Integrated Research Ltd ABN 76 003 588 449
Level 9, 100 Pacific Highway, North Sydney NSW 2060 Australia
t: +61 (2) 9966 1066 e: investor@ir.com

28 February 2024

ASX Market Announcement - Investor Conference Call Transcript

Integrated Research Limited (ASX: IRI), encloses for release to the market a transcript of the Investor Conference Call held on 22 February 2024.

By Authority of the Board.

Will Witherow
Company Secretary
Integrated Research Limited
ABN: 76 003 588 449

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MARKET ANNOUNCEMENT

Investor Conference Call Transcript

Sydney, 28 February 2024 – Integrated Research Limited (ASX: IRI), advises the following is a transcript (excluding Q&A) of the Investor Conference Call held on 22 February 2024 at 10:30am. The Conference Call was conducted via the Open Briefing format of Orient Capital. References to slides are the slides contained in the Half Year Results Presentation released to the ASX on 22 February 2024.

Start of Transcript

Operator: Ladies and gentlemen, good morning. My name is [Abi], and I will be your conference operator today. At this time, I would like to welcome everyone to the Integrated Research Limited first-half fiscal year '24 results investor conference call. Today's conference is being recorded, and all lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during that time, simply press the star key followed by the number 1 on your telephone keypad. If you would like to withdraw your question, press star-1 a second time. Thank you. I will now turn the conference over to Mr John Ruthven, Chief Executive Officer. Mr Ruthven, you may begin.

John Ruthven: Thank you, Operator. Good morning, and welcome to the first-half FY24 results briefing for Integrated Research. My name is John Ruthven, and I'm the CEO at IR. With me today is Matthew Walton, our outgoing CFO, and Christian Shaw, our incoming CFO.

I will open the presentation, and then hand the presentation to Matthew to take us through a detailed financial review. He will then hand back to me to talk through strategy and key priorities for FY24. At the conclusion of the presentation, we will open the call for questions. This morning, we posted our results presentation to the ASX website, which we will be referring to during this call. You can also find a copy of it in the investor relations section of our website at ir.com.

Moving to slide 2, Integrated Research, or IR, as we're better known, is a global software company providing performance and experienced monitoring solutions for critical business systems. We have three product lines: Collaborate, for Unified Communications and UCaaS, or Unified Communications-as-a-Service; Transact, which is in the payment space; and our Infrastructure product for Hewlett-Packard Enterprise or HPE NonStop environments. Common to the customer use cases that we support are complexity, mission criticality, and scale.

Slide 3 highlights the underlying strength of IR's business model, our customer base. Our customers are large global enterprises across a range of industries, including technology, telecommunications, financial services, government, healthcare, higher education, and retail. Key to our business are multi-year non-cancellable contracts with mission critical requirements.

I am on slide 4, CEO key messages. We are on a turnaround journey, and, having improved our working capital position for the Company with cash at bank and a level of profitability, we now turn our attention to growth. In the first half, we benefited from our strong renewal base of blue-chip customers. This coupled with cost control has improved our profitability and cash position.

Transact and Infrastructure performed very well in H1, leveraging several large contracts along with some good run rate business. At the same time, our Collaborate product line faces some headwinds as we maintain our focus on large enterprises with complex environments as well as industry segments where our value proposition is most relevant. Against this backdrop, our cash position now gives us the opportunity to pursue product-led growth opportunities.

On slide 5, we summarise our statutory results. The Company achieved profit after tax for the half of $11.2 million. Statutory revenue for the period was $40.8 million, up 6% over the prior half. The strong performance was a consequence of improved sales execution, a larger renewal book, and healthier external trading conditions.

Cash receipts from customers totaled $32.4 million, up 2% over the prior period. The Company continues to benefit from term-based non-cancellable licence contracts with a high-quality customer base, driving an increase in cash receipts and an increase in cash at bank, which continues due to a strong focus on cash management.

Now on slide 6, and switching to proforma results, the performance indicator, total contract value or TCV, was $41.3 million for the half, up 6% on the prior corresponding period or PCP. We continue to report revenue on a proforma subscription basis, which we believe is more reflective of the long-term underlying performance of the business.

Subscription revenues for the period were $32.9 million, 4% down as a result of lower new business sales and lost clients. Revenue increased from services partially offsetting the period-on-period decrease in total proforma subscription revenue, with proforma revenue down 2%. Proforma EBITDA dropped 6% as a result of lower recurring revenue and cost increases due to inflationary pressure. Our cash conversion rate for the half improved to 87% as a result of the strong cash collection.

Slide 7 captures the priorities we set for FY24. At the halfway point, we provide the following update: good performance in the Americas and Europe in the first half, which was underpinned by a solid renewals book, with TCV growth expected for the full year. We won 13 new customers, which was behind our expectation, and anticipate an improved result in the second half.

Good sales execution on renewals in the first half, benefiting from the ongoing process improvements and discipline. NRR or net revenue retention improved to 95% in constant currency. Expenses were down 21% in the half, and we expect operating expenses to be down for the full year.

We maintained our customer-centred approach to product development, and, at the same time, we've brought on a new head of product to ready us for the next phase of product-led growth, as referenced earlier. Our working capital position has improved, with statutory profit and cash for the full year expected to be up on PCP. I will now hand over to Matthew to take you through a detailed review of our financial performance.

Matthew Walton: Thanks, John. We're on slide 9. Slide 9 shows the linkage between total contract value, statutory revenue, proforma revenue, and annual recurring revenue. It's worth unpicking this for a moment. Total contract value, the black line, is the total value of a revenue-generating contract written in the year. This includes software licence and related maintenance, cloud, testing, and consulting services revenue.

TCV is a function of the term of the contract and the annual value of the contract. For example, client TCV can reduce significantly if the term is reduced, even though the annual value of the licence subscription has increased.

Statutory revenue, the red line, is revenue recognised per the accounting standard. This has a strong upfront revenue recognition profile with less revenue recognised over the life of the contract. As a consequence, there is a strong alignment with TCV.

Proforma subscription revenue, the middle blue bar, is the licence and maintenance revenue from the contract spread over the life of the contract. It's a non-statutory and unaudited view that we believe represents the recurring nature of the contracted revenue streams.

Proforma revenue, the left purple bar, is performance subscription revenue plus other non-recurring revenue streams, typically professional services and one-time through testing services. Recurring revenue, the blue bar, is the end of period subscription revenue multiplied by six, and best represents the ongoing or recurring value in the stream.

This chart highlights that while there is more volatility in TCV and statutory revenue, there is more consistency in the revenue streams over time, as represented by proforma and recurring revenue. Furthermore, while TCV and statutory revenue may grow, proforma and recurring revenue may decline as renewals and new business are more than offset by churn and down sell.

Two key points to address in this slide are the convergence of TCV and statutory revenue over time is driven by the shift to SaaS with less upfront revenue recognition, and the recent relative stability of proforma and recurring revenue compared to the volatility of the lead indicators of TCV statutory revenue highlights that growth of proforma and ARR occurs as new clients in TCV is added to the renewal base, and the renewal base is extended through price increase, offsetting any lost revenue through client exits and down sell, adjusted for foreign exchange movement.

If we turn to slide 10, slide 10 presents our TCV, stat revenue, proforma subscription revenue, and recurring revenue on a geographic region and by product set. This revenue should be considered in conjunction with more detailed slides in the appendix. Points to highlight include the Asia-Pacific chart shows the consistently strong proforma and recurring revenue growth is plateaued with the downturn in TCV stat revenue from a high prior period.

Collaborate headwinds continue on both lead and lag measures. New Transact sales will grow future proforma revenue and recurring revenue. New leadership in the Americas and Europe is focused on driving TCV licence growth.

On slide 11, we focus on the key metric underpinning value, namely, the change in components of recurring revenue. Total recurring revenue declined 5% to $64 million. New logos in Collaborate, upsell in Collaborate from new capacity and price increases, and Transact were overshadowed by the loss of clients and down sell price reductions in Collaborate and Transact, and foreign exchange headwinds. Collaborate is experiencing headwinds in all geographies. Further information is in the appendix.

We turn to slide 12 titled Operating Costs. IR has continued to manage costs tightly. Costs have decreased 21% on the prior period. This is a result of managing the headcount, and active cost management. Natural attrition continued through the period as the market for technology staff was competitive. Pleasingly, IR continues to replace all critical roles quickly with high-quality candidates. Our innovation agenda has been reset, with a focus on customer-driven solutions focused on near-term opportunities.

We're on slide 13. This slide on additional metrics underpinning value, namely, the level of recurring revenue, the contract length, and the proportion of new business to renewals in the period. Recurring revenue has remained constant as a proportion over the prior period. Contract length has remained constant over the prior period, with the average length of the contract written in the period stable at four years. Renewals dominated the half with circa $33 million in renewal TCV, up from $23 million a year prior.

Turning to slide 14, cash flow is illustrated on slide 14 with cash at bank increasing $2.9 million or 16% over the period. Significant focus was paid to ensuring receivables are aged below 60 days. Cash paid to employees and invested in development reduced compared to the last year, reflecting ongoing expense management discipline.

We're on slide 15. While the Company had statutory EBITDA of $11 million, $3.5 million of cash was generated from operations. The primary drivers of this difference are over time revenue/cash conversion compared to statutory upfront revenue recognition, combined with improvements in working capital of $600,000 as a result of a lower cost base and improved collections, offsetting historic debtor factoring of $2.1 million, which is now concluded, and income tax paid. We should emphasise that the Company is not factoring any receivables, and the current factoring completed in December 2020.

The balance sheet shown on slide 16 shows a pleasing 19% lift in net assets to $71 million. Cash and trade receivables increased $7.5 million on the prior half. Receivables remain a strong source of cash flow in the current and future years, and the Company remains debt-free. I'll now pass back to John for the rest of the presentation.

John Ruthven: Thank you, Matthew. Now moving to strategy progression on slide 18. As we reflect on our journey, it's pertinent to both project the path ahead as well as the progress being made. We are a company in turnaround. Phase 1 of this journey was to improve our working capital to earn the right to pursue growth opportunities.

Coming out of H1 FY24, we are pleased with the progress: cash at bank of over $20 million, a solid balance sheet that will increase in net assets of nearly 20%, and statutory EBITDA of $11 million. As we consider growth options, all options are available. Leveraging our core capability as a platform company, you might ask, what are the adjacent opportunities either from new products or simple product enhancements? We are well progressed with customer-led requirements in this arena. Our focus is now on how we can scale this.

While M&A has not been a significant part of the Company's strategy today, there is an appetite to explore options to accelerate growth. Synergy to our core competence and customer value proposition is key to this factor. A lower risk growth opportunity is partnership in adjacent new product areas. Key to this is access to new market segments whilst leveraging IR's core capabilities. A good example is the recent product launch of RemoteInsight through an expansion of an existing partnership with PathSolutions.

Getting the growth phase right will inevitably lead to the scale-up phase. In this phase, fast fail innovation is critical: new ideas, new technologies. We will also need to flex our business model, including the revenue model, our go-to-market, and our approach to product and engineering. We are well placed coming out of the capital management reset of the business to consider and pursue growth options.

Now on slide 19, we'll take a look at a couple of the key wins for the first half in the Collaborate portfolio, both the renewals in the sweet spot of large enterprise with complex communications environments. Airbus in Europe is a large complex organisation with a workforce of over 100,000 users. They've been an IR customer for over a decade, and this renewal was for a rich set of products supporting an interim project called Smartphone For All. IR's Collaborate product suite provides end-to-end visibility of the multi-vendor ecosystem in a single product solution.

Moving to the Americas, CDW is a large technology reseller and managed service provider, who have been an IR customer for 10 years. This renewal and expansion of the full suite of Collaborate products for 135,000 users will assist CDW in integrating some acquired organisations as well as meeting SLAs or service level agreements for their managed service customers.

On slide 20, we profile three Transact and Infrastructure customer wins in the first half. Fiserv is a large global financial technology company, who have been an IR customer for over 20 years, and signed a new five-year agreement that is a renewal and expansion. This deal was structured to renew existing products, increase capacity, and add a newly developed IR product, Business Insights. IR provides critical insight to network performance in support of Fiserv's service to their customers.

Worldpay are the second-largest non-bank payments acquirer in the US, processing over a billion transactions per month. Another longstanding IR customer signed a five-year renewal for solutions that help ensure their merchant networks are operating at very high availability levels. They operate multiple payment hubs with high transaction loads, and must achieve very demanding SLAs.

Moving to the Middle East, Network International, or NI, are the largest payments processor in the region. They renewed and expanded their contract with IR for another three years. NI are expanding in the region, and, at the same time, modernising their payment platforms to support new payment types and services. In support of this, they expanded their current IR solution by adding Transact real-time payments monitoring and upgrading to Transact cards and NonStop Plus solutions.

Coming to slide 22, I would now like to remind you that IR does not provide specific guidance. However, at the halfway mark of FY24, we've made the following observations to keep the market informed. Customer sentiment is steady, and we are not encountering budgets being cut or withdrawn. This gives us a cautious optimism for growth.

The FY24 renewal book is expected to exceed the prior year, which is now weighted to the first half, following a strong renewal result in H1. The renewal book is also now weighted to Transact and Infrastructure, following the successful closure of a number of large renewals. While we expect Collaborate churn to persist, we will increase our focus on large complex organisations better suited to our value proposition and price point.

In the second half, we expect a larger contribution from new business, both new customers and upsell, noting that our new business pipeline is up from PCP. We anticipate growth in the Americas and Europe, with APAC a little down over a strong prior year. We also expect an improved cash balance at year end, based on higher sales, lower costs, and ongoing collections focus.

I'm on the final slide. As I conclude today's first-half FY24 earnings announcement, I'd like to close with the same key message or messages that I shared earlier in the presentation. IR is on a turnaround journey, and we are at a critical stage where we move our focus to growth, leveraging our improved working capital position. We have cash in bank, are profitable, and have momentum coming out of H1.

Our first-half results leveraged our strong renewal base, in particular, our Transact and Infrastructure portfolio. We again proved our ability to sign seven-figure deals with large global enterprises. Whilst our Collaborate product line faces some headwinds, we maintain our focus on large enterprises with complex environments, playing to our strengths.

We are positive in our growth outlook, noting that the second half is more reliant on new business. Finally, as we look to the future, our cash balance provides the foundation for us to pursue a product-led growth opportunity focus. Operator, that concludes the presentation.

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About Integrated Research Limited (ASX: IRI). Integrated Research (IR) is a leading global provider of user experience and performance management solutions for payment transactions and collaborative systems. We create value through our real-time, scalable & extensible hybrid cloud platform and our deep domain knowledge to optimize operations of mission critical systems and improve user experience through intelligent and actionable insights. We enable many of the world’s largest organizations to simplify complexity and provide visibility over systems that millions of people can’t live without – systems that allow them to transact and collaborate. For further information on IR, visit www.ir.com.