envirosuite
(ASX: EVS)

ASX Release

Investor briefing questions

11 March 2021

Envirosuite Limited (ASX:EVS) advises that following the release of its H1 FY2021 results on 26 February 2021, CEO Jason Cooper and CFO Matthew Patterson presented a series of presentations and webinars with investors and analysts. For the benefit of those unable to attend, EVS provides the following summary of questions received by investors and accompanying responses along with other questions put to the Directors and management.

What gives you confidence to increase sales in the second half considering the lower sales in the first half?

Our forecast for Q3 is based on deals that have reached the negotiation phase of the sales cycle by the end of February and that we believe will close during this period.

Whilst sales from the first half of the year were affected by COVID-19, as well as the impact of bringing two businesses together, we have seen a steady increase in deal volumes and pipeline for the second half of the year, with business confidence increasing as vaccination programs are rolled out.

Can you quantify the impact of discounting in the airports business across the first half?

Due to COVID-19, the impact of discounting was approximately $1m on the first half reported revenue, however, discounts for some of these customers started to unwind in December 2020.

At your current scale, what gross margin improvements do you expect from the initiatives outlined on page 8 of the presentation?

The gross margin will be impacted by various factors including revenue mix across our three main product lines, the mix of recurring and non-recurring revenue, as well as overall revenue growth. However, we expect that based on our current level of business, that the cost initiatives should provide a gross margin of ~50-55%. As the mix of revenue shifts more towards the EVS Water software solution, we expect the gross margin to further improve.

What sort of incremental margin do you expect on new revenue?

EVS management focus on a metric called 'contribution margin' which is revenue less the direct variable costs and excludes internal overheads (gross margin includes the allocation of internal overheads and non-variable external costs related to supporting customer). The contribution margin is what we view as the incremental margin on new deals and assumes we can leverage our existing overhead cost base in relation to customer support. The contribution margin that we achieve on new recurring revenue deals is ~80% and should continue to improve the gross margin.

Given your outlook, are there any changes to previous revenue and EBITDA targets for the next few years? Has there been a change to when EVS expects to be breakeven due to COVID-19?

Over the past 12 months the results have been affected by two main factors: foreign exchange and COVID-19. The Australian dollar appreciated ~10% against the USD during the 6 months ending 31 December 2020, which has meant our reported revenue has been reduced by an equivalent amount for those contracts based in USD (~25% of total revenue came from the North America region of which the majority was in USD). COVID-19 has seen a reduction in the discretionary expenditure (one-off projects) by airport customers, and this has led to a temporary decline in our profitable non-recurring revenues. In addition, EVS has elected to support some of our airport customers, particularly in the EMEA region, with temporary discounts, some of which started to unwind in December 2020.

The above factors have slightly pushed back the timeframe for EBITDA positive result but EVS still expects, based on current operations, and forecasted recurring and non-recurring revenue to be EBITDA positive in Q4 FY21.

What is your view on the role of China in your future plans?

The China market is rapidly evolving and has the potential to be a significant market for Envirosuite's products with its increased focus on environmental protection and digital transformation across water, air, and noise. EVS is still exploring the optimal pricing model, go-to-market strategy and overall product mix to take advantage of this growing market.

China continues to represent a vast opportunity for our Airports, Industrial and EVS Water solutions noting China's most recent 5-year plan. We are mindful of ensuring that our products are the right fit for the market in China and that we can be successful in that market. This includes leveraging our existing operating model as well as relationships that we have with our existing global client base that have operations in the China market.

Historically, the focus has been on six sectors, why has that reduced recently?

As part of our strategy review the Company has decided to focus on 4 major sectors: Airports, Waste, Mining and Water. This will bring discipline and focus for our product, sales, marketing, and operations teams to ensure we build market and product leadership in these sectors. We will continue to explore opportunities in other sectors (such as construction or cities) as we can address them with our existing solutions, but we will not proactively pursue these opportunities.

Tell us a bit more about the buying cycles of the sectors that you're focusing on? Which sector will lead the charge as Airports have a long cycle?

Buying cycles are typically dependent on the sector. Airports typically buy via a procurement and tender process, and plan budget cycles annually. Typical lead times for new opportunities are therefore approximately 12 months. Lead times for upsell of solutions at existing airport customers can be much shorter (3-6 months). This is balanced by the long term committed revenue that airports offer (often 5-year contracts with additional options).

For Industrial (Waste and Mining), lead times vary by procurement method, but typically are in the 3-6-month timeframe. For our EVS Water solution we have already seen that lead times can be much shorter for non-government entities (2-4 months), as the cost benefit analysis for this product is obvious and drives quick acceptance.

How much revenue is exposed to Airports?

It is important to note that our customers are Airports and not airlines. Airports have regulatory requirements that we address regardless of flight volumes. At the moment, we have approximately 65% of our revenue from the airport sector. Whilst we see further growth in airports, we expect our Water and Industrial portfolios will grow at a faster rate.

Are all your products on a single platform? If not, when do you expect this to be the case?

With the recent appointment of Andrew Barron as our Head of Product, we are developing our product strategy to build products that delight our customers and allow them to access the full range of our solutions.

The major driver of cost in our products, and the greatest opportunity for convergence, is the infrastructure layer. We are currently executing our 'One Cloud' strategy which is migrating all of our applications into a common cloud platform. Whilst we do expect to have a hybrid approach to our infrastructure, our cloud migration will be complete in the next 12 months and benefits will be realised during this time.

Jason, given you've had 8 months with Envirosuite before stepping into the CEO role, can you outline your focus for Envirosuite?

One of the compelling reasons why I chose to join Envirosuite originally was based on our vision to harness the power of environmental intelligence so industries can grow sustainably, and communities thrive. We have strong product market fit and there is an increasingly strong need for what we do across the world.

My time in Silicon Valley working in high growth technology companies has helped me to understand what drives global, scalable businesses. With a deep understanding of the business within operations and reflecting on our vision the key focuses for me are to improve our discipline and focus across sales and marketing, optimise our global operations, invest in our product to build world-class technology that continues to solve customer problems across our focus sectors and move us deeper into their operations, and continue to build out the leadership team with experienced talent.

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