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# CoreCard Corp. (CCRD)

Q2 2022 Earnings Call



## CALL PARTICIPANTS

### Executives

**James Leland Strange**

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*CFO & Corporate Secretary*

### Analysts

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## MANAGEMENT DISCUSSION SECTION

**Matthew A. White**

*CFO & Corporate Secretary*

Good morning, everyone. With me on the call today is Leland Strange, Chairman and CEO of CoreCard Corporation. He will add some additional comments and answer questions at the conclusion of my prepared remarks. Before I start, I'd like to remind everyone that during the call, we will be making certain forward-looking statements to help you understand CoreCard and its business environment. These statements involve a number of risk factors, uncertainties and other factors that could cause actual results to differ materially from our expectations. Factors that may affect future operations are included in filings with the SEC, including our 2021 Form 10-K and subsequent filings.

As we noted in our press release, our second quarter results were in line with our expectations. Our professional services revenue remained strong. We saw sequential and year over year growth in processing and maintenance. And as expected, we had license revenue for the quarter of \$1.8 million. Total revenue for the second quarter of 2022 was \$15.2 million, a 14% increase compared to the second quarter of 2021. As a reminder, we recognized approximately \$600,000 of maintenance revenue from our former customer, Wirecard, in the second quarter of 2021. Excluding the one-time impact of this revenue in the second quarter of 2021, revenues grew 19% in the

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second quarter of 2022 compared to 2021. The components of our revenue for the second quarter consisted of license revenue of \$1.8 million, professional services revenue of \$7.6 million, an increase of 25%, processing and maintenance revenue of \$4.5 million, an increase of 8%, and third party revenue of \$1.3 million. We continue to onboard new customers both directly and through various partnerships we have with program managers such as Deserve and Vervent. We currently have multiple implementations in progress with new customers that we expect to go live in the coming months. We are working on launching a new program with an existing customer, Cardless, on a co-branded card with American Express. Once live, we'll have a direct connection with American Express similar to what we have with Visa and MasterCard today and we will be able to process other customers who want to use the American Express Network.

We say this a lot, but as a reminder, there are always several parties involved in implementations other than the issuer processor, including banks, networks and other third-party service providers. Issues with any one of these can cause delays in a program launch.

As I mentioned, processing and maintenance revenues grew 8% in the second quarter of 2022 compared to the second quarter of 2021. From the recently added customers mentioned above who are now live and continued growth from existing customers. Processing and maintenance growth over the same periods was 26%, excluding the Wirecard impact discussed earlier.

Revenue growth, excluding our largest customer and excluding the impact of Wirecard, was 30% in the second quarter of 2022 compared to the second quarter of 2021. One thing to note about our revenue from Goldman Sachs, they closed on their acquisition of GreenSky at the end of the first quarter of 2022. GreenSky was an existing customer for us for a portion of their business and starting in the second quarter of 2022, these revenues are now included in the "Customer A" total in our quarterly and annual filings.

Turning to license revenue, we recognized another license tier in the second quarter of 2022, as expected, resulting in \$1.8 million of license revenue for the second quarter. We do not expect a new license tier in the third quarter, but could achieve a new tier in the fourth quarter of 2022.

Professional services revenue remained strong in the second quarter. We anticipate professional services revenue in the third quarter in the range of \$6.7 to \$7 million. We consider this revenue to be repeating as evidenced now by four plus years of significant growth in professional services. However, there are still fluctuations quarter to quarter, and we can still have both positive and negative surprises from what we expect although we don't anticipate any huge surprises either way.

Turning to some additional highlights on our income statement for the second quarter of 2022. Income from operations was \$3.5 million for the second quarter 2022 compared to income from operations of \$3.9 million for the same time last year. Our operating margin for the second quarter of 2022 was 23% compared to an operating margin of 29% for the same time last year. The decrease is primarily driven by lower license revenue and continued hiring in India and in our Colombia office that we opened in October 2021.

Our second quarter tax rate was 23.9% compared to 26.3% in the second quarter of 2021. Earnings per diluted share for the quarter was \$0.33 compared to \$0.32 for Q2 2021. We remain incredibly optimistic about our long-term prospects and believe the investments we've made in our infrastructure and in hiring and training new people will continue to yield new customer wins and revenue growth.

Due to our solid performance during the first half of 2022, we are confident in top line growth expectations of at least 30% for fiscal 2022 compared to our previously provided guidance of a range of 25% to 30%. The opportunity ahead of us is significant and CoreCard remains a growth business focused on meeting the evolving

needs of modern issuers while generating long term value for our shareholders.

With that, I'll turn it over to Leland.

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### **James Leland Strange**

*Chairman, CEO & President*

Okay. Thanks, Matt. I guess I should comment first on the increase in top line growth estimate for 2022, where you moved it up to 30%, at least 30% from 25% to 30%. But I'm going to hold that to the end. Let me emphasize and expand on several things that Matt said, because I want to be certain that we understand the importance. He mentioned that in the previous year we booked approximately \$600,000 in revenue from Wirecard. And in this quarter we had none from Wirecard. That is revenue that we had to make up in order to grow about 14%, which we did. As Matt said, 19% growth after factoring that in.

Now it's not okay to play the numbers like I just did it, if in fact you lost the business. We often get asked by new potential investors to talk about customer losses or churn as it's typically characterized. CoreCard has not experienced any customer losses that I can remember over the last 10 years where the customer decided to go to a competitor or even go use their own internal software. Wirecard, for those who do not know the history, was a German public company that had been, I think, market valued at \$27 billion at its peak. It was called Europe's greatest FinTech. They were a bank and their primary business was the acquiring segment of the payment space. They had licensed and were using our issuing software for the Middle East. It turned out that they were a house of cards. Their major auditing firm had been hoodwinked and they crashed into bankruptcy and criminal charges were filed against the executives. And they're still prosecuting those cases. So we lost that business which was actually extremely profitable and is slowly disappearing from our comparables.

I'll also mention Greensky who was and is a customer that's been acquired by Goldman Sachs. We believe the vertical portion of the business that they use CoreCard for will probably be discontinued, and that's just my best guess. But it's another hole that we'll need to build to maintain growth. Fortunately, it's not nearly as large as the Wirecard business was, so will also be easier to backfill and probably take a longer period for them to go from where they are to zero as they – if and as they would wind down.

I guess the last one I will mention is Kabbage. Kabbage was a very significant customer and they sold their business for I think around \$800 million to American Express. The legacy customers were not part of the sale. So we continue to service and receive income from the old Kabbage, but eventually that also is likely to go to zero. On the other hand, we've picked up American Express as a processing customer to process their small business offering, utilizing the customized software we developed for Kabbage. I guess I probably should not have said customized, it's really the heavily parameterized standard CoreCard offering that allows AMEX to do things they cannot do easily with their own software. So when you ask us to tell you the customer we've lost, the message can get confused if we were to say no longer service WireCard, Greensky, or legacy Kabbage. Well, it may be true we did not lose the business due to a better offering either internally or to a competitor. So we typically lose no business to churn, but we do have to sometimes fill some revenue holes. I can just want to clarify that because we talk about the business being sticky and we believe it is really sticky.

Another comment I want to expand on is the upcoming launch of a card with the American Express logo. You all know that American Express is both an insurer as a bank and a processor for the AMEX card. They have what we call rails with merchants similar to the rails of MasterCard and Visa. Historically, AMEX was the only processor that could process the AMEX card. But due to all the new FinTech offerings, AMEX does not want to be left behind, and they need processor partners that can meet the requirement of new innovative cards as well as respond quickly. We're all familiar with the Delta AMEX Card. It is issued and processed by AMEX, but the

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Cardless program that we'll be using for the AMEX card will be processed by CoreCard. We have several other programs lined up. We're going live either late this year or early next year, and a couple of those are with AMEX logo on them. All are small in the beginning and all hope to eventually be large. Some will successfully grow into large programs and some will not. None of us are smart enough to predict in advance which will be the big ones or which will not. So we take a chance by investing resources to get them into the market. I think we often remind the investment market that we took the chance with Kabbage and it became one of our top 3 revenue generators in the past quarters. And we took a chance on a small company called Final, which actually did not succeed as a card program, but was helpful in our eventual relationship with Goldman Sachs, which actually bought Final.

Another topic that's often tabled concerns naming or doing press releases on our customers. We believe it's up to our customers to tell the world what they want to tell them about their business. It's not up to us as their vendor. We generally don't do that, but we do make exceptions either because we feel it's in our customer's best interest or maybe they want us to, or because of a regulatory requirement. We previously named Deserve as one of our best and I always use the word esteemed customers. Deserve serves as a program manager for several name brand card programs and they use CoreCard as their primary credit processor. Deserve has many things CoreCard does not have such as customer service and they offer other services that compete with what we offer. But they're very good and very knowledgeable in the credit space, particularly in origination and they provide great value in the card issuing chain. Together, we're pretty formidable as we can do the more complex credit offerings that many of their customers want. They're private and, at least before the general valuation meltdown, they had reached private capital for some of the more sophisticated investors, as well as some other industry players at very high valuations.

One of our other long term licensees that I don't know that we've named in the past, but I think it's okay to mention, is a New York company called PEX. Again, a well run company that has a particular niche market in what I would call commercial card light. Another licensee is AmerisourceBergen who purchased one of our licensees and now has a specialized pharmacy card. The company they purchased was our first licensee many years ago that's undergone many transitions before being purchased.

I have previously mentioned Gemini, which is one of our customers. And I guess after mentioning some of these customers I can guess and I'll probably be asked in future calls, "Well, how's the Gemini Card doing" or "how fast is the Cardless AMEX card growing?" And I'll tell you, you can project my answer now. I'm not going to be talking about someone else's business growth. You need to ask them and we'll only talk about a rollup number and we'll tell you what the expected growth percentages are for the group. Based on history of what we see happening, knowing some will undershoot and some will outperform. And hopefully, we've averaged the number for our growth projection. For those uncomfortable with that I think I can safely say that our rolling projections of the company's average growth rate each quarter for the past four years has been pretty reliable when you look at our projections.

And I'll go back to one other area of Matt's comments, and that's gross margins. I stated in 2019 that I believed that our goal was to grow at a 20% to 25% average annual growth rate over the next five years. And I said we should do that while remaining profitable. That continues to be our goal. Our operating margin is lower in the second quarter, and that's not our marker that one can use for future predictions. The margins will vary for many reasons, including the amount of license revenue recognized in a particular quarter and also investments that we make for growth. There are companies in the FinTech space that prioritize top line growth over profits, believing it's a land grab contest. Whether they're right or wrong can't really be determined at this point. But I believe the right answer is in the middle. CoreCard has and will continue to balance top line growth with profitability. We believe that this is a better benefit for shareholders, of which I happen to be a large one rather than going all in for top line revenue growth. We could buy business and grow top line much faster, but we would not be able to provide the premium service which we currently provide our customers. So our focus will continue to be moderate,

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I guess moderate if you consider 20% to 25% to be moderate, growth and have reasonable profits that allow us to continue to invest to stay on the course. And no matter where we indicated, we expect to grow at least 30% this year. I just don't want that to be the ongoing target as part of that growth comes from a healthy, larger contribution of license revenue that I don't see repeating in the next couple of years. You notice, as I said, next couple of years, I didn't say it wouldn't happen again. We continue to expand on our very robust revolving credit software platform and the potential for other very large licensees does loom in future years. At the present time, we have two focuses: continuing to grow our processing businesses and provide the very best services possible to our largest customer and their processing customers, while simultaneously investing in developing the next product to our platform for the future and expanding our trained employee talent base. I think let me stop there and just take any questions that we may have.

## QUESTION AND ANSWER SECTION

**Operator:** Thank you. [Operator Instructions] Our first question is from Mark Palmer with BTIG. Please proceed.

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### **Mark Palmer**

*Analyst, BTIG LLC*

Q

Yes. Thank you and good morning. If you can provide a little bit more color at a granular level if possible with regard to professional services revenue. Certainly appreciate the guidance that's provided each quarter and understand the recurring nature of this. But it would be helpful to understand what are the drivers of the changes from quarter to quarter in professional services revenue and to what extent is that correlated with increased license revenue for example?

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### **James Leland Strange**

*Chairman, CEO & President*

A

Yeah. I'll take the first shot and let Matt weigh in. It – It's really – It's probably really hard to correlate it with license revenue. I've seen where you're coming from there. But see things can – it could be higher simply because one of our either license or non-license customers wants to do a lot of specialization, customization or use more of our services for a future product. That doesn't necessarily mean that we'll get more license revenue from it. It could mean that, but it doesn't necessarily mean that. I think the license revenue is more driven by how much promotion and marketing our customers put into growing their portfolio rather than what we're doing. Now, there is a caveat. Obviously, if you have a very large customer coming on and it takes a year of extra professional services to get them ready, that could be a driver for that. But often when that happens, if it's a license customer, they tend to back off with some of the other stuff they're doing, so you don't get the full impact of it. So I'd say, Mark, it's really hard to use that as a predictor. Matt, you want to...

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### **Matthew A. White**

*CFO & Corporate Secretary*

A

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Yeah, yeah, I think the idea from our customers that are demanding new features or new functionality for their customers is that that would result in new sign ups. But it's – it doesn't always translate into new active accounts that would then translate into new license revenue.

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### James Leland Strange

*Chairman, CEO & President*

A

It may be. It may be they have to do that just to continue to expand with their current rate they're expanding at, right?

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### Matthew A. White

*CFO & Corporate Secretary*

A

Right. Yeah. It could just be keeping up with the market.

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### Matthew A. White

*CFO & Corporate Secretary*

A

It could be something new that drives growth, but it's hard to translate that directly. But, if our customers are growing, we expect to continue to have strong license revenue, I mean strong professional services revenue. So, it's an indication of at least expected future growth.

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### Mark Palmer

*Analyst, BTIG LLC*

Q

Thank you. And one more question. Could you give us an update on the roadmap with regard to building out your platform, the next version of your platform, where you are in that process, and how you were thinking about the cadence of investment during the balance of 2022 and then beyond that?

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### James Leland Strange

*Chairman, CEO & President*

A

Yeah. Well, software is a little bit of a moving target, of course. I wish I could tell people to a lot more, but it's always a moving target. So we're really, really investing in two things. We're investing in a totally new platform. I say, totally new. We'll use part of it in the old. But we're also continuing to work on the, gosh, I hate to call it an old platform, but the current, let's call it in the current platform. We still have to continue to make changes with the current platform, so we're really spending on both sides. I don't know how to quantify that in terms of dollars. It really – a little – goes back a little to my comment when I talked about operating margin. We're just going to keep

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doing what we need to do in order to grow the top line at a very profitable basis over the long term. Matt, could you granularly say anything more on that? It's hard to...

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### Matthew A. White

*CFO & Corporate Secretary*

A

The amount we're capitalizing is – hasn't been that significant. And but there is a – an impact on R&D expense for the amount we're not capitalizing. So there's certainly been incremental costs. And, those will continue to be at a similar pace in future quarters to what they've been so far in 2022.

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### James Leland Strange

*Chairman, CEO & President*

A

And even, Mark, it even gets more confusing both for us and probably more so for you, and try to analyze it in the sense that some of the expense on the current platform is paid for by a customer as part of professional services so both we have expense on it, some of professional services are paying for current platform changes, and then we incur all of it, 100% of what I'd call the future platform.

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### Mark Palmer

*Analyst, BTIG LLC*

Q

Very good. Thank you very much.

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### James Leland Strange

*Chairman, CEO & President*

A

Thanks, Mark.

**Operator:** Our next question is from Anja Soderstrom with Sidoti. Please proceed.

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### Anja Marie Theresa Soderstrom

*Sidoti & Company, LLC*

Q

Hi. Thank you for taking my question and congratulations on a great quarter. Can you just talk about how the buildup of the teams in India and Colombia is going and sort of how the labor market is there for you?

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### James Leland Strange



A

Sure, glad to. The good news is that I think we're coming up to speed pretty well where we want to be in terms of India. Not quite there, but pretty close. Things have gotten a lot looser. We're able to hire a whole lot better. We've got a bunch of interns, maybe as much as a couple of hundred interns there that, so we're growing our base there for – to take care of our future revenue, that we will have to be looking for more space there, I think, before long and figure out what we're going to do there in terms of the campus. So, the India team is growing and doing real well. Still getting the turnover that is a little higher than I would like to have. I'm kind of hoping some of that might also settle down in the next couple of months as the markets settle down, but generally it's good. Now, Colombia, likewise, we have about 30 people there. What are the difficulties there? And one of the things that affects our current operating margin is that we expected to use them a lot for our largest client. And because it's Colombia, we've had problems getting approval based on technical risk to use them there. So we're not getting the output from them in terms of billable or I guess that's the best way to say...

Q

Revenue generating. Yeah.

**James Leland Strange**

*Chairman, CEO & President*

A

These are not generating revenue for us, but they're getting trained well. And we'll transition them more to our current processing environment if we have to. We'll probably slow down hiring a little bit. We'll continue to expand some. It's been fairly expensive there more than what I anticipated. We do send our India team also to Colombia to help train. That's also been a lot more expensive than we anticipated. I – it was hard for me to believe that airline tickets are \$3,000 between India and Bogota right now. And that's what we've been paying recently when we send folks there. So we're going to slow that down. But generally, we're very pleased that we're – I think we're finally getting a good bench and we'll have a good trained group of people for, in the next six months, they'll allow us to give some larger customers the confidence that we can take care of them.

**Matthew A. White**

*CFO & Corporate Secretary*

A

And one thing to add on that for the interns just to clarify, we're not including those in our numbers, in our 10-Q filing since they're not full-time employees. But once they become full-time employees, if we do decide to make them a full-time offer. We'll include them in the total.

**James Leland Strange**

*Chairman, CEO & President*

A

So you'll see some big jumps in terms of our employee base in India.

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**Anja Marie Theresa Soderstrom**

*Sidoti & Company, LLC*

Q

Okay. Did I hear you right that you're planning a use in Colombia for your largest customers?

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**James Leland Strange**

*Chairman, CEO & President*

A

Well, we had intended to use them primarily for largest customer. But because of the perception of the – what we call tech risk working out of Colombia, we've had a difficult time getting it approved. So, we are probably going to transition them more to our own processing platform over the next six months. Right now, they're in training anyway, so you're not going to get any revenue generation from them. We'll have to do some other things for our largest customer. And actually...

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**Anja Marie Theresa Soderstrom**

*Sidoti & Company, LLC*

Q

But that would be for your existing largest customers, right?

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**James Leland Strange**

*Chairman, CEO & President*

A

Yeah.

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**Anja Marie Theresa Soderstrom**

*Sidoti & Company, LLC*

Q

Anticipated larger customer.

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**James Leland Strange**

*Chairman, CEO & President*

A

Yeah. I'll go – Yeah, I'll go a little further on that. We're actually moving about several, half dozen or so folks from the India office to the US side. So you'll see our US payroll go up as a result of obviously a different compensation plan. So the moves – the movements of our key people here is also probably primarily for our largest customer.

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**Anja Marie Theresa Soderstrom**

*Sidoti & Company, LLC*

Q

Okay. Thank you. And how I'm – is there any color you can give on how the discussions are going with other Is there any color you can give on how the discussions are going with other potentially large customers. How – has the sentiment sort of changed due to the economic environment or?

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**James Leland Strange**

*Chairman, CEO & President*

A

There's really been no change. There are discussions about things around a couple of years away from the – from our standpoint on our processing environment. I think it's interesting also, and I'll just quote it here, what happened in the Goldman Sachs earnings conference call a few days ago. I think there was a question asked David Solomon – I'm going to pull it up here said, "Hi. Good morning. I know you've got Greensky in the belt, a General Motors card out, Apple is doing gangbusters, so I just wanted to get a sense from you about how you're thinking about other opportunities." And his answer was, "There's a lot of partnership opportunities and lots of people coming to us, given our relationships, our technology, et cetera. They're interested in doing things with us at some point, we've done a bunch in the course of the last five years to build this business, and as we said, we put a couple of big partnerships on the ground in cards. I think our intention at the moment should be focus on integrating these successfully and making sure we execute at a very high level. Certainly as we get out to 2023 and 2024 we'll be more open to other partnerships." So that's kind of a quote from David Solomon. And I would say, we kind of say the same thing is that we've done a whole lot and our intention at the moment is to focus on making sure we execute at a very high level.

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**Anja Marie Theresa Soderstrom**

*Sidoti & Company, LLC*

Q

Okay. Thank you. That was all for me.

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**Operator:** Our next question is from Khadir Richie with Ritchie Capital Group. Please proceed.

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### **Khadir Richie**

*Ritchie Capital Group*

Q

Hi. Good morning, Matt and Leland. Congrats on a good quarter. Just had a couple of questions for you. And they're more forward facing, big picture questions. You know, I love the investments that you're making on infrastructure and the near-term visibility that you have and the new offices that you're building out. And I was just wondering, how do you think about the business, you know, longer term in terms of increasing the recurring revenue streams that you have that are predictable and possibly reducing some of the lumpiness, as well as the customer concentration. How are you thinking about balancing those or achieving those types of goals in addition to, you know, remaining profitable? How do you think about that?

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### **James Leland Strange**

*Chairman, CEO & President*

A

Well, I think about it sort of as two separate businesses in a way that I want to grow both of them as – as quickly and as – as responsibly as I can. So in terms of diversification of – from a concentration, I don't know that we're going to do that for a long time because I want to grow that business. It's a – it's a good business. It's a star customer. And I just want to do what I can and then focus our resources to make sure they're happy and do what we can do with them. At the same time, I also want to grow the other side of the business, but I'm not – I'm not optimistic and I'm certainly not sad either about the fact that I don't think I can grow the other side of the business much faster than I can grow the concentrated customer side of the business. It'll grow a little faster, perhaps because it's smaller. So at this point, you'll see higher percentage growth. But I want to grow on both sides. It's – it's just a good business, you know, it's the kind of customers we have. A lot of people would pay a lot of money to get those kinds of customers. And we're not going to do anything that would disrupt that. So I'm going to give them my – my attention just like – just like I just quoted you David Solomon said he was going to give his the kind of customers he's got, his best attention. We're going to do the same thing. So I wouldn't – if I would – I just would not focus alone on the fact that our concentrations is going to go down below 50% from our largest customer, I don't think that's going to happen for several years, because I think they're going to grow.

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### **Khadir Richie**

*Ritchie Capital Group*

Q

Okay, thank you. And the other question I had is, you know, as you think about your longer-term projection from 2019 of that 20% to 25% growth. If you were to significantly deviate from that growth trajectory in any sort of way, what would be the causes of that?

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### **James Leland Strange**

*Chairman, CEO & President*

A

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Good question. And certainly Matt, we're looking at each other thinking...

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## Matthew A. White

*CFO & Corporate Secretary*

A

There's a lot of different ways you can deviate from that significantly if we fail to execute certainly we'd deviate in a negative way. And if we were to get, as we said before, we got lucky with our current largest customer, if we were to get lucky again and – and land a big one, maybe we'd have...

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## James Leland Strange

*Chairman, CEO & President*

A

A little faster growth, but you – you're still limited by numbers of people.

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## Matthew A. White

*CFO & Corporate Secretary*

A

Right.

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## James Leland Strange

*Chairman, CEO & President*

A

Nobody grows without any people no matter what they talked about scalability. I'm sure we scale. I think we've proven that really well. I've got other statistics that kind of show that. But I don't really see anything that could significantly cause a deviation from that. I'm wanting to get a little more focused on the next five years. I am not ready to go there yet, so I'm still thinking just the next few years at this point. I think we need to probably put up another pretty good sized customer under our belt on our own processing to be able to get a better projection say over a longer term. But right now, I am pretty comfortable. I am real comfortable with that.

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## Khadir Richie

*Ritchie Capital Group*

Q

Okay, great. Thank you both. Congrats again.

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## James Leland Strange

*Chairman, CEO & President*

A

Thanks.

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**Operator:** Our next question is from Avi Fisher with Lancaster Advisors. Please proceed.

**Avi Fisher**

*Lancaster Advisors*

Q

Hi, Leland. Hi, Matt. Thanks for all the good work you're doing. It sounds like and from reading the Q and other people sort of asked about this. You are investing ahead and you've grown your employee base quite significantly and staff to 2x over the last two years to over 900 employees. It sounds like some of them aren't really allocated to generating revenue yet. And I wonder if you could sort of estimate what portion of that is still sort of not at scale revenue yet?

**James Leland Strange**

*Chairman, CEO & President*

A

I would have no way of trying to estimate percentages or numbers there. But it's absolutely true that a good number is not going to be generating revenue yet. And I mean I should stick to the business view, it takes several years for to be able to generate good revenue from the training that we give them. I hope we end up with a bench at some point that would give a large customer at some point that would give a large customer comfort that we could take care of it. And so – so if you're in that with a bench like that, you're going to end up with, you know, a 150 people that are not generating revenue, but they're doing things, but they're not generating revenue. They may be simply shadowing other people who are doing revenue. They may be, and it may be a different kind of allocation. You may have – you may have people working, you know, 20 hours in – in revenue and 20 hours not generating revenue. And so it's just – you just can't clear cut that.

**Avi Fisher**

*Lancaster Advisors*

Q

Okay. Ask another way, what could – you know, your service is gross profit margins were at one point in the 50% range, and they've dipped from that because of these investments, do you expect to get back to 50% – north of 50% over the long term?

**Matthew A. White**

*CFO & Corporate Secretary*

A

Yeah, gross profit margin. We focused more on operating margins. So, you know, we think, you know, something closer to, you know, high 30s, 40%, somewhere in that range. You know, there was a lot of overtime involved in – in getting to those 50% margins back, you know, several years ago. And as Leland said, that's not very sustainable for our people. And, you know, so, you know, getting back to that point, but – but then the business will be a lot different in the future. You know, the – the processing revenue will be a higher percentage of the total and it's still kind of too early to determine what the margins are on that. So, you know, it's really – it's really just too early to focus on too much on margins. But, we're going to stay profitable as we've – as we've said.

**James Leland Strange**

*Chairman, CEO & President*

A

Yeah, we're – I'm not trying to target that. I'm trying to stay reasonably profitable and growing the business for the long term.

**Avi Fisher**

*Lancaster Advisors*

Q

And okay. So I guess, I can't nail a number down with you. And it was just my best effort to understand because with the – if you just sort of apply that 50% gross profit margin to your current COGS, I mean you would be on track for services revenues of north of \$60 million a year. And I just – is it safe to assume you have your target on a higher number than that?

**James Leland Strange**

*Chairman, CEO & President*

A

No. I mean at some point. Yeah, but not short term. I mean your gross margins, I mean how much license revenue do you have in calculating that? I mean it's just distorting the heck out of it.

**Avi Fisher**

*Lancaster Advisors*

Q

Just looking at the services gross margins which is all I have, all I can look into. But at 30% to 40% operating income, we can infer where this could look like down the road?

A

Yes, the long term.

**Avi Fisher**

*Lancaster Advisors*

Q

All right. And then just finally – and I think you may have talked about this earlier. But are you – It sounds like you're expensing your equipment and not capitalizing it.

**Matthew A. White**

*CFO & Corporate Secretary*

A

We capitalize certainly anything that's hardware. For software, it kind of depends on the accounting rules. And so there is a portion of our software that's capitalized.

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**Avi Fisher**

*Lancaster Advisors*

Q

And that's running through COGS also.

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**Matthew A. White**

*CFO & Corporate Secretary*

A

Well, the depreciation would run through COGS when the platform is live. So for example, the new platform we're working on, we haven't started depreciating that because we haven't started using it. So that's – any costs that are capitalizable, we are capitalizing and then ultimately when we start depreciating it when it goes live that are run through COGS and depreciation expense.

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**Avi Fisher**

*Lancaster Advisors*

Q

I mean just to clarify the 10Q I think called out that COGS was – had increased, cost of revenues increased because of investments in infrastructure. So I assume that was hardware.

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**Matthew A. White**

*CFO & Corporate Secretary*

A

So, infrastructure investments is more along the lines of equipment for increased processing power. And so the depreciation related to that would go through COGS.

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**Avi Fisher**

*Lancaster Advisors*

Q

So not necessarily this quarter's purchases, but prior quarter's purchases and that related depreciation?

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**Matthew A. White**

*CFO & Corporate Secretary*

A



Yeah.

**Avi Fisher**

*Lancaster Advisors*

Q

Got it. Thanks so much. Really appreciate it.

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A

Yeah.

**Avi Fisher**

*Lancaster Advisors*

Q

Talk soon.

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**Matthew A. White**

*CFO & Corporate Secretary*

A

Thanks, Avi.

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**Operator:** We have reached the end of our question-and-answer session. I would like to turn the conference back over to Leland for closing comments.

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**James Leland Strange**

*Chairman, CEO & President*

A

Okay. Well, we – there was a couple of questions in here. Let me touch on one. One shareholder asked about the GM conversion, and I can't really speak for what other people say about the success of it. We consider it – but they want to know kind of how people feel about in the industry. I would believe – I believe the industry would probably say it was very, very successful. We think it's successful. Given what we know about conversions, I've got very long history to understand how big a disaster the conversions often are. I mean that's really one of the things that we think we're really very good at is conversions. So I will just try to answer to that extent that we think it went very well. So with that answer – with what the answer to that question, we'll go ahead and close the call. We thank all of you for being on the call and hope that you're satisfied with the way your investment is going. And we're going to continue just trying to execute at a high level. Thank you very much.