



GAME SQUARE

GameSquare Esports Inc.

First Quarter Fiscal 2022 Financial Results Conference Call and Webcast Transcript

Date: May 31, 2022

Time: 8:00 AM ET

Speakers: **Kevin Wright**
Chairman and President

Justin Kenna
Chief Executive Officer

Paul Bozoki
Chief Financial Officer

Operator:

Good morning and thank you for joining us to discuss GameSquare Esports' First Quarter of Fiscal 2022 Financial Results Conference Call and Webcast.

On the call today, we have GameSquare CEO, Justin Kenna, CFO Paul Bozoki, and President and Chairman, Kevin Wright.

If you would like to join the conference by phone, please click on the link at the bottom of the webcast. During the call, all participants are in listen-only mode. Following the presentation, we will conduct a question-and answer-session.

Before Management discusses the results, I'd like to remind everyone that certain statements in this call may be forward-looking in nature. Any such forward-looking statements are based on certain assumptions and are subject to risks, uncertainties, and other factors that could cause actual results to differ materially from those expressed or implied in our forward-looking statements. Forward-looking statements speak only as of the date of this call, and there can be no assurance that the forward-looking statements will prove to be accurate, and you should not place undue reliance on such statements. Please refer to the forward-looking disclaimer and the risk factors in the Company's MD&A for the period ended December 31, 2021, which can be found on the Company's profile at [sedar.com](https://www.sedar.com) and on the Company's website. The Company undertakes no obligation to update such forward-looking statements except as required by applicable law.

I will now turn the call over to GameSquare's President, Kevin Wright.

Kevin.

Kevin Wright:

Thanks, Eugenia, and good morning, everyone. I'm Kevin Wright, President and Chairman at GameSquare Esports and I'd like to welcome you to today's conference call to discuss our Q1 2022 financial results for the period ending March 31, 2022. We have filed on [sedar.com](https://www.sedar.com) yesterday, along with the MD&A.



I'd highlight that, commencing this quarter, the Company changed its presentation currency from Canadian dollars to U.S. dollars to reflect our interest in future potential listings in the U.S., as well as to reflect our focus on pursuing business opportunities in the large and rapidly growing U.S. gaming and esports market.

I would also like to remind you that during today's call we will be making comments containing forward-looking information. I invite you to read our financial disclosures for risks and uncertainties that may affect GameSquare's performance in the future. As such, actual results may differ materially from the views expressed today. For further information on these risks and uncertainties, consult our most recent MD&A and filings on SEDAR, and unless otherwise indicated, please note all figures are in U.S. dollars unless otherwise noted.

With that formality out of the way, and given that we just spoke with you a month from now, we'll try to keep this quick. I'll turn it over to GameSquare CEO, Justin Kenna.

Justin.

Justin Kenna:

Thanks, Kev. Good morning, everyone, and thank you for joining us.

We held our Q4 call just over a month ago, so we won't rehash all the exciting opportunities and progress that we discussed then. Transcripts and recordings are available on our website at investors.GameSquare.com.

What I do want to talk about is the great progress that we've made in the last couple of months to give you a sense of the high growth that we're driving, as well as how we're doing on our path to profitability.

Despite a seasonally soft Q1, I'm pleased that we have exceeded our internal sales targets, and with a month to go in Q2 we have already met our internal sales projections for the quarter. We're really pleased with the sales execution, and there are some great opportunities within our sales pipeline across all of our businesses. We've had high profile wins with Lenovo, ARterra Labs, Army, and Dairy MAX at Complexity. (Inaudible 0:04:01) were recognized for innovative work that they've done for Jack-



in-the-Box and Cash App, and we've closed some nice recurring revenue opportunities at GCN and at Code Red.

As we were active with M&A throughout last year, year-over-year comps are tough; but if you look at how Code Red has trended (inaudible 0:04:18), and you can find this in our MD&A, their revenue grew by more than 50% and their gross margin has nearly doubled. This is indicative of how we're managing our business: high revenue growth with margin expansion as a focus.

We have also launched new revenue opportunities which are capitalizing on the growing activity and brand evolution within esports and gaming. Fourth Frame Studios is a great example. Since launching, it has been active providing content production services to existing GameSquare clients and winning business with new brands in esports orgs. Our expectation is that Fourth Frame will be a very near-term contributor to profitability and is a great case study about how we can build new businesses that complement our existing business and bolster the incredible talent that we have within the Company. Based on the early success of Fourth Frame, we are assessing other opportunities that can profitably serve the esports and gaming market as we seek to offer customers more choice.

We have also talked about optimizing our businesses with a focus on eliminating expenses that are not supporting the high revenue growth that we are showing across the business. We have our densified areas that we can optimize, which include internalizing outsourced costs and ensuring that spending on external contractors is the right decision to support high growth and profitability in the near term. Even before these cost cutting measures, we believe that our private placement and credit facility provide us with the access to capital that will enable us to meet our business objectives, including our recently increased revenue guidance of US\$23.5 million to US\$25 million, or CA\$30 million to CA\$32 million, without having to rely on additional equity financing in the near term.

We believe that we have built a great platform with great people doing great things, and our audience of more than 220 million is leading to more brand opportunities, as evidenced by Lenovo, Jack-in-the-Box, Cash App, ARterro Labs, and many more. The trend in esports points to growing engagement by global brands and we believe the GameSquare family of companies is at the intersection of culture, commerce and investment.

With that, we'll turn it over to our financial performance.

Paul Bozoki:

Thanks, Justin.

Before diving into our financial performance, I'll just remind you this is the first quarter that we reported in U.S. dollars, which does reflect our focus on pursuing the big business opportunities in the large and growing U.S. gaming and esports market, and the majority of our revenue is expected to be in USD, so we'll be doing that this quarter and going forward.

As we talked about in the past, Q1 is the softest quarter, with Q4 typically the strongest. Revenue for the three months ended March 31, 2022, was US\$5 million, or roughly CA\$6.5 million. Q1 2021 included only Code Red, and when we compare a like-for-like to Q1 2022, that business grew by 54% year-over-year. Gross margin for Q1 2022 was 32.6%. Again, if we look at a year-over-year basis looking at Code Red's performance, which is our only comp from '21, gross margin nearly doubled. On a quarter-over-quarter basis, gross margin compressed somewhat, which reflects lower activity within the high margin digital media segment due to seasonality, which we did discuss during our Q4 2021 last month.

What we like about the structure of our business is that we've built the foundation for growth so there's very little incremental investment required; which means that as we drive revenue growth in seasonally busier quarters and continue to focus on margin expansion within each of our businesses, we expect to see the positive impact of operating leverage as the reoccurring and recurring revenue grows within our high margin agency business and as we monetize the high margin content inventory within our team segment.

The Company generated an adjusted loss for the three months of \$2.7 million, which is in line with the operating cash flow prior to changes in working capital. As mentioned, we have identified areas of optimization across the Company and we're implementing cost savings that we expect to reduce annual burn by approximately \$1 million to \$1.5 million.



The Company ended the quarter with \$1.7 million of cash and \$3.8 million of working capital. This does not reflect the already announced \$3 million private placement, or the \$5 million credit facility to be established by Goff Capital and Blue & Silver Ventures, a Jerry Jones-owned company. All told, we have access to roughly \$10 million in cap.

I'll turn the call back to you, Justin.

Justin Kenna:

I'm happy with the results in Q1 and the initial progress that we've made in Q2. We have a strong pipeline, and across the Company we are focused on monetizing our existing high margin inventory, creating incredible outcomes for clients which is leading to repeat business, and we are competing for and winning large RFPs. This gives us confidence that our guidance of US\$23.5 million to US\$25 million is on track. Further, we are starting to see cash flow-positive months which are not yet offsetting outflows for the quarter, but we are on track to report positive cash flow in the later stages of the year and we're encouraged by material improvements in our cash flow profile.

We discussed the strength of our sales pipeline on the last call and, as mentioned, we are seeing good conversion from RFP to contracted deals and the size of RFPs is impressive. Our sales team has gelled under the leadership of our CRO, Sean Horvath, who is leading positive change for the Company. We have a number of exciting collab projects underway, and we are looking forward to being able to share the work publicly in the coming weeks and months.

On behalf of the Company, I want to thank you for joining the call and for your continued support.

With that, I'll turn it to the Operator to take any questions.

Operator:

Thank you. We will now begin the question-and answer-session.

To join the question queue over the phone, you may press star then one on your telephone keypad. You will hear a tone acknowledging your request. If you are using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star then two. Alternatively,



you may type in your question in the box at the bottom of the webcast. We will pause for a moment as callers join the queue.

The first question is from Robert Young with Canaccord Genuity. Please go ahead.

Robert Young:

Hi, good morning.

Maybe the first question I'll ask is you said that you'd exceeded your internal target for Q1, but you didn't change the guidance, and so I was just curious if you could maybe talk about the macro. I know there's a few things out there that worry some investors, like the snap results, Wal-Mart and Target and things like that, and so it sounds as though you're seeing a lot of good pipeline growth and demand, and so maybe you could put those two things into context for us and just maybe give us a sense of whether you see any troubling developments around demand, or if that's just something you're not seeing at all.

Paul Bozoki:

I'll jump in first on the guidance.

We set our guidance a month ago with pretty good visibility to how Q1 was trending, so we didn't see any reason to increase our guidance this quarter; but certainly as we go through q2 and start to see the progress that we're seeing in Q3, that's when we'll look to adjust our guidance, if that's appropriate.

In terms of the trends that we're seeing and the RFPs, Justin, do you want to jump in, and then I can fill in any colour afterwards?

Justin Kenna:

Yes, absolutely.

We commented in the call on our sales team and sort of starting to get really resourced in that area under Sean Horvath and his team, so we have an extremely strong pipeline so we do feel really comfortable. That's not to say that we aren't affected by some of the trends that we're seeing out there



that are going on in the world, but I think our teams' been really strong and really successful in being able to pivot and being flexible in terms of any adjusted scopes, so we have seen a couple of RFPs that I think in a more normal world we may have won where we've had to pivot, but we've had a real ability to still be able to win work, bring clients in, deliver and really deliver value to build those longer-term relationships that we think you'll start to see. Again, we talk about recurring and reoccurring revenue. We're putting those wins on the board that we think will convert into a number of larger AOR-type deals. So yes, there's no doubt that we are seeing some dollars that may normally be there be a little cut back, but I think we've been able to pivot really well, and I think our offering across the group really helps us.

Again, having Fourth Frame studios internal to the business, being able to keep content production costs internal, and the ability to up-sell into our media network and so forth, so definitely seeing and have seen some trends on that front, but I think the teams' pivoted really and, as we said, we're continuing to execute and then see a really, really strong pipeline.

Robert Young:

Great, and then, I guess, just on the pipeline, you said you'd seen significant growth in, I think, number and size, if I remember correctly, and then I think one of the last press releases just before the quarter were related to Dairy MAX, I think it was a renewal, was an expansion and adding on the creative agency of record. Maybe if you could just talk about how that dynamic—is that something you're seeing across all of your customers, this sort of movement towards maybe being a creative agency of record for esports, that would be really interesting, and then maybe just on the growth in number and size of RFPs, if that's what you're seeing.

Justin Kenna:

Yes, I can take that one, Kevin, and feel free to jump in.

I think, Rob, that's one of the really strong points to our model. In the past, Dairy MAX has been a great brand partner of Complexity Gaming, being our esports org. But now having the ability to have Cut+Sew internal, who do have that creative agency offering, and having Fourth Frame from a content perspective and having GCN from a media agency perspective, as well as Code Red who can introduce influences that, again, all stay within the org, so it's actually a really good example, Rob, and



a good case study for us on a multitude of ways that we can actually now touch brand partner deals, whereas in the past Complexity on their own just didn't have that offering.

We are continuing to look at ways that GameSquare can be a one-stop shop for brands in this space, trying to connect with these huge audiences that we talk about, and I think this is a really good example of that, is a continued and upscaled brand partnership deal with Complexity, but also then having the offering for that creative agency from Cut+Sew, so a really good example, and there's a number of these case studies where we are touching brands in a multitude of ways and actually keeping revenue internal, and I think whether it's Cut+Sew or Fourth Frame, that additional offering has been really valuable to us.

Kev, do you want to touch on RFPs?

Kevin Wright:

Yes, and there's two pieces there as we go into the RFP discussion, too. It's multiple entry points into the business with the great sales folks and the relationships that are within the business, so we're seeing that flow through, and so as we're starting to look at RFPs and speaking with brands, we're able to add on additional pieces, so because we have our media network, we're adding media onto all of the proposals that we do. Because we have our content studio, we're able to add the content studio in, and in some cases that leads to higher revenue, and in other cases it's higher margin because we're not outsourcing.

In terms of size of the RFPs, if I go back to a year ago when we were talking about deals that were in the low six figures, we're now bidding on RFPs that are in the low seven figures, not all of them, but we're seeing more of those start to come through the door, and I think that's a reflection of the quality of work that our agency businesses have been doing and brands just seeing the value and the multiple ways that they can work with GameSquare. It's not just a one-to-one business relationship anymore.

Robert Young:

Okay, that's great. Last question I think for me would be around the last comments in your prepared comments about positive cash flow, some great commentary. I think I missed whether you were saying that you'd be positive cash flow in a quarter as you exit the year, or is that still on a month-by-month



basis? Maybe if you could maybe put a little more context around that so we can understand just for modeling purposes, and then I'll pass the line.

Paul Bozoki:

Yes, so I think the way to look at that is we're not ready to give guidance on the positive cash flow; but, like we said, we're seeing positive cash flow months right now from time to time, but those aren't offsetting months where we're still cash flow negative. We are still burning cash, as evident in the quarter, but we do think in terms of the trajectory that we have that we are getting closer to talking about being cash flow positive by the end of this year. Whether that ends up being that fourth quarter is cash flow positive, or whether it means November-December are cash flow positive, we still have to see how that unfolds this year, but we're seeing really good progress in terms of, one, the growing revenue, and then as we add more of the digital media business to our revenue profile, that's going to show the growing margins.

Robert Young:

Okay, that's great colour. One last little one just on the gross margins. (Inaudible 0:19:53) that margins ticked down in Q1 (inaudible 0:19:58)—

Paul Bozoki:

Rob, I don't know if it's just on my end, but you're breaking up. Do you want to start that question again?

Robert Young:

Sorry about that. Maybe that's better?

Paul Bozoki:

That's better.

Robert Young:

It is? Okay. The gross margins, you noted that they ticked down in Q1. I think you said it was seasonality, but you also said that you expect expansion. Is that quarter-over-quarter sequential expansion through the year do you think, or are you talking about year-over-year, sort of a comparison



expansion as you go forward? Maybe a little more colour over that so I can understand, and then I really will pass the line.

Justin Kenna:

Yes, I can jump in on that one.

Yes, absolutely, Rob, so we spoke about seasonality in Q1. I mean, you'll see the large margins that we get from our agency businesses. In Q4, that was a really large, substantial part of our overall make-up. We spoke about Q1, the overall make-up of that being slightly less, given those added brand dollars as prevalent really early on in the year, so that was expected. We would see margin expansion as being sequential quarter-over-quarter and absolutely year-over-year; but as we spoke about, given M&A, the year-over-year quarters are a little harder to compare right now. But we are in good shape for Q2. And again, speaking to our RFP pipeline and our brand pipeline of some of these larger deals moving forward, very confident that you will see sequential quarter-on-quarter margin expansion as those agency—you know, we spoke about Dairy MAX being able to up-sell into our creative agency. As we continue to see growth through Cut+Sew, GCN, Fourth Frame, you will continue to see that sequential margin expansion, so no surprises around Q1; but, yes, you'll look to see that continue to grow throughout the year.

Robert Young:

Okay, thank you very much. Thanks for taking the questions.

Operator:

Once again, to join the question queue over the phone, click the link at the bottom of the webcast. Once connected, press star then one on your telephone keypad. You may also type in your question in the Ask a Question box.

There are no other questions on the phone at the moment. I would like to turn it back to Management for webcast questions, if any.



Kevin Wright:

Okay, I think with that, we're done with our Q&A, so this concludes the GameSquare Esports First Quarter 2022 Financial Results Conference Call. I'd like to thank everybody for joining.

And Justin, any closing comments, or just a quick goodbye?

Justin Kenna:

Yes, again thanks for the continued support. Looking forward to continuing to update the market on some of the exciting projects that we're working on. Thanks very much.

Operator:

This concludes GameSquare Esports Inc. First Quarter of Fiscal 2022 Financial Results Conference Call. You may disconnect your lines. Thank you for participating, and have a pleasant day.