Intellicheck, Inc.
Third Quarter 2022 Earnings Call
November 14, 2022

Presenters
Gar Jackson - Investor Relations
Bryan Lewis - Chief Executive Officer
Jeffrey Ishmael - Chief Financial Officer

Q&A Participants
Scott Buck – H.C. Wainwright
Rudy Kessinger – D.A. Davidson
Luke – Northland Securities
Daniel – Craig-Hallum Capital Group

Operator
Greetings. Welcome to Intellicheck's Third Quarter 2022 Earnings Call.

At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation.

If anyone should require operator assistance during the conference, please press "*", "0" on your telephone keypad.

Please note, this conference is being recorded.

I will now turn the conference over to Gar Jackson, Investor Relations. Thank you. You may begin.

Gar Jackson
Thank you, operator. Good afternoon and thank you for joining us today for the Intellicheck Third Quarter 2022 Earnings Call.

Before we get started, I will take a few minutes to read the forward-looking statement. Certain statements in this conference call constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended.

When used in this conference, call words such as will, believe, expect, anticipate, encourage and similar expressions as they relate to the company or its management as well as assumptions made by and information currently available to the company's management, identify forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements are based on management's current expectations and beliefs about future events. As with any projection or forecast, they are inherently susceptible to uncertainty and changes in circumstances, and the company undertakes no obligation to and expressly disclaims any obligation to update or alter its forward-looking statements, whether resulting from such changes, new information, subsequent events or otherwise.

Additional information concerning forward-looking statements is contained under the headings of Safe Harbor Statement and Risk Factors listed from time to time in the company's filings with the Securities and Exchange Commission.

Statements made on today's call are as of today, November 14, 2022. Management will use the financial term adjusted EBITDA in today's call. Please refer to the company's press release issued this afternoon for further definition, reconciliation and context for the use of this term.

We'll begin today's call with Bryan Lewis, Intellicheck's Chief Executive Officer; and then Jeff Ishmael, Intellicheck's Chief Financial Officer, who will discuss the Q3, 2022, financial results.

Following their prepared remarks, we will take questions from our analysts and institutional investors. Today's call will be limited to one hour. And I will now turn the call over to Bryan.

Bryan Lewis
Thank you, Gar, and welcome, everyone, to the third quarter 2022 Intellicheck earnings call. A couple of things to note for the numbers that we believe show that we are on the right track.

First, we continue to grow with SaaS revenues up 22%, over the same period a year ago. As you will hear, we continue to expand within our existing clients, and we are growing customers, across many very use cases. And note that our gross margins remained very healthy at greater than 90%.

Second, I think a concern many had is that we would need to raise money to fund operations. That is not the case. Adjusted EBITDA for Q3 was a positive $75,000, compared to a negative $272,000 for the same period last year and a negative $583,000, last quarter.

There are two things I've said many times and I stand by what I told you before. That is, we see no need to raise money for working capital and we do not need legions of people to run the company or handle explosive growth.

The only primary areas where I see continued increases in spending are sales and marketing, and those increases should create increased growth. We'll be watching those expenses, closely, and aligning hiring and spending with growth.

Before I get into some of the wins of the quarter, I want to remind everyone of the magnitude of the problems we are solving. I think it gives insight as to why our customers continue to expand usage and why we are seeing new prospects coming to us with growing frequency.

In 2021, traditional identity theft grew 79%, with losses almost doubling over 2020 to $24 billion. The mean fraud amount loss each time increased $200 to $1,551, and that's up $500, since I started in 2018.

And if you were one of the 15.3 million Americans who were hit by this crime it cost you, on average, nine hours of your life and $224 to clear your name.

Account takeover fraud is the fastest-growing fraud because the bad guys found it was a much larger haul each time at a mean fraud amount of $2,169. Total takeover account fraud grew 90% to $11.4 billion. And unfortunately, if you were the victim of that crime, it cost 14 hours of your life and $515.

For our clients and prospects, it is important to stop these crimes in the most simple, frictionless way possible. If they don't, not only do they suffer the monetary losses, they potentially lose a customer and their lifetime value. Studies show that up to one third of people will move their banking relationship, if their identity is stolen.

Our clients and prospects need something that is accurate and fast-and that is Intellicheck. I believe the fact that 26 state-level law enforcement agencies use our services to validate an ID is proof of our accuracy.

And as to speed, we determine the validity of a license in 44 milliseconds. To put that in context, that's less than half the time it takes to blink.

The other distinction I would like to remind everyone of is that Intellicheck's technology solutions require no new hardware. Unlike the companies that use a photo of the document to compare to a template, we work with the existing scanning devices at retail locations and the check readers at the teller work stations.

At the same time, our APIs make it easy to integrate into any traditional brick-and-mortar system, as well as any mobile app or website.

We believe that it's quite the competitive advantage when every study shows that the vast majority of transactions still happen in-person. A *Business Week* article recently said, research from UBS shows that online shopping back to pre-pandemic levels, so down.

And data from the U.S. Census Bureau showed that online growth has trailed sales gains of the overall retail industry for the last five quarters.

So moving on to highlights of the quarter. I am happy to say that Financial Services Company, Number 3, completed their renewal and signed a 3-year term that includes a price increase and a commitment to a minimum of a 20% increase in transactions in the first year of the contract.

Currently, this client does not do anything in the digital world but in addition to expanded usage on-premise, they intend to open digital channels in 2023. This leads me to believe that the larger increase in volume will be towards the back half of the year.

Number 3 continues to be one of our best reference clients and I believe this 3-year renewal with a contractually committed increase in volume tells you the certainty they have in our products.

Financial Services Company Number 4 has seen a 67% increase in transaction volumes. This is coming from multiple areas. They continue to bring live retailers. They are winning from competitors, which is increasing volume.

They also have our technology solution now completely integrated as call center software, and call centers are a large vector for account takeover fraud, so we see continued usage, there.

We have also completed the renewal with a large Midwestern bank client with over 1,100 branches in 10 states, again, with the price increase. I was recently on a quarterly business review with this account and they spoke of the large amount of bot attacks they are seeing, aimed at account takeover. And they said they are a nightmare for any company, without accurate ID validation.

The bank also said they consider themselves a data hungry organization. I shared that with you in light of the fact that they have just completed the migration to the new platform. So, they are very interested in and are evaluating all the new signals they have access to.

Remember, the first step in proper AML process is to make sure that it is, in fact, Bryan Lewis, and then make sure I can and want to do business with Bryan Lewis. That is what the platform allows our clients to now do.

Last quarter, we spoke about the omnichannel multi-biometric platform for banks, marketplaces and health care systems that is reselling our ID validation tools. They started with us in January of this year and purchased a bucket of 500,000 transactions, which they had to replenish, when we last spoke. They have since gone through that bucket and are purchasing another.

On the automotive front, in addition to receiving multiple inbound leads and closing those, we've signed an agreement with a reseller working with the CRM and sales engagement software provider to the automotive space.

Their software is used at over 1,000 dealerships, and they feel confident that most, if not all, of those dealerships will be interested in the software.

An important upsell opportunity to the existing and new auto dealerships clients are those same AML signals that let me know if I can and want to do business with a person. Dealerships have told us this data was important to them.

Most of them, though, were using our portal product on a handheld device for our portal plus web product, which allows them to validate a person whether they're standing in front of them or thousands of miles away. We have now incorporated these signals into these products. So, these dealerships now have access to another great opportunity for the sales team.

On the age-restricted front, a couple of new unique sales. We are now live with two companies that distribute vending machines for the sale of cannabis products. When someone wants to make a purchase, they scan a QR code which kicks off the ID validation and facial biometrics process to make sure that, not only is the license real, but I am the one holding it before the product can be dispensed. They have just begun distribution of the machine, so it will be interesting to see volumes, going forward.

I'd also like to say, we are now live with a nationwide consumer goods, food and age-restricted delivery company that operates in 650 cities. Our validation tools are integrated into their delivery driver mobile app for checking on age-restricted deliveries. They've rolled out for testing purposes to one Northeast city but anticipate a nationwide rollout in 2023.

At the same time, we are coming out with new products, particularly around data. At the end of the quarter, we introduced Business Intelligence. This is a tool our clients can use to dive into the patterns and uses trends of their transaction data.

This is sold as an annual subscription with annual seat license fees by user. We've already made the first sale of it to the media company using us for e-mail password resets, and we are encouraged by what we are seeing in client interest.

Currently, it is just each client's own data but we believe, and our clients seem to agree, that pooling anonymized community data for comparison purposes is worth even more, and we plan to release that in 2023.

The two regional bank prospects we spoke about last call are going well. We are working through the master services agreements with both and the top three bank continues to slowly move through their process.

I'm also pleased to report that the reboot of the sales team is going exceptionally well. We now have six senior salespeople, all of whom come from identity or cybersecurity sales focusing on financial services and AML, KYC use cases.

In addition, we have three senior account managers focusing on expanding our footprint at existing clients. While these existing clients all continue to grow, we feel those accounts should grow even faster, and we believe dedicated resources will make that happen.

Another area we are strengthening involves inbound leads. We have two hungry, motivated people handling those inbound leads, which marketing continues to do a great job of bringing in.

Our expanded focus on efficiencies has included a great deal of efforts spent on automating all of our processes for scale, many of which Jeff will speak about in just a few minutes.

On another front, we've taken another step toward including machine learning in our systems to detect fraud pattern attempts. Again, here is an opportunity to provide data that we think will be valuable to our clients, and we will be including it in Business Intelligence for a fee.

Sales operations is also providing insight and accountability to our processes, which is a valuable step forward.

Finally, we have some new certifications that are important to our clients. We are now SOC 2 Type 2, and we have received word that we have verbal confirmation that we will be receiving ISO 27001 and 27701 certification. The latter two certifications are very important, as they are the first steps in our compliance ,which is key for international client base expansion.

In closing, you can see that a lot is happening here at Intellicheck, as we make important strides forward with continued existing growth, the introduction of new products and the addition of new people to further our progress.

This is just the beginning. We have been setting the stage for what we believe will be even greater growth and innovation in the future.

I will now turn it over to Jeff.

Jeffrey Ishmael
Thank you, Bryan. Turning now to our third quarter results. Revenue for the third quarter of 2022 declined $819,000, or 17%, to $4.12 million compared to $4.831 million in the same period of 2021. Last year's third quarter revenue included $1.5 million of nonrecurring hardware sales.

Our SaaS revenue for the third quarter of 2022 grew $725,000, or 22%, to $3.970 million from $3.245 million for the same period in 2021.

Gross profit as a percentage of revenues was 91.1% for the third quarter of 2022, compared to 68.7% for the same period of 2021. The increase in gross profit percentage was primarily driven by, significantly, lower equipment sales for the third quarter this year versus last year.

Operating expenses which consist of selling, general and administrative, marketing and research and development expenses increased $32,000, or 1%, to $4.378 million the third quarter of 2022 compared to $4.346 million for the same period of 2021.

This increase is primarily driven by higher recruiting and professional fees, as well as higher marketing and advertising expenses.

Included within operating expenses for the third quarter of 2022 and 2021 were $729,000 and $712,000, respectively, of noncash equity compensation expense.

The company reported a net loss of $724,000 for the third quarter of 2022, compared to the net loss of $1.26 million for the same period of 2021. The net loss per diluted share for the third quarter of 2022 was $0.04, compared to the net loss per diluted share of $0.06 for the same period of 2021.

The weighted average diluted common shares were 18.9 million for the third quarter of 2022, compared to 18.6 million for the same period of 2021.

Adjusted EBITDA for the third quarter of 2022 was a gain of $75,000, compared to a loss of $272,000 for the same period of 2021.

Turning to the company's liquidity and capital resources, as of September 30, 2022, the company had cash of $11.8 million. Working capital, defined as current assets minus current liabilities of $9.2 million. Total assets of $24.1 million and stockholders' equity of $18.3 million.

The company has a $2 million revolving credit facility with Citibank that is secured by collateral accounts. There are no amounts outstanding under this facility.

As of September 30, 2022, we had a net operating loss carryforward of approximately $23.4 million.

It's been an exciting first five-plus months at Intellicheck. One of my objectives after taking the CFO role was to streamline the financial processes and procedures and improve our reporting, so that we can operate the business with real-time data to guide our decisions.

Things move fast in our industry, and we need to adapt quickly to these changes. We believe that we're close to regaining the momentum we had prior to COVID and need to be properly positioned with the right platforms in place to scale the business, quickly.

Let me share with you a few internal initiatives that were accomplished during the third quarter. One of our larger initiatives was to implement a robust equity management platform, and I'm excited to say that this is done.

The platform utilizes cloud-based technology developed by a leading global fintech company and is deployed across more than 100 countries. This new platform offers a full suite of services ranging from capital management to full equity program management, as well as brokerage services. This new equity platform replaces previous internal and manual processes.

In further support of increasing our internal efficiencies, we have also brought automation to our previously manual financial reporting processes. This platform will improve and support our statutory reporting requirements and allow us to operate with much more efficiency.

Our chosen partner has 19 offices, globally, and more than 5,300 customers. We have also made some changes on the auditor front. During the third quarter, we welcomed Forvis LLP, as our new audit and tax partner. Ranked among the top 10 public accounting firms, Forvis has 5,500 dedicated professionals serving clients across all 50 states.

Over the last 12 weeks, we have deployed best-of-breed platforms and vendor selections that will allow the sales and executive teams to focus on driving future revenue growth, which we believe has been hampered by a collection of manual processes.

My commitment to Bryan, when I joined the company, was to address these legacy processes and to provide the highest quality data and metric reporting that we believe will position the team to drive growth and operate more efficiency.

We believe that we are much better positioned than we were only months ago to scale this business to new levels and drive shareholder value.

I'll now turn the call over to the operator to take your questions.

Operator
Thank you. If you would like to ask a question, please press "*", "1" on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press "*", "2" if you would like to remove your question from the queue. And for participants using speaker equipment, it may be necessary to pick up your handset, before pressing the star keys.

Our first question is from Scott Buck with H.C. Wainwright. Please proceed.

Scott Buck
Hi, good afternoon, guys. Thanks for taking my questions. First one, Bryan, I was hoping that you might be able to talk a little bit about the retail environment. A lot of talk about consumers

pulling back in light of some heightened economic uncertainty. I'm wondering if you guys are seeing any of that, as we move into the stronger fourth quarter.

Bryan Lewis
So far, when I go back and compare numbers, other than for some retailers that are having just certain overall issues, I'm not seeing a big pullback of any sort. And we generally can see that basically in real time, as we did with COVID when things were opening and closing, we get the numbers in real time. So we can see that. So not good so far, not yet.

Scott Buck
Okay. And can you remind us how much of that legacy business makes up of total revenue?

Bryan Lewis
The—you're saying--

Scott Buck
--Card applications and card-not-present transaction?

Bryan Lewis
That's the vast majority of the retail. I'd say that it used to be upper 90s. It's probably a little bit less now because so many more of the banks are using us in their--at the teller workstation. So, that has been a big growth driver but it's the majority of the revenue, still.

Scott Buck
Okay. That's helpful. And then my second question, positive adjusted EBITDA this quarter, how should we think about you managing the business on a go-forward basis? Are we managing to breakeven? Or how are you--I guess, how are you handling the push-pull between investing in additional growth versus maintaining that positive EBITDA?

Bryan Lewis
Yeah, the good thing about sort of investing in that additional growth, it's not a lot of money to invest. It's really advertising and people. So, managing to breakeven, slightly positive, as we flesh out the sales team that I think that we need to be able to make sure that we're hitting all the verticals that we should be in.

I think one of the really good things that we've done is our salespeople are now focused on a vertical, which means they understand the business and speak the language. And there are different verticals, like automotive.

Again, I think we're doing so well there. If we had people focused purely on automotive, from that industry, we do better. So, that's how we're looking at additional spend, smart verticals, right people to speak the language and the right advertising to go after it.

Scott Buck
Alright, super. That's it for me. Thanks, guys.

Bryan Lewis
Thank you.

Operator
Our next question is from Rudy Kessinger with D.A. Davidson. Please proceed.

Rudy Kessinger
Great, thanks for taking my questions. On the price increases, both with, I think, FinServ Number 3, in one of the Midwest banks. Do those come in, in line with the past price increases that you said were low double-digit? And then secondly, on FinServ 3, I want to be clear, you said they're committing to a 20% increase in transactions in the first year of that new contract. When did that contract renew?

And so the 20% increase in transactions, I guess, as we think about the revenue increase, it would be the 20% increase in transactions, plus the price increase. I want to make sure I'm understanding that right, as well.

Bryan Lewis
Yeah, so, a couple of things on that. This is a contractual commitment to be doing a lot more. So, we traded a little bit of increase for the contractual commitment because they are going to do it or cut us a check at the end of the year, if they miss what they have committed to doing.

The--and really the way to think about these price increases, as we renew and renew and renew, we're bringing people up to what I would consider more market pricing, some of the deals that were struck or negotiated--negotiations begun.

Before I got here, we were at much lower rates. So, they certainly had significant price increases. I think now what we can look at is more sort of COLA adjustments, EPI type adjustments for most of our clients going forward because we have pretty much everybody kind of at market pricing, now.

Rudy Kessinger
Got it. And then as we think about Q4, as you sit here kind of halfway through the quarter, is there any kind of bounds you could point us to for Q4, as it relates to kind of a more typical seasonality in Q4, as you get back to a more normal in-person Black Friday, relative to maybe the last year or two or pre-COVID? Just what kind of seasonality should we expect in Q4 versus Q3?

Bryan Lewis

Yeah, if we look at our main clients, they seem to be getting back to where they were, pre-COVID. And typically, in a normal year across all of the retailers, we get about 33% of all transactions would come in, in Q4, and 23% in Q2 and Q3 and 21% in Q1. So, it appears, it's feeling like the world has gotten kind of back to where it was. So that, I think, is about where we should be.

Rudy Kessinger
Got it. And then just on the new sales reps. I know you had hired a handful that started just recently. Maybe it's a bit too early, maybe not. But just how are they ramping relative to expectations? And I guess, more importantly, how are they ramping relative to the past reps who you had hired over the last year or two and didn't work out?

Bryan Lewis
I think that they're ramping a lot faster. Chris actually had an off-site with his team and they did a lot of training. One of the things I think that we did differently was how we went about hiring the people and making sure we've got people with industry knowledge which makes it so that, one, the ramp is a lot quicker. You're not explaining the industry to them.

Two, they all came here knowing that they would make less money than they did last year because they all had pipelines and everything, but the opportunity they saw made them want to come.

So that's, I think, a very exciting thing. And between the training program that Chris has put together and is working with them on, their industry knowledge, I'd say that they're ramping faster.

Rudy Kessinger
Got it. And then just last for Jeff. How should we think about kind of the normalized OpEx run rate from here? You stepped down about $400,000 on GAAP from Q2 to Q3 on non-GAAP, a bit more of the ex-Op comp. What's kind of the right OpEx run rate we should use for Q4, going forward?

Jeffrey Ishmael
Yeah I think--Bryan and I've been talking about the OpEx, a lot. We've talked about being much more efficient in the deployment of that spend, and I think we're going to keep a pretty high critical eye on that spend, going forward.

We anticipate that we're going to have additional spend, as we ramp out the sales and marketing teams but again, we're going to look at percentages that are going to be in the same approximate range.

Rudy Kessinger
Got it. Thanks, that’s it for me.

Operator
Our next question is from Mike Grondahl with Northland Securities. Please proceed

Luke
Hi, guys. This is Luke (PH) on for Mike. I just wanted to start with the new products and use cases and expanded digital applications, which you guys had mentioned in the press release and touched on earlier with the Business Intelligence.

But I was just wondering if you could expand a little more on this or give a little more color as to the types of products, use cases and how this is expanding digital applications. And just any color there would be helpful.

Bryan Lewis
Yeah, well, if you think about sort of the drivers, mobile apps now for age-restricted delivery, which that's all using our APIs, SDKs, all of our banking clients are certainly--we are in their mobile apps now.

Number 3, it certainly said that '23 is going to be a digital year for them. So, everything from their retailers' websites for credit to their online banking tools, so those types of things.

So again, what people realize we continue to grow in the digital world but we continue to grow faster in the on-premise world because that is growing faster than the digital for most things where people are applying for something like we have. But the products work; we've got plenty of clients using them, and the digital use continues to increase every quarter.

Luke
Got it. That's helpful. And then I just want to touch on those two southern banks that I think you guys mentioned were supposed to be impacted in 3Q. I think last call, you mentioned one of them actually finished the pilot but was waiting for some software updates to the teller workstation and then the other was going through an InfoSec review. Any updates to call out there?

Bryan Lewis
Yeah, so, both of them are now working through the contracts. One of them, I was just--just a few hours ago, talking to Chris about it. They want to be live in Q1--early Q1. So, we're putting a big push on there. Both are going exceptionally well; both are very happy with everything that we looked at and tried. And now, it's just dotting the I’s and crossing the T’s on everything that goes into a master securities agreement with the bank.

Luke
Well sounds good. Well thanks, guys, that’s it for me.

Bryan Lewis
Thank you.

Operator
And our next question is from Daniel Hischman with Craig-Hallum Capital Group. Please proceed.

Daniel
Hey, guys, thanks for taking my question. This is Daniel (PH) on for Jeff. Just first off, just looking at the billings, just kind of looking at how we calculate that. Looks like it's down, year-over-year.

I'm just wondering about your satisfaction with the bookings and whether or not that's meeting your expectations in terms of ramp and how the sales reps are doing.

Bryan Lewis
Well, the SaaS revenue is up, and I think that's one of the things that, I think, I guess maybe screening tools and what people are looking at.

We had two extraordinary large hardware purchases spread out across two quarters last year that we did as an accommodation for Number 3 because they thought it would help them roll out to their teller workstations faster, if they just bought it through us, since they already had an MSA.

They had to go negotiate it. We figured it would take them forever. And having negotiated with this bank, I know it takes a very, very long time. So, I think that kind of skews the picture a bit.

Now--and then we got to look at two things. There was the sale of people that we had who we no longer have because it just wasn't ramping fast enough. Thankfully, through some of the folks that were good, we had a pretty robust pipeline. And we also have clients who continue to find new use cases. We're doing that while the team--the sales team ramps.

And the good thing, too, is it's not like we need the sales team, the new team to be experts on everything. They just need to be able to get meetings because then, myself and Chris and anybody else in the company can get on the sales calls with them.

So, that's one of the reasons that we wanted to focus on people that had connections. We're selling into the space, because all we want is a meeting. So and then they can learn by listening to us do the calls in the meeting.

Daniel
Okay. Thanks for that color. And then you mentioned the pipeline. Just any color on the pipeline and how that's changed, over the last three months?

Bryan Lewis
I think the main way it's changed is different--new and different verticals. And often, I think that's because of some of the existing folks that we brought in, who had sold sort of large deals from some of our competitors.

They're here now calling up where they sold those deals and saying, I know you had issues, I'm here because it works a lot better. So, that's bringing us into, I think, new markets. But our focus is still on stopping identity theft in financial services because that's an area of pain, right. We can, immediately, stop losses.

So many other areas are, it's nice. The law still says for age-restricted products, all you have to do is look at a license. We don't have to try and validate it. So, we try bank opened this company and it's like the delivery service we're working with, who want to make sure they're doing the right thing and going beyond that.

But it's easier to sell and stop into pain and stop the pain, and we've got the reference clients that every one of our competitors would want. So, we've got a great advantage there and we'll continue to focus on that.

Daniel
Okay, that's it for me and thanks for taking the question.

Bryan Lewis
Thank you.

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

Bryan Lewis
So, I'd just like to thank everybody for attending. As always, all of us here at Intellicheck are excited about what we're doing, what we're stopping. The crime we stop, the pain we stop, both the banks and the victims from going to ,and we continue to do it. We've got a great team in place and I look forward to speaking to you all in the next call.

Operator
Thank you. This does conclude today's conference. You may disconnect your lines at this time and thank you for your participation.