TRANSCRIPTION

Company:	**Sezzle**
Date:	**9 August 2023**
Time:	**10:30am AEST**
Duration:	**20 Minutes**
Reservation Number:	**10032520**

[START OF TRANSCRIPT]

Operator: Thank you for standing by and welcome to the Sezzle Inc second quarter earnings conference call. All participants are in a listen-only mode. There will be a presentation followed by a question and answer session. If you wish to ask a question, you'll need to press the star key followed by the number one on your telephone keypad. I would now like to hand the conference over to Mr. Charlie Youakim, CEO. Please go ahead.

Charlie Youakim: Thank you. Good morning everyone, or for those joining us from Sezzle's home in the US, good evening and welcome to Sezzle's 2023, second quarter earnings call. My name is Charlie Youakim, I'm the CEO and Executive Chairman of Sezzle. I'm joined today by my Co-Founder and President, Paul Paradis, our Chief Financial Officer, Karen Hartje, and our Head of Corp Dev and IR, Lee Brading. I'm going to get started with the presentation now, which you can find posted on the ASX website if you'd like to follow along. Before we get into the quarterly results, I would like to touch on our journey as highlighted on slide three. In roughly five short years, we have built something special here at Sezzle. We have handled over 5 billion in volume, representing more than 50 million orders and had more than 15 million consumers sign up for Sezzle. I think it is a resounding yes that our product helps consumers and the proof is in the numbers.

While I'm clearly proud of the journey and the benefits we have provided merchants, consumers since our launch, I'm extremely excited to talk about our accomplishments over the last 12 months. We started on our path to profitability in the first quarter of 2022, which required us to make some tough decisions. Those tough decisions have turned out to be good decisions and have allowed us to drive and expand our product offerings to better serve our merchants and consumers. Again, the proof is in the numbers. Our profit margin at the net income line was 5.7% for the last 12 months, while we also grew our top line in the double digits. I'm not aware of any other pure play buy now pay later companies that can say they have grown the top line in the double digits and then profitably over the last 12 months. Even more, I don't think any other pure play buy now pay later can say they made a quarterly profit, much less a profit over the last 12 months.

I believe we have done it the right way and so do others. We have been recognised for our achievements by CNBC, Forbes, Fortune, and the Wall Street Journal, to name a few. What does it mean when we say we are doing things the right way? Slide four tells the story of our all-inclusive stakeholder approach. As you look at the details underlying each of the pillars, justice, integrity, stewardship, and advancement, notice that within each our stakeholders, merchants, consumers, shareholders, employees, and community are front and centre. Assisting people on their financial journey is a great responsibility that we do not take lightly. As the only buy now pay later company that is a certified B Corp, we believe our actions speak louder than words.

Giving consumers the opportunity to spread payments out, avoiding interest and building credit fills an important gap for people that may be facing financial difficulty in their daily lives. Since our inception, we have been committed to driving change to financially empower people on their financial journeys. Turning to slide five, you can see how we've been driving change with numerous product launches, with the goal of becoming an all-encompassing payment services platform for consumers. We started simply the paying core product offering, offered at select merchants and have continued to evolve to meet the needs of our users, adding such offerings as Sezzle up, Premium and Anywhere. We recognise that consumers need more than what we currently offer, so we aren't done and we plan to continue to create ways to help consumers on their financial journeys.

Speaking of expanding to meet the needs of consumers, our subscription offering highlighted on slide six is clearly meeting the needs of consumers. We now have over 195,000 subscribers of Premium and Anywhere combined. Since July 1st, we have been adding on average over 700 subscribers a day to Premium and Anywhere, on a combined basis. If that's not enough to convince you, our net promoter score ratings have been off the charts, with Premium and Anywhere receiving consumer NPS scores over 60 and 70 respectively. For some context, an NPS in the 50 to 70 range means you are amongst the most beloved brands and anything above a 70 is generally considered the holy grail of scores.

What's good for the consumer is also good for us. Our subscription products experience greater frequency of use compared to our non-subscription products, which leads to higher consumer LTVs. Because of the ease of use of Sezzle Anywhere, we're also becoming our user's top of wallet payment method. With more purchase activity, we are seeing the AOB come down, but purchase frequency is more than offsetting the AOB decline. We are also seeing a step-up and offline use as the product is used anywhere Visa is accepted. It's exciting to see us truly become an omnichannel option. Now let's get to the reason we're holding this call, to discuss second quarter results.

Turning to slide seven, I must admit life is a lot easier when there is green in the columns versus the alternative and in Q2 it's green across all our key financial metrics. Total income increased 5.7 million or 19.4% year over year to 34.9 million. This improvement is just a small part of the story. More importantly, we went from a net loss of 15.1 million in the second quarter of 2022, to a net income of 1.1 million this quarter. We did it through a combination of revenue enhancements, unit economic cost improvements, and lowering non-transactional related expenses. What this team has accomplished is truly phenomenal. Our adjusted EBITDA margin rose to a positive 18.3% compared to a negative 32.2% in the prior year. And our unit economics or gross margin, was a healthy 53.7% compared to only 32.7% in the prior year. And lastly, our non-transactional related operating expenses billed a 54.2% of total income compared to 84.8% in the prior year. Kudos to the team.

Our engagement scorecard on slide eight is mostly positive. We have been winning the race where it matters, increasing repeat usage, subscription growth, driving traffic through our marketplace and in the process diversifying our revenue streams away from being completely reliant on merchant processing fees. The decline in merchant count might seem concerning, but it is not. Generally these ultra micro merchants do not drive our business. We implemented some minimum hurdles for merchants to remain on our platform due to the cost of supporting them, and thus have seen a drop in count. Our results show that these merchants were not driving our performance. We have seen some decline in consumer count, but we are encouraged by recent activity that this will start to level off soon. Further, we believe that we have several future initiatives that will put this on the growth path again. I'm now happy to turn the call over to our CFO, Karen Hartje, who will go over the quarterly results in greater detail. Karen.

Karen Hartje: Thank you, Charlie, and hello to all. Before we dive in, just a reminder that our second quarter results are unaudited and presented in US dollars. Turning to slide nine, although we experienced a year over year decline in UMS in second quarter, total income rose 19.4% year over year to 34.9 million. Our top line improvement at 9.1% of UMS was driven by the diversification of our revenue stream, as 44% of our total income in second quarter was derived from non-merchant processing fees compared to only 19.3% in the prior year. We are encouraged by the sequential gain in UMS from first to second quarter, of 3.6%, which also reflected a pickup of inactivity in June relative to April and May. For the month of July, UMS was up 4.1% year over year to 147 million, which also represents a 13.5% increase compared to June, 2023.

Without giving too much detail, for the early days of August, we are seeing an additional pickup in UMS relative to July. In fact, one of the days in August already represents our best day this year in terms of volume. Yes, we are excited by what we are seeing. On slide 10, second quarter '23 transaction expenses comprised primarily of payment processing costs, improved 34 basis points year over year to 2.1%. We believe we can further lower our payment processing expenses as we continue to push for consumers to use ACH, renegotiate terms with network partners as our volumes grow, and expand products such as pay in two and pay in full, they reduce our fixed instalment processing costs. As discussed on our first quarter '23 earnings conference call, we anticipated that our provision for credit losses would increase and that is the case in second quarter, as shown on slide 11.

However, the provision remains relatively low despite raising 66 basis points to 1.1% of UMS in second quarter from 0.5% in first quarter, it represents a 76 basis point improvement year over year. We continue to expect that a pursuit of top line growth in 2023 will cause an increase in the provision for credit losses, but we still predict it will outperform last year's provision of 1.7% for the full year. On slide 12, you can see that second quarter '23 total income less transaction related costs, which include transaction expense, provision for credit losses and net interest expense rose almost 100% year over year to 18.8 million. Our unit economic margin measured against underlying merchant sales and total income of 4.9% and 53.7% respectively, position us well to expand our profitability going forward. As shown on slide 13, it is great to see that we are leveraging our non-transaction related operating expenses.

For the quarter, we saw them decline on an absolute basis by 23.7% year over year and decrease is the percentage of total income by over 30 points to 54.2%. Further, all core non-transaction related operating expenses including personnel, third party technology and data and marketing declined in the second quarter of 2023 compared to the prior year. In future periods, we anticipate non-transaction related operating expenses will rise modestly as the company develops and launches additional growth initiatives. On slide 14, second quarter gap net income of 1.1 million draws a strikingly positive comparison to the 15.1 million net loss in second quarter last year. This now represents the fourth consecutive quarter we have delivered positive gap net income.

As Charlie mentioned earlier, we are not aware of any other pure play buy now pay later company that has done so. On an adjusted EBITDA basis, we've reported 6.4 million in the second quarter of 2023 compared with a negative 9.4 million in the second quarter of 2022, yet another example that our initiatives are working. Our capitalization, as shown on slide 15, remains stable and healthy. Given our positive operational performance and healthy liquidity position, we are comfortable with our current capital structure. With that, we are now happy to take your questions. Operator, will you please open the lines for Q&A?

Operator: Thank you. If you wish to ask a question, please press star one on your phone and wait for your name to be announced. If you wish to cancel your request, please press star two. If you're on a speakerphone, please pick up the handset to ask your question. Your first question comes from Phil Chippendale with Ords. Please go ahead.

Phil Chippindale: Hi team. Thanks for your time. First question, just on the bad debts and probably a question for Karen, about three months ago you indicated that they would rise for the June quarter and they did. Now that you're north of that 1% mark, where should we expect it to go from here? Is this sort of about, broadly speaking, the right level for your business?

Karen Hartje: That's a great question, Phil, and while we're not providing any kind of guidance, what we are saying is last year our full year was 1.7% and we will be lower than that.

Phil Chippindale: Okay, great. Thanks. In terms of the bank partnership, this is something that you guys have sort of flagged as being on the horizon for a little time now, and maybe this is a question more for Charlie, but when do you think we'll be in a position to talk about that in some more detail?

Charlie Youakim: Definitely before the end of the year, Phil. It's an important project for us. One of the things we're looking for in terms of offerings with the customer is just providing more to them and the partnership allows us to do that. So it is an exciting one for us and one we're really pushing on right now.

Phil Chippindale: Last one from me, just on the active customer numbers and Charlie, you mentioned that number's down to 2.64 million now and you're probably not that far away from getting to a more stabilised position, but again, is that sort of a three-month outlook where you think it might sort of flat line and potentially grow from there?

Charlie Youakim: I think we'll see before the end of the year. I'm going to hand off to Paul Paradis to give a little more colour on that. Paul.

Paul Paradis: Yeah, can you hear me, Phil?

Phil Chippindale: Clear as a bell.

Paul Paradis: So I think the primary causes to that number declining have been number one, the offboarding of unprofitable merchants, if you think about our merchants, they are the primary channel through which we acquire customers. We also tightened underwriting a good deal, to get our bad debts down and then an increase in competition has been some factor. What we've seen though is that some of the new products that we've launched have been growing really fast, especially Premium, Anywhere, and we also are renewing focus on growth, after focusing on really getting to profitability for the past year, we're growing our sales and marketing teams. Now that we have the best unit economics and VNPL, that'll allow us to be more aggressive with merchant acquisition. And we're already seeing some of those shorter term active user metrics starting to increase again. So as Charlie mentioned, we expect that to flatten if not start to go back up by the end of the year, but it takes time. You have to acquire more merchants first and then that leads to more customers.

Phil Chippindale: Thanks Paul. Appreciate the extra colour. That's all for me.

Operator: Thank you. Your next question comes from Elise Kennedy with Jarden. Please go ahead.

Elise Kennedy: Oh, hi there. I've just got two quick questions. First, I just wanted to ask, you mentioned there were some initiatives just around growing consumers and merchants. Are you willing to share any insights as to is that new products, is there something else in the pipeline that we can think about?

Charlie Youakim: Well, the existing products, the ones we recently launched, premium was launched about 12 months ago, has been a great success. Anywhere, just recently launched, another great success. Up's been in the mix for quite some time, it's a great engagement tool with consumers, a great differentiator for us. Those continue to be great products in terms of keeping our consumers active. Keeping consumers active is, I would say, more than half the battle of creating a great company in financial services. The other half, I think Paul covered with the questions with Phil, basically as our unit economics are getting stronger and stronger and strongest in the industry, it allows us to be more aggressive with our merchant acquisition. And so I think in combination with the great product offerings that we have, the greater unit economics that we've got and this push towards getting back on the growth machine, I think all of those combined is our view as why we're going to be turning that around.

Elise Kennedy: Great. And I just wanted to ask about that record August that you've mentioned that you've had, can you know what's at play there, how much is a function of what Sezzle's doing as opposed to the economic backdrop or is it a combination of both?

Charlie Youakim: I would say it's 90% Sezzle, at least in many ways, I think even though we're a larger company than a startup, by a lot of means, we're a decent sized company, we're still not a company that's really driven primarily by the economy. It's really our initiatives and our actions that drive the results one way or the other. And so what we're already seeing is that growth is coming from our initiatives and Premium and Anywhere being a big part of it.

Elise Kennedy: Great. Thanks for your time.

Operator: Thank you. Once again, if you wish to ask a question, please press star one on your telephone and wait for your name to be announced. We'll now pause a moment to allow for any final questioners to register. Thank you. We are showing no further questions at this time. I'll now hand back to Mr. Youakim for closing remarks.

Charlie Youakim: Thank you. In closing, I'd like to send another shout out to the Sezzle team. They've really stepped up to make Sezzle a great success. We're continuing to work diligently on launching additional product offerings while we continue to grow and improve our existing offerings. So all around it's been a great year and a great six months here in 2023. And one thing to note, we're actually holding a board meeting this week and a team on site this week in Minneapolis. I'm looking forward to seeing everyone. It should be a great get together. And to the investors and analysts, thank you all for listening and for your interest in Sezzle. We will talk next when we report our Q3 results in November. But one note before we go, our 10Q will be filed with SEC next week on August 15th, in case some of the listeners were wondering. Have a great rest of your day and thank you.

Operator: That does conclude our conference for today. Thank you for participating. You may now disconnect.

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