

Intellicheck
First Quarter 2020 Earnings Conference Call
May 6, 2020

Presenters

Gar Jackson, Global IR
Bryan Lewis, Chief Executive Officer
Bill White, Chief Financial Officer

Q&A Participants

Scott Buck - B. Riley
Jeb Armstrong - Clear Harbor Asset Management

Operator

Greetings, and welcome to Intellicheck's first quarter 2020 earnings conference 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 star zero on your telephone keypad. As a reminder, this conference call is being recorded.

It is now my pleasure to turn the call over to your host Gar Jackson with Global IR. Thank you. You may begin.

Gar Jackson

Good afternoon, and thank you for joining us today for the Intellicheck first quarter 2020 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," "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 statements and risk factors listed from time to time in the company's filings at the

Securities and Exchange commission. Statements made on today's call as of today, May 6, 2020.

Management will use a 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 will begin today's call with Bryan Lewis, Intellicheck's chief executive officer, and then, Bill White, Intellicheck's chief financial officer, who will discuss the Q1 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 would now turn the call over to Bryan.

Bryan Lewis

Thank you, Gar, and welcome, everyone, to the Q1 2020 earnings call. It's amazing how much the world has changed since the eight weeks since the last call. I think I've started earnings call by letting you know how excited I've been about our performance and what we believed our prospects to be.

This time instead, I'll start by saying how saddened I am by the loss of the life due to this pandemic. Its impact has been felt in a personal way. One of our team members lost his mother to this disease.

Fortunately, I also see hope and recovery as I'm also happy to report that one member of our team has fully recovered from the virus. Both of these teammates have continued to give their all during these trying times. It has humbled me and made me want to work that much harder to ensure our continued success. I am proud of all the enduring hard work of all of our team members, and I remain excited to be part of this team.

Looking at our quarterly results, the momentum we had in the fourth quarter of 2019 continued into 2020, at least the first 11 weeks of the quarter. Total revenues for the quarter were just over \$3.1 million, which is up eight percent over Q4 and 144 percent greater than Q1 2019. SAS revenues for the quarter were just over \$2.2 million. This is down 12 percent from Q4, as we anticipated, due to the lower post holiday scan volumes, but was up 160 percent from Q1 2019.

I am pleased with the SAS members that validate that we are on track with our plan for Q1. If you recall, we said that 21 percent of annual scans coming in Q1, 23 percent in Q2 and Q3, and 33 percent in Q4. So, a 12 percent drop in a typical quarter would be expected. We had great momentum leading into mid March, and I believe that if we hadn't been impacted by the pandemic, then we would have seen an increase in total SAS revenues quarter over quarter.

That being said, it is a different world in the near term, and undoubtedly this large shutdown of retailers, bars, restaurants, and many bank branches will have a significant impact on Q2. More on that later.

We also had an unusual amount of hardware orders this quarter that accounted for 28 percent of our revenue, resulting in a drop in gross margin. Gross margins typically run in the 85 percent range.

So, let me now draw your attention to some highlights in the quarter. Financial services company number one, a top ten bank, brought live a ten member jewelry consortium. This is a newly won client for number one, and it is interesting to note that number one made a condition for them to get in the card program the mandatory usage of Intellicheck's retail ID mobile to authenticate IDs as a first step of the credit application process. I think this, again, shows that banks can use the fraud fighting power of Intellicheck to gain a competitive advantage and provide better rates on their credit card programs and induce prospects to switch banks for better rates.

Financial services company number two, one of the largest providers of private label credit cards, continues to move forward with implementation progressing. We now have 15 implementations completed and have ten in the pipeline since we renegotiated their contract. And they continue to work with us to bring more of their clients live.

As I said last call, financial services company number three, a top ten bank, placed a large order for scanners for the telework stations in Q1. As I also said on the Q4 call, this company's project is significantly delayed on their end, and although they hope to roll out in April, their project's delayed again. On the credit card side of the business, they've been diligently working on their large home improvement retailer and are currently targeting to go live with that client end of September. This will be the second of four large retailers that they are trying to get live by year end.

Financial services company four has completed the rollout of their challenge use cases. Some examples of these use cases include when someone wants to link a PayPal like Google Pay, Apple Pay, PayPal, et cetera to their account or when someone asks for access to their digital account or if an employee wants to log into certain systems. They will all be required to authenticate. They are using our person not present tools to remotely authenticate the caller's drivers license and grant access. Number four continues to find new ways to implement our core authentication tools.

Financial services company number six, the provider of subprime unsecured loans continues to roll out to their over 700 locations with 488 now live.

We put out a press release in April about financial services company number seven, the global financial services company providing payment, travel, and expense management solutions.

They were seeing such a spike in online fraud, they expedited and expanded the implementation of our web product to their call centers. The (unintelligible) due to roll out as soon as we get 18 approvals from the Canadian telecom providers to send text messages.

The pilot for the Canadian lender, financial services company number eight, is underway and about halfway through the pilot with great success as we are effectively stopping fraud for them. They are very pleased with the results they are seeing so far.

I'm excited to announce that we have two new financial services firms as clients. Financial services company number nine is a regional bank headquartered in the Midwest. They have over 1,100 branches in ten states. This bank has completed the integration into their teller platform and are beginning to start training their employees on the product. They will be using Intellicheck technology solutions to authenticate people prior to certain teller transactions like cashback, money orders, cashier's checks, and any transactions \$2,000 and above. This client is on our per scan model with monthly minimums, and they have rushed this as a COVID-19 project and are targeting June 15th to have it completely rolled out.

Financial services company number ten provides loans for medical procedures and are also on our per scan model with monthly minimums. Their goal is to help healthcare providers explain their client base and make medical procedures affordable for patients. This client, that went live in March, is using our web tools to authenticate patients before providing financing.

Some of you may have seen a press release we put out on the 40 store Midwest furniture chain. Given that their stores are closed but people still need furniture, they were taking orders over the phone for curbside pickup. Their problem was payment was in advance and the card numbers were manually entered for processing. This means that the credit card EMV chip is not activated, and the retailer was eating the losses. Given how easy it is to buy stolen credit card numbers online, this was getting expensive.

They decided the way to stop this was to use our no integration web product. All they need to do is log into our website, and they are authenticating in a person not present environment. They send a text to the purchaser, which instructs them to scan the barcode and take a picture of the front of the license. In seconds, the sales associate sees on their screen whether the license is real or fake. The losses instantly stopped.

During the quarter, we further invested in our camera technology capabilities, a feature that we believe is becoming more and more relevant to the online authentication process. We acquired the source code for the mobile and web camera technology that we currently lead. I have spoken in the past regarding my sense that a company that provides this technology might potentially be a logical acquisition from a vertical integration standpoint so that we own more of a comprehensive product offering.

Instead of buying a company, we were able to acquire rights to the source code, which our programmers are able to improve upon and build out the product to our specific parameters. We believe this business transaction was carried out on much better terms than a purchase of a company. In addition to controlling the development, we believe it should pay for itself in less than four years versus continuing to pay the yearly leasing costs. And most importantly, we control our technological destiny.

While I've very excited about what we accomplished in Q4 and the momentum that carried in Q1, the current unfortunate situation in our country and the world impacts our business. In our nationwide stay at home orders, however, do not mean zero revenues. We have a growing online with 14 retailers, allowing customers to apply for credit on the website and multiple of our financial services companies are using our web tools and the call centers for everything from card applications to account changes. All of our clients, even those on a per scan model, have minimum monthly payments.

Finally, many of our clients were deemed essential services. So, they remain open. Office supply stores, electronic stores, and big box stores that sell everything from groceries to tires remain open for the most part. However, there were still many high scan volume stores that completely shut down. Given the current market and what we know today, we are hoping to achieve about 60 percent of the SAS revenue in Q2 that we had in Q1.

From there, we anticipate things will begin to ramp back up as more retailers and restaurants open up and we see increased transaction activity. I am excited to say that we believe that we are beginning to see light at the end of the tunnel. The good news is our company has been 100 percent capable of working from home. Implementation work has continued. New product development continues to make progress. And, as you can see, sales did not stop.

Our clients' IT departments can also work from home. So, implementations are making progress, and the weekly status meetings continue. States are beginning to loosen restrictions, leading to limited and then increasing stores, restaurants, and bars opening. Major mall owners are discussing their opening plans and Simon (sp), the nation's largest operator of shopping mall properties, has already opened 49 of their malls, the majority of which are located in the states of Texas, Indiana, and Georgia.

It is important to remember that even during this pandemic, fraud did not stop. Identity thieves just moved online faster. Where some of our clients did not think that online fraud is much of an issue, they do now, which is one of the reasons that, in addition to continued demand for our on premise solutions, we're seeing the increased demand for our person not present web and mobile authentication solutions.

Fraud has not stopped, and neither has identity theft. The reality is that identity theft is not going away. We know that information required for a criminal to take your identity is everywhere. Over eight billion records were breached in 2019. The record setting pace of data

breaches in 2019 continues in 2020, and the cost of identity theft continues to grow. Javelin Strategy and Research (sp) published their research in their annual report on identity theft and found that the amount of money lost to identity theft in 2019 grew by over \$2 billion to \$16.9 billion.

Both published research and customers tell us that while new accounts and card not present credit card theft is on the rise, growing at an even faster rate is account takeovers where the criminals completely take over your savings and checking accounts or get e-debit or credit cards sent, all easy enough to do with the right information and a call to a call center. This just recently happened to our office manager. Somebody called her bank, had enough info to convince the bank they were her, that she had moved, and had lost her credit card and needed a new one sent. Had that bank been using our call center web product, that wouldn't happen. This bank was financial services company number four, and that is now one of their challenges use cases.

As account takeover fraud is growing at a tremendous rate, Transunion estimates that it grew by 347 percent in 2019. Intellicheck provides the easiest, low restriction way to authenticate a person and stop account takeover. The person clicks on a text, activates their camera, and they don't even have to focus. Just put the barcode in the crosshairs, and Intellicheck solutions does the rest.

As we have earlier said, you can even add facial recognition to match a face to the front of the license. As we see more and more need for enhanced authentication, we believe that we are well positioned to respond. I think this is of significant importance because I believe that increasingly enhanced authentication will become the norm.

The important takeaway here is that, while the coronavirus has put quite a damper on our near term trajectory, it has not put a damper on my enthusiasm or optimism given the basic fact that the fundamentals have not changed. We still stop identity theft in real time with over 99 percent accuracy. Our clients continue to be our best supporters and references. And demand for what we do, we believe, will continue to grow. As our country and Canada work towards a full opening and recovery, we believe we'll be right back on that growth trajectory we were experiencing pre-COVID-19.

With that I will turn it over to Bill to discuss the financials.

Bill White

Thank you, Bryan, and a good day to our shareholders, guests, and listeners. I'd like to discuss some of the financial information that was contained in our press release for the first quarter ended March 31, 2020, which we released this afternoon.

I'll begin with our first quarter results. Revenues for the first quarter ended March 31, 2020 grew 144 percent to \$3,115,000 versus \$1,279,000 for the same period last year. Our SAS

revenue, which was approximately \$2,238,000 for Q1 of 2020, a 160 percent increase from \$861,000 in Q1 2019.

Gross profit as a percentage of revenue was 77.8 percent for the quarter ended March 31, 2020, compared to 85 percent for the quarter ended March 31, 2019. During the quarter, the company sold scanning equipment to a bank preparing to roll out our software to their bank branches, which are normally sold at lower margins.

Operating expenses, which consist of selling, general and administrative, and research and development expenses increased four percent or \$92,000 to \$2,398,000 versus \$2,306,000. Company posted net income of \$27,000 for the three months ended March 31, 2020, compared to a net loss of \$1,213,000 for the quarter ended March 31, 2019. The net income per diluted share was zero versus a net loss per diluted share of eight cents in the prior year.

Adjusted EBITDA for the quarter ended March 31, 2020 was \$144,000, compared to a negative \$787,000 in the quarter ended March 31, 2019. Interest and other income was negligible for the quarters ended March 31, 2020 and 2019.

Now, I'd like to focus on the company's liquidity and capital resources. As of March 31, 2020, the company had cash of \$3 million, working capital defined as current assets minus current liabilities of \$3.1 million, total assets of \$14.3 million, and stockholders' equity of \$12.1 million. During the three months ended March 31, 2020, the company used net cash of \$341,000 compared to net cash used of \$535,000 during the three months ended March 31, 2019. Net cash use and operating activities was \$461,000 for the three month period ended March 31, 2020, compared to \$542,000 for the same period in 2019. Net cash used in investing activities was \$115,000 for the first quarter of 2020, compared to net cash generated by investing activities of \$7,000 for the three month period ended March 31, 2019.

During the quarter, we generated cash of \$235,000 from financing activities for the three months ending March 31, 2020, while we did not have any financing activities during the quarter ended March 31, 2019. The company has a \$2 million revolving credit facility with Citibank in its secured collateral accounts. There are no amounts outstanding under this facility, and we currently anticipate that our available cash as well as expected cash from operations will be sufficient to meet our anticipated working capital and capital expenditure requirements for at least the next 12 months. As of December 31, 2019, the company had net operating loss carry forwards of approximately \$17 million.

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

Operator

Thank you. At this time, we'll be conducting a question and answer session. If you'd like to ask a question, please press star one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star two if you would like to remove your line

from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment while we pull for questions.

Our first question comes from Mike Rondall (sp) with New Orleans Securities. Please proceed with your question.

Mike Rondall

Congratulations on the growth and sort of the operating leverage in the model. It's nice to see net income positive too. First question for me is--can you guys talk at all about monthly transactions sort of February, March, April just so we can kind of get a sense of how April is being affected a little bit?

Bryan Lewis

I guess my--it kind of goes to the 60 percent of where we're hoping to be. We were flying along, I'd say, Q1 until stores started closing down. I think the best thing--the closest we can get to giving something is the fact that we anticipate--our goal is to get 60 percent of the SAS revenue.

Mike Rondall

Got it, okay. Do you have any sense for lost revenue in the quarter due to COVID? Have you attempted to estimate that at all?

Bryan Lewis

Well, where we are compared to plan is--things that we're looking at--having the world be shut down is certainly an impact. Now, again, as I said, we've got--a lot of our clients were considered essential services. But, it doesn't mean that business is back the way--just because they're opened--you can't go to the store. You've got to buy in advance, or you can walk around the store but they're limiting to maybe 50 percent of capacity. So, that's--all those things impact the scan logging. And if you only have 50 percent of people in stores, you only--that gives you a pretty good idea potentially what you're saying, what you might see in terms of scan loss.

Mike Rondall

Got it. Maybe Bill, could you help us out with just sort of the delta or the difference between the \$3.1 million total revenue and the \$2.2 million of SAS revenues, sort of--what's that roughly \$900,000 difference between those?

Bill White

During the quarter, we had over \$700,000 in hardware sales to a major bank that's rolling out to their bank branches. So, that's really a material portion of the difference. There is--.

Bryan Lewis

--We had--yeah--part of it was to the bank. Part of it was to a telecoms provider. So, we had sort of--three different clients came in and said, "We need hardware," which is, from our end of it, kind of an anomaly. Hardware's not our goal. But, if it makes it easier for the client to be able to install our system, then it's easier for them to order it through us, we'll do it. But, it's definitely a different margin because we're just--we add a markup to it--.

Mike Rondall

--Sure, any of that planned for 2Q or 3Q that you're aware of?

Bryan Lewis

No, not--at this point in time, I don't see anything like that. No.

Mike Rondall

Okay. And then, maybe lastly, of the financial services customers you're now up to ten, what one or two really stuck out for you in the last 90 days?

Bryan Lewis

By meaning stick out--are you saying who do I see the most revenue from or what I think are large?

Mike Rondall

Yeah. I mean, who embraced you the most, or where do you see the most incremental upside?

Bryan Lewis

Well, the thing I'd say is all of them, once they see what we do for them, embrace us. I hate to say that I have favorites because it's like trying to pick your favorite child. But, number four finds all sorts of ways to use us. Number seven is figuring out how they roll us out even faster. Number one continues to be a great partner with us, and I love the fact that it's very obvious they use our fraud fighting capability to get a new client. And I think we'll see more of that. And number two--I keep saying here--here's a new client, one of their retailers that they want to bring on board.

So, I've got to say, since they're all--the world that we were focusing on were the top ten banks and then Amex and Discover being the majority of credit card issuers. And since everybody we're talking about is in that space, I've got to say, we're doing very well with all of it. And now, we're even moving into the super regional banks. I think the healthcare financing space is going to be really big for us. So, I look at them all as, again--we believe--we're still just scratching the surface of each and every one of these financial services companies that we have as clients because it's early days of roll out and integration.

Mike Rondall

Perfect. Okay. Hey, thanks, guys.

Bill White

Thanks, Mike.

Operator

Our next question comes from Scott Buck with B. Riley. Please proceed with your question.

Scott Buck

Hey, good afternoon, guys. It sounds like you have some delayed implementations, and then, you've added a handful of new customers as well. I know the beginning of the year you were thinking implementations for the full year would be similar to 2019. Do you mind telling us where you are now and kind of what direction you see that going through the remainder of the year?

Bryan Lewis

Yeah. And Bill can give you the exact number because that all falls under him. But, the implementations are--the work behind the scenes hasn't really dropped off. And that's part of, thankfully, our ability to be a remote company and most of our clients also being able to have their IT companies work remotely.

Obviously, if a store's not open, they're not rolling out the product. So, that might delay the actual first scan. But, it doesn't mean that we're not working on the integration and the logistics behind the scenes. And Bill, do you want to--what's the number of implementations that your team's working on now or have scheduled?

Bill White

Yeah, Bryan. In Q1, we completed six integrations, and we have 34 integrations in place currently.

Scott Buck

Okay, great. That's helpful. And the current team is sized to be able to handle that kind of volume, or will you need to add some heads there?

Bryan Lewis

No. I would say that the current team can handle probably even double that. We don't need to go on site. It's all completely done virtually. We--part of what we did in 2019 was the professionalization of that team. And we've got packages. When somebody says they're ready to go, here's a package. We send them everything they need to be able to catch and get the data to us in the way that we need. So, I'd say they're really good.

Eventually, might I look at hiring somebody to do customer supports? Most of the time, our customer support doesn't do--it's nothing to do with any of our large retail clients. It's some bar owner locked himself out of the web application and needs to figure out how to get a new

password. And that's also something that we look at. Probably cheaper to outsource that, get a call center that can do password reset.

So, we don't anticipate a major amount of employees needed to make the company even twice the revenue.

Scott Buck

Great. That's helpful. And last one for me--yesterday, you made the announcement of your first foray into the healthcare space. How do you think about that vertical longer term? What's the opportunity there versus what you've been doing on the financial services side and how should investors think about your ability to ramp up in that space?

Bryan Lewis

Well, I think that certainly there's a large industry, I guess, of people that provide loans into that space. And there's also, I think, a significant amount of fraud that goes on in the insurance space. So, the next thing I want to make sure the guys are working on--are we talking to all the major insurers, Medicaid, Medicare, Aetna, the folks we get our insurance from, Blue Cross Blue Shield, whatever? What do they need in the way?

I'm told from doctor friends of mine that there is fraud in this space and identity theft happens. So, again, we're such a simple solution. Do you need something embedded into the system, or do you just need it on a phone and scan a license and weed out the bad guys? What I like is we are definitely set to be able to deliver authentication, on prem, off prem with multiple delivery vehicles. So, I--my hope is that there's something significant to be had there for us.

Scott Buck

Great. Appreciate the color, guys. Thanks a lot.

Operator

Our next question comes from Jeb Armstrong with Clear Harbor Asset Management. Please proceed with your question.

Jeb Armstrong

Good afternoon, Bryan. I hope you guys are well.

Bryan Lewis

Yep, you too, Jeb.

Jeb Armstrong

I just wanted to fire a question at you about your interest in getting a loan via the paycheck protection program, your thoughts surrounding that.

Bryan Lewis

We did. I think that the--if you look at the types of companies that they were looking at, I think for this, we fall right into it being, thankfully, all 34 of our employees are still employed. So, we thought it makes sense, and we did.

Jeb Armstrong

Was there anything that you were able to get because of that? How much were you able to get, I guess, is the question?

Bryan Lewis

Uh, \$796,100.

Jeb Armstrong

Okay. Was that after the end of the first quarter?

Bill White

It was in April.

Jeb Armstrong

It was an April, okay. I want to turn to a press release you put out just at the end of April talking about providing free online, the--providing a free 90 day--cost free 90 day trial and sort of your thoughts around that and how you think you'd be able to monetize that opportunity.

Bryan Lewis

Well, I guess a couple things we looked at. Certainly, the statistics we were seeing showed that online fraud was happening more. And if you look at the furniture company that we were looking at, you know, that used it now for the credit card purchases and curbside pick up. As a team, we were talking about it, and it really kind of annoyed all of us that, in this really crazy time--the last thing I need to do is to have my identity stolen.

And in 2019, the cost that consumers bore on this fraud doubled to \$3.5 billion because so much of it is--it's hard to prove it wasn't you. So, I guess a couple things. One, in a very altruistic manner, we decided let's stop this. And then, my bet is, if somebody uses it and they realize--they see how good we are at what we're doing, then hopefully we can monetize it. But, right now, what we just decided is, as a company, we wanted to do was--let's not make a bad situation worse for somebody who might be unemployed, might not have the wherewithal to even pay their bills and then they're screwed by a crook stealing their identity.

Jeb Armstrong

Has there been--how much interest has there been so far in accepting that free 90 day trial?

Bryan Lewis

I think there's been definitely interest. The sales teams are talking to people now. And the good thing from our end is, again, what we're offering them is this simple web product, which

all they need to do is log into a website, and there's no integration required. They can be up and running as soon as they're comfortable with it.

Jeb Armstrong

Great, thanks, Bryan. Have a great day.

Bryan Lewis

Yeah, you too, Jeb. Have a good day.

Operator

We have reached the end of the question and answer session. At this time I'd like to turn the call over to Bryan Lewis for closing comments.

Bryan Lewis

Closing comments are always--I always forget about. I never write them into my script. But, I just want to thank everybody. I've spoken to many of the investors. What I'd like to say is I want to thank you for your continued support in the company and the team. It means a lot to me. We're working through this. I see good things happening, hopefully, on the other side. And I just hope everybody stays healthy. So, thank you.

Operator

This concludes today's call. You may disconnect your lines at this time, and we thank you for your participation.