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Call Participants

EXECUTIVES

Alan Louis Urban

CFO & Secretary

Peter Victor Derycz

Founder, CEO, President & Director

ANALYSTS

George Melas-Kyriazi

MKH Management Company, LLC

Glenn Arbeitman

Presentation

Operator

Good afternoon, everyone, and thank you for participating in today's conference call to discuss Research Solutions' Financial and Operating results for its Fiscal Second Quarter 2020 ended December 31, 2019. Earlier today, the company issued a press release discussing these results and a copy of the release is available for viewing and can be downloaded from the Investor Relations section of the company's website. Joining us today are Research Solutions' President and CEO, Peter Derycz; and the company's CFO, Alan Urban. Following their remarks, we will open the call for your questions. Then before we conclude today's call, I will provide the necessary cautions regarding any forward-looking statements made by management. I will also provide information regarding the company's use of non-GAAP financial information. Finally, I would like to remind everyone that this call will be recorded and made available for replay via a link in the Investors section of the company's website. I'll now turn the call over to Peter Derycz, Research Solutions' President and CEO.

Peter Victor Derycz

Founder, CEO, President & Director

Thank you, operator, and good afternoon, everyone. Overall, we are pleased with the progress we made in our second quarter as we maintained our momentum with strong relative growth in both our platform and transaction businesses and continued gross margin expansion on a consolidated basis. At the beginning of last quarter, we shifted all marketing resources to focus on growing our enterprise customer base through business-to-business campaigns. The initial results are positive, giving us confidence in our decision to focus on the enterprise. We also further optimized and fine-tuned our prospecting activities to ensure we are getting in front of small to medium-sized organizations that are driven by R&D, which could greatly benefit from the research tools our Article Galaxy platform offers.

During the fine-tuning process, we found that once potential customers get in front of our sales team to learn more about our capabilities, our conversion rate increases significantly. So we really focused on further optimizing our appointment setting methods, which is an important step in the lead nurturing process to ensure our sales team is getting as many shots on goal as possible. We also continue to make improvements as we do every quarter to the platform's user experience and interface, along with rolling out multiple updates to various gadgets based on the feedback we received from our customers. Our platform's best-in-class capabilities and our ability to provide the most innovative solutions for researchers is the backbone to our success and we remain committed to consistently evolving our platform to meet our customers' needs. I will give greater detail on the various platform enhancements we made throughout the quarter, along with providing some insight into the initiatives we have planned for the future. But first, I'd like to pass it over to Alan to walk through our fiscal second quarter 2020 financial results. Alan?

Alan Louis Urban

CFO & Secretary

Thanks, Peter, and good afternoon, everyone.

Jumping right into our fiscal Q2 results. Our platform subscription revenue increased 42% to \$950,000, driven by a 27% year-over-year increase in total platform deployments from 267 to 338, which translates into 18 net incremental deployments in Q2. We also continued to benefit from the consistent upselling and low churn of our current platform customers. The quarter ended with \$3.7 million in annual recurring revenue, up 6% sequentially and 38% year-over-year. Please see today's press release for how we define and use annual recurring revenue and other non-GAAP terms.

Our transaction revenue increased 4% to \$6.6 million compared to \$6.3 million in the same year-ago quarter. Transaction count increased from approximately 203,000 to 213,000 and total active customer count grew from 1,071 to 1,139. Within the total active customer count, the number of corporate customers was up 3.5% to 856, while academic customers were up 16% to 283.

Together, these businesses delivered consolidated revenue of \$7.5 million, an annual increase of 8% compared to \$7 million in the same year-ago quarter.

Moving on to gross margin, our Platform business saw gross margin increased by 120 basis points to 82.9% compared to the same year-ago quarter. This increase was driven by continued proportional decreases in third-party data costs, as our expanding scale provides leverage to become more cost effective with our third-party providers. Our target gross margin in the platform segment remains in the high 70% to low 80% range. Gross margin in the Transactions business declined slightly to 22.6%, primarily due to proportionately higher personnel cost, slightly offset by lower copyright costs. As a result, consolidated gross margin increased 180 basis points to 30.2% compared to the same year-ago quarter. The increase was primarily driven by a continued revenue mix shift to the higher-margin Platform business, which we anticipate will continue improving as our Platform business becomes a higher percentage of revenue.

Our total operating expenses were \$3.0 million compared to \$2.7 million in the same year-ago quarter. The increase was primarily due to continued investment in sales and marketing associated with the expanding platform business.

Net loss from continuing operations totaled \$592,000 or negative \$0.03 per share compared to a net loss of \$592,000 or negative \$0.03 per share in the same year-ago quarter. Adjusted EBITDA was down slightly to negative \$184,000 compared to negative \$148,000 in the year-ago quarter.

Moving on to the balance sheet. Cash and equivalents at December 31, 2019, increased to \$6.8 million versus \$5.4 million at June 30, 2019. There were no outstanding borrowings under our revolving line of credit, and our balance sheet continues to remain clean with cash and receivables comprising nearly all of our assets and accounts payable, accrued expenses and deferred revenue representing nearly all of our liabilities. This completes our financial summary. I'll now turn the call back to Peter. Peter?

Peter Victor Derycz

Founder, CEO, President & Director

Thanks, Alan. First, I'd like to walk through the various new platform enhancements we made this quarter and what we have planned for the future. As I mentioned earlier, we are committed to continually evolving our platform and providing a best-in-class research platform, which is why our team remains hard at work to consistently introduce new gadgets and update existing ones. We completed updates to more than 15 of our current gadgets throughout the quarter, which ranged from allowing users to download visual graphs in various life sciences gadgets to adding new search features for our library gadgets that make the search process more intuitive and efficient. We also continue to make improvements to our flagship gadget, Reference Manager gadget, bringing better functionality and stability. Our development team prides itself on continually looking for ways to improve our core capabilities, deliver great features and enhance current gadgets. Along with listening to customer feedback to ensure the customer experience on our platform is exceptional.

In addition, we launched our Research and Discovery gadget earlier this month, which allows users to perform comprehensive literature searches and access full text documents across multiple databases, all within the article Galaxy Platform dashboard. Within this new gadget, we also included the ability for a user citation directly to the reference manager gadget, providing seamless integration and easier access to the research data. We have already received excellent feedback from this launch and we plan to further enhance this new gadget by including additional capabilities geared towards biotech, patent and clinical trial databases in the coming months.

We also continue to make progress on building out new features for the overall platform along with completing various user experience and interface enhancements. In fact, we completed building out the Article Galaxy scholar during the second quarter and are currently in the initial test phase. As a reminder, Article Galaxy Scholar will be a new aspect of the platform that is specifically tailored to the university and academic markets. We have a growing list of universities that have been joining us as customers. However, they've been using features and functionality designed for corporations. Thanks to their support and feedback, we are happy to now deliver an aspect of Article Galaxy, better design for

the way universities deliver information resources as well as how they budget for them. In addition to launching Article Galaxy Scholar, we have plenty in the tech development pipeline over the next couple of quarters. We are working on making various framework improvements to enable additional end-user data storage capabilities, including expanding functionality to search through data, adding prospect driven system enhancements and further developing back end automation that we anticipate will continue improving our gross margins along with our ability to sell. Another key aspect to our growth strategy is pursuing highly complementary partnerships that expand our presence within the research community more efficiently. Our most recent partnership with evidence partners launched during the second quarter and has already proven to be successful in allowing our 2 user bases to use specific tools from evidence partners to connect to scientific literature via the Article Galaxy platform. We are continually finding synergies between the 2 platforms while working on technical integrations and we believe these will play an important role in driving new users to the platform and generating awareness of all the benefits we have to offer together. We remain active in searching for similar partnerships that we feel provide the best benefits for the customers of both companies. In fact, we have another very exciting partnership in our pipeline, which we anticipate will launch in the back half fiscal 2020 that we believe will be highly beneficial to our customers and significantly expand the content and data resources we have to offer on Article Galaxy. We look forward to updating the market on this partnership once it has been launched.

Lastly, I wanted to provide a brief update on the rebranding efforts, which began this quarter. As a reminder, we transitioned our 3 existing brands into 1 company name, Research Solutions and 1 product name, Article Galaxy. As a result, our sales team is now completely integrated and pitching 1 brand to all customers. We launched this initiative as part of our desire for greater simplification and to eliminate confusion between platform users and transaction buyers. Since launching the rebrand, our sales and marketing teams have received nothing, but positive feedback from potential customers, existing users and transaction buyers. We are confident that this consolidation under 1 brand name will further expand our reach and drive more of our transaction buyers to our platform offering.

As we look to the back half of fiscal 2020, our focus will remain on generating new enterprise customers, along with introducing our unique capabilities to an expanded audience through highly complementary partnerships to accelerate platform revenue growth. Our ability to provide an innovative research platform that is consistently evolving to meet the needs of our customers combined with our retooled sales and marketing strategies, gives us confidence that we will continue executing our growth strategy for the remainder of the year and beyond. With that, I'd now like to turn the call back over to the operator for Q&A. Operator?

Question and Answer

Operator

Operator Instructions]. At this time, this concludes our question-and-answer session. Before we conclude today's call -- pardon me, we have some questioners. I have George Melas with MKH Management.

George Melas-Kyriazi

MKH Management Company, LLC

I was just wanting to ask if you could give us a little bit more color on the sales and marketing. And what are maybe some of the changes that you've made in the last quarter or 2 quarters in the sales and marketing? And how are you going to market right now?

Peter Victor Derycz

Founder, CEO, President & Director

Sure. Yes. So as you know and we mentioned we've transitioned all of the sales and marketing to focus on enterprise accounts, B2B. And what that means is that the marketing materials on the marketing side, the content that we're providing is really oriented towards enterprise customers. So in the past, we were -- we had experimented those with going after what we call the B2C market, trying to get individual users, individual scientists using the platform directly, we found that we have had -- we had more success on the enterprise side. So now if you look at our marketing materials, white papers, blog posts, everything we're doing on marketing side, outreaching campaigns, it's all focused on that enterprise customer. And on the sales side as well, we've really -- as a result of that whole shift to folks at enterprise, we've really been able to fine-tune our experiments into who do we really want to talk to, who do we really want to go after and have conversations with. And so over the last couple of quarters, we've pretty much, I think, gotten very focused on the size of the account that we have the most success with, how to approach them, how to get our sales reps in front of them, and really give the prospect a chance to learn about our solution and sales rep a chance to close the deal. So it's just a lot of fine-tuning and I think we've sort of gotten into a bit of a rhythm now. We were able to close a little bit -- a few more deals now as a result. So we plan on continuing to execute on that.

George Melas-Kyriazi

MKH Management Company, LLC

Okay. And you mentioned, Peter, that your close rate really -- I guess it makes sense, part of the sales process involves giving a customer -- a salesperson in front of a customer. Just from a question, there was typically face-to-face meeting? Or are you doing them online? And -- or is there a big difference between the 2 in terms of success in terms of closing?

Peter Victor Derycz

Founder, CEO, President & Director

Yes. No, mostly, it's remote and online demos, phone calls. There are a few face-to-face, depending on the size of the prospect and where they're located. And yes, so we really fine-tune that -- the ability to do it online is -- there's just so many great tools to do that with now. And so the key aspect really is not getting face-to-face with them in terms of being there in person, but rather just having the time allocated in the prospects bandwidth to spend that time with one of our sales reps to really look into the platform and discuss the cost savings and efficiencies and so on that we achieved by adopting the platform.

George Melas-Kyriazi

MKH Management Company, LLC

Okay. And once you do a demo, what is your close rate? Can you give us that number? Or...

Peter Victor Derycz

Founder, CEO, President & Director

No, we can't give you the number. We cannot give you the number. All we can say that it's improving quite a bit. So we think we've gotten into a rhythm and that means that we've been able to sort of prospect the right people to talk to and we've been able to successfully make sure that we're not just sending e-mails and we're looking at our website, but in addition to that, that phone call of that online demo actually takes place. So since we've been able to fine-tune our prospecting and our appointment setting capabilities that -- but we can't give you a number. I can't confirm that it's improving quite dramatically.

George Melas-Kyriazi

MKH Management Company, LLC

Okay. Can you -- are you tracking how long people spend on the platform? And can you give us what are the key apps that they're using? And with -- and how long do they generally stay on the platform, whether it's per day, per week, kind of if you're tracking some metrics there?

Peter Victor Derycz

Founder, CEO, President & Director

Yes. We are tracking exactly what they're using and so on. We don't put out those metrics publicly, but I can say that a key component of this -- of the whole user experience and staying on the platform. And one of the reasons for our high renewal rates is the fact that we do provide some training and onboarding. So we make sure that everything is set up properly. We make sure that the users and the power users and the administrators are aware of the capabilities and train through those. And so it's really the -- I think the training that really drives the success because once you know how to use the platform and are going to walk through it, that's what you tend to stick with us. And so we make sure we have some sort of flagpoles on the horizon that we make sure that when we reach that flagpole, we'd do some training. When we reach that flagpole, we'd do some communicating and so on. So it's really more about that than the quantity of usage per se.

George Melas-Kyriazi

MKH Management Company, LLC

Okay. And then maybe just one final question on Reference Manager. Some of your customers switching to your Reference Manager and by that, I mean, no longer subscribing to the stand-alone reference manager in the market? Or is it possible for you to see that? Or maybe it's not.

Peter Victor Derycz

Founder, CEO, President & Director

Yes. I'd say it's early days now in Reference Management world. So I wouldn't be able to just giving you numbers like that, but I could say, yes, it's early days. We've listened to customers, made some changes, improved some improvements and stability improvements and so on. So I think a little bit early to give any guidance or feedback on that.

Operator

[Operator Instructions]. Our next question comes from Glenn Arbeitman with GlennAllen Advisors.

Glenn Arbeitman

Another fine quarter. I'm sure I might pay investors on the call and invested with you that never get tired of seeing you improve those margins. So really well done for a good job to the whole team. I was a little curious, just gave us a little tease toward the end of the call there about a new impending partnership that sounds like to be very promising. I realize you're not going to comment too specifically there until it's done, but is that part of a shift to include other industry's publications and articles that you see as good fruit for picking and scale? Or is this something still within science technology that is relating to the sort of products we've been delivering?

Peter Victor Derycz

Founder, CEO, President & Director

Yes. Well, our forte is science technology. So yes, most of what we're doing, especially since we're so enterprise-focused is really science, technology and medicine related. So it's really about expanding what customers can access on our platform about improving the user experience, ease of use and ease of access to more information. And so it's sort of in that vein of just becoming a more robust platform that's got a lot more compelling reason to join. And then, yes, you'd really miss all the stuff if you lack. So it's really within XTM to kind of show.

Glenn Arbeitman

Okay. Great. I look forward and good luck getting across the finish line. On an unrelated more stock sort of question. Last quarter, you'd mentioned there's some discussion about the national market listing and a possible -- I don't know if you're going to go out raise money or what your plan was, but can you give us an update on sort of where you are on that plan?

Peter Victor Derycz

Founder, CEO, President & Director

Yes. So we -- as we mentioned on the last call, our -- we maintained our application with NASDAQ current. So we -- it's a live application in current. There are a couple of criteria. One is just cash on the balance sheet, we're about \$1 million short. Whether or not, we want to address that through a capital raise or through any other means, yes, I can't comment on. The -- and then the other one we're trending a little bit low on just sort of a new criteria was average daily trading volume, just a bit shy on that. Sometimes we're there, sometimes we're not. So I think now that the stock is getting a little bit more noticed, I think we'll be able to clear that hurdle. The stock is moving in a nice direction. The company is moving in a nice direction. There are no negative surprises. We seem to be executing on a good growth plan and gross margin improvement plan. So I think that at some point, hopefully not too far in the future, we'll get there. And it's one of my key objectives. We know that the NASDAQ would be a better exchange for our shareholders, including myself. And so it's one of my key priorities.

Operator

At this time, this concludes our question-and-answer session. Before we conclude today's call, I would like to provide Research Solutions' safe harbor statements that include important cautions regarding forward-looking statements made during today's call as well as statements regarding the company's use of non-GAAP financial information. Statements made by management during today's call contain forward-looking statements that include information relating to future events and future financial and operating performance. Examples of such forward-looking statements in this presentation include, but are not limited to, statements regarding the expected continued improvement and market acceptance of the company's products and services and the expected continued growth in transaction and platform deployments and revenue that the company will be successful in executing its sales and marketing strategy, that the company will maintain and continue to develop its proprietary software and that the company faces tough barriers in terms of achieving greater global expansion and revenue growth. Such forward-looking statements should not be interpreted as guarantee of future performance or results and will not necessarily be accurate indications of the times at or by which the performance or those results will be achieved. The forward-looking statements were based on information available at this time. They are made and are management's good faith belief as at that time with respect to future events and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed and/or suggested by the forward-looking statements. Important factors that could cause differences include, but are not limited to, changes in economic conditions, general competitive factors, acceptance of the company's products in the market, the company's success in obtaining new customers and new platform deployments, the company's success in technology and product development, the company's ability to execute its business model and strategic plans, and all the risks and related information described from time to time in the company's filings with the SEC. That is the Securities and Exchange Commission, including the financial statements and related information contained in the company's annual report on Form 10-K and interim quarterly report on Form 10-Q. The company undertakes no obligation to publicly update or revise any forward-looking statements, whether because of new information, future events or otherwise. The company also assumes no obligation to update the cautionary information provided in the presentation. Today's presentation also included financial measures

defined as non-GAAP financial measures by the SEC. The presentation of this financial information is not intended to be considered in isolation or as substitute for the financial information prepared or presented in accordance with the generally accepted accounting principles accepted in the U.S., otherwise referred to as GAAP. Please refer to more detailed discussion about the company's use of non-GAAP measures and their reconciliation to the nearest GAAP measures in today's earnings press release. Finally, I would like to remind everyone that the recording of today's call will be available for replay after 8:00 p.m. Eastern Time -- Eastern today and through March 5, 2020. Please refer to today's press release for dial-in instructions. Thank you for joining us for the presentation. You may now disconnect.

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