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POSaBIT Systems Corporation. (OTCQX:POSAF) Q2 2023 Earnings Conference Call August 24, 2023 4:30 PM ET

Company Participants

Oscar Dahl - Chief of Staff at POSaBIT Systems

Ryan Hamlin - Chief Executive Officer

Matthew Fowler - Chief Financial Officer

Conference Call Participants

Mike Reagan - Excelsior Equity

Gary Ribe - Accretive Wealth

Operator

Good day, ladies and gentlemen and welcome to the POSaBIT Systems Corporation Second Quarter 2023 Earnings Call. [Operator Instructions] It is now my pleasure to turn the floor over to your host, Oscar Dahl. Sir, the floor is yours.

Oscar Dahl

Thank you, operator. With me on this call are Ryan Hamlin, Chief Executive Officer; and Matthew Fowler, Chief Financial Officer. I would like to begin the call by reading the Safe Harbor statement. This statement is made pursuant to the Safe Harbor for forward-looking statements described in the Private Securities Litigation Reform Act of 1995. All statements made on this call with the exception of historical facts, maybe considered forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Although the company believes that expectations and assumptions reflected in these forward-looking statements are reasonable, it makes no assurances that such expectations will prove to have been correct. Actual results may differ materially from those expressed or implied in the forward-looking statements due to various risks and uncertainties.

For a discussion of such risks and uncertainties, which could cause actual results to differ from those expressed or implied in the forward-looking statements, please see risk factors detailed in the company’s annual report and subsequent filed reports as well as in other reports that the company files from time to time with SEDAR. Any forward-looking statements included in this call are made only at the date of this call. We do not undertake any obligation to update or supplement any forward-looking statements to reflect subsequent knowledge, events or circumstances.

The company may also be citing adjusted EBITDA in today's discussion. Adjusted EBITDA is a non-IFRS measure used by management that does not have any prescribed meaning by IFRS and that may not be comparable to similar measures presented by other companies. The company defines adjusted EBITDA as net income or loss generated for the period as reported before interest, taxes, depreciation and amortization. It's further adjusted to remove changes in fair value and expected credit losses, foreign exchange gains and/or losses and impairments. The company believes this is a useful metric to evaluate its core operating performance.

Now I would like to turn the call over to Ryan Hamlin, Chief Executive Officer. Ryan, please proceed.

Ryan Hamlin

Thanks Oscar and welcome, everyone. As a reminder, all numbers that I'll be talking about today are in U.S. dollars. Let's begin with our financial results. Q2 was our best quarter in the history of POSaBIT, a nice rebound from the typical seasonality of a slow Q1.

For the quarter, revenue was nearly \$13.5 million, up 64% year-over-year, versus \$8.2 million in Q2 of last year. Gross profit was also up to \$2.7 million, versus \$2 million in Q2 of last year. Our quarter-over-quarter and year-over-year growth remained exceptional, especially in an industry where so many businesses right now are struggling to get by. Our balance sheet continues to be in a great position, with a sustainable amount of cash on hand to execute on our short and long-term goals.

I want to repeat, Q2 was a record quarter for POSaBIT, keeping us on track to hit our 2023 guidance and continuing our streak of quarter-over-quarter growth. Despite all the turmoil within the industry and the economy at large, we continue to grow as we have since the company's inception.

As noted in previous calls and press releases, our acquisition of Hypur closed on April 1st of this year. In Q2, we spent time bringing the Hypur team and technology into the fold, and I'm proud to report that Hypur has been fully integrated into POSaBIT. The expertise and tech solutions we've gained through this acquisition have been and will continue to be an invaluable asset for POSaBIT, as we continue to grow and gain market share. Additionally, the Hypur base of PIN Debit merchants has bolstered our customer base in a meaningful way, the impact of which is reflected in our Q2 revenue numbers.

Now I want to address the recent news that many of you are aware of regarding Mastercard and the use of Mastercard services in the cannabis industry. In fact, I would guess many of you likely heard some chatter within the industry regarding a Bloomberg article that quoted a recent Mastercard shutdown. While there have been a number of payment technology providers and dispensaries impacted by this recent shutdown, it is business as usual for POSaBIT. Let me repeat, at POSaBIT, its business as usual.

We have built this company with an incredible high standard for compliance. We've been doing this for over eight years. We go above and beyond when it comes to transparency and regulatory matters. This won't change, and being built on the backbone of compliance has served us quite well over the years. Of course, with this recent news, it once again points to the need for safe banking and other legislative measures regarding descheduling that are needed now more than ever before.

Now I'd like to touch on a couple of personnel changes we've made recently. Michael J. Sinnwell, Jr, who came over to POSaBIT in the Hypur acquisition, has recently been promoted to Chief Product Officer. Michael has decades of experience in the FinTech space and will lead our product development team for both our point of sale and our payment solutions.

Chris Baker, previously in the role of Chief Strategy Officer, has been given the title Chief Operating Officer. Chris joined the team late last year after 18 years at IBM to help us out with a handful of important strategic opportunities, including the Hypur acquisition, and proved himself to be an excellent operational asset whose knowledge and experience will serve us well as we continue to grow.

Lastly, effective today, we have promoted Matt Fowler to Chief Financial Officer for our parent company, POSaBIT Systems Corporation. Prior to this, Matt has been our CFO for our wholly owned U.S. subsidiary of POSaBIT U.S. Inc. Please join me in virtually congratulating Chris, Matt, and Michael on these new leadership roles within POSaBIT.

Now let's talk a little bit about our POSaBIT sales growth. POSaBIT continues to generate an abundance of new business with over 600 stores already live and hundreds more currently in the pipeline. We anticipate installing a significant number of those stores by the end of the year. Our sales success can be attributed to a couple key factors. One, our compliant debit solution is the best in the market and the industry has responded very well to our on-going compliance efforts amid confusion and turmoil in the industry.

Two, our point of sale is the dominant player in our home state of Washington with over 40% market share and growing. And three, a seasoned team of payments and point of sale experts with decades of experience in software and FinTech.

I'd like to briefly touch on the state of the cannabis industry. There have been no shortage of trials and tribulations in cannabis over the past year. This is not surprising, given the newness of the industry and the general excitement around it. Despite these growing pains, it is our firm belief that the smartest, best-run, and most compliant business will win out. To that end, POSaBIT fits the bill. Even with the challenges the industry has faced, we have remained steady. We continue to grow at a rapid pace. Our quarter-over-quarter and year-over-year growth, for instance, comes despite a downturn in the average ticket price for debit payments in Q2 versus Q1.

Our growth continues despite store closures and industry consolidation. All that is to say, we have the confidence and ability to stay on plan, no matter what the industry throws at us, which leads me to a few comments I'd like to share with our investors today. POSaBIT's market valuation is unfortunately not reflective of the great results the team has been able to produce over the last eight years. We have doubled revenue for five years in a row, and our overall unit economics for the business remain at an all-time high. Yet the stock fails to accurately reflect this value. Some of this I chalk up to investors being weary of the cannabis industry, and others just concerned about our U.S. economy as a whole. I do want to say thank you to our loyal investors who believe in the vision and have stuck with us, even in these down times across the industry recently.

I jokingly say to my friends and family that it is my goal to make all investors that have sold POSaBIT disappointed sometime down the road. We will keep executing as we have over the years, and hope this will get rewarded in the public market at some point in the near future. All right, enough about that.

I'm going to now turn -- end my comments, and I'll turn it over to Matt Fowler, our CFO, for a more detailed review of our financial results for the second quarter ending June 30, 2023.

Matthew Fowler

Thank you, Ryan. Transactional sales through our payments platform were $162.6 million, up 26% compared with $129.3 million in the second quarter of 2022. Looking quarter-over-quarter, transactional sales were up 19% compared with $136.4 million in the first quarter of 2023. This was driven by a combination of increased same stores, transactional volume, and for new merchants coming online.

Transactional sales is a non-IFRS measure and one of the key drivers for our business. Total revenue was $13.5 million, up 64% compared to $8.2 million in the second quarter of 2022. Gross profit was $2.7 million, or 20% of revenue, up 39% on a dollar basis compared to $2 million and 24% of revenue in the second quarter of 2022. The decrease in gross margin percent year-over-year is tied to a change in the products we offered in Q2, 2022 versus Q2, 2023.

Operating expenses were $6 million compared to $5.9 million in the prior year's quarter. The primary driver of the increase in operating expense was hiring that has taken place over the last 12 months. The acquisition of Hypur, which added nine full-time employees and higher professional fees. Sequentially, operating expenses were up 13%, largely driven by higher people costs. Professional fees and stock-based comp compared to Q1 2023. Administrative expenses, which are primarily people costs, were $3.7 million in the quarter.

Stock-based compensation for the second quarter of 2023 was 761,000, and there was a negative impact in foreign exchange valuations of 123,000, both non-cash expenses. Net loss was $1.8 million, inclusive of the impact of a $1.6 million non-cash change in the fair value of derivative liabilities. This compares to the net gain of 400,000, inclusive of the impact of a $4.7 million non-cash change in the fair value derivative liabilities for the second quarter of 2022.

The mark-to-market of embedded derivative liabilities is tied to our convertible debt is a non-cash accounting entry required by IFRS. It can cause significant differences in the net income or loss quarter-to-quarter. Fluctuation to this line item of our income statement may be more extreme during periods of increased volatility in the price of the company's stock.

Adjusted EBITDA was a loss of $2.2 million, or negative 16% of revenue, compared to an adjusted EBITDA loss of 7,000, or negative 8% of revenue in the second quarter of 2022.

Cash on hand at the end of the first quarter was $4 million. This compares to $3.1 million at the end of 2022. Our debt balance remains low at $3 million of long-term debt, consistent with SBA loan convertible notes in a 3-year term loan.

Finally, we do not have anything new to report about up-listing the company's stock to NASDAQ or the TSX. Other than to reiterate, a positioning company's investors can easily invest remains important to management and the Board, and we continue to discuss all options with the counsel.

With that, I will turn the call back to you, Ryan, for closing remarks.

Ryan Hamlin

Thanks Matt. I will end our call today by reiterating our guidance for 2023. We are on track and growing as planned. For the full year 2023 we expect revenue of $58.5 million to $61.5 million and gross profit of $12.5 million to $14.5 million and to be slightly negative on an adjusted EBITDA basis.

This represents a 62% increase in revenue year-over-year at the midpoint and a 35% increase in gross profit dollars year-over-year at the midpoint. I want to thank everyone for listening in today. Operator, we'll now open up the call lines if there are any questions.

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] The first question comes from James McGlanis, private investor. James, please proceed.

Unidentified Analyst

Hey everyone. Thanks for taking my question. Matt, congratulations on the expanded role and to everyone else as well that got promoted too. I guess, so I appreciate the commentary on kind of the industry dynamic and calling out the stabilization X in Q2. Is there anything you can talk about as far as kind of July and August trends? You mentioned same-store sales growth and the quote in the press release. If we could just talk about kind of what you're seeing in the industry and sort of what that means for your go-forward outlook.

Ryan Hamlin

Yes, thanks James. Thanks for the question. Good to chat with you. I'll make a couple comments and Matt certainly welcome to add to this. What we're seeing in the industry is very in line with what we saw. If we're just looking at it from a positive standpoint, it's very similar to what we saw last year where you have a low Q1, you recover in Q2 and then you really come back with a strong Q3, Q4.

So, if you look at last year and you look at the percent of revenue that was represented in our guidance at that time, we had about 42% of our revenue already accounted for in the first two quarters. And then in the last two quarters, we got 58%. We're tracking very similar to that. Meaning, if you look at our overall guidance and you look at where we're at the revenue, we're somewhere in that same kind of 40-ish range and we fully expect that over the next two quarters, we will do just like we did last year. So, from a positive standpoint, it's trending right in line with what we've seen in years past. So, that's good for us because that kind of just gives us affirmation on our guidance.

The second thing, just around the industry as a whole, we started to see, and I mentioned in here that the average ticket was down. It was down like a buck between Q1 and Q2, but overall volume obviously went up because we had more stores and our same store growth did more transactions. So, while the average ticket was down slightly, obviously, overall sales were up. I would expect, and as you probably have listened in to some of the big MSO public companies, they ended up hitting their Q2 and in some cases, beating it a little bit by a few percentage points. We're seeing that same trend and even more so as we now go into Q3.

So, I would expect that the Cannabis industry as a whole is going to have a healthy Q3. I think we will obviously reflect that as well. And again, it's just comforting to know it's kind of tracking along the same projections that we saw last year.

Unidentified Analyst

Got it. That makes sense. Really helpful, color. I appreciate that. It's fantastic to see the industry starting to kind of find what I hope is a bit of a bottom and to be inflected from here. And I think that bodes really well for you guys. And I think we'll highlight and hopefully people wake up to the valuation point you called out because this is just silly.

So, on the sequential step-up in payment volume, I'm sure a lot of it was stores coming online, but can you talk about that number, because that really stood out to me as a very strong number.

Ryan Hamlin

Yes. So, clearly we had the Hypur-acquisition, which kicked in, which is great. So they brought over with them approximately 100-plus stores. And then we grew our own volume. I'm looking at that by anywhere between 30 to 40 stores on top of that. So you had a pretty big increase in overall stores. And again, a big part of that was the Hypur-group that came over.

The other thing, we looked at same-store growth because this is something we always look at. It's relatively the same, proportional to what we've seen quarter-over-quarter meaning we have a really nice strong same-store growth. It's pretty consistent now where we know what to expect the first couple of months and then once they hit past that three-month mark, they tend to kind of get to a number that is pretty much the same quarter-over-quarter. So long answer to your question, James, is that a big chunk of it was same-store was a new store, but same-store still continues to be a nice source of revenue growth quarter-over-quarter.

Unidentified Analyst

Got it. Makes sense. And how is Hypur performing? You talked about the integration, but potentially how is that doing?

Ryan Hamlin

Good. I mean, that app that Matt even mentioned out here, we only brought over nine headcounts so from a cost standpoint, it was relatively inexpensive when it came to just OpEx and they brought over, last year's revenue was $5.5 million. So, it's good for us to get that revenue coming over and that revenue growing slightly and -- it also brought some really great resources. I mean that team, I called out Michael Sinnwell. I mean, Michael is a really deep expert in this industry and has been in FinTech for a long time and it's been really great to have another person that has all of the connections into the industry from a processing standpoint and from a banking standpoint. So we got some great, intelligence with that acquisition as well.

Unidentified Analyst

Yes. No, that much is clear to me. I'm really excited to see where you guys can take this asset. I think it's a home run deal for the company. And my last question too is, so I guess you talked about kind of percent of revenue through the year, so maybe this is rehashing an answer you already gave me, but just I guess what has to happen for you to achieve or beat your revenue guidance for this year?

Ryan Hamlin

I mean basically we got to, I mean, we got to hit our store count that we have in our forecast, which we're feeling optimistic about right now. I mean I already, I gave you the number of literally hundreds of stores in the pipeline. So the pipeline is full. It's a matter of getting the stores through underwriting and onboarding them. But I would say, you look at our Q3 and Q4 forecast it's still very attainable given the current pipeline we have.

So, we're not, I mean, I'm not giving you an exact number, but if you just look back kind of historically, you could probably come to that number yourself pretty easily on looking at about what, how much revenue per store brings in. And then if you look at the pipeline, we have more than sufficient pipeline for that.

Unidentified Analyst

Right. Yes, it makes sense. I mean, it looks like the exit rate for this year will be a really strong number. And then taking into account too, the fact that revenue is understated given the accounting treatment of the subscription deal or the licensing deal you guys signed. So, anyway, I think the future is very bright for the company. That's it for me. Thanks so much for answering my questions.

Ryan Hamlin

Yes, thanks, James. And James, you did bring up a good point. I'm just going to; this is your bonus question. I think you brought up a really good comment, which is the revenue that we had to recognize last year because of the point of sale licensing deal. We had to recognize the majority of that last year, which is a great deal. It's a great cash deal for us. So, you have to remember we finished one year of a four-year deal. We have three more years of guaranteed cash coming in every single month. And so that cash is great for our capital and expenditures. And while not all of it gets reflected as a revenue line item, only a portion of it. So yes, you are correct in saying that we view that as kind of bonus. But when it comes to the actual cash side of it, it's great to have that known cash infusion every single month now.

Unidentified Analyst

Yes, fantastic. Thanks again, guys.

Ryan Hamlin

Thanks, James. Good talking to you.

Operator

The next question comes from Mike Reagan from Excelsior Equity. Mike, please proceed.

Mike Reagan

Hi, thanks for taking the question. A lot of them got answered before, but especially on the transaction ticket versus volume. So obviously the ticket down a dollar, but the volume is more made up for it. Anyway to think about that in sort of percentage terms? About what the one dollar is versus the transaction volumes?

Ryan Hamlin

Good question. I'm looking at that. Off the top of my head, I'm trying to think of like a calc on that. Yes we would, we could easily probably come up with that Mike, and follow up with you. It's just basically taking that one dollar times the number of transactions and then look at overall transaction growth. But yes, I'm sorry. I can't answer that just off the tip of my tongue, but I'm happy to follow up with you.

Mike Reagan

Yes, okay, but it's something I think a lot of people underappreciate in the whole industry, especially with pricing declines. The price goes down, but then the transactions usually go up. There's elasticity. So, it sounds like, your customers are seeing that along with along with the overall transactions. And the second question on Mastercard is you were highlighting how you're completely compliant so their announcement has nothing to do with you. Have you seen any increases in inbound queries from stores that maybe weren't compliant and now have lost their processing system that are now calling you up because you are still actually processing I guess both Mastercard and Visa transactions?

Ryan Hamlin

Yes. Good question, Mike. And this is the -- I had a meeting with my team earlier today and we were talking through some things. But this industry as a whole, for those of you that aren't as familiar with the cannabis industry and then you add payments on top of it, it's a very interesting space to be in. And even more so just in the last couple of weeks with the Mastercard demo. Yes. I mean, certainly we have a -- our inbounds are pretty consistent. We -- we're -- our name is known in the industry now and so we have a pretty steady stream.

As things change, there's always alternative solutions still creeping up. So it's a bit of a -- I don't want to say whack-a-mole, but that's kind of what this payment industry reminds me of a little bit is that while one might go down, two other credit solutions that aren't compliant will pop up. And so it's this constant battle between what payment company do you want to work with that is today versus what payment company you're going to bet on that's going to be here for the long-term. And so that's kind of what we've been selling to our customers and telling our customers. And so, yes, when this came out, I mean, it's calming our merchant base, explaining to them where we are. This is the cannabis industry. This is payments in cannabis. There is always changes. And so what we try to do is make sure we build full redundancy in our systems and alternatives. And so, yes, we have seen an influx in inbounds, but what I tell everybody is this is a game where you have to be along for the long haul. You have to be ready to live through the ups and the downs because; it's not just payments, its states. When they come out with new states, they have different limitations for how much you can buy. It's different every single state. Taxation is different every single state. This industry changes, literally on a daily basis. And so what we've been saying and our message has always been, you want to bet on POSaBIT. You want to bet on POSaBIT. We've been in this business for eight plus years. We understand how to do payments. We understand how to do it in a compliant manner. We understand how to support you, even in times where things get a little chaotic.

And so, sorry, long answer your question, but I wanted to make sure I shared that opinion with our investors because it's an important differentiation for how POSaBIT views this than a lot of others in this industry.

Mike Reagan

Great. Thanks a lot.

Ryan Hamlin

Thanks Mike.

Operator

The next question comes from Gary Ribe with Accretive Wealth. Gary, please proceed.

Gary Ribe

Hey, Ryan. How are you?

Ryan Hamlin

Hey, Gary. Good.

Gary Ribe

I'd like to ask like a slightly different question. You guys are investing heavily in growth through your income statement. Could you just give investors just some idea of like the extent of the growth investment that's running through the P&L? Or maybe put it the other way, like what stage do you start to get some serious sort of lift and flow through to the operating income line?

Ryan Hamlin

Yes. No, good question. And it's really, I view it as we've been in heavy growth mode over the last many years and really investing our capital. We've done a nice job. We haven't raised a lot of capital, but the capital we have raised, we're putting it in the business. There's definitely a focus now on profitability and the importance of increasing our gross margins. And you will see that emphasis as we go forward, especially. I think we're at the point now where we understand how to scale this business. We've got the systems in place. We've got the technology written. So a lot of the expensive work associated with building up the kind of systems that we needed to have to scale are now there.

So you'll start to see the efficiencies where it's less about developing a lot more and more about just operating. And that's where we're going to get the economies of scale. We can add 100 new merchants and only have to hire, let's say, one more customer support or two more customer support people. So we're in a much better position from an OPEC standpoint as we grow than we ever have been because we've made all of those investments in the past.

Gary Ribe

Got it. Because if I look at your guide, I mean, the first six months, you guys were what minus nearly five million in EBITDA, give or take?

Ryan Hamlin

Yes.

Gary Ribe

And to be slightly minus for the year, I mean, that implies some pretty big lift as you get to the back half of the year for that back half, sort of.

Ryan Hamlin

Yes. Yes. And, yes. And again, some of that, we, on our, I mean, I'll let, I mean, actually, Matt, I'll let you address that. But I know, there's some things that are going to have an impact on our expenses in the next quarter that you will share.

Matthew Fowler

Yes. No, I mean the -- as we're going to go into it, a lot of the costs that we needed to invest in headcount and into tooling to really build into our growth and get that machine running, that's really complete. Now, it's really just focusing in on building with what we have and bringing in new merchants and top-ups, just increasing same-store sales growth.

Gary Ribe

Got it. Okay. Cool. And then people asked about the Mastercard thing, so I won't go there, but I think you guys did a good job with addressing that. But what does the M&A pipeline look like for you guys, given everything that's going on in the industry?

Ryan Hamlin

Good question. You get asked that quite a bit. I mean, obviously, we had the Akerna acquisition, and we passed on that. And then we had which, that's kind of early in the year. And then we obviously moved forward with Hypur, closing that. It's interesting because, yes, now more than ever, those companies that didn't have a really good business model to sustain what the industry has been going through over the last 12 months and didn't raise enough capital when they had the opportunity, kind of, now that it's kind of dried up, those are the ones that are struggling.

So yes, there's still, opportunistically, we're looking. And the criteria I always tell my team is it's about distribution. So, if we find a good opportunity that gives us a bulk set of merchants at a reasonable price that makes sense, then that's a good acquisition for us. Because we know we have great technology, so we can move them into our great technology. And we know we can monetize them through our payments business.

So for us, it's less about technology gaps, because we don't feel like there's really any technology gaps. For us, it's all about distribution. And so, if the right opportunity comes along, or you can add 100, 200, 300 merchants, and we can do that in a bulk capacity at a reasonable price, then yes, we'll take a look at it.

Gary Ribe

Okay. I got it. That makes sense. I appreciate it. Thanks, guys.

Ryan Hamlin

Cool. Thanks, Gary.

Operator

Okay. We have no further questions in queue. We have reached the end of the question-and-answer session. This concludes today's conference, and you may disconnect your lines at this time. Thank you for your participation.

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