Sylogist Ltd.

First Quarter 2023 Earnings

Conference Call Transcript

Date:	**May 11, 2023**
Time:	**7:00 AM MT**
Speakers:	**Bill Wood** President and Chief Executive Officer
	Sujeet Kini Chief Financial Officer
	Rudy Shirra Director, Business Development and Operation Strategy

Operator:
Welcome to the Sylogist Limited Earnings Call for Q1 2023.

As a reminder, all participants are in listen-only mode, and the conference is being recorded. After the presentation, there will be an opportunity to ask questions.

I would now like to turn the conference over to Rudy Shirra, Director of Business Development and Operation Strategy. Please go ahead.

Rudy Shirra:
Thank you, Sachi, and good morning.

Joining me to discuss Sylogist's Q1 Fiscal 2023 results are Bill Wood, our President and Chief Executive Officer, and Sujeet Kini, Chief Financial Officer.

This call is being recorded live at 09:00 AM Eastern time on Thursday, May 11, 2023. Our investor presentation and the press release we issued earlier this morning are available for download along with our Q1 MD&A, financial statements and accompanying notes, all of which have been filed with SEDAR.

Please note that some statements made on the call may be forward-looking. Actual events or results may differ materially from those expressed or implied, and Sylogist disclaims any intent or obligation to update or revise any forward-looking statements, whether as of a result of new information, future events or otherwise. The complete Safe Harbour Statement is available both in our MD&A and press release, as well as on sylogist.com. We encourage our investors to read it in its entirety.

We are reporting our financial results in accordance with International Financial Reporting Standards, or IFRS. As before, we will also discuss non-IFRS performance measures, which should be viewed as supplemental. The MD&A contains definitions of each one used in our reporting.

All of the dollar figures expressed on this call are Canadian unless otherwise noted.

I'll turn it over to Bill first for opening remarks, then Sujeet will make some introductory comments before reviewing our Q1 financial performance. Then Bill will conclude with an outlook on our business and markets, following which we will open it up for questions.

With that, Bill?

Bill Wood:
Thank you, Rudy, and good morning everyone.

As most of our listeners will know, Sylogist is a software-as-a-service, or a SaaS company, that provides mission-critical solutions to over 2,000 customers worldwide, primarily in three public sector verticals: education, non-profit and non-governmental organizations, and government. We help mid to upmarket public organizations more effectively fulfill their missions with flexible, advanced software solutions that address their unique needs. Our platform scale deliver clear ROI and provide cloud-based user-friendly and secure technology to manage an entire organization.

Before I get into the details of another exceptionally strong growth quarter, let me say how proud I am to be introducing Sujeet Kini as Sylogist's new Chief Financial Officer. With over 20 years of experience as a financial and operational leader, Sujeet's resume includes executive leadership roles at HootSuite, Solium and BlueCat. I look forward to meeting investors together with Sujeet at our upcoming Investor Day in Toronto in June, details of which are to come. Now, back to our results.

Momentum has continued in Q1 with Sylogist achieving record quarterly revenue of $15.9 million. That's an organic growth rate of 21% or 17% on constant currency basis. This growth was broad-based across the business. Recurring revenue was strong in Q1 at $9.8 million, a 12% year-over-year growth rate. This was led by our cloud revenue which grew 14% year-over-year. We see this growth as a validating measure of how successfully we are executing our profitable growth strategy.

This growth is supported by a strong foundation of profitability. Sujeet will offer more details momentarily, but I am pleased with this quarter's overall posture of 45 against a Rule of 40 benchmark.

Bookings were excellent this quarter, adding to our backlog of future revenue. We closed $7.7 million in bookings, reflecting expanded strength in demand, the quality of our pipeline, and our team's ability to convert opportunities into wins.

I'd also like to share some of the in-flight initiatives we are excited about, which we believe will help capture even greater improvements to our top and bottom lines.

First, we are continuing to strengthen our go-to-market efforts, including our partner ecosystem. Building out a high-quality, high-performing partner channel is a key 2023 priority as it allows us to increase our reach to further expand our highest value creation level, that of subscriptions. We have recently established several important new partnerships, including one with a highly regarded accounting and consulting firm that has a material North American public sector practice.

Second, we are seeing traction in both our government and education strategic initiatives. Two of our first SylogistGov customers are set to go live in July, with other early adopters and new logos queueing in our pipeline. There is an exciting opportunity to win new business in the municipal government market and we're just getting started.

On the SylogistEd side, we have successfully lifted and shifted the IP we acquired that was formerly known as WenGAGE from Oklahoma to North Carolina, to become the centrepiece of our SylogistEd offering. I'm very pleased to report that we have one of the top 10 largest school districts in North Carolina going live on SylogistEd within the next couple of months at the end of their school year. Several other districts are expected to do the same later in the year, including existing and new customers, solidifying our position as a leading player in the State and proving out the geographic expansion of our SylogistEd platform beyond Oklahoma as our acquisition and value creation thesis spells out. To that end, conversations are already underway with school districts in two other states as well.

Finally, as I mentioned at the outset, I am very pleased to introduce our new CFO Sujeet Kini, who has been on the job just a little over a week. I'll pass the call to him for a few introductory comments and to go through our Q1 financial performance. Sujeet?

Sujeet Kini:

Thank you, Bill.

I'm delighted to be here and excited to be working with such a strong team. I joined Sylogist because I believe in its mission and its prospects for growth and value creation. And now that I'm in the role, that conviction is deepening. As I continue my ramp up and study the Sylogist business and operating models, I look forward to meeting and listening to our investors, our customers and our employees. Specifically, and of interest to the investment community, I plan on reviewing the SaaS metrics we discuss and disclose and considering which the Street sees as most indicative, and packaging those in such a way that best informs our investors and our performance. I plan to spend a good deal of time meeting our investors, analysts, and reconnecting with others, all in an effort to increase Sylogist's profile across the financial community and introduce more people to the exciting path we're on.

And with reference to the disciplined approach we take to managing our business, I will be working with the Finance team to develop an operational scaling strategy that defines how the Sylogist culture and organization evolves as we continue successfully executing on plan, gaining market share, and adding scale. This will include putting in place processes and tools to monitor operations and the health of our growing business, and at an expanded level of granularity which I believe will translate into relevant insights and consistent KPIs for investors to measure and compare our performance.

I'll now take you through the highlights of this quarter's financial performance.

This quarter again demonstrates the successful execution of our profitable growth plan. Revenue was $15.9 million, up $2.8 million or 21% relative to the three months ended March 31, 2022. This is largely the result of our team successfully executing and delivering on organic growth initiatives.

For calendar year 2023 as a whole, we continue expecting organic growth to be in the low double digits as higher year-over-year comps ramp up to a new baseline.

Our gross profit grew by 30% in Q1, and represented a gross margin of 60%, slightly less than last year on a percentage basis.

Adjusted EBITDA was $3.8 million, essentially flat with last year, resulting in an EBITDA margin of 24%, lower than last quarter for the following reasons.

Firstly, last quarter (i.e. Q5 of 2022) benefitted by approximately 400 basis points from some one-time tailwinds including a company-wide vacation accrual change, a greater-than-expected portion of ELT and key employee annual bonuses being paid in share units versus cash. This is due to our Board's shift of management compensation philosophy from a short-term incentive plan orientation to a long-term incentive plan orientation, further aligning it with investor interests.

Secondly and conversely, this quarter was negatively impacted by a few specific nonrecurring expenses. These costs brought EBITDA margins down by 300 basis points for Q1.

And most importantly though, as Bill has pointed out on several previous calls, it reflects ongoing investment behind higher ROIC organic growth initiatives that the Company has queued up and is now executing on. We expect Sylogist's EBITDA margins during this early go-to-market phase to be in the mid 20s over the coming quarters.

At the end of this quarter, the Company had $13 million in cash and cash equivalents. We maintain a strong disciplined balance sheet with debt holding steady at $21.2 million, and as part of our disciplined approach to capital allocation, we repurchased in Q1 99,600 shares, representing $567,000 through our NCIB. We will continue to allocate capital in a disciplined way, including buying back our own stock when advantageous to our shareholders.

I'll now hand the call off to Bill for some final thoughts, and look forward to connecting and reconnecting with you, with many of you very soon. Bill?

Bill Wood:
Thank you, Sujeet.

In closing, Sylogist has now had two consecutive strong growth quarters and is extremely well positioned to continue seizing opportunities to growth both organically and inorganically. We have the most experienced and dynamic management team in the business. We have modern and competitive SaaS solutions that our target markets are anxious for, and we have the self-funding capacity and access to capital necessary to execute our strategy. That includes inorganic growth via strategic acquisitions that add customer density and complementary IP to our platforms. Lots of discussions are taking place on the M&A front and we look forward to making further acquisitions that make sense financially and strategically. In doing so, we will continue driving profitable organic growth and operational excellence, the main contributors to investor value creation.

We are convinced that prioritizing profitable organic growth and operational excellence combined with telling our story more broadly will drive long-term share value appreciation. The effective execution of our profitable growth strategy combined with our already envious financial profile will continue to separate us from other tech companies that are reeling with market challenges, low employee morale, poor customer satisfaction, stagnant, organic growth, dated technology, and growing financial pressures. None of those attributes apply to us.

I want to end by personally thanking our customers for their confidence in us, and every team member at Sylogist for their incredible engagement and energy. I am extremely proud to represent you every day.

We'll now turn it over for some questions. Operator?

Operator:
Thank you. We will now begin the question-and-answer session. We will pause for a moment as callers join the queue.

The first question is from Nick Agostino from Laurentian Bank Securities. Please go ahead.

Nick Agostino:
Yes, good morning, guys. I guess two questions on my part. First, you guys called out that there was one-time expenses that had about a 300 basis point impact on the EBITDA margin. Can you just qualify what those expenses were, and given that they're one-time in nature, were they not considered to be removed from the Adjusted EBITDA number that you reported?

Sujeet Kini:
Bill, do you want me to take that?

Bill Wood:
Please do.

Sujeet Kini:
Hi Nick. Great to be talking to you. Nick, fundamentally what those expenses really relate to is these are expenses that typically we would not see on a continuing operating basis. Essentially, a good way to think about it is it's almost the opposite of the tailwinds we saw in the previous quarter.

Then in terms of your question around whether we did consider adjusting it out of Adjusted EBITDA, we did have that discussion internally and the overall consensus internally was it's appropriate to include it within EBITDA, more from the point of view of just overall fidelity to GAAP. But I go back to my comment that we would not be expecting to see these expenses on a continuing operations basis, therefore we felt that the most appropriate positioning would be to include it in the calculation of Adjusted EBITDA, however, offer it out as an explanation in terms of an item that has impacted us but will not impact us on a continuing basis, if that makes sense.

Nick Agostino:
Yes, that's makes sense. Then my second question is, I think you mentioned in your prepared remarks you're guiding to mid 20s EBITDA margins in the short term. If I recall, just on prior calls, you guys were talking about increasing the level of spend, sales and marketing, to support some new marketing rollout initiatives that we'll already see in the marketplace. I'm just wondering how long do you guys anticipate being in that mid 20s percent range. I think that was up until the second half of this year. Are you expecting it to be longer than that?

Bill Wood:
Let me get this point, Nick. We're pleased with the ROI we're getting on the investments relative to go-to-market. We'll continue to step on the gas, but there will be a point where there's a certain amount of inertia that those start to cause, those activities start to cause. As I've said, new wins lead to those customers sharing their reasons why with colleagues. As I've said, it's not a competitive marketplace; it's very collegial and I think one leads to two, two leads to five, five leads to 13 kind of an exponential growth. So, I do see a point where obviously our overall margins will strengthen. I believe that the guidance and the outlook that we're giving through year, we feel pretty confident it's the best use of

capital as to invest behind those right now, and to make sure that we have that inertia really kicking in as we head into ’24 and beyond.

Nick Agostino:
Because you used the term through this year, can I assume then that it’s mid 20s plus or minus for the balance of 2023, and then to be determined for 2024? Is that a fair conclusion?

Bill Wood:
It is.

Nick Agostino:
Okay. Thank you.

Bill Wood:
As we look at the business, we do see the opportunity for those to improve over time. It’s really that balance between profitable growth is what we’re certainly committed to. We use that term very purposefully, and to that end the ability for us to continue to see that organic growth mature and to see that SaaS revenue continue to build into our overall profile has a very interesting effect on us going forward, a very positive effect as we really then shift to a full SaaS model and the annuity opportunity that creates.

So our spend over time from an EBITDA standpoint I see will settle to be able to increase that profile over time as that inertia kicks in.

Nick Agostino:
Okay. Is it also fair to say that given you’re always targeting a Rule of 40, you will keep margins down at 25 percent if you’re going to get organic growth of at least 15%? Is that another way to look at it?

Bill Wood:
It is. I think our commitment to a Rule of 40 has been kind of our gospel North Star that I’ve shared since joining. I believe we don’t need to drain the piggybank by any means to try to kick into simply a growth-at-all-costs kind of a mode. It’s not where I see Sylogist being or what I believe is best for our overall profile going forward. I do think that that Rule of 40 will generally be plus or minus our guiding

principle, but it's not simply celebrating if that turned into all growth at 45% with no profitability. I just don't think that's in anything that we feel is going to be required or that we're looking to try to get to that kind of a posture.

Nick Agostino:
Okay, great. That's all for me. I'll pass the line.

Operator:
The next question is from Gavin Fairweather from Cormark Securities. Please go ahead.

Gavin Fairweather:
Oh, hey, good morning. Thanks for taking my questions. Pretty good bookings this quarter while a bunch of your peers that sell into the commercial market are kind of looking at bookings slowing down now. Bill, you've kind of been in the not-for-profit and government space for some time. Maybe you can just discuss kind of whether you would expect any kind of material change to the sales environment, or whether your verticals should be relatively insulated from any kind of macro shift.

Bill Wood:
Hi Gavin. Yes, great question. I do feel much like a shared on our last call that I feel quite good about what we're seeing in terms of pipeline activity, both top and mid, and our ability to matriculate deals to close to wins.

I do not see in our space and the anxiousness that we're seeing of people who are very interested in our all-SaaS kind of wall-to-wall solutions and platform that we're offering. We're seeing quite an uptick. I think that that is at the expense of some of our competitors who may not be of the technology posture or maybe customer wellness that we are. So at a time when maybe others are feeling more pressures in terms of their own profile, we're feeling quite emboldened to be able to move forward and not only win new opportunities and new logos, but we're also seeing wallet share expansion where customers looking at more IP on the platform they already have, and I think that's been complemented by our platform versus product strategy, a couple of the acquisitions that we've made that rounded out kind of the thesis strategy that I articulated from the get-go. And to continue to make sure that the budget dollars that are coming through, we're in a position where our ICP and our ideal customer profile is very clear where we're going out and putting ourselves in front of those and giving them a reason to select us.

Gavin Fairweather:

Great to hear. Then just secondly for me, lots of initiatives in place kind of across the verticals. You've got your new SylogistGov solution for muni. You've got SylogistEd kind of regional expansion and then kind of ongoing cross-sell and not-for-profit. I guess, where are you expecting to get kind of the most traction? Which verticals are you having the most success with right now? Where do you see the other verticals kind of picking up? What kind of time delay on those?

Bill Wood:

As you just teased out, the tail of the Eds and the Govs are tied to both the bringing to market of those two offerings and the SylogistGov and SylogistEd in the new modern platform, and in the Ed side beyond Oklahoma, as I shared in my remarks.

We saw a very strong quarter in the Mission side, and I think that is because of the cross-sell where we already have a footprint on either the CRM side or on the ERP side, that we are now having customers come back and say, "We love our relationship with you, and now we know that you have more. We'd like to talk to you about how we can use more of the platform or more of your offerings."

As I said, that is largely, I think, at the expense of some of our competitors. We're pretty hyperfocused on a few that we think we have real growth momentum and displacement opportunities around. But the Ed and the government side, we did have, as I mentioned in the remarks, we have a good pipeline that's building there and their buying cycle puts it more toward the end of this year and when they would light up into our overall profile next year, but that really is unchanged from what we forecasted and planned it to be, which was demonstrate with good early implementations on the Ed and the Gov side. Those are the new platforms. The customer enthusiasm around allow them versus getting out over our skis, demonstrate our ability to light them up and be successful, and then move very aggressively in lighting up others shortly thereafter. So, latter part of this year and then into next year, the realities, I think, for those markets will start to contribute to us.

Gavin Fairweather:

Okay, great. Then next for me, obviously very strong services performance this quarter. Curious how much of that relates to your software and turning on new recurring revenue, and how much we can think about that as kind of a leading indicator towards subscription and maintenance growth in kind of the next one to two quarters.

Bill Wood:

Good tease out. It is exactly a good leading indicator. The services growth that we're seeing is largely associated with our IP. That means the bookings are matriculating to project services to light up new customers and then we get the opportunity to recognize that SaaS revenue over the horizon.

It is a good indicator that we have the capacity, as I've mentioned. We've built in the capacity to go not only win new business but be able to light them up successfully and then be able to hopefully expand that IP opportunity with them over time if they didn't bite off the whole elephant right at the beginning.

So, good, astute question there, and we do believe that that project services side is a very good indicator for us as we think about strength of the Company overall.

Gavin Fairweather:

Just lastly for me, you talked about partners being a key initiative over the course of this year. Maybe you can just expand on your strategy there and what kind of products, what markets you see the channel as being best fit to sell for you. That's it for me. Thank you.

Ben Wood:

We're exercising that across all the markets. Most specifically, the Gov side is predominantly a partner strategy relative to our go-to-market. Once we prove out we do want to make sure that we ourselves have proven out the sales motions and the implementation motions with the early adopters and new logos to be able to have partners to kind of shadow us during that, to understand our DNA, that we aren't just about the technology but how we really develop a partnership as a trusted partner for our customers and how important that is to us as a differentiator versus our competitors.

That overall profile of customers also applies to Ed because when we think about the footprint of multiple states, we want local presence to make sure that the idiosyncrasies of those states or districts are reflected in how we're going about serving and making sure that they're successful with the platform.

The Gov side really is the predominant. The Ed side it will be a large portion. And interestingly enough, it's also a growing portion of the Mission side when we're looking at partners that have longstanding credibility in this space and they're stewarding typically a charitable organization that said, "I'm just not able to go forward with this platform that I have in the way that I want." Typically, they'll go out to a consulting entity to give them a purview of what's going on in the industry. Well, we're quite popular right now within those segments and those different shops because of our customer wellness. It all stems from that in terms of our ability to continue to grow, so we're getting more consultative partners that are actively encouraging people to not only explore us but then partnering with us to transition that particular organization onto our platform. So, it's across the board.

Gavin Fairweather:
Thank you.

Bill Wood:
Thanks, Gavin.

Operator:
The next question is from Robert Cooper from Acumen Capital. Please go ahead.

Robert Cooper:
Hey guys, a quick one from me. When I look at your business, you've had to spend to move growth higher as it was stagnant and that's good, but at what point does the business model start to exhibit operating leverage where your incremental revenue starts to come in at a higher margin? Is that this year? Next year? Or do you have to keep on spending? I'll turn the line back over. Thanks.

Operator:
Bill and Sujeet, your lines are open.

Bill Wood:

Hi Robert. Sorry, I thought Sujeet may want to take that, but I'll take that because I think the overall lens for us is we do see the effect of our overall revenue, especially from a SaaS standpoint, really starting to more materially show up in full rev rec and margin expansion as we head into '24 and beyond. So, undoubtedly the effect of our overall profile and the investments we're making now, with a longer lens into the SaaS bookings that we're making now showing up and showing up in a very profitable way for us as passive revenue in terms of on a month-by-month basis does certainly bode to help our margins as we head into '24.

Operator:

The next question is from Adam Wilk from Greystone Capital Management. Please go ahead.

Adam Wilk:

Hey, good morning. Thanks for taking my questions. Can you guys hear me?

Bill Wood:

Yes, we can.

Adam Wilk:

Great. Most of my questions were answered, but I was hoping to just maybe get an update on M&A. I know you provided some colour just about the deal pipeline. I guess I'm kind of looking for some commentary around being on track to still hit that, I think it was $20 million to $25 million in acquired revenues for this year. Just what are you seeing out there in terms of private market valuations, conversations, etc. would be helpful. Thank you.

Bill Wood:

Hey Adam, as I've tried to kind of tamp down over the last quarter or so, we still feel that private company valuations are more of a premium than we feel makes sense right now. We have continued to earnestly have conversations and stack deals, if you will, that we believe are actionable, but ultimately we think time is on our side to allow some of the realities that I've mentioned before of pressures that are now starting to come to bear, some of the realities of those playing into our hand as we think about acquisitions that make sense for us strategically, and also that piece financially.

So I believe we are not necessarily putting that as a pin right now. That $20 million to $25 million for this year is where we will be, and it's only because we just don't think the valuations are where we want them to be, to be able to do that. So it's within our crosshairs in terms of deal cadence, but ultimately we think settling right now and being patient is working in our favour.

And to honest, on top of that, the execution we're seeing on the organic side, frankly, I think I'm also ensuring that our overall management team is not distracted from those things that we believe present the greatest ROIC, which is the organic initiatives that we've queued up and are now executing on.

Adam Wilk:
Thank you. I can appreciate that and it's great to hear the conservatism and also the comments around organic opportunities.

I guess you also touched on this a bit; I'm wondering if there's any more colour on share repurchases. I don't want to say while you wait, but in the meantime, given your free cash flow yield and your internal initiatives, it's good to see some of the activity in the quarter. But are you guys kind of thinking about that, I guess, in light of being patient with M&A and then making your internal investments, given that every repurchase at this valuation will be pretty accretive. Thank you.

Bill Wood:
It's a great point. It's one that we are aligned with and the Board is actively in discussions relative to the continued ability to look at the NCIB as a way to breed accretiveness as well as the idea of shareholder value. And to that end, we still feel the stock is in a—at a price point that is ridiculously low relative to the overall flight path that we see in terms of value creation, and we're going to continue to take that as an opportunity to buy into the stock and to allow us to enjoy the benefit of that over time as we encourage our investor community to do the same.

Adam Wilk:
Great. I appreciate that very much. That's it for me and look forward to hopefully meeting in person at the Investor Day. Thanks for taking my questions.

Bill Wood:
Thanks Adam. Us too.

Operator:

This concludes the question-and-answer session. I would like to turn the conference back over to Bill Wood for closing remarks.

Bill Wood:

I just want to thank you all very much for joining today's call and for your continuing support and interest in Sylogist. We are very excited about the path we're on and the quarters ahead, and look forward to continuing to report our progress on those initiatives as we mentioned at the upcoming Investor Day, which we think will be an exciting opportunity for our community of those that are interested in the story and those that we feel have been hanging around the rim for some time to see what's going on kind of first-hand, to meet more of the executive team and the great work that they're doing every day. And if that's not an opportunity for us, please certainly we welcome the opportunity to have conversations one-on-one in addition to help and answer any questions that you may have about what we're doing and why we're doing it.

Thank you very much for your continuing support and we look forward to the quarters ahead. Thanks for your time.

Operator:

This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.