FINAL TRANSCRIPT

ProntoForms Corporation

Second Quarter 2019 Conference Call

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PRESENTATION

Operator

Good morning. My name is Sylvie, and I will be your conference Operator today. At this time, I would like to welcome everyone to ProntoForms Second Quarter 2019 Conference Call. 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 this time, simply press *, then number 1 on your telephone keypad. And if you would like to withdraw your question, please press *, followed by 2. Thank you.

Mr. Babak Pedram, you may now begin the conference.

Babak Pedram — Investor Relations, Virtus Advisory Group Inc.

Thank you. Good morning, everyone. Thanks for joining us this morning.

Before we begin, I will read our cautionary note regarding forward-looking information. Certain information to be discussed during this call contains forward-looking statements within the meaning of applicable security laws, including, among others, statements concerning the company's 2019 objectives, the company's strategy to achieve those objectives, as well as statements with respect to management's beliefs, plans, estimates, and intentions, and similar statements concerning anticipated future events, results, circumstances, performance, or expectations that are not historical facts. Such forward-looking statements reflect management's current beliefs and are based on information currently available to management, and is subject to a number of significant risks and uncertainties that could cause actual results to differ materially from those anticipated.

Also, our commentary today will include adjusted financial measures, which are non-GAAP measures. These should be considered as a supplement to and not as a substitute for GAAP financial measures. Reconciliations between the two can be found in our Management Discussion and Analysis, which is available on sedar.com and our website.

And finally, note that because we now report in US dollars, all amounts discussed today are in US dollars unless otherwise indicated.

With that, I will hand over the call to our CEO, Mr. Alvaro Pombo.

Go ahead, sir.

Alvaro Pombo — Chief Executive Officer, ProntoForms Corporation

Thank you, Babak, and thank you, Sylvie. Good morning, everybody, and welcome to our company's conference call.

Before I hand the call over to our CFO, David Croucher, to discuss this quarter's financials, I would like to take some time to discuss the ProntoForms business in terms of its strategy, our 2019 execution on where we see the business heading over the next 24 months. The engine of this company continues to be recurring revenue and our main focus is to keep refining our business model to create more of it.

Q2 was another good quarter for us, as growth in recurring revenue increased by 5 percent over Q1 2019 to 3.3 million, and our ARR base continued at 26 percent annual growth. That is now six consecutive quarters of 5 percent or over growth.

Enterprise growth continues to be very favourable to us. Our largest accounts are now becoming even bigger. Today, we have 30 percent of our base made of customers with more than $100,000 of ARR, up from 23 percent in June 30, 2018. We have a base of more than 100 enterprise accounts with low penetration and now we have reached a good EBITDA level. We are continuing to invest in sales to perfect the motions to further penetrate these large accounts.

Also from a market perspective, the news is good. We have been selected by a lead IT analyst firm as a relevant niche player in a very large automation segment for building apps without requiring code. The need to enable line of business analysts to build apps to accelerate the company digital transformation never been greater, and our unique approach to enable the rapid building of field-centric apps has been clearly recognized. This is just the beginning of the journey of being a player in a well-identified, rapid growth market.

Another important element of our equation for getting closer to larger customers is our product. We hosted our first enterprise customer event in Ottawa this past June and it was a great success. We share our product direction, new features, and approach to innovation, and received a very good reception.

To wrap up, the demand for our product continues to grow. The complexity of field workflows is growing every day. More sensors, more digital twinning, more machine learning, more data ingestion requirements. Large organizations have made very clear decisions about enabling their line of business analysts with low-code and self-serve application development capabilities. More intelligent workflows are needed in the field, and the old way to dealing with them through building custom apps is not sustainable, particularly for enterprise operations. Our product deliver on both needs at scale so I see no end in sight to the problems we solve.

With that, I will hand over the call to Dave to discuss our financial performance for the quarter.

Dave?

David Croucher — Chief Financial Officer, ProntoForms Corporation

Thank you, Alvaro, and good morning, everyone. I'll go through the financial highlights but I won't repeat all the detail included in our MD&A. I would refer people to read that as well.

Total revenue for the second quarter of 2019 was 3.7 million, representing a 5 percent increase over Q1 2019 and a 26 percent increase over the comparative Q2 2018. Of this total revenue, 90 percent was recurring.

Recurring revenue in the second quarter was 3.3 million, representing a 5 percent increase over Q1 and a 26 percent increase over the comparative Q2 of 2018.

In terms of revenue bookings, ARR base at June 30, 2019 was 13.7 million, representing a total increase of 26 percent year over year and a 5 percent increase over March 31, 2019. As Alvaro mentioned, our ARR base is shifting to a higher proportion of larger customers. Customers with greater than 100,000 of annual equivalent recurring revenue has grown to be 30 percent of our base versus 23 percent at June 30 last year.

Revenue from professional services was 372,000 for Q2 compared to 358,000 in Q1 and 281,000 in Q2 2018. Gross margin on total revenue for the second quarter was 84 percent, up from 81 percent in Q1 and 83 percent in Q2 2018. This is a blended rate from both professional services and recurring revenue components. The recurring revenue portion was actually 90 percent of recurring revenue, an increase from 89 percent in Q1 and 88 percent from Q2 last year.

Operating expenses for the second quarter were 3.5 million, up 7 percent over Q1. The increase in Q2 was primarily attributable to our continued investment in product and research and development.

Just to add a bit of colour, Alvaro mentioned that we are investing in sales and marketing as well, and we did. It didn’t have an impact on the Q2—an increase over Q1 in sales and marketing—but we did add more headcount later in the quarter. So we are continuing to invest there, and we can go into more detail in the Q&A if people are interested.

Loss from operations for Q2 2019 was 417,000, up slightly from the first quarter of 2019 of 398,000. Net loss was 530,000, effectively flat from 532,000 in Q1. Non-GAAP op loss for Q2 was 335,000, an increase from 286,000 from the first quarter of 2019 and a decrease from 582,000 from Q2 last year.

Our cash balance at the end of June was 5.75 million compared to 3.3 million at December 31, 2018. The increase in cash is attributable to the exercise of US$2.4 million in warrants.

Also of note, cash flow from operations for the first half of the year was slightly positive. The biggest contributing factor here is the increase in cash from prepaid contracts, offsetting a significant portion of the non-GAAP loss for those same six months.

In summary, we are pleased with the trends in our key metrics. We added 5 percent sequential growth in recurring revenue in the quarter, adding to our string of steady growth there. Our enterprise base grew in proportion to our total base, mostly through expansion of existing customers. Prepaid contracts from these customers contributed to our cash flow to mitigate our already reduced operating losses. Cash flow from operations was actually up slightly over the first six months of the year.

Our non-GAAP op loss increased slightly as planned, and as we mentioned last quarter, as we grow revenue we want to reinvest that growth into enterprise product development and sales capabilities. While we may see variability in growth in the short term, as we continue to build out our enterprise capabilities we are continuing to invest in sales and marketing to add depth and be able to take advantage of the continuing strong demand that we are seeing.

That concludes the financial highlights. With that, I'll ask the moderator to open up the line for questions. Thanks.

Q&A

Operator

Thank you. Ladies and gentlemen, if you do have a question, please press *, followed by 1 on your touch-tone phone. You will then hear a three-tone prompt acknowledging your request. And should you decide you would like to withdraw your question, simply press *, followed by 2. And we do ask that if you're using a speakerphone to please lift the handset before pressing any keys. Please go ahead and press *, 1 now if you do have a question.

And your first question will be from David Kwan at PI Financial. Please go ahead.

David Kwan — PI Financial

Hey, guys.

Babak Pedram

Morning, David.

David Croucher

Hey, Dave.

David Kwan

Morning. Morning. Good job on the quarter. Jumping on the sales and marketing side, you guys—Dave—I think you talked about some of the stuff that you were doing towards the end of Q2 that's going to impact Q3. Can you provide some more details there?

David Croucher

Yeah. So just to put it in perspective, I guess Michael Cho started not quite a year ago, he started Q3 last year, and really made some significant changes in the sales team going into 2019, as one would expect, reorganized the team. So we did see a bit of change in that group and some turnover in Q1. Got back on track in Q2 and added some good strength. Took a little while to add people there; he wanted to make sure he was getting the right people. So now we've built that team up and we feel like it's got some bench strength going forward.

Just to give you a sense, I'll give you some numbers. So quota-bearing reps at the end of last year were 10, and then that decreased to about eight by the end of Q1. And at the end of Q2, that was up to 12, and mid-quarter, so as of last week, we were up to around 15. So making good progress there.

David Kwan

No, that's helpful, Dave. Thanks. Thanks for that. I guess, is Michael and are you guys happy with that level now? Or is there plans to add some more?

David Croucher

Yeah. We're going to—we needed to make the gap up and we feel like we've made good strides there, but we're not stopping. We want to keep building that team out and make sure that the growth rate there is consistent with the growth in the business at least and even more. So we want to—we don't want to be in a position where, if you have changes within the group that that's a significant portion of the group. We want to make sure we've got lots there to get to critical mass so that any changes wouldn't have an impact, so.

David Kwan

All right. Are these people that you guys are adding, are they experienced reps? And such, they hopefully will get up the curve quickly and get to their full quotas?

David Croucher

Yeah. We've added a few more in the States as well, and they are, David. I mean, historically, most of our sales came from marketing leads and then we started to have partner leads, and I'm talking about the last couple years. So they would really just have those leads qualified and then they would jump in and work on closing them. The team that we're adding now are capable of certainly that, plus doing more outbound, being able to talk to enterprise reps. And we're getting into more IT as part of the sales, and those people would have more better skills in that respect. And maybe I'll pass it over to Alvaro to comment more on that.

Alvaro Pombo

No. You said it well. And all lines of business, I mean, the commercial and the enterprise, continue to have substantial demand. So, yeah, we're going to push the gas pedal and continue to do it. We've never been doing things crazy. I mean, we're steady and driven by numbers and productivity. And the numbers are there, so we're going at it.

David Kwan

No, that's good to hear. I guess, looking at some of these reps. So you've had previous growth to date, kind of the land-and-expand strategy. A lot of the growth has been with your existing customers. Do you feel that you're in a better position to kind of go out and win some larger deals with newer customers with this team in place? Or do you still expect kind of a continuation of the strong and steady growth within your existing customer base?

Alvaro Pombo

Yeah. Great question. I think we're starting to see that the combination of partners, what I mentioned there about that quadrant and that recognition by—we'll put a press release soon—but by that analyst firm, it's very relevant. I mean, the space is very clearly delineated now. We have a very clear value proposition and a very clear differentiation within that space, and I think that's bringing us into some very interesting conversations. So partnering activity continues, which is the fastest way to get to some of those IT or senior line of business managers conversations. So we're starting to see a lot more of them happening.

A lot more interest, as well, from those large enterprises. It's still coming through our website. The description of what we do is very—I think is well-placed, and you will see some tweaks and moves and changes refining it even further. So I think it's working and we're getting to those conversations. Yes, we are, and it feels good.

David Kwan

Okay. Perfect. On the R&D front, that ticked up this quarter. Was there anything in particular that drove the increase? Or was it just timing? And kind of looking forward, is this kind of the base that we should be looking at in terms of a run rate?

David Croucher

There was a few different factors. First of all, we had an IRAP program that we claimed in Q1, so that brought the expense down a little bit in Q1. So when you're comparing Q2 to Q1, that has an impact.

What we did add was some strength on the product management, product marketing side. We've got new tiers coming out, and they've been building that out and building the messaging, working with the analysts to come up with better communications to customers and out to the public, so built up some strength there. And then, yeah, did add some on the development team as well, but nothing as dramatic there. But we're going to continue to build that steadily, but really what you're going to see going forward is more growth in the sales and marketing area.

We're always—we had that IRAP program that ended in Q1. We're working on more so we'll see what comes through, but that's a nice thing where we can add headcount but not have the expense related to it.

David Kwan

Okay. You weren't using a bunch of subcontractors or whatnot this quarter? It was more in-house spend?

David Croucher

It was—we have a mix, but no real change to it. But what we've been doing is adding more in-house. And we're always looking at different ways to bring in talented people internationally, and we actually did bring in some people. There's five junior engineers that came in, so adding a lot of depth to the organization but less costly, and they're getting great experience and we're getting great benefit from their capabilities. So always looking at ways where we can add that.

David Kwan

Perfect. Just one more question from me on the gross margin side. Nice to see the pickup here. Was there anything going on that drove that? And kind of how sustainable was there—how should we be looking at that line going forward?

David Croucher

Yeah. Good question. So on the recurring revenue, we hit 90 percent, so up a little bit. I think the way that that margin works or the way the cost of sales works against that is sometimes it's a bit of a step function. So we've been steadily growing the revenue base and the costs didn't go up quite as much, so got the benefit there.

Now that could and will likely change going forward in terms of when we add new features, there might be another step function in terms of a cost related to that, but nothing significant. So I think, when you're talking our margins, it's been very consistent in that 88 to 90 percent range for a long time. So it might come up and down a little bit in that range but still pretty steady there, I think. Does that help, David, or?

David Kwan

So overall—so I guess overall, though, including in the special service side which can be a bit more lumpy, kind of low-80-percent range is still kind of what we should modelling in?

David Croucher

Yeah. So overall—so sorry, just on the professional services and that, while we're there. So actually, it was pretty decent. I think it was 29 percent in that area of the margins there. And historically, that's been lower, and we've had a mix of, we call it professional and other services. And the other services tends to be lower-margin where we're doing marketing programs so a lot of it's more cost, third-party costs that are involved there. We didn't have that in the last two quarters, actually. So really, it's been the production of that team that have been doing deployment services and those types of activities, so running at a pretty efficient rate and getting pretty much pretty close to 30 percent margin there. So that looks good. There will be always some variability up or down, but—so that should be fairly consistent in that range. So overall, that blended to 84 percent. Now that's a tougher one because it depends on the mix. But I think that's reasonable in that range. Maybe, once again, maybe a variability of 1 to 2 percent.

David Kwan

Sounds great. Thanks, guys.

David Croucher

Yeah.

Alvaro Pombo

Thank you, Dave.

Operator

Thank you. As a reminder, ladies and gentlemen, if you do have any questions, please press *, followed by 1 on your touch-tone phone.

And your next question will be from Gabriel Leung at Beacon Securities. Please go ahead.

Gabriel Leung — Beacon Securities

Good morning, and thanks for taking my questions. So a lot of the details have already been provided. But maybe, Alvaro, you can talk a little bit about, as you go through the sales process within the enterprise, are you running into scenarios where you're getting pushback from some of the smaller accounts who could become bigger accounts in terms of expanding? And what are some of the pushbacks you might be hearing from them? Or is it really just a timing thing in terms of if and when they deploy? Larger, anyways.

Alvaro Pombo

Yeah. Good question. So I spoke last time about the 120, 140 large enterprise customers; how our classification of large enterprise means 2,500 employees or more. So the first fact is that it continues to increase. So we keep on bringing new people in the top of the funnel with that characteristic, which goes back to the message and the positioning, et cetera. The second part of it is, as you engage with them, the large existing ones put it, the ones that have already bought on, they're expanding faster and deeper, which is a great set of—which is great news, too.

So then the question is, how do you take those in the middle and what are the dynamics associated with them. What we're seeing is that there are two flavours of them. Line of business-driven expansion, and on those, we have use cases and it just cycles. It is you're engaging with them, they use the product in a geography, we're expanding to another geography, and we go—and it works, I mean, it's starting to work. We have to add more resources to it, no question about it. That's what we're doing and we're starting to see it coming through.

The other flavour, that is the one that touches closer to the analyst report that I mentioned is an IT-driven expansion. And that's a very important one to talk about. That's one where IT is now saying, I need a tool to enable more line of business or self-serve automation. And that's a very powerful one, and that's the one that we have a product for them, and we're tweaking a little bit more the messaging. And that's one where we're starting to see it's a new source of that conversation. So as you can hear what I just said, I mean, there are different flavours of them. We're specializing different motions to go after them.

Gabriel Leung

Gotcha. And maybe one more question, just as we think about M&A and maybe the future evolution of your platform. At this point, you guys are obviously focused on what you have in place right now, the products you have in place right now, and getting deeper into some of your existing customers. But where's the thought process in terms of how's this platform going to evolve over time? What major pieces do you think you could add to it, whether it be workflow-related or maybe content management-related? Is that something you guys have been thinking about? Is that something we can expect to see in the near future?

Alvaro Pombo

Yeah. So I think I go back to the same analyst piece, which basically sets the, call it the definition of the space, more clearly. So the first part that is happening is that the form's story—I'm going to say something and I will characterize it in a second—the form's story is past. Okay. The Form, what is it? A set of questions and answers that was an easy way to get these people to look at a workflow and building an app, that it was done in an efficient manner. I think that's behind, and with that, we leave as well a set of competitors and a set of capabilities, because we have a top-notch product that does that and a lot more.

So as we've been enhancing that product, we're getting into some other things you mentioned, I mean, which is sort of like how do workflows operate, how do you ingest better data in the field, how do you do a lot of those things where our product is very good and differentiates against many people. And then, in the bigger picture, it's going to be, okay, so what kind of LCAP tool we want to be. And in the current positioning, I mean, is we are a field-centric one, and the field-centric gives us a set of issues that we're going to continue to specialize on. So from now on, yes, bring in new technologies, whether we OE aiming or, in the future, we can be looking other ways of bringing those technologies in to get deeper in that area. We had hired some help to size how big that market is and the verticals that we're going after, and it's very, very sizable. So there is no end in sight to that thought process.

And then, as we continue to evolve it, yes, now we're in a position where we're adding people. We have a good balance sheet, we have more cash, we have a lot more freedom to entertain some of those higher-growth thoughts, and we are talking about those already.

Gabriel Leung

I gotcha. And sorry, Dave, one last question. Sorry to make you repeat yourself, but I missed the part about sales and marketing and what additional costs or headcount additions we should expect to see in Q3.

David Croucher

Okay. Well, I went through the numbers. I'll just repeat them. So we ended the year at—or 2018, we ended the year with 10 producing reps, and that was down a little bit to eight at the end of Q1, and up to 12 at the end of Q2. And then mid-Q3, we were at about 15. And we want to continue to add at the pace of the business or more in that area. More in that area until we get to a critical mass where, in Q1, I think we were hurt a little bit. Like eight quota-bearing reps, they were mostly making their living off of the existing customers that were expanding, and we had very good leads from other sources and just weren't being dealt with with enough attention.

So now that we have more depth in the organization, if we make any changes or if anything happens, then we have that critical mass to carry on. And then we want to get into a good rhythm, continuing to go forward with a good rhythm of adding reps at either the pace of our growth or even a little more, to make sure we're ahead of it and not falling behind that. So our priority is growth, and we want to make sure we're feeding that at the right level.

Gabriel Leung

Gotcha. Thanks for the feedback. Thanks a lot, guys.

David Croucher

Okay. Pleasure. Thanks, Gabriel.

Operator

Thank you. Once again, ladies and gentlemen, if you do have any questions, please press *, followed by 1 on your touch-tone phone.

And at this time, we have no other questions, so I would like to turn the call back to Mr. Pombo.

Alvaro Pombo

Thank you, Sylvie. We see a stronger demand, as I said, supported by industry experts, and we believe that we're on the right track, investing in our enterprise product and sales team to take full advantage of that. We're very excited about what's ahead for the business.

Once again, thank you very much, everyone, for spending your time with us this morning. And as always, I would like to thank you all for your continued support. Have a good day.

Operator

Thank you, sir. Ladies and gentlemen, this does indeed conclude your conference call for today. Once again, thank you for attending. And at this time, we do ask that you please disconnect your lines. Enjoy the rest of your day.