

Sezzle Inc.

Fourth Quarter Financial Results Conference
Call

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CORPORATE PARTICIPANTS

Charlie Youakim - *Executive Chairman, Chief Executive Officer*

Paul Paradis - *Co-Founder, President,*

Karen Hartje - *Chief Financial Officer*

Lee Brading - *Head of Corporate Development, Investor Relations*

Presentation

Operator

Welcome to Sezzle Inc. Fourth Quarter Financial Results Conference Call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the "*" key followed by "0." After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press "*" then "1" on your touchtone phone. To withdraw your question, please press "*", "2." Please note, this event is being recorded.

I would now like to turn the conference over to Charlie Youakim. Please go ahead.

Charlie Youakim

Thank you. Good afternoon, everyone, and welcome to Sezzle's 2023 fourth 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 Corporate Development and IR, Lee Brading.

In conjunction with this conference call, we filed an earnings announcement and presentation with SEC and posted them to our investor website on sezzle.com. Additionally, if you sign up with our IR email distribution list, you can get these releases prior to our presentations at each quarterly release. So, please do so if you haven't already. Please go to either the sec.gov website or find our presentation on our website if you'd like to follow along.

Before we get started, I just want to touch on what I feel is an important landmark in our company history. This earnings call is our first since completing our NASDAQ listing and ASX delisting. It really does feel like the beginning of a new chapter for the company, one in which we'll focus on profitable growth, increasing margins and OPEX reduction, all while pleasing our key stakeholders. We operate this company with a sole proprietor mindset to produce returns for our shareholders. If that aligns with your investment philosophy, please stay on the line.

Now let's dive into the presentation starting with slide three. At Sezzle, we're helping a great number of people on their financial journey, and our historical numbers speak to this. Since our launch, we've had over 18 million consumers sign up, processed over 6 billion in volume, and initiated over 63 million transactions.

Additionally, our subscription service that was initially launched in June of 2022 at Sezzle Premium, and then expanded in June of 2023 with Sezzle Anywhere, has grown to over 300,000 members.

The use of our company can be compared to the use of our users, who are just getting started on a financial journey. Keeping with that comparison, Sezzle continues to grow up. We're now at a stage of the company's history where we're focused heavily on profitable growth. We're incredibly proud of that transition. And if you look back at our historical numbers, you can see why.

In 2021, we booked just under \$115 million in revenue and a net loss of over \$75 million. We've improved both numbers dramatically in two years. For 2023, we booked over \$159 million in revenue and a net income of over \$7 million. That's an \$82 million improvement in net income in two years.

Many companies point to the Rule of 40 as a successful benchmark, and we agree with them. If you use the looser definition of profit margin in the Rule of 40 as EBITDA margin, then we would have achieved the Rule of 40 in 2023 with an EBITDA margin of over 18% and a revenue growth rate in excess of 26%. But we plan to hold ourselves to a higher standard and plan to use net income margin as our standard instead of EBITDA margin. We're not quite there yet holding the higher standard in play with a net income margin of 4.5%. But it's that higher standard for the Rule of 40 that we will strive for in 2024 and beyond.

Last but not least, from a shareholder standpoint, we delivered a return on equity of 46% in 2023. I'm not aware of any other pure play Buy Now, Pay Later that can say the same. Our success did not happen overnight, nor was it easy, but it occurred through creativity, dedication, and hard work from each employee at Sezzle. It also could not have happened without a strong connection to the consumer, evidenced by having received 4.9 out of 5 stars on the Apple App Store and 4.6 out of 5 stars on Google Play. Those customer review metrics really speak to the stakeholder approach we have at the company. When we see negative reviews come through, we actively think about what we need to do to improve, which is why you continue to see strong review metrics from our user base.

Sezzle is also the only Buy Now, Pay Later company that is a certified B Corp, which shows how strongly we feel about the stakeholder approach to doing business and our mission of financially empowering the next generation. This approach also includes four areas of emphasis, as shown on slide four.

By giving consumers, the opportunity to spread payments out, avoid interest payments, and build credit, Sezzle fills an important need for our younger prime to be consumers. Since our inception, we have been committed to driving change to empower our consumers on their financial journeys.

As shown on slide five, there are a number of reasons consumers and merchants are turning to Buy Now, Pay Later, and to Sezzle in particular. Merchants are choosing us because they see our product drive incremental sales, and because we can introduce millions of consumers to their business. Meanwhile, consumers face a number of challenges to find credit and Buy Now, Pay Later assists those that often face challenges in accessing traditional credit options and serves as a tool for managing their cash flows.

Our long-term goal is to build an all-encompassing financial services platform with a focus on increasing the lifetime value of the customer, as shown on slide six. We started with direct integration with merchants back in 2017, and we have expanded our consumers' universe to anywhere Visa is accepted. We are incredibly excited about the future and the next set of financial products and services we launch for consumers with some launches coming out in 2024.

Consumers are voting for us with their feet as we have surpassed 300,000 members in our subscription-based products, Sezzle Premium and Sezzle Anywhere, as shown on slide seven. The amount of engagement has been phenomenal. Compared to nonsubscribers, our Anywhere customers shop more in-store and purchase more frequently. Our Anywhere members are shopping at a broad array of locations and are making everyday purchases at general merchandise retailers, grocery stores and restaurants to meet their discretionary needs. Again, going back to our mission, through these subscription services, we continue to financially empower the next generation on their journey through life.

To gauge the satisfaction of our users, we track net promoter scores closely through a random survey implemented by a third-party tool. In case you aren't familiar with net promoter scores or NPS, anything above 50 is fantastic. And if you're above 70, well, that's the Holy Grail. So, to have Sezzle Premium sitting at an NPS of 53 and Sezzle Anywhere at 71 means we're doing something right.

In the early stages of Sezzle's history, our marketing efforts were completely targeted towards the merchant. And while the majority of our spending still is targeted toward merchants, we are expanding our efforts with the consumer as shown on slide eight. If you haven't viewed our YouTube live sessions, you should check them out. We just launched the channel late last year, and we now have over 64,000 followers.

Our latest marketing campaigns have featured a new character, Cash, and his journey towards financial freedom. We are also testing a number of alternative consumer marketing tactics, such as direct mail, mall banners and streaming ads. Our marketing team is an extremely creative bunch. I am looking forward to seeing what they will come up with next.

Please keep in mind that investors don't have to worry about unnecessary spending with these campaigns though as all of these efforts are made with a very mindful eye on short payback periods and low CAC-to-LPV ratios.

Slide nine provides a snapshot of our past initiatives and the positive impact they have had on our results. All parts of the company have been involved in these efforts. Through new product initiatives and launches and by tying into affiliate systems, we've increased our revenue. And we also went through our operating expenses with a magnifying glass to remove numerous costs throughout the business.

We are excited about our plans for 2024, and we are scheduled to finalize our bank partnership and launch a number of new products. We're also focused on minimizing operational costs while we use this.

Our upcoming product marketplace is one of those product initiatives. The idea there is quite simple. Serve up relevant products to our consumers through the app and let them directly shop through us for products, with the idea that every purchase can be financed through Sezzle. We tested this concept in our app in the past holiday season and noticed incredible engagement from our users throughout the test. The result of that test led to the rapid decision to launch the product marketplace as a full-scale product.

Another upcoming product initiative is payment streaks. Payment streaks will allow our shoppers to gamify their experience in Sezzle through proper repayment. The more consistently a customer pays us back, the more levels they rise in the system. We'll be tying some nice benefits to those tiers over time as we learn more about the LTVs of each specific behavioral group. We believe that by gamifying repayment, we'll also have more ways to teach our typically younger customers about the additional benefits you get in life from good repayment behavior.

It seems these days everyone's bragging about their AI capabilities, so we wanted to make sure investors were aware that we are also embracing such capabilities and that we have been for years. We're big believers in embracing technology to improve productivity and results.

We are embracing AI through our own proprietary models, and in some areas, buying from third parties instead of building where it's more efficient to do so and less of a core function. For example, underwriting and fraud are core areas to Sezzle where we have built neural network models. The profit score is one of those examples.

Future proprietary models include models that optimize payment processing and models that optimize the products and merchants presented to our customers to personalize their shopping experiences. Meanwhile for an area such as customer support we have found it makes more sense to engage an outside third-party provider to help us utilize AI to the fullest.

Our engineering teams have also been given a green light to maximize their performance through the leveraging of generative AI tool sets, such as co-pilot. We want our teams to try to connect their capabilities, even if they can, through these tools.

Turning to slide 11, it's quite clear that our initiatives have made a positive difference. There's a lot of green on the screen. A couple of items to point out. We went from a negative EBITDA margin of 16% in fiscal 2022 to a positive EBITDA margin of 18.8% in 2023. We achieved this by improving our unit economics and reducing our operational construction.

In fiscal 2023, our gross margin improved to 50.8% of total income from 37.5%. And our non-transaction related OPEX, as a percentage of total income, declined to 46.9% from 75.5% the year prior.

Similarly, as you can see on slide 12, our annual engagement scorecard reflects a number of positive trends. We have been winning where it matters most. Increasing repeat usage, growing subscribers, increasing consumer order frequency, and diversifying our revenue streams. With our launch of Sezzle Anywhere in June 2023, shoppers are taking us everywhere. In fiscal 2023, shoppers use this at over 250,000 different merchants, as consumers are moving us toward the top of their wallets.

In the past, we showed an integrated merchant count. But we don't believe that tells the complete story, as many of the integrated merchants are micro merchants that don't drive our business.

The only red on the screen relates to the annual change in active consumers. I think the active consumer metric dropping over the last two years shows you just how seriously we took the path to profitability. As the company makes that transition, it has to decide which consumers are good and which are not. We've made the tough decisions in the past and we've improved our business dramatically in the process. Despite all that, I'm happy to note that we believe the drop in active consumers has bottomed out as it is slightly up when compared to Q3 of 2023.

With that, I'm happy to turn the call over to our CFO, Karen Hartje, who will go over our quarterly and annual financial results in greater detail. Karen.

Karen Hartje

Thank you, Charlie, and hello to all. On to slide 13, seasonally, the fourth quarter is our strongest UMS quarter due to the holiday period. But we also had a strong quarter on a year-over-year basis as UMS increased 33%. The increase in our UMS led to total income for the quarter increasing 28% year-over-year to 48.9 million. The annual results tell a similar story for total income growth as it increased 27% year-over-year driven by subscription and UMS growth.

On slide 14, 2023 transaction expense which is primarily payment processing costs, improved by 18 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, expand products such as Pay-in-Two and Pay-in-Full, and as noted earlier, introduce AI into the process.

As discussed on previous earnings conference calls, we expected our provision for credit losses, as shown on slide 15, to increase throughout the year, but still outperform for fiscal 2023 compared to 2022. Going forward, we will continue to evaluate the balance of growth versus losses with what makes the most sense.

Turning to slide 16, we can't emphasize this enough. Our unit economics measured by total income less transaction-related costs puts us in a strong financial position. Our total income less transaction-related costs are now around 50% of total income. A significant improvement compared to 37.5% in 2022. The key to our success has not only been the improvement in unit economics, but our ability to reduce non-transaction-related operating expenses. Without both, we would not have become profitable.

As shown on slide 17, non-transaction-related operating expenses declined by \$20 million in 2023 and fell to 46.9% of total income compared to 75.5% of total income in 2022. We believe we can continue to leverage our infrastructure as we remain vigilant on costs.

As noted, without these dynamics of improving unit economics and managing down operating expenses, we wouldn't have accomplished the profitability shown on slide 18. I must admit this is a fun slide to look at. We have net income every quarter with a significant annual change in net income from positive...negative to positive. Not to mention the significant flip in adjusted EBITDA. To say that we are excited about the future is an understatement.

Slide 19 displays select balance sheet metrics. Bottom line liquidity remains healthy, and we continue to add to Stockholders' Equity. Our capitalization is stable, healthy, and continues to show improvement each quarter. We are in discussions with lenders to refinance our current line of credit. We expect the result will be to improve availability and lower our borrowing costs. We are not at liberty to disclose more at this time.

Turning to slide 20, we are providing guidance for 2024. We will continue to innovate with an eye on bottom-line profitability as we expect to more than double net income in 2024 to \$20 million. We expect to get there through a combination of growth and expense management.

With that, I would like to turn the call back over to Charlie. Charlie.

Charlie Youakim

Thanks, Karen. With that, we're happy to take your questions. Operator, will you please open up the lines for Q&A?

QUESTION AND ANSWER

Operator

Thank you. We will now begin the question-and-answer session. If you have a question, please press "*", "1", to remove yourself from the question queue, please press "*", "2." If you are using a speakerphone, please pick-up your headset before pressing the keys.

Our first question comes from Nico Sacchetti with RBC. Please proceed.

Nico Sacchetti

Can you guys hear me?

Charlie Youakim

Yes. Hey Nico.

Nico Sacchetti

Hey, Charlie. How are you?

Charlie Youakim

Good. How are you?

Nico Sacchetti

I am good. Do you...sorry...I saw that I was prompted to send in some email questions here, but would you rather just take them over the phone here?

Charlie Youakim

Yes, that works.

Nico Sacchetti

You guys are knocking it out of the park, so I'm just curious if there's any way that you can kind of walk us through how you've been able to achieve profitability at such a small scale compared to some of your competitors that are out there?

Charlie Youakim

I really think it's a vigilant attack on both sides of the equation, Nico. I mean, we didn't sit on our laurels. We've innovated on the product side quite a bit over the last two years, which has helped us dramatically, and the subscription services are a big part of that. Sezzle Premium, Sezzle Anywhere. But there are a number of other initiatives we've taken throughout the last two years in the company to really push on the revenue side. But I'd say even bigger than the revenue side, or maybe equally as big, is how vigilant we've been on the cost side. I wouldn't say that Elon Musk is like my disciple. I am more of a Jeff Bezos fan. But you know, when you see what Elon Musk did with Twitter, cutting the staff by 75% and still running that company, I think it kind of speaks to how you can run a company pretty lean, and really accomplish a lot of things. We had to make some tough decisions over the past two years. We exited a lot of markets, Europe, India, Brazil, but really kept to our core in North America. And even though we're sticking to that core, we also were really cost-conscious about all our operating expenses. And between the two of those things, we've really pulled off what I think is an impressive feat over the last few years. And we're, I think, just getting warmed up at this point. We really understand how to run the business and how to run it really efficiently. We've got a whip-smart team that's really hard working and we're happy with where we are. And we just want to keep on marching forward now.

Nico Sacchetti

So, is there some cost coming down the pike here that would lead to just a reduction in the profitability or is it something that as you continue to grow, you'll continue to scale and as profitable as you are now, it should improve in an ideal situation?

Charlie Youakim

Yes. I think this business scales incredibly well. I still talk about our first holiday season when we were a little runt of a company, and we basically have the software run the systems without the team doing in the office during the holiday season. That just showed me firsthand how powerfully the product can scale. So, I think we plan to continue to show the operational scaling effects by growing top line while trying to keep our operational expenses down throughout this time period.

Nico Sacchetti

Do you...is it worth, I mean, it's such a stark difference from looking at some of the valuation metrics around what I would say "is your peer group." Do you think it's fair to say that there are competitors of yours to try to draw parallels to your business, the Affirms, the PayPals of the world. Do you view them as competitors? Are they competing for the same customers as you?

Charlie Youakim

I think some are closer than others. Affirm is closer than PayPal as a competitor, even though PayPal has a similar product set. Our closer competitors are probably Afterpay, Klarna, Zip, probably even more closely aligned to what we do. And yes, we've noticed what you are saying. But I'm a big believer in the Benjamin Graham, Warren Buffett approach that just over time, you know, in the short term the market is a voting machine. In the long term, it's a weighing machine. And we're going to put the pressure on the weighing machine.

Nico Sacchetti

Just had a couple of clarification questions. So, you put the stock buyback in place or you approved it. Did you buy back any stock in the quarter?

Charlie Youakim

We can't disclose that at this time. The first update you'll see for that will be in our May release after the first quarter.

Nico Sacchetti

Sure. Okay. The other one, you put out a term total income. Is that just a reference to your revenue, correct?

Charlie Youakim

Yes. That's just because of GAAP dynamics. That's revenue...traditional revenue top line.

Nico Sacchetti

So, when I'm looking at these numbers, 2023 revenue was \$159.4 million, and your guide for 2024 is 20% year-over-year growth of revenue growth. That's correct, right?

Charlie Youakim

Exactly.

Nico Sacchetti

Okay. And then net income for the trailing 12 months was \$7.1 million, and you're expecting...so you gave an exact guidance of \$20 million of net income for 2024?

Charlie Youakim

That's correct.

Nico Sacchetti

And so, if my math is right, you're looking at close to 3.60 a share in earnings based on those numbers in the share count?

Charlie Youakim

My maths is not as quick as yours, but I'm going to go through a calculator.

Nico Sacchetti

Okay. Alright. That's...I think that's...last one was, you talked about EBITDA percentage, EBITDA margin expansion being up around 18%, 19%. Do you have a target in place for where you think you can achieve? You mentioned such a stark turnaround there. Is there...is this kind of the run rate that you're expecting or is there a number above and beyond this high teens level?

Charlie Youakim

No, we want to keep on improving. I'll give you an example like we mentioned the Rule of 40. Internally, we've started to talk about an idea of like sort of related to the Rule of 40, but more it's 20%-60%-20%, 20% revenue growth, 60% gross margins and 20% profit margins...net income margins, which is the goals. That's not the guidance. Those are the goals. That's what we want to hit as a company. We think...I mean, my personal view is, if you have those sort of numbers as a company, you're doing a great job. I want to get the company to those sort of metrics.

Nico Sacchetti

Well, I appreciate the time and the questions. It was...I mean, it's a great story. Thanks, Charlie.

Charlie Youakim

Thanks, Nico.

Operator

Once again if you have a question, please press "*", "1." Please hold. This concludes our question-and-answer session. I would like to turn the conference back over to the management for closing remarks.

CONCLUSION**Charlie Youakim**

Thank you. In closing, a big thank you to the Sezzle squad, not only has the team pulled off this massive two-year improvement, but it's also stuck together through a difficult market with many smiles and laughs along the way. I don't think there's a smarter, harder working group out there right now. I really feel like we can take on just about anything with this team, kudos to the team. And thank you to the investors on the call and have a great day.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.