AudioEye, Inc.

First Quarter 2024 Earnings Conference Call

April 23, 2024

## CORPORATE PARTICIPANTS

**David Moradi**, *Chief Executive Officer*

**Kelly Georgevich**, *Chief Financial Officer*

## CONFERENCE CALL PARTICIPANTS

**George Sutton**, *Craig-Hallum*

**Zach Cummins**, *B. Riley*

**Scott Buck**, *H.C. Wainwright*

## PRESENTATION

**Operator**

Good afternoon, and welcome to AudioEye's First Quarter 2024 Earnings Conference Call. Joining us today are AudioEye's CEO, Mr. David Moradi, and CFO, Ms. Kelly Georgevich. Following their remarks, we will open the call for questions from the Company's publishing analysts. I would like to remind everyone that this call will be recorded and made available for replay via a link available in the Investor Relations section of the Company's website at www.audioeye.com.

Before I turn the call over to AudioEye's Chief Executive Officer, the Company would like to remind all participants that statements made by AudioEye management during the course of this conference call that are not historical facts are considered to be forward-looking statements. The Private Securities Litigation Reform Act of 1995 provides a Safe Harbor for such forward-looking statements. The words *believe, expect, anticipate, estimate, confident, will*, and other similar statements of expectation identify forward-looking statements. These statements are predictions, projections, or other statements about future events and are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could material differ because of factors discussed in today's press release and the comments made during this conference call and in the risk factors section of the Company's annual report on Form 10K, its quarterly reports on Form 10Q, and in its other reportings and filings with the Securities and Exchange Commission. Participants on this call are cautioned not to place undue reliance on these forward-looking statements, which reflect management's beliefs only as of the date hereof. AudioEye does not undertake any duty to update or correct any forward-looking statements.

Further, management's remarks today will include certain non-GAAP financial measures. A reconciliation of the most direct comparable GAAP financial measures to use these non-GAAP financial measures is available in the Company's earnings release or otherwise posted in the Investor Relations section of its website at www.audioeye.com.

Now, I'd like to turn the call over to AudioEye's Chief Executive Officer, Mr. David Moradi. Sir, please proceed.

**David Moradi**

Thank you Operator.

While it's been approximately six weeks since our last earnings call, several developments have occurred that we are excited to discuss today. As our last earnings call mentioned, the fourth quarter was a significant inflexion point. We generated record Adjusted EBITDA and positive free cash flow while generating solid ARR growth. We are pleased to report that this momentum is continuing and driving the increase in our full-year guidance, which I will cover later in the call. But first, I'll discuss the changing regulatory landscape, which we expect to impact the business significantly in 2025 and beyond.

On April 8, the Department of Justice signed a final rule under Title II of the Americans with Disabilities Act. These regulations mandate that state and local government entities ensure their websites and mobile applications are accessible to people with disabilities, following the Web Content Accessibility Guidelines 2.1AA. The documents published by the Justice Department estimate $17 billion in implementation cost over the first three years, and $2 billion annually after the initial phase.

The regulation requires the public schools, community colleges, universities, public hospitals and clinics, state and local police departments, courts, election offices, and state and local government offices that provide benefits or social services, like food assistance, health insurance, employment services, libraries, transit agencies, and a range of other government-related entities.

The new market opportunity under Title II is significant, with most public sites not being accessible today. We are uniquely positioned to meet the demand increase with our direct sales team and our reseller channel.

On the reseller side, we are already partnered with the leading SaaS platforms that serve cities, municipalities, and K through 12 education websites. We estimate that these partners serve over 80,000 websites, which must all become compliant over the next two to three years. We are currently penetrated only in the single digits today in these resellers.

A scalable approach like ours is required to meet this significant demand increase. AudioEye continues to improve its best in class technology platform, including investments in the latest artificial intelligence and scaled infrastructure to serve billions of end user sessions and millions of potential customers.

In addition to the Justice Department, we are excited about the opportunity in Europe. As discussed last quarter, the European Accessibility Act takes effect in June 2025 and requires digital accessibility for websites and mobile apps by that date.

We are also seeing regulatory developments in additional jurisdictions, including California's AB1757 proposal. If passed in its current form, it would expand and solidify the requirement that businesses operating in California must have accessible websites and mobile devices.

As noted, we are not including any benefit from these upcoming requirements in our guidance for this year; but we expect meaningful demand increases in 2025 and beyond.

Since joining the Company in 2019, the customer count has increased from 3,500 to 112,000 and revenues have more than tripled. We are prepared to support this significant demand increase from the public sector.

With the final rule just announced two weeks ago, we are still early in the planning phase, and we will share more about our outlook beyond 2024 as the year progresses.

In the first quarter, we achieved system and organizational controls or SOC2 Type 1 compliance. This important milestone underscores our commitment to upholding the highest security and data privacy standards. Achieving SOC2 Type 1 compliance was a priority for us, as we continue to expand our enterprise channel and service large enterprise organizations.

SOC2 Type 1 attainment and products rolled out this past year will further support the enterprise channel's growth initiative.

The Board and management remain highly aligned with shareholders. Over the last two and a half years, the number of shares outstanding has remained at similar levels, while we have continued to invest in growth.

In the current stock buyback, as of April 23, we have repurchased 548,000 shares at an average price of $5.73. In addition, under our previous buyback announced in June 2022, we bought 139,000 shares at an average of $5.44.

Combining both programs, we have purchased approximately 6% of common shares outstanding over the last two years, at a valuation of around two times revenue, for the benefit of long-term shareholders.

Moving on to guidance. We expect quarterly revenues to accelerate throughout the year, without significant additional expense, resulting in increased operating leverage and free cash flow generation.

For the second quarter, we are guiding revenue between $8.4 million and $8.5 million, representing an annualized growth rate of high teens. We also expect to generate Adjusted EBITDA between $1.4 million and $1.5 million, and adjusted EPS between $0.12 and $0.13.

We are increasing 2024 revenue guidance to between $34.3 million and $34.7 million. We are also increasing our Adjusted EBITDA guidance by approximately $1 million, to between $4.5 million and $5.5 million, with adjusted EPS between $0.38 and $0.46 per share.

I'll now turn the call over to AudioEye's CFO, Kelly.

**Kelly Georgevich**

Thank you David.

As David discussed, revenue again hit record levels, with Q1 2024 revenue at $8.1 million, marking our 33rd quarter of record revenue.

Annual recurring revenue or ARR at the end of the first quarter of 2024 was $32 million, an $800,000 increase from the end of the fourth quarter of 2023, and representing an ARR annualized growth rate of 10%. We expect this growth to accelerate notably as 2024 progresses.

Our two revenue channels are continuing to deliver strong results. The partner marketplace channel includes all revenue from our SMB-focused marketplace product, and revenue from a variety of partners to deploy these same products for their SMB customers. In the first quarter of 2024, this revenue channel grew 9% year over year, representing 59% of revenue and around 60% of ARR.

We continue to see expansion of existing partners and new partners contracting with AudioEye, which continues to drive growth.

AudioEye's enterprise channel consists of our larger customers and organizations, including those with non-platform websites, who generally engage directly with AudioEye sales personnel for pricing and solutions. The enterprise channel grew 4% sequentially, and we expect to resume year-over-year growth in Q2 2024. In the first quarter, the enterprise channel contributed 41% of revenue and around 40% of ARR.

On March 31, 2024, our customer count was approximately 112,000, an increase from 95,000 customers on March 31, 2023, and an increase of approximately 2,000 customers from December 31, 2023. The increase in customer count was driven by additions in the partner and marketplace channels.

Gross profit for the first quarter was $6.3 million or 78% of revenue, compared to $6.1 million and 78% of revenue in Q1 of last year. We believe the gross margin has room to expand in future quarters.

While revenues increased approximately $300,000 from the first quarter of 2023, operating expenses decreased approximately 14% or $1.2 million to $7 million. The decrease was primarily due to increased efficiencies in sales and marketing, the completion of significant initiatives in R&D, and lower G&A expenses. Our total R&D spend in Q1 2024 was approximately $1.8 million, with approximately $490,000 reflected as software development costs in the investing section of the cash flow statement. This was down from approximately $2.2 million in Q1 2023. The total R&D spent is about 22% of our revenue this quarter, versus 29% in the comparable period of prior year, and consistent with Q4 2023 investment. We continue to believe the current investment in R&D is appropriate for 2024.

Net loss in the first quarter of 2024 was $800,000 or $0.07 per share, compared to $2 million or $0.17 per share in the same year-ago period. Total net loss decreased by 59% or $1.2 million from the prior year's comparable period, driven by an increase in revenue, strategic and efficient spending in all departments, and technological investment.

Our Q1 Adjusted EBITDA was $920,000 or $0.08 per share, a $1 million improvement year over year. The primary adjustments to GAAP earnings and EPS for Q1 2024 were non-cash share-based compensation, depreciation, amortization, interest expense, and other non-reoccurring items.

Our balance sheet is well capitalized, with $7 million of cash as of March 31, 2024. Cash decreased by approximately $2.2 million in the quarter. primarily due to $1.7 million share repurchased. The remaining decrease was primarily due to the timing of customer payment.

Free cash flow, calculated as $920,000 of Adjusted EBITDA less $490,000 in software development costs, was $430,000 in the first quarter. We expect to generate positive free cash flow throughout 2024, with improvements as the year progresses.

With that, we open up the call for questions. Operator, please give instructions.

**Operator**

Thank you. We will now take questions from the Company's publishing analysts

(Operator instructions)

The first question comes from George Sutton with Craig-Hallum. Please go ahead.

**George Sutton**

Thank you. Very nice results, congratulations.

So, we're obviously early relative to both the European and also the DoJ opportunities, in terms of those going into play. Can you talk about what sorts of things you're doing to prep for that? You mentioned resellers specifically, but it's interesting, you're increasing your EBITDA guidance in spite of the fact we would expect you might invest a little bit more aggressively into that. So, any thoughts?

**David Moradi**

Yes. We're just clicking on all cylinders here with the enterprise and the reseller channel, so it's business as is. I think R&D investment's been a major factor. We have a full product suite to meet the customer wherever they are, a small business or a large enterprise, so the process offering is a major competitive advantage, we're outgrowing the market I think.

So yes, we're clicking along here, business as usual, and I think you're going to see a significant uptick in demand as you go on to 2025, with the multitude of regulations coming.

**George Sutton**

You mentioned being positioned with some of the key resellers that will ultimately be taking you to market, particularly I think in the U.S. with the DoJ impact. Can you walk through some of the reseller relationships that are key, and how are those typically structured? Are you, in many cases, the key player they are going to market with, or are they going with multiple partners? Any help there would be great.

**David Moradi**

Sure. Those are exclusive relationships. I mentioned our current partners on the government side serve around 80,000 websites, and our penetration rate is in only the single digits, so we think there's a massive opportunity to grow here. We don't see any reason why this is not going to be close to full penetration over the next two to three years. You can get to full penetration with our current reseller partners on the government side, that's going to dramatically change the current business.

**George Sutton**

Lastly for me, Kelly mentioned additions in the partner and marketplace channel being behind the strength you saw this quarter. Can you just give any specificity as to specific partners that drove that, new partners or new relationships with those partners?

**Kelly Georgevich**

I can take that…

**David Moradi**

Yes, go ahead Kelly.

**Kelly Georgevich**

I was going to say, we're seeing growth in both expansion with existing resellers, which we continue to see every quarter and we think there's additional opportunity there as David mentioned, but we also are contracting with new resellers, so that growth is coming from both of those buckets, which we're happy to see.

**George Sutton**

Beautiful. Okay. Thanks guys.

**David Moradi**

Thank you.

**Operator**

(Operator instructions)

Our next question comes from Zach Cummins with B. Riley Securities. Please go ahead.

**Zach Cummins**

Hi, good afternoon, David and Kelly, thanks for taking my questions and congrats on the solid results.

I really just wanted to hone in on the margin leverage that you're seeing in the model here. I mean, can you just talk about maybe what's really the key underlying factor that's driving kind of the upside in terms of the Adjusted EBITDA margin that we have, especially exiting this year?

**Kelly Georgevich**

We've been able to prove we can be efficient with capital and scale revenue without increasing expenses, essentially decreasing expenses. As David mentioned, we expect Q2 to have Adjusted EBITDA margins of the high teens, and if you look at guidance we expect that to continue in Q3 and Q4, it's really, we've been able to figure out the formula and generate that extra revenue without needing additional expenses.

**Zach Cummins**

Understood. David, in terms of incremental investments into the direct channel, I know you have relationships in place with major partners, especially on the public sector side, but any additional investments that you need to make with your direct channel to really take full advantage of the growing demand opportunity?

**David Moradi**

Not right now. We're still formulating the plans, we think we're pretty well balanced between growth and profitability, and it's been a tremendous effort to get to this point, to get to high teens EBITDA margin. So, we're happy with that.

**Zach Cummins**

Understood. Final question for me is just around capital allocation. I mean. with the business continuing to generate positive free cash flow, how are you thinking about just investments in the organic business versus maybe even potentially looking at incremental M&A?

**David Moradi**

We don't really comment on incremental M&A. I'm sure you can understand that. There have been a number of financings and M&A in the space. The latest acquisition of Userway was at 8 times ARR.

We're going to look at LCV to cash, and increase that potentially more on sales and marketing and R&D, if we see that go favorably. But, we think these operating margins are sustainable going forward, and we like them.

**Zach Cummins**

Understood, well, thanks for taking my questions and best of luck in the coming quarter.

**David Moradi**

Thank you.

**Operator**

Our next question comes from Scott Buck with H.C. Wainwright. Please go ahead.

**Scott Buck**

Hey, good afternoon, guys, thanks for taking my questions.

David, you guys have obviously been fairly aggressive in repurchasing shares here so far this year. Curious what your thoughts are on the stock today, given the move in shares, versus the opportunity you see here over the next 12 to 24 months.

**David Moradi**

Yes. It still seems pretty cheap to me. I think last I checked it was around four times revenue, and we’re approaching rule of 40 now. I think we can exceed rule of 40 as we go into next year, so those companies tend to trade over 10 times revenue.

**Scott Buck**

Yes. Makes sense.

Then second one for me, it sounds like from the commentary that not only are we looking at accelerating revenue in ’24 and likely ’25, it looks like you’re actually set up pretty well already for ’26. So, this momentum has legs, right?

**David Moradi**

I think this is going to go on for a few years, with high growth rates and high EBITDA margins.

**Scott Buck**

All right, perfect. That’s good to hear. I appreciate it, guys. That’s it for me.

**David Moradi**

Thank you.

**Operator**

At this time, this concludes our question-and-answer session. I’d now like to turn the call back over to Mr. Moradi for his closing remarks.

**David Moradi**

Thank you for joining us today. As always, I want to thank our employees, partners, and investors for their continued support. We look forward to updating you on our next call.

**Operator**

Before we conclude today's call, I would like to remind everyone that a recording of today's call will be available for replay via a link available in the investors section of the Company's website. Thank you for joining us today for AudioEye's First Quarter 2024 Earnings Conference Call. You may now disconnect.