FlexShopper, Inc. Second Quarter
2019 Earnings Conference Call
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Operator: Greetings and welcome to the FlexShopper Second Quarter 2019 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 one on your telephone keypad. As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Jeremy Hellman of The Equity Group. Thank you, Sir, you may begin.

Jeremy Hellman: Thank you. I would like to remind everyone that we have posted an updated investor presentation within the IR section of the company website www.flexshopper.com. This presentation includes forward-looking statements that are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements reflect our current views with respect to future events and involve inherent risks and uncertainties which could cause actual results to differ materially from our historical experience and present expectations or projections as a result of various factors including those risks and uncertainties described in the risk factors and the management's discussion and analysis of financial condition and results of operations sections of the company's most recently filed annual report on Form 10-K and subsequently filed quarterly reports on Form 10-Q.

One can find many, but not all, of these statements by looking for terms such as belief, expect, hope, project, may, will, should, would, could, seek, intend, plan, estimate, anticipate, and similar terms. All statements other than statements of historical facts included during this conference call including statements regarding our strategies, prospects, financial condition, operations, costs, plans, and objectives are forward-looking statements. We urge you to consider those risks and uncertainties in evaluating our forward-looking statements.

We caution listeners not to place undue reliance upon any such forward-looking statements which represent our estimates and assumptions only as of the date hereof. Except as required by law, we undertake no obligation to update any forward-looking statement whether written or oral that may be made from time-to-time whether as a result of new information, future developments, or otherwise. We anticipate that subsequent events and developments will cause our views to change. With that, I would like to turn the call over to FlexShopper's CEO, Brad Bernstein. Please go ahead, Brad.

Brad Bernstein: Thank you, Jeremy. And welcome everyone to our 2019 second quarter earnings call. I'll start by providing several business highlights from the quarter and then I'll hand the call over to our CFO, Russ Heiser, who will discuss our financial results and balance sheet in more detail and then I'll return for some last comments before we open the line-up to your questions. First, I'm very pleased to report another quarter of solid positive adjusted EBITDA which was $1.7 million for the second quarter.

Combined with our strong first quarter adjusted EBITDA results, we have already exceeded our prior guidance for the year of $4 million, and as a result, we're raising our adjusted EBITDA guidance. Russ will discuss this along with our other guidance metrics shortly. As we come into the second half of the year, I want to remind everyone that beginning with the back-to-school season and through the Holiday season in Q4, we increased our direct-to-consumer marketing efforts since our services are in greater demand.

Historically, we have generated more than 45% of our B2C originations in the fourth quarter. With this demand, our marketing spend is typically the most efficient and optimized during this period. While the increased spend seasonally mutes fourth quarter results compared to other quarters, these originations drive revenues, gross profit and adjusted EBITDA in future periods. Each year, going back to the time we started FlexShopper over five years ago, we have been building upon building lease originations which has led to this inflection point of a critical mass of annual lease originations.

We are now very focused on surpassing that point and continuing to generate more adjusted gross profit, adjusted EBITDA and continued improvement in bottom line results. In the second quarter of 2019, gross lease originations increased 43.4% to $13.2 million from $9.2 million for the same quarter last year. Driving that growth was a combination of repeat customers along with new customers particularly through our B2B partners.

Through June 30, 2019, our B2B retail channel contributed approximately 25% of all lease originations compared to less than 7% in the same period of 2018. I'm very pleased to report that during the second quarter, we completed rollouts to over 560 locations between two regional retailers that increased our total retail store count and national footprint to over 1,200 retail locations compared to 322 locations this time last year.

The full impact of these rollouts will obviously be seen in future quarters. Again, this is a testament for innovative lease purchase finance approach at the point of sale and our mobile lease to own technology which is turnkey integrationless and pays the retailer immediately.

We're very focused on parlaying this success into more retail partnership opportunities. Obviously, having satisfied retailers as points of reference is very helpful in growing this business. For Q2 2019, we continue to lower our average cost to acquire customer, which came in at $58 compared to $167 for the same period in 2018.

Our overall acquisition cost of benefiting from the growth in our B2B retail channel, which is a great source of lower acquisition cost customers for FlexShopper. I'm also pleased to report that repeat customers represented approximately 45% of lease originations in Q2 2019 and this is representative of the payback we get in future periods when we invest in our direct-to-consumer channel flexshopper.com. I'm now going to hand the call over to Russ Heiser, our CFO, to discuss our financial performance and provide an update on our 2019 outlook. Then I have some final commentary before we open the call for some questions.

Russ Heiser: Thanks Brad. Let me quickly highlight some of my comments from previous calls.

Russ Heiser: Apologies, I'm not sure what happened there. But we'll start off with my section again. So, I wanted to highlight some of my comments from previous calls and review how ASC 842 changed the way we record revenue this year versus previous years. Historically, FlexShopper reported all lease revenue, which is analogous to all of our charges, and then the operating expense section of the income statements had a provision for bad debt expense. That is the estimate of charges that would not be paid based on historical results.

In this year's filings and going forward, the provision for bad debt expense will not be broken out separately, but net against the lease revenue number on the income statement. Therefore, in MD&A section, we will continue report in a manner consistent with prior periods in order to facilitate period over period comparisons and provide the gross revenue metric used for company guidance. Next given that the online business still represents the majority of our lease originations, I want to remind everyone of the trends in our online business and how that translates into revenue and EBITDA trends for the entire company.

As Brad mentioned earlier, there is significant seasonality in our online business. As such, a large portion of our online marketing spend takes place in the fourth quarter. However, revenue from those holiday period late fourth quarter leases isn't really seen until the following year as we recognize the revenue over the life of the lease, which is typically 52 weeks. Therefore, in looking at our online business quarterly, it's important to note that the first quarter combines the rapid growth of revenue from online leases originated in the previous quarter but is usually the quarter of the lowest online marketing spends to produce the highest online EBITDA of the year.

In the fourth quarter, conversely, revenue only has the tail end of the previous year's holiday season originations. It has the highest online marketing spends and therefore the lowest online

EBITDA of the year. The intervening quarter simply post online revenue and EBITDA numbers between those two extremes. Therefore, projections and guidance are about forecasting the seasonality of the online business balance against the patterns of the quickly growing retailer rollouts that create step function increases in both gross profit and EBITDA during these rollouts. This is best illustrated by the increase in guidance aligning with the growth in new retailer doors.

Midway through the year, we're tracking ahead of plan across the board. While our top line has grown very nicely with net revenues and gross profit up over 50% for the first six months, we were also able to moderate our marketing expenses which were down 52% from last year. Coupled with a 10% reduction in salary and benefit expense, we've been able to really leverage the top line growth and seeing it translate into growth of adjusted EBITDA, which is up over $5 million versus the first six months of 2018.

I will now move on to discuss changes in management's guidance. As shown in the press release, which is available on flexshopper.com and in the investor presentation, we are again increasing guidance and now expect gross revenue greater than $112 million, which is $2 million increase, adjusted gross profit greater than $26.5 million, which is a $1 million increase, adjusted EBITDA, greater than $5 million for $1 million increase and gross originations greater than $72 million or $2 million increase from prior guidance. Here's Brad for some final thoughts.

Brad Bernstein: Thanks Russ. In closing, we're very pleased with our second quarter results. Halfway through the year, we have delivered adjusted EBITDA of approximately $4 million resulting from the development of, in our view, a well-rounded business executing on multiple fronts. This includes steady lease portfolio returns, continued lease origination growth, continued repeat business and other channels kicking in such as our B2B retail channel. Towards the end of last year, we were guiding everyone that we would get to this inflection point, and now it is here. More importantly, we believe we have only just begun penetrating the $25 billion virtual lease to own market opportunity. With that, we'd be happy to take your questions.

Operator: Thank you. Ladies and gentlemen, at this time we will be conducting the question-and-answer session. If you would like to ask a question, please press star one on your telephone keypad. A confirmation tone will indicate that your line is in the question queue. You may press star two if you'd like to remove your question from the queue. For participants using speaker equipment, is may be necessary to pick up your handset before pressing the star keys. Our first question comes from Theodore O'Neill with Ascendiant Capital Markets. Please proceed with your question.

Theodore O'Neill: Thank you. Congratulations on the good quarter and the raised guidance.

Brad Bernstein: Thank you, Theo.

Theodore O'Neill: Yeah. Just a quick question here, if I'm doing the math right, it looks like the cost of lease revenues went up slightly in the June 2019 compared to 2018. Is that a mixed issue? Is that any highlight you can give us on that?

Russ Heiser: Sure, Theo. It's essentially as we move through the 90 days same as cash from the prior holiday quarter, we see a change in bad debt expense.

Theodore O'Neill: Right, got it, okay. Thanks very much. That's it for me.

Brad Bernstein: Thank you.

Operator: Thank you. Once again, to ask a question at this time, please press star one on your telephone keypad. Our next question comes from Richard Deutsche with National Securities. Please proceed with your question.

Richard Deutsche: Yes, thank you for taking my call and thank you for a great quarter. We really appreciate it. I have a question though. Your quarter has been accelerating through your vertical in business to business. After starting your business on retail customers, this part of your business is on fire right now. And I'd like to see if you can give us a little color about your pipeline of potential new business customers, your client acquisition costs are plunging, your margins are rising sharply. And I'd like to see if you can give us just a little bit of insight as to how your marketing and, of course, success breeds success here. So, I'd really like to see, if you can give us a little look under the skirt here and tell us what you see going forward in business customer sign-ups?

Brad Bernstein: Yes, thanks Rich, appreciate the question. So, obviously, we're very bullish and confident about our retail pipeline. We don't disclose retailers but we're very excited about building upon the momentum we have. I mean, look, we rolled out to another 560 locations in the second quarter. Our footprints over 1,200 compared to 322 same time last year. And at the end of the day, our business development team is equally excited that they have a great product to sell which is our lease to own mobile integrationless technology that pays the retailer at the point-of-sale. I know I've said this many times but I really want to get across that that we really have broken down the barriers for the retail in terms of accepting lease to own in their store by not having to do an integration and by paying them immediately at the point of sale.

And we believe that a lot of the success that we're having is the traction that we're getting with this product. And obviously, we're also moving this product into multiple verticals that include furniture, electronics, tires. So, to answer your question, I can't give you details but I could say that we feel very strongly about the pipeline and we're very confident in terms of building upon this momentum that we've had in the last six, nine months.

Richard Deutsche: Okay, Brad. Thanks for that. But in the past, you have mentioned that you've taken on tests with new customers. And I just want to see if there was any way you could comment on just your expectations. I know it's not done until it's done but this is a tremendous driver of your financials and just wondered if you could talk a little bit, you've in the past mentioned some of these onboarding processes. Anything else you could say about that?

Brad Bernstein: Well, I mean I could shed light that that every retailer is different. Some retailers like to start with a test, a pilot, and some don't. So, for example I think a couple of months ago, we announced that we were rolling out to 120 plus store retailer that was just, okay, let's roll out to all the stores. No pilot, no test. Let's do it. We parlayed basically demonstrations or references and they just wanted to get the product in the stores and start getting incremental sales.

So, every retailer is different, not every single one is going to start with a pilot or a test. Obviously, and retailers also like to play close to divest and not sure what they're doing. But again, all I could say is just because we haven't announced any pilots has nothing to do with how we feel about the strength of our pipeline and continuing to build upon our success.

Richard Deutsche: All right, let me throw one more at you. This is a softball again. The chains that you've already opened up, is there room for them to continue to add more or are these fully at 100% or at the level that they want to stay at?

Brad Bernstein: That's a good question, Rich. And I have to say, from the time we started with some of these retailers, we worked very closely with them. We build, we help them build what we're doing on a lease to own basis into their store dashboards, so they can see how they're performing every day. We give them monthly recaps on performance and then we guide them on how to get more out of the program. And I have to say, working hand-in-hand with these retailers, we are seeing successive increasing results in the stores, and at the same time, it's always nice when you do have a retailer, which we have that is kind of on the acquisition hunt, and hear they're buying stores which, obviously, adds to, you know, our pot, also. So, no we've actually been very successful in terms of starting out and continuing to optimize and increase the leases that are getting generated out of these retail locations.

Richard Deutsche: All right, thanks for that. Just one final and I'll go back into the queue. I'm also interested in your third vertical which is payment option. We've had massive run-ups in certain FinTech companies in the past. That also seems an area where you have great margins and I see that business is just now starting to grow, also. Can you talk a little bit about what you're looking at in payment option?

Brad Bernstein: Very significant channel with very significant opportunity for us. And Rich, what you're talking about is that's where we're seamlessly saving the sale for a third-party e-commerce sites with a patented payment method where a consumer can check out with the items in that cart on a lease to own basis.

And yes, we're going to be executing a lot of marketing campaigns just to get that business. Fantastic channel, another low acquisition cost channel just like retail stores are too. And by the way, there are just pure play e-commerce sites that we're targeting and we go after with our payment solution but, obviously, also, a lot of retailers also have e-commerce sites and we work hand-in-hand with them and we're already saving the sales for them on those sites too.

Richard Deutsche: All right. Thanks. So, I'll get back in the queue. Thanks a lot, Brad.

Brad Bernstein: Thanks, Rich.

Operator: Thank you. Once again, to ask a question at this time, please press star one on your telephone keypad. Thank you. The next question comes from the line of Steve Emerson with Emerson Investment Group. Please proceed with your question.

Steve Emerson: First of all, congratulations, excellent quarter. Keep up the great work.

Brad Bernstein: Thanks, Steve.

Steve Emerson: In your guidance, I'm trying to get a sense of is this more directional or ultra conservative. And does the--if I take the numbers out for the rest of the year, it implies slower, slower EBITDA growth, which to me means you're upping your marketing spend for the second half of the year?

Brad Bernstein: Yes, I'll let Russ provide some more color, but yes generally yes going into the fourth quarter, we did last year in the fourth quarter we did about $27.5 million of gross lease originations. We did over 45% of our business. And obviously, that has to do with increasing our marketing spend on the direct-to-consumer side.

So, yes, as I said in the narrative, that marketing spend does mute our earnings for that period. But I think what everyone has to know what's really important is, what does it do for next year. What does it do for the following years? This is building upon, building upon, building of gross lease originations where we get payback for future years to come. So, you really do have to look at it that way. So, you're correct, we're obviously going to spend more marketing dollars in the fourth quarter, which does meet our earnings, but what does that mean going forward. So, Russ, if you'd like to add anything?

Russ Heiser: Sure, just to focus on one part of that. You know, I think that given that so much of the fourth quarter originations is sort of based upon the seasonality that we've discussed in the past, we are just being careful in the way we think through it and really just making guidance predictions about what we can truly see. You know, whether you want to think of that as ultra conservative or we just think it's a prudent way to move forward. But as I mentioned before in my piece that marketing spend will increase in the fourth quarter.

Steve Emerson: Can you give us by how much or sort of a dynamic number?

Russ Heiser: We've not made any--given any guidance around marketing spend for this quarter.

Steve Emerson: Okay. So, if I understand your tone, your increase to $72 million originations from $70 million is more a directional statement and that number could be considerably higher. It's more a very conservative kind of number, if I hear you right.

Russ Heiser: It is our best insight into where we stand today.

Steve Emerson: Thank you.

Brad Bernstein: Thanks, Steve.

Operator: Thank you. We have reached the end of our question-and-answer session. So, I would like to turn the floor back over to Mr. Bernstein for any additional concluding comments.

Brad Bernstein: Yes. Thank you for joining us today. We look forward to speaking with each of you again on our third quarter earnings call. Thanks again.

Operator: Ladies and gentlemen, this does conclude today’s teleconference. Again, we thank you for your participation and you may disconnect your lines at this time.