

Information Services (ISC)(Q1 2023 Earnings)

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Corporate Speakers:

- Jonathan Hackshaw; Information Services Corporation; Senior Director of IR & Capital Markets
- Shawn Peters; Information Services Corporation; President & Chief Executive Officer
- Robert Antochow; Information Services Corporation; Chief Financial Officer

Participants:

- Scott Fletcher; CIBC; Analyst
- Jesse Pytlak; Cormark Securities; Analyst
- Stephen Boland; Raymond James; Analyst
- Trevor Reynolds; Acumen Capital Finance Partners; Analyst

PRESENTATION

Operator^ Welcome to the ISC Q1 2023 Earnings Conference Call and Webcast. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Jonathan Hackshaw, Director of Investor Relations and Capital Markets. Please go ahead.

Jonatan Hackshaw^ Thank you, [Antoine], and good morning to everyone joining us today. Welcome to ISC's conference call for the first quarter ended March 31, 2023. On the call today with me are Shawn Peters, President and CEO; and Bob Antochow, Chief Financial Officer.

This morning, Shawn will take you through some of the highlights of the quarter and Bob will then provide some financial (technical difficulty) will to speak to some refinements to certain metrics before passing the call back over to Shawn for some closing remarks.

Before we begin, we would like to remind everyone that we will only be summarizing results today. The company's financial statements and MD&A has been filed on SEDAR and are available on our website. We encourage you to review those reports in the entirety. I would also like to remind you that any statements made today that are not historical facts are considered to be forward-looking statements within the meaning of applicable securities laws. The statements may involve a number of risks and uncertainties that are described in detail in the company's SEDAR filings. Those risks and uncertainties may cause actual facts to differ materially from those stated.

Today's comments are made as of today's date and will not be updated except as required under applicable securities laws. Today's conference call is being broadcast live over the internet and will be archived for replay shortly after the call on the Investors section of our website.

I would now like to turn the call over to Shawn.

Shawn Peters^ Thank you, Jonathan, and good morning to everyone joining us for today's call. Our start to the year has been positive and in line with our expectations. The acquisitions we completed in 2022 made a positive contribution to our performance, more than offsetting the expense of contraction in the Saskatchewan market. Our services business is well diversified and continues to grow organically even in the face of changing Ontario Business Registry dynamics.

For our Technology Solutions business, as we've described in our previous conference calls, we've seen a return to procurement activities by clients and jurisdictions. As a result of our success in those activities, I'm pleased that during the quarter, we were active on 2 new exciting contracts. The first is an implementation of an integrated registry [platforms for the Government of] Cyprus, and the second is the next phase, an online Register of cCharities and Non-Profit organization for the States of Guernsey.

We also noted that we completed the development of corporate registry technology for Bonaire, Sint-Eustatius and Saba (technical difficulty) as a service offering. The Cyprus project will deploy the RegSys platform, a complex and significant government department, the Department of Registrar Companies and Intellectual Property and is expected to revolutionize registry operations for the Government of Cyprus, bringing significant productivity increases, regulatory compliance and streamlined user experiences for individuals and companies who interact with these registries.

Total value of the contract to ISC over the life of the project is EUR 5.7 million or approximately CAD 8.4 million. On the Guernsey project, in late 2022, the States of Guernsey launched the first phase of the online Register of Charities and Non-Profit Organizations to the public, operating on the RegSys solution and transforming the way charities interact with the States of Guernsey.

That first phase of the project is an important milestone for Guernsey as registers will be used by Guernsey to demonstrate the compliance during the imminent MONEYVAL evaluation, which is an examination of measures taken in the financial, regulatory and criminal justice sectors to combat money laundering and terrorist financing in the European Union.

The second phase of the project began in the first quarter of 2023, bringing the corporate beneficial ownership and Intellectual Property registers onto the new RegSys platform to provide an integrated solution for the States of Guernsey. The total value of the 2-phase projects, including implementation and support and maintenance, is expected to be GBP 7.7 million or approximately CAD 12.9 million.

The revenue for these projects will be recognized in 2023 or begin to be recognized in 2023 as we deliver services against the contract. And as we've indicated previously, we're excited about the opportunity for our technology solutions business as the market continues to return to normal, and we continue to see this increase in procurement activity.

As an organization, we continue to focus on the delivery of our services and customer satisfaction while ensuring (technical difficulty). As always, we look for growth that is complementary or adds additional or new competencies to our existing business, [outside] of diversifying our revenue streams. The results for this quarter and the impact of our acquisitions in 2022 are a demonstration of the success of this strategy.

I'll now turn the call over to Bob to discuss some financial highlights before providing some closing thoughts.

Robert Antochow^ Thank you, Shawn, and good morning to everyone. As Shawn said, our 2022 results were in line with our expectations, considering our exceptional 2021 and the economic tightening that occurred in 2022. This performance was driven by a number of factors, but more specifically, revenue was \$49.1 million for the quarter, an increase of \$4.9 million or 11% compared to the first quarter of 2022 due to revenue from Registry Operations, new Property Tax Ontario Assessment Services division following the acquisition of Reamined Systems in June 2022.

Continued growth in transactions and customers in the services segment also contributed to the overall increase in revenue over the prior year. This was partially offset by a decrease in the Saskatchewan Land Registry revenue as transaction volumes trended toward pre-pandemic levels. Net income was \$6.9 million or \$0.39 per basic and \$0.38 per diluted share compared to \$7.4 million or \$0.42 per basic share and \$0.41 per diluted share in the first quarter of 2022. The decrease in net income results from higher amortization related to intangible assets arising from acquisitions in 2022 as well as higher net finance expense.

EBITDA was \$14.7 million compared to \$13.8 million in the first quarter of 2022, primarily driven by increased EBITDA in Registry Operations and services and a decrease in share-based compensation compared to the prior year quarter. EBITDA margin was 29.9% for the quarter compared to 31.3% in the first quarter of 2022. The change in margin year-over-year was largely due to the return of the Saskatchewan land registry volumes to pre-pandemic levels, accompanied by reduced EBITDA in Technology Solutions, partially offset by the decrease in share-based compensation due to the decline in the company's share price during the quarter.

Adjusted EBITDA was \$14.5 million for the quarter compared to \$14.6 million in 2022. Adjusted EBITDA margin was 29.5% compared to 33% in the first quarter of 2022. The change in margin year-over-year is largely due to the return of the Saskatchewan Land

Registry volumes to pre-pandemic levels, accompanied by reduced EBITDA in Technology Solutions.

Free cash flow for the quarter was \$10.1 million, flat compared to the first quarter of 2022 due to slightly higher cash provided by operating activities net of changes in working capital, offset by increased interest expense.

I would also like to note that commencing January 1, 2023, following a review of comparative financial information and practices by other publicly traded companies, ISC elected to refine its definition of free cash flow to present ISC's free cash flow on a levered basis. As such, free cash flow now includes interest received and paid, interest paid on lease obligations and principal repayments on lease obligations.

The impact of this change to free cash flow in the prior period was a \$0.9 million decrease in the previously reported amount of \$11 million. We believe this will help provide a clear picture of our free cash flow position for shareholders in the market.

Turning now to our balance sheet. With respect to our debt, as at March 31, 2023, the company had \$56.1 million of total debt outstanding compared to \$41 million as of March 31, 2022. During the quarter, we made a \$10 million voluntary prepayment against our revolving facility due to excess cash and a [rising] interest expense.

After all this, as at March 31, 2023, we held \$24.2 million in cash compared to \$23.4 million as at March 31, 2022. Further details on our debt and our credit facilities can be found in our MD&A and financial statements. In February, we provided our outlook and guidance for 2023 and are reiterating our guidance.

As a reminder, we've guided that for 2023, revenue is expected to be between \$200 million and \$205 million. Net income is expected to be between \$27 million and \$32 million. Earnings before interest, taxes, depreciation and amortization is expected to be between \$58 million and \$63 million. Adjusted EBITDA is expected to be between \$65 million and \$70 million.

Before I turn the call back over to Shawn, I'd like to finish by highlighting that we also announced yesterday that our Board of Directors approved a quarterly cash dividend of \$0.23 per share. That dividend will be payable on or before June 15, 2023, to shareholders of record as of March 31, 2023.

We also filed an updated version of our MD&A this morning with the correct land registry volumes chart. All the information provided in MD&A is accurate as of the date of filing.

I'll now turn the call back over to Shawn for some concluding remarks.

Shawn Peters^ Thanks, Bob. As I stated at the outset, we're pleased with the start of the year. We expected some contraction in our Saskatchewan registry market with a higher

interest rate environment, and that's what we've seen. We expect that will continue for the balance of the year, and we factored that into our guidance. But as you've seen, the business is still showing strong results.

Similarly, our Services business continues to grow and is now very much a core part of our business. Since acquiring ESC in 2015, we've been very deliberate about diversifying the revenue streams and services knowing full well that at some point, access to the Ontario Business Registry would be expanded. To date, that has meant that this has been less impactful for us due to our ability to continue to grow organically.

We've continued our investment in people and technology in the first quarter, all geared to continue to serve our customers well and to be able to respond to new growth and to new opportunities. Naturally, there's still some concern in the market around (technical difficulty) economic. However, as we've proven consistently over the last 10 years, ISC remains a robust business and well positioned to grow to our existing business as well as appropriate acquisitions.

With that, I'll now turn the call back over to Jonathan.

Jonatan Hackshaw^ Thank you, Shawn. [Antoine], we'd now like to begin the question-and-answer session, please.

QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) And our first question comes from Scott Fletcher from CIBC World Markets Inc.

Scott Fletcher^ I wanted to ask a question on the reiterated guidance. I'm just wondering where the land registry volume came in? If that was sort of -- if those numbers were maybe slightly worse than expected, but the technology contracts and the better-than-expected performance in services sort of internally helped you let you, sort of, reiterate the guide? I'm just wondering if there was maybe some mix in your internal forecast as to how to get to the total guidance number?

Shawn Peters^ I'll maybe start on that. I mean we've reiterated guidance. It is the first quarter, and we do have seasonality to our business. To your question, it was the land volumes sort of different than we expected. I think they're trending in the direction that we expected. We do see variances, as I said, for seasonality in first quarter. And first quarter is often the lower quarter. So pretty early in the year to decide if those transaction volumes are going to be up significantly. But overall, we're still confident in the land registry volumes that we predicted for the year. And the technology contracts that we've talked about today, we had forecast that into our guidance as well.

So I think sort of across the board, we're pretty confident in all sectors of our business and all segments that -- where we thought we were headed is where we're still headed.

Scott Fletcher^ And then I just wanted to ask on the Services. The margin was strong in the quarter and an improvement sequentially. I understand there's some seasonality, but how should we be thinking about the services and margins going forward for the rest of the year?

Robert Antochow^ Yes. So our Services business, if you look at our historical margin profile, that's I think what you should consider. We do have seasonality and there's a product mix that we see from over -- on a quarterly basis. So you should think of it from the annual Services margin perspective.

Operator^ Our next question comes from Jesse Pytlak from Cormark Securities.

Jesse Pytlak^ Just coming back to those Technology Solutions project wins. Can you just give us a sense on the time line when you might start to recognize some of the first milestones?

Robert Antochow^ Yes. The majority of the work really is commenced -- we'll be commencing in Q2 as we go forward. So we'll be recognizing the revenue as the work progresses. But you'll see the revenue pick up in the next quarter.

Jesse Pytlak^ And then in terms of kind of the expense line in Technology Solutions, is there still further investment to go with these projects? Or is this kind of a new run rate level?

Robert Antochow^ Yes, we are -- we invested in people and some -- to support these projects. So part of that cost increase is (technical difficulty) as we move forward with completing projects that we've got in the (technical difficulty) advance on these new projects. There will be some additional investments in people which we have factored into our guidance that we provided.

Shawn Peters^ Yes. And Jesse, I might just add. As we talked about late last year, we saw the return to procurement happening and so started, as Bob said, those investments in people. And so part of what you're seeing in the expense line is the gearing up [now] that. I think we're getting fairly close to that. But as Bob said, there's probably a little more -- a little incremental -- yes given that we see a pretty exciting pipeline for technology this year. But we're getting closer to your question to more of a run rate given the volume of business that we anticipate.

Jesse Pytlak^ And then maybe just one last one. Are you able to quantify the impact this quarter from the changes in the OBR on the services business?

Jonatan Hackshaw^ Jesse -- sorry, Jesse, just repeating for Bob. The [changes impact] on services from the changes in the OBR opening up a bit if we're able to quantify that.

Shawn Peters^ Yes, we don't -- unfortunately, we don't have an exact number on that, Jesse. We're monitoring it. We're -- from a high level, we've been expanding our

technology to provide more services to customers in that area to create the stickiness with them. We also have expanded services within our registry complete software to offer filing products across the country as well as Ontario to support that stickiness.

So at this point, we can't quantify. We'll be monitoring that [happens to be] the upcoming months. But at this point, there is an impact. But in terms of the absolute dollar amount, we're not able to quantify that at this point.

Robert Antochow^ And I'd add to that, that all those activities we've taken to diversify the business, knowing that as I said, that this would come at some point. So as you've seen in our results, the impact to us is not material. It's not probably something that we'll disclose in the future even once if it's sort of quantifiable, but we don't expect it to be material to us.

Operator^ Our next question comes from Stephen Boland from Raymond James.

Stephen Boland^ Is there -- I might have missed this, but is there other changes coming to the Ontario Registry? I can't remember if -- sorry, I read the MD&A. Or is that the only changes now that have been put into effect?

Shawn Peters^ It's -- I mean there's two phases sort of to the opening of the OBR. One happened some time ago, and the second one is opening more now. And I think it happened in March. I imagine that will continue to sort of open, but there's no further changes other than the continuation of the project that they've started.

Stephen Boland^ And then the second question is just on the land registry. The high-value transactions took a big jump. And I know there was COVID hangover for a couple of quarters at those transactions. But is this a sustainable level in your view? Because it seems like it was a pretty material jump.

Robert Antochow^ Yes, it was -- for the quarter, we had some high-volume transactions, a little bit higher than what we expected. And that fluctuates with economic activity in the province. And it's large transactions, it's hard to predict. It was higher than what we anticipated. But it's -- we still expect the return to pre-pandemic levels is what we're seeing.

But again, as that's (technical difficulty) acquisitions that happened in the economy. And there was a couple of transactions that occurred in this quarter. And -- But our expectation is that we're seeing that return to more pre-pandemic levels.

Stephen Boland^ And I apologize if this question is obvious, but when I look at your revenue and your adjusted EBITDA, you're close to -- you did \$49 million, you're almost right in the range of \$200 million to \$205 million for the year, meaning pretty flat. But there is a jump when you look at EBITDA, adjusted EBITDA, \$14 million. If you annualize that, it's well below your \$65 million to \$70 million.

So maybe you've answered this in the past. Where is the margin increase? What segment is it coming from?

Shawn Peters^ Yes. Well, maybe I'll start on that and let Bob jump in. I think the revenue is an increase over last year, not flat. But adjusted EBITDA as well, the increase in the margin -- as Bob mentioned earlier in the call, we do see seasonality in the business. And so sometimes that's a shift in either the season or the types of transactions that we see. And so when we budgeted overall, that's what we're looking at, not so much on a per quarter basis. So that's where (technical difficulty) if there's any adjustment in the margin either up or down, that's because of the annualization of what -- so it's a little tough to take the first quarter and take it out by 4, and it doesn't totally work.

I understand the what you're getting at, but there is the seasonality and different types of transactions involved.

Stephen Boland^ And can you -- the seasonality, which -- I guess, means it's probably registry, obviously. Is that the main bucket that you see the seasonality or expected in your guidance?

Robert Antochow^ Yes, Steven. So registry operations accounts for roughly about 70% of (technical difficulty). It's the largest contributor. And quarter 2 and quarter 3 are the highest quarters in that business. Obviously, there's more of the summer spring . And so there's a lot more real estate transactions that occurred during that time period. So those orders will have higher EBITDA versus Q1 and Q4 historically.

Operator^ And it looks like our last question is coming from Trevor Reynolds from Acumen Capital.

Trevor Reynolds^ Just on the technology contract, what's kind of the term of commissioning or deployment on that in terms of revenue recognition? How long do you expect that contract to go forward?

Shawn Peters^ Yes. Typically, it's -- they're very typical contracts. So these are right in our sweet spot with the registry solution in the corporate registry, and we said it can be deployed in other ones. So this is an IP and patent type registry. But very similar deployments of RegSys that we've seen in the past. So they range anywhere from sort of 12 months to 18 months, and that's where you should see the revenue recognized.

Trevor Reynolds^ And then do you see other opportunities in some of these tax haven countries? Do you see this as kind of a proof of concept for some of these countries and just kind of what the outlook is there on the technology front?

Shawn Peters^ Yes. We absolutely see opportunities. As we said, there is a return to procurement. We are seeing a lot more activity in that market and the deployment of our RegSys technology just continues to expand. The use of the one project here where it's an

IP registry, that's certainly technology that we can deploy in other jurisdictions and you become a stand-alone IP registry. So we do see lots of opportunities.

Activity is strong in the market. We're actively involved in that. And so we're pretty excited about this space for ISC.

Trevor Reynolds^ And then apologies if I missed this, but just maybe an update on the recovery business and where that kind of sits today relative to expectations and kind of where the credit cycle is at?

Shawn Peters^ Yes, Trevor. You'll see that the revenue was basically essentially flat over the quarter. We are seeing assignments pick up, which is a good indicator. The part of it is there (technical difficulty) how much versus sold. We make -- the margin profile is different on [case] file that's redeemed versus sold, and we make -- the majority of them are (inaudible) files. And so that's the piece that we're watching.

So it's possible, we're getting more pieces through the door. It's just the moving them to more of -- the sold is where we make the margin. And that's where -- we're seeing a trend towards more sold, but that -- not significantly over what we've seen in the prior periods.

Trevor Reynolds^ And then maybe just the last one, just how you guys are looking at the housing market in Saskatchewan these days?

Shawn Peters^ I think our view continues to be the same. We talked about the surge we saw during COVID and the activity, and that would return to pre-pandemic levels. We're still above 2019 or predicting to be above 2019. But the interest rate -- as you all are aware, the interest rate does impact that. And so we see a little bit of contracting. There's no real danger signs in it. The -- Most of the commentary around the market in Saskatchewan, I mean we're leading in GDP here. And the actual housing market is expected to fare quite a bit better than the rest of Canada. And so that continues (inaudible). It has an impact on our registries as we've seen even this quarter, but the strength of the business helps offset that, and it's still a good business, no matter what.

Operator^ (Operator Instructions) It looks like we have no more questions. So I would like to pass it back over to Jonathan Hackshaw for closing remarks.

Jonatan Hackshaw^ Thank you, [Antoine]. With no further questions, we'd like to thank you all once again for joining us on today's call, and we look forward to speaking with you again at our next reporting period. Have a good day. Thank you.

Operator^ Thank you for your participation in today's conference. This concludes the program. You may now disconnect. Thank you.