to our customers. These have also helped us to enable to build out our expansion sales efforts, helping to drive continued growth in platform adoption and

average revenue per account. And finally, the build out of our European go to market efforts, setting us up well to grow our European business over the coming quarters.

With these big investments behind us and in response to the current macro environment, we are positioning the business for profitable growth through a multi-prong strategy with a focus on expanding our operating leverage, initiatives are already underway to improve sales efficiency and utilize low cost geographies to drive down operating expenses. Combined with our gross margin expansion, this will bring forward our commitment to cash and EBITDA positive by H2 2023 well in advance of our prior expectations. This acceleration will ensure we remain very well capitalized through to profitability, while also ensuring we remain very well positioned to deliver strong growth moving forward.

Finally, I'm pleased to announce some recent news here with Donna de Winter accepting our role as permanent CFO. I'm just super excited to be working with Donna each and every day. And her contributions to our efforts are our have already had a big impact and really looking forward to future quarters.

And so, with that, I will pass it over to Donna to take you through the financial results and then we'll have our Q&A session. So, over to you, Donna.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

Thanks so much, Darrell. Good morning, everyone. I'm really looking forward to immersing myself in the CFO role and continuing the work with the team to lead our financial strategy. As Darrell covered during the second quarter, we continued our progress against our overall strategy and vision despite the current market dynamics and we are able to continue executing our growth strategy, focusing on product deployment, development and innovation. Diving into the numbers, we saw flat sequential quarterly revenue directly impacted by the market conditions and partially influenced by disproportionate percentage of our Q2 sales closing in June and not providing any revenue benefit in the quarter.

With continued growth and expansion selling and Q3 sales occurring such that it can contribute to the end quarter revenue we expect to restore modest growth in the current quarter. Our total revenue for the second quarter was \$13.8 million, representing an 11.5% growth in normalized revenue over the same quarter in 2021 of \$12.3 million. This excludes the impact of the onetime VSM revenue from last year. The revenue growth was driven by expansion sales into our client base of subscriptions as well as additional platform services. The impact of including the \$5 million VSM revenue in Q2 2021 results in a 20.5% decrease in revenue year-over-year. We made the decision to discontinue the VSM business line last year due to its non-strategic fit and pressure to our long-term gross margin expansion.

Our capital market platform revenue grew by 9.4%. Excluding the VSM revenue from the comparable quarter last year. The increase in normalized revenue can be attributed to our new logo acquisition as well as our efforts to drive higher ARPA into the client base. Notably, our platform services grew by 41.2% on a year-over-year basis, attributed to the increased demand for value added website services. Our ability to be a one stop shop is incredibly valuable to our clients in all market conditions. And our revenue base continues to be highly predictable. With 89% of year-to-date capital markets platform revenue coming from recurring and long term customer contracts, ensuring our core business remains strong and intact.

At the end of the second quarter, ARR was \$53.3 million, an increase of 12.4% year-over-year, driven in part from 107 existing customers purchasing additional subscriptions with us. It is exciting to see so many customers increasing the scope of their relationship with us. Our investment into the development of additional subscription

offerings that are valuable to our existing clients, coupled with the ramping investment in our expansion sales capabilities has fueled this growth channel. As well, our bundled sales approach focusing on selling platform has continued to work very well with annual contract value of new sales increasing in both North America and Europe. However, the acquisition of new logo slowed as a result of tougher market conditions that dramatically impacted the pace of new IPOs in the market and corporate customers delaying their IR spending.

Average revenue per account or ARPA was \$18,642 at the end of the quarter. This represents a 4.1% increase over the prior year and also generates an increased growth rate compared to the first quarter compared to the first quarter's 3.2%. Expanding our offerings into the existing customer base contributed the majority of the ARPA growth in Q2 and delivers early ROI on the investments to build that expansion capability. The combined efforts of our expansion sales and our client success team produced the highest quarterly increase of ARPA on record. Additionally, our team continues to enact renewal billing increases to ensure we can absorb the increasing inflationary costs while maintaining the highest quality service levels.

Product adoption continues to move towards customers, leveraging two or more products. This quarter, 65.4% of ARR was generated from these customers, up from 63.2% a quarter ago. These clients also have a strong propensity to engage with us for value-added services supporting overall revenue growth. Our integrated platform strategy is evolving as anticipated as shown in the chart, with clients buying a higher number of solutions and services, driving increased value in the hands of the clients and increased retention for us. It is a true driver of ARR and ARPA. As customers adopt additional products and gain unique values through our platform approach, we are further entrenched in the customer workflow. This creates a strong moat around our core business and will help us retain customers. In the second quarter, we saw the addition of 79 new clients, of which 61 became subscribers. Our quarter ended with 2,685 customers on the platform.

A notable strain on our ARR growth and retention during the quarter was uncontrollable churn tied to M&A in the public markets causing customer consolidation. This trend continued from Q1 when we saw the majority of our revenue churn come from these uncontrollable types of events. However, our controllable logo retention remains strong at 96% consistent with last quarter. Our low churn levels supports the durability of our business and our ability to be valuable to customers in tough economic times. Looking at gross margin in the second quarter, we saw costs impacted by inflation, which, when combined with lower revenue, slowed our gross margin expansion, resulting in gross margin for the second quarter being relatively flat for the comparable quarter last year at 56.5% and 56.8% comparatively. It decreased slightly in sequential quarters, primarily because of inflation. And that unfavorable trend is being addressed with additional margin expansion initiatives.

We are still tracking to exit 2022 with mid-60s gross margin and mid-70s next year. We remain focused on the original pillars of our gross margin expansion strategy, but we feel that they alone are insufficient to deliver the margin outcomes we expect. The first of our original pillars is to consolidate and reduce the fixed cost of our data and other direct costs. On a percentage basis, these costs reduce over increased revenue volume, but we have also targeted an assessment and rationalization of providers to generate absolute savings. The second pillar, which is the vertical integration of our virtual events platform, delivered significant progress this quarter. We completed the migration of our North American customers and will continue with the migration of our European customers over the next quarter.

The third pillar relates to investments we are making in product automation to improve the customer experience with less manual effort for us and the customers. As Darrell mentioned earlier, the launch of the website management app is a perfect example as it has made it easier for customers to manage their websites, while also making it much easier for us to manage these requests. But to help us realize our gross margin expansion, we have added two additional pillars. The fourth pillar is an expansion of our workforce into new lower cost

geographies, where we don't currently operate, while remaining intensely focused on service excellence. This hiring strategy is underway and will impact COGS in Q3 and beyond. And the fifth and final pillar is to increase prices to offset the negative impact of inflation on our costs, while maintaining our ability to provide premium customer service. These price increases began rolling out in Q2 and will positively impact Q3 and future quarters.

As you can see, maintaining our customer base through service excellence is our paramount strategy. We also believe that a strong balance sheet and income statement creates a sustainable ability to serve these customers. In the second quarter, operating expenses, excluding depreciation and amortization, foreign exchange loss and other expenses totaled \$17.3 million. This quarter's operating expense was at our highest planned level of spend. The leading investments we made in sales and marketing and research and development this quarter provide the foundation for our future growth with a solidified infrastructure and the ability to scale our platform sales without further investment.

Sales and marketing costs were \$6.5 million or 47% of revenue, an increase of \$2.1 million, compared to Q2 last year. The increase included necessary investments in our expansion and European sales capabilities. Research and development came in at \$5 million or 36% of revenue, an increase of \$2.2 million, compared to the second quarter costs last year. The increase supported the continued investment in both the improvement of current products within our capital markets platform and the development of new offerings. G&A for the quarter was \$5.8 million or 42% of revenue for the quarter.

This increased \$1.2 million from the comparable period in the prior year when we were private, primarily because of the expenses associated with operating as a public company. G&A expenses will level off as a percentage of revenue into the back half of this year as we scale and find leverage on our costs associated with going public. Our adjusted EBITDA was negative \$8.7 million or negative 63% of revenue for the quarter. This reflects the high investment levels associated with the hyper growth strategy that we feel is challenged in this macroenvironment. As we execute our accelerated plan to profitability, which I'll touch on in a moment, this loss will narrow considerably over the second half of the year and become positive in 2023. In terms of our balance sheet, our core working capital metrics remain strong and consistent with historical trends, ending with a working capital balance of \$40.2 million.

As of June 30, 2022, we had \$45.1 million in cash. Net of net operating – negative operating cash flow in H1 of \$18 million. As described, this is primarily the result of investments made across sales, marketing and research and development. As of June 30, we had no outstanding debt with a total revolving facility of \$22.5 million. Our balance sheet continues to be well-positioned to execute against both our organic and inorganic growth opportunities. Our intention is to maintain that strength.

We have weathered previous cycles of challenging macroeconomic conditions. We've recognized the durability of our business model and the importance of adapting the pacing of our strategic priorities to combat the headwinds we are facing. As such, we are taking deliberate measures to shorten our timeline to profitability through enhanced focus on cost management and business efficiency. I wanted to reaffirm that we are still expecting gross margins to exit this year in the mid-60s and in the mid-70s for 2023. As I mentioned earlier, our strategies on this front are well underway and will impact Q3 and Q4 in an effective manner.

Of equal importance to EBITDA is the optimizing the return on OpEx. With initiatives for improving sales efficiency and utilizing low cost geographies to drive down OpEx, expanding our operating leverage through the remainder of 2022 and 2023. This will result in being – in the business being cash flow and EBITDA positive in the second half of 2023, ahead of our earlier expectations of reaching EBITDA positive in early 2024. Accelerating this path to

profitability, will ensure that business remains well-capitalized, giving us the ability to singularly focus on executing our organic growth strategy, while ensuring we have ample capital for inorganic opportunities.

And with that, I'll now pass it back to Darrell.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

Fantastic. Thanks, Donna. That was great. And with that, we'll now switch over to the Q&A session. So I will pass it back to Sara to kick us off.

QUESTION AND ANSWER SECTION

Sara Pearson

Director-Investor Relations, Q4, Inc.

A

We're back on the Q&A for the Q4 earnings call. We're going to go back to our first question with Kevin McVeigh of Credit Suisse. Kevin, if you're on the line, can you please join?

Kevin McVeigh

Analyst, Credit Suisse Securities (USA) LLC

Q

Yes. Again, thanks so much Donna and Darrell. Congratulations on the execution in a tough environment. Just hoping to get a little bit of sense of the sequencing of the revenue in Q3 and Q4, just to try to reconcile that against the gross margin objectives as possible.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Sure. Thanks, Kevin. I'll let Donna answer that question. But first, I just want to just acknowledge that the outage that we just had on the broadcast, it was due to an Internet outage that happened with one of our video partners. So just our apologies for the delay. Hopefully, you've stuck with us during the call and we look forward to going through the Q&A session with the analysts. And so with that, I'll – now we'll take your question Kevin and over to you, Donna. Thanks.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Great. And thanks, Kevin. When we think about the gross margin expansion, it is in the context of modest sequential quarterly revenue growth, not our historical growth rates. So the margin accomplishment will be in that modest environment on the top line, and not against, as I said, historical trends. So there's a high certainty to getting to those levels.

Kevin McVeigh

Analyst, Credit Suisse Securities (USA) LLC

Q

That's great. And then, as we think about the incremental pillars because it's just really, really impressive that you are able to maintain that. Currently what you think about what the potential benefit from pillars four and five are and obviously it offsets probably some revenue headwinds, things like that. But just, if we think about the components of what those incremental actions help on the margin line, if at all?

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

We're not providing absolute guidance on the magnitude of the dollars, except to say that it brings forward our EBIDTA into H2 2023 positively EBITDA versus 2020 – early 2024. But I think the – we know now, Kevin, what the size of the service and the type of the service that it takes to be truly excellent with the clients. So it is about then creating that environment at non-North American cost levels and really exploring how to attain both, having some resource availability in lower cost geos and having North American talent, as well. And so that combination drives to the margin materially.

The second one is more point in time, having experienced the inflation over the last 12 months and really adjusting our understanding of how to flow that through maintaining and our obligation to maintain the premium service levels. So it is as much about retaining clients and giving them the value that they come to expect from us, and balancing that with the inflation that we're experiencing as an operating entity.

Kevin McVeigh

Analyst, Credit Suisse Securities (USA) LLC

Q

Very helpful. In terms of [ph] again even (00:29:26) more control of the outcome than we did six months ago which is a great outcome. Thanks so much.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Absolutely.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Absolutely. And thanks for that.

Kevin McVeigh

Analyst, Credit Suisse Securities (USA) LLC

Q

Our pleasure. Thank you, Kevin. Back to you, Sarah.

Sara Pearson

Director-Investor Relations, Q4, Inc.

A

Thanks. Our next question is going to come in from Stephanie Price.

Stephanie Price

Analyst, CIBC World Markets, Inc.

Q

Talk a little bit more – hi, good morning. I was hoping you could talk a little bit more about the demand environment, what prospects you're seeing and if you've seen any impact to the sales cycles, just given the difficult macro-environment?

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Sure. So maybe I'll take that one. And Stephanie, thanks for joining the call today. So I think, as I mentioned in the prepared remarks, the macro environment is really as a result of kind of the dramatic change that happened starting in Q1, but really during Q2. And I think when you see kind of a dramatic re-pricing in valuations happened

across the board, there is a, I would call it, kind of like a shock factor of companies. Now, as I mentioned, the ones that are existing customers, their adoption and use of our products and our services actually increases during that environment because they're looking for more help to be able to understand what's going on, understanding what's going on with their peers in the market as they execute their programs.

But the other – just other aspect is when we're having conversations with customers, they are looking at the valuation has changed dramatically. And so what ends up happening is it takes longer to convince them to kind of move over to a new vendor during that environment. I think what you've seen is in a lot of cases, companies also looking at cost cutting, looking at budgetary aspects.

So in that environment when you have kind of like hiring freezes happening or procurement freezes happening, that's what makes it a little bit harder to be able to close those new customers onto the platform, and certainly it impacts IPOs as well. But what I will say is that that is really kind of a like a shock to the system that occurred during the second quarter. I think what we see going forward is not – valuations have certainly come down and I'm not forecasting the market but it's not – we don't think there's a huge other leg to come down in the market. So we think we have bottomed out from the impact it has on our business. So we should be able to get back to not experiencing that same dynamic as much in the third quarter and the fourth quarter. So that's how we're thinking about it now and hopefully that's helpful.

Stephanie Price

Analyst, CIBC World Markets, Inc.

Q

That is helpful. Thanks. And maybe a follow-on to that. On the existing customer base, you mentioned more than 100 customers have upgraded subscription. Can you talk a little bit about the key services that are driving that cross-sell and upsell?

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Sure. So the one thing I'll mention to I know in the remarks we made was about 100 buying additional subscriptions and that's what drives ARR and that's what drives ARPA. But the other thing that happens is customers also buy what we call like attachment products. So these are really kind of upgrades within their existing product category. So that would be things like additional like redesigns on their website or onetime events or Investor Days or things that are not typically kind of like ARR in nature. So the ARR products that they're buying are really around CRM, analytics and other packages that would be like virtual event kind of subscription packages. So that would be like add-ons to their like earnings events, but done as a subscription annually. So it's predominantly the onetime stuff ends up being mostly kind of web and events but it's CRM and analytics. And the one final thing I'll mention as well is we have additional subscription products in ESG and in accessibility, and there's been actually a lot of demand on the accessibility side. So we've been able to package all of those as incremental subscription purchases.

Stephanie Price

Analyst, CIBC World Markets, Inc.

Q

Great. Thank you very much.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Our pleasure. Thanks for the question.

Sara Pearson

Director-Investor Relations, Q4, Inc.

A

Our next question is going to come in from Stephen Boland from Raymond James. Stephen?

Stephen Boland

Analyst, Raymond James Ltd.

Q

Thanks. Can you hear me okay?

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Yeah.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Absolutely.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

We can hear you. Thanks, Stephen.

Stephen Boland

Analyst, Raymond James Ltd.

Q

Okay. Maybe the first question is on total deferred revenue that number fell quarter-over-quarter, and I always thought that was like a signal of billings that would be basically earned over the period of the year. So what does it – when it falls, maybe just give me an idea of what that means, again, is that that revenue is – although you're saying it's modestly going to grow, but maybe not all revenue goes through deferred revenue, maybe just explain that decline?

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Yeah. I think there is some – one of the comments made in the prepared remarks, Steve, was around the fact that the linearity of the selling that occurred in the second quarter and it really being loaded into June and [indiscernible] (00:34:43) being in June not hitting deferred – not hitting revenue, but definitely not hitting deferred revenue. So there is what I would say an adjustment going to happen early in July, when all of that late stage invoicing makes its way onto the [indiscernible] (00:35:00). Those products go live with clients, whether it's CRM, analytics or websites. And the more robust deferred occurs, the only other impact, I'd say in the quarter was the inventory [ph] return (00:35:17) and that impacting our renewal – what we would call renewal deferred revenue. But it is really just speaks to the freshness of the bookings in Q2 and fully expecting that to restore in Q3.

Stephen Boland

Analyst, Raymond James Ltd.

Q

Okay. So, when you said – sorry, when you say, sales closing in June, there is a lag between that sale translating into deferred revenue. Is that [indiscernible] (00:35:48).

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

That is correct. Yeah.

A

Stephen Boland

Analyst, Raymond James Ltd.

Okay. Okay. That's great. And then the second question, Darrell, I mean, you mentioned the cash down \$18 million year-to-date. I mean, when I look at that versus what is going to occur probably for the rest of the year and then coupled the M&A strategy on that. I mean, are you in a position now where you're being priced out of certain acquisitions that you may have looked at three months ago or six months ago in terms of having available capital to execute?

Q

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

So, I think when we look at the market out there and the targets that we are most interested in, I think, we are certainly very cognizant in terms of what cash do we have available to put against the M&A strategy as well as what availability we have from a debt perspective. Those two things, as well as utilizing to a degree our own stock and facilitating those deals. So, when we look at kind of the available financing options that we have, whether cash, stock, bringing on leverage, we still feel that we are very well suited to execute the strategy that we've mentioned in terms of this accelerated path of profitability, while also ensuring that we remain – that we have cash – we have resources available to continue executing on M&A. I mean, certainly with that, it's not unlimited. We don't have – kind of we can't do every single deal out there, because there is certainly a certain amount that we can utilize, but that's something that we feel gives us all the firepower that we need for the targets that we're looking at.

A

Stephen Boland

Analyst, Raymond James Ltd.

Okay. Thanks very much.

Q

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

Pleasure. Thanks for the question.

A

Sara Pearson

Director-Investor Relations, Q4, Inc.

Our next question is coming in from Richard Tse at National Bank.

A

Richard Tse

Analyst, National Bank Financial, Inc.

Hey, everyone. Hope you can hear me and I just sort of [indiscernible] (00:37:51) log in now. So I apologize if I repeat any questions. In terms of the environment, it's changed a lot since you first became public. I'm curious to see if there's anything that strikes you as surprising or things you didn't expect in the business now that the environment has normalized somewhat?

Q

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

So first off, Richard, thanks for joining and apologies for the technical glitch that happened there, but it's nice to speak with you again. I think that certainly when we went public, which was the end of October, the market was certainly still at a very high point. So I think kind of the – we certainly weren't expecting the market to continue to be at record highs forever. However, I think that when you look at the second quarter and just how quickly the valuations came down, I think that and how broadly that impacted the entire market. I think that for us, along with – and I think probably everyone in the market that was certainly unexpected, the kind of the velocity that occurred during the second quarter.

Now, I'll say that, when you look at kind of a longer timeframe, you think about how many periods have been like this that have had that. We go back to kind of financial crisis of 2008, I think early in the pandemic maybe it looked like it, but as we all know, that rebounded incredibly quick. So when you look at that, we really look at the second quarter being quite an isolated event in terms of in terms of the change.

Now going forward, what we're not assuming is that we're going to get back to kind of record high valuations like nine months ago. But we do believe that as the market stabilizes, then we're able to continue executing our plan, bring new customers onto the platform, expand their spend et cetera. So we think kind of Q3 and Q4, we get into much more normalized patterns versus the dramatic change that happened in the second quarter from a market perspective.

Richard Tse

Analyst, National Bank Financial, Inc.

Q

Okay. And sort of I guess my second follow-up question related to that. Has that caused you to sort of permanently change how you run the business in any way, like I understand it, you're obviously moderating your spend, but in terms of whether it's practices on the sales side or the marketing side given a normalized environment, what is sort of changed permanently here going forward?

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

So maybe I'll ask Donna to answer that.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Hi, Richard. How you're doing? I'm going to assume you are doing...

Richard Tse

Analyst, National Bank Financial, Inc.

Q

I'm good. Thanks.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

I think it's a great question and I think the first part is that the tenants of the business that went public a year ago or nine months ago remain intact. The plan's being executed and I don't see that changing in any meaningful way, where I think age, experience and durability in the model says, no, you can't – you have to have a better balance of short-term, mid-term and long-term priorities. There can't be as many go gets or leading investments that have

a longer time to ROI. So I think those are really important aspects that you have to overlay on a three-year vision. It was a three-year vision and we're nine months in. So you don't abandon that kind of business strategy and business value.

So it is more about making sure that every dollar has an ROI, making sure that there's balance in that ROI, making sure that what has been built has both scalability to come out of it quickly to respond when we're coming out quickly, but that, it's also highly efficient in this challenging macro.

So I would say, it doesn't change the strategy, but definitely the [ph] data – day (00:41:56) execution has more focus and more certainty around ROI, more certainty around revenue and spending against that certainty instead with less [ph] bleeding (00:42:08) against some of the more uncertain growth.

Richard Tse

Analyst, National Bank Financial, Inc.

Q

That's great. Thank you.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Thank you, Richard.

Sara Pearson

Director-Investor Relations, Q4, Inc.

A

Perfect. So our last question is coming in from Doug Taylor. He sent in his question via our Q&A application. So I will read the question out to you guys. The question is, there's a lot of increased discussion about achieving cash flow and EBITDA breakeven earlier than previously targeted. What are the revenue growth assumptions required to do so versus the prior 30% growth target?

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

You want to take that one?

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

I can take that one.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Sure.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Thanks, Doug. So as we talked about in the prepared remarks, we think about modest sequential revenue growth, not in – half in that kind of range of what we would have experienced in headier markets. And so our margin targets are against that modest revenue outlook and not against historical trends or historical growth patterns.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Maybe what I'll add to that as well as that our ability to execute in marketing we talk a lot about customer service and customer success. That aspect coupled with our ability to sell when we talk about kind of different modest growth rate, bringing that down while looking for efficiencies across OpEx and delivering on that gross margin expansion, all of which brings profitability sooner. We're also making the assumption that although, as I mentioned, it's not another shock kind of is coming like the second quarter, but we're also not expecting kind of like high growth market that's coming back with those assumptions. So we are being conservative in terms of what the health of the market is going to be, what the demand cycle is going to look like in the interim while we execute this. And I say that because as the market does return and as we all know, the market will return, growth will come back. And as growth comes back and we will be very well positioned to be able to continue executing to drive that kind of accelerated growth into [indiscernible] (00:44:28) during that period.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

Yeah, I think our conservativeness when we refer to double digit growth as modest.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Yes.

Donna de Winter

Chief Financial Officer & Chief Operating Officer, Q4, Inc.

A

I hope we're conservative in our approach and thanks for adding that context [ph] to Doug (00:44:42).

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

A

Yeah. Absolutely.

Sara Pearson

Director-Investor Relations, Q4, Inc.

A

That was our last analyst question. So with that, we're going to wrap up the call.

Darrell Heaps

Founder, Chief Executive Officer & Director, Q4, Inc.

Okay. Very good. Thank you everyone for joining us on the call and again apologies for the technical glitch we had halfway through. Thank you for sticking with us during the call, if you're still here. And have a wonderful day, everyone. Take care.

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