PaySign Inc.
Third Quarter 2019 Earnings Call
November 5, 2019

Presenters
Mark Newcomer, CEO
Mark Attinger , CFO

Q&A Participants
Mark Palmer - BTIG
Austin Moldow - Canaccord Genuity
Jon Hickman - Ladenburg Thalmann
Eric Wright - BW Investment
Jeff Feinberg - Feinberg Investments

Operator
Greetings and welcome to the PaySign Third Quarter 2019 Earnings Conference Call. At this time, all participants are in only-listen mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press star zero on your telephone keypad. As a reminder, this conference is being recorded.

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Mark Newcomer
Thank you, Kevin. And good afternoon, everyone. On behalf of PaySign, I'd like to welcome you to our third quarter 2019 earnings call. I'm Mark Newcomer, Chief Executive Officer here at PaySign. I will provide a brief review of some of the highlights for the third quarter and will reinforce our strategic direction. Following my remarks, I'll turn it over to our Chief Financial Officer, Mark Attinger, to take us through the third quarter results. Following Mark's review, we will then field your questions.

PaySign is both a vertically integrated processor and a prepaid card program manager. We develop, customize, and innovative payment solutions in support of corporate, consumer, and government programs. To learn more about our history and the services we provide and to review a copy of our most recent investor presentation, you may want to visit the investor section of our website at www.paysign.com.

I'm very excited to share the results for an outstanding quarter. We experienced record revenue and earnings. We continue to execute on our growth strategy and have gone live with our premier card, rolling this out to our cardholders at one of our plasma clients. Year-to-date, we have added 54 new card programs, 45 in plasma, 7 in pharma, and 2 other corporate incentive programs. As expected, all scheduled plasma centers were onboarded at the end of September, increasing the total number of centers we service by 13%.

As of September 30th, there were 2.86 million cardholders on our platform. In summary, revenues were record 9 million, an increase of 40% compared to the prior year. Net income was 3 million, also a record and up 270%. And adjusted EBITDA was 3.3 million, an increase of 124%. We continue to experience excellent growth and expect to see higher revenue in the fourth quarter, benefiting from recently onboarded new card programs. Guidance remains 35 million to 37 million and adjusted EBITDA of 10 million to 12 million.

Strategically, and consistent with our prior communications, we will continue to broaden and diversify our market focus for our prepaid card programs, and we'll seek to introduce new products. We are evaluating the expansion of our premier card offering to other corporate incentive industry verticals. Lastly, we are making considerable progress in evaluating several opportunities on the M&A front. However, there is nothing definitive to share at this time. As I shared previously, we will selectively pursue acquisition candidates that have long-standing replications, corporate culture of innovation, and that have demonstrated growth and profitability. At this time, I would like to turn it over to Mark to take us through the numbers in a little more detail.

Mark Attinger

Excellent. Thanks, Mark. So, I'm going to take us through the third quarter and the year-to-date top line numbers and provide some variance commentary. Any references to year-on-year improvement or percentage changes, unless stated otherwise, refers to the third quarter ending September 30, 2019, as compared to third quarter of 2018. Revenue for the quarter ended September 30, 2019, was 9,008,117, an increase of 40.3% compared to the analyst consensus estimate of 8.98 million and the prior year of 6,421,396. This increase in revenue was attributable to continued growth in plasma programs and our new pharma business, which represented proximally 22% of revenue for the current quarter.

Revenue for the nine months was 24,901,678, an increase of 50.4% year-on-year, compared to $16,558,438. Gross profit increased 76.3% to 5.4 million, or 59.6% of revenues, compared to 3.0 million and 47.4% of revenue in 2018. The 1,216 basis point improvement was primarily driven by a favorable mix towards higher margin card programs. The operating expenses were 3.1 million, down from 3.4 million from the prior quarter and compared to 2.3 million in 2018. The quarter three year-on-year increase consists primarily of 0.3 million in incremental salaries and benefits, 0.3 million increased stock-based compensation, and a 0.1 million increase in outside professional services.

Benefiting from higher cash balances, interest income is 114,000 compared to 37,000 the prior year. Net income for the third quarter ended September 30, 2019, was 2,960,078, $0.06 per basic share, an increase of 269.6% compared to 800,862, or $0.02 per basic share, in the prior year.

Fully diluted was $.05 versus $0.02. For the first nine months, net income was 5,570,540, or $0.12 per basic share, an increase of 186.3%, compared to 1,945,425 million, or $0.04 per basic share the prior year. For the nine month period fully diluted earnings per share was $0.10 versus $0.04 in the prior year. Non GAAP adjusted EBITDA was 3,252,332, or $0.07 per basic share, an increase of 123.6% compared to 1,454,224, or $0.03 per basic share, the prior year.

Furthermore, the adjusted EBITDA margin improved to 36.1%, up 1,346 basis points from 22.6% in the third quarter 2018. For the nine month period, adjusted EBITDA was 7,563,486, or $0.16 per basic share, an increase of 123.1% compared to 3,390,833, or $0.07 per basic share, the prior year. We loaded $210 million to the card for the quarter versus 172 million the prior quarter--excuse me, compared to 172 million same quarter the prior year, and our revenue conversion rate of gross dollar volume loaded on cards was 4.29%, or 429 bps, compared to 3.72%, or 372 bps, the prior year. Worth noting, and reflecting the new business on boarded in the third quarter, in October, $88 million were loaded onto the card, compared to an average per month in Q3 of just 70 million loaded to cards.

From a balance sheet perspective, consolidated cash including restricted cash has increased 30.2%, or 9.6 million to 41.2 million, compared to 31.7 million at year-end 2018. As a comparison, consolidated cash at October month end was 49.8 million, up 8.6 million from September. Working capital increase to 13.1 million, compared to 9.5 million at June 30, 2019, compared to 5.9 million at year-end. The 7.2 million improvement compared to last year was due primarily to increased consolidated cash but also due to increased AR from higher client billings and decreases in accounts payable, partially offset by an increase in the card funding liability. Our liquidity, as measured by adjusting the current ratio, excluding restricted cash and cardholder funds from both sides of the balance sheet, respectively, was 7.5 up from 5.4 at year-end.

As we look to the fourth quarter, we do expect to benefit from revenue contributed from the recently on boarded and signed new business. Also, considering the mix, we expect slightly lower gross margins. And I believe that concludes my remarks. At this time, I'll turn it back over to our moderator to begin a question-and-answer session. Thank you.

Operator
Thank you. We'll now be conducting a question-and-answer session. If you'd like to be placed in the question queue, please press star one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star two if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing star one. One moment, please, while we pull for questions. Our first question today is coming from Mark Palmer from BTIG. Your line is now live.

Mark Palmer
Yes, thank you very much. Question on the restricted cash balance, which decline sequentially from the second quarter, it had been, I guess $42.6 million, and it was $33.2 million at September 30. I know that from our conversations after the second quarter, investors are not supposed to look at this as indicative of the health of the Pharma co-pay business. But if you could just give some commentary on what happened sequentially and what investors should take from that, please?

Mark Attinger
Thanks, Mark. Appreciate the question. Good to hear your voice. So, one of the things we did point to is an increase in restricted cash and consolidated cash, as of October month-end. It increased by 9.6 million--excuse me by 8.6 million back up to 49.8 million from the quarter-end. I know you like to look at that number. It is a good number on trend over time. The other thing I would point to is that we did sign new clients in the pharma space, and, as we talked about before, this particular product provides funds to assist patients and consumers with their out-of-pocket expense on their prescriptions. And early in the year for any given program, typically, these programs load more. So, there is seasonality to it. Once their deductible is met, the loads start to subside, and then you'll see those loads go right back up in the first quarter.

So, part of this is normal seasonality, part of this is timing, which is why we wanted to point to the October month-end restricted cash. And part of this, we have actually new clients coming on board in the pharma space. That's probably the best way to answer it, is timing, new clients and seasonality.

Mark Palmer
Okay. So, just to confirm, in terms of the 49.8 million, that's a consolidated cash number at the end of October? I just wanted to see what the restricted cash number was the end of October?

Mark Attinger
Before we get to the end I'll see if I can pull it up. I don't have it handy this very moment, but the restricted cash is roughly—of that 49, it's going to be roughly 42 million of that is restricted, but I'll check that number to confirm it.

Mark Palmer
Okay. Very good. And also just wanted to see with regard to the PaySign premier program, if there is any initial indication of traction being gained on the go live that you have with one client, and I will get back in the queue.

Mark Newcomer
We've been certainly signing up new customers, but it's too early, and we do point to and have continued to reiterate that the material benefit from that program we expect to be in 2020, but we are making good progress.

Operator
Thank you. Your next question is coming from Austin Moldow from Canaccord Genuity. Your line is now live.

Austin Moldow
Hi. Thanks for taking my questions. First, quick housekeeping question. I'm not sure if I missed it or not. But what was the Pharma revenue contribution in the quarter, and then the follow-up would be, can you give some color or context to your pharma pipeline in terms of customers and campaigns and how you feel about those relationships yielding revenue next year? Thanks.

Mark Attinger
Good question. Thanks, Austin. So, pharma represented approximately 22% of the revenue for the quarter, and that was up from approximately 20% in the second quarter, as you may recall. And picking up a little bit on Mark's question, pharma continues to be a strength for us and continues to grow nicely, and, Austin, to that latter part of your question, yes, we have signed new business in the third quarter. I think Mark mentioned that we signed four new programs on the pharma business in the actual third quarter, and three of those are regular prepaid. As we see in the revenue, the other is actually a co-pay pharma program. In terms of the pipeline, yes, there's several new opportunities that we're evaluating and in discussions with our clients on, and, as you know, we work through channel partners who introduced us to a number of programs.

Austin Moldow
Great. And then, my last question is--can you talk about what you're seeing in the plasma space in terms of competition? I know that the batch that you just brought, is that something you won from a competitor. And, as you expand your market share, are you able to tap into any new relationships, or is it mostly expanding within larger networks where you already have small footprint or something?

Mark Newcomer
No. Our expansion in the plasma space is due to several factors, but primarily, there's always the new center build. We're expanding by that method. And then, there is winning business from our competitors. And, yes, we were successful on what was marked 33, 34 centers. Those were directly across from the customers.

Mark Attinger
32 centers that we brought across on September 30th basically from with an existing client. Something that we had been hoping to secure earlier in the year, as you probably know.

Mark Newcomer
But that was a win from another customer--another competitor. So, one of the things that we've shared with you is a couple of our larger clients actually split our volume between us and our largest competitor, and so we continue to look to differentiate in our performance to win new business and increase our share of those two clients. And, to Mark's point, this is exactly that example.

Austin Moldow
Got it. Thanks very much for taking my questions.

Operator
Thank you. As a reminder, ladies and gentlemen, it's star one to be placed in the question queue. Our next question today is coming from Jon Hickman from Ladenburg Thalmann. Your line is now live.

Jon Hickman
Hi. Thanks for taking my question. Could you tell me what the cash flow from operations was this quarter?

Mark Attinger
John, I'll have to get back with you on that. I don't have that handy.

Jon Hickman
Okay. So then, could you talk a little bit more about why the revenue conversion was up? I mean, it's almost 50 basis points.

Mark Attinger
Yeah, so, typically the revenue conversion rate on the pharma business is higher, and so that higher mix towards pharma results in a higher composite.

Jon Hickman
Thank you. Nice quarter. Appreciate your time.

Operator
Thank you. Our next question is coming from Eric Wright from BW Investment. Your line is now live.

Eric Wright
Thanks, guys. First off, congratulations on the record quarter and consistent results and also the launch of the new premier cards, and a lot of the questions have been covered. But I know margin have been increasing substantially these days, and a large portion of that is attributed to the product mix. Is there any other factors that is causing the margin to increase this much? And I see also that operating expenses in Q2 2019 versus Q3 2019 actually decreased. So, can you also comment that?

Mark Attinger
Good questions. We will see that taper a little bit on the gross margin in the fourth quarter as you see those new plasma centers come on board and run at that rate that we saw last year on that gross margin for the plasma business. So, that'll bring it down on a consolidated basis a little bit. Not too much of a move but just keep that in mind. From operating expense standpoint, most of that was timing of expenses that we were getting taken care of on the--getting through our audits, getting to our outside professional services, and recognizing the expense for some 401(k), things that hit in the second quarter that we didn't have in the third quarter. So, I just want to--I would expect the fourth quarter for our operating expenses to come back up a little bit, be a little bit closer to what they were in the second quarter.

Eric Wright
Okay, that's great. And if we're trying to gage in terms of operating leverage, do you guys have the capabilities that you guys need to continue to execute on this growth trajectory that you guys are doing and, if so, how variable is that operating expense line?

Mark Attinger
It's a great question, and one thing we continue to talk about with all of you analysts and on these calls is that we are seeing improvements in operating leverage. If you look at last year's year-on-year, the growth in OpEx was about 80%. This year, we're in about the mid-30 percent range on a year-to-date basis. And so, we do not expect that to grow at the same rate that we have our revenues growing. So, we should get better and better margins.

Eric Wright
Okay. That's great. Thanks a lot, Mark.

Operator
Thank you. As a reminder, ladies and gentlemen, that's star one to be placed in the question queue. Our next question today is coming from Jeff Feinberg with Feinberg Investments. Your line is now live.

Jeff Feinberg
Thank you very much. Nice job, guys. I just want to make sure—it look to me like you did beat the consensus revenue. I think you mentioned in the prepared call. What was that coming in? I know we did a little over nine (sp).

Mark Attinger
Looks like it was 8.98 million as what we saw on a couple of sites that took a composite of the four analysts that cover us.

Jeff Feinberg
That's what I got, too. Okay, great. With regard to the margin profile, couple people asked about, I like to look at it this way. The incremental EBITDA margin this particular quarter was 70%, $0.70 every dollar dropped through, and for the nine months it's 50%. Can you provide more perspective with the mix shifting towards the higher margin business overtime PaySign premier and (unintelligible) opportunities, how we can think about incremental margins for next year?

Mark Newcomer
Yeah, that's a good question. Let me just kind glance over at the models and take a quick look at it. I think that we will see, probably, things settle in that 60% range on a gross margin basis. We got to get a better read on exactly how well we're seeing conversion on the premier card, and there's a number of factors in the premier card that affect the gross margin on that products. We're going to get some learning's on that. We have a number of new pharma programs that just went live that we want to see how those perform. We have a really good read, obviously, on plasma, and then were also looking at some other corporate incentives programs that we'll need to factor in, as well. So, there's a number of dynamics here, but I think probably on a go forward basis, at least into 2020 as premier card comes on, kind of a tweener between the pharma gross margin and the plasma gross margin. I think you'll see it around 60%. I don't think you'll see that level in the fourth quarter, and, again, I don't believe will be a 59.6% where it was this quarter.

Jeff Feinberg
I'm referring to the incremental EBITDA margins. I understand completely on the gross margin, but for every dollar of revenue this particular quarter, $0.70 will flow through to the EBITDA, for the nine months its $0.50. It sound like the way to think about next year, that the incremental

EBITDA should probably be somewhere between maybe 60% or so. So, hypothetically, the analyst are right, we grow the 60 million in revenue up from 25 million incremental revenue. 15 million or so, that would that would flow through. Is that the way to think about it?

Mark Attinger
Yeah, I think that's fair, if you look at our full year EBITDA margins this year, right, we're looking at--on adjusted EBITDA, at least through the third quarter, we did 36%. We'll see that taper in the fourth quarter and finish probably closer to 30% on a full year basis. So, when you look to next year, that still look like a reasonably good composite on a full year basis.

Jeff Feinberg
Pretty exciting. If I do the math, it gets just mid20 in EBITDA, and I really appreciate the time. Thank you.

Mark Attinger
You bet.

Operator
Thank you. We reached end of our question-and-answer session. I'd like to turn the floor back over to management for any further or closing comments.

Mark Newcomer
Thanks, Kevin. Again, we're very pleased with this quarter and with our progress overall. And we continue to focus on building a world-class payments company. We appreciate your listening and for participating in this update and have yourselves an outstanding week.

Operator
Thank you. That does conclude today's teleconference. You may disconnect your line at this time and have a wonderful day. We thank you for your participation today.