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# Neopost SA (NEO.FR )

Q3 2018 Sales and Revenue Call

By FactSet CallStreet, amended by Neopost

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Geoffrey Godet

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## OTHER PARTICIPANTS

Martin Boeris

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Nicolas Tabor

*Analyst, MainFirst AG (France)*

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Hello and welcome to the Q3 2018 Sales Call. My name is Courtney and I'll be your coordinator for today's event. For the duration of the call, you will be on listen-only. However, you will have the opportunity to ask questions. [Operator Instructions]

I will now hand you over to your host, Jean-François Labadie to begin today's conference.

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Jean-François Labadie

*Chief Financial & Legal Officer, Neopost SA*

So, thank you. Good evening and welcome to our 2018 Q3 sales conference call. I'm Jean-François Labadie, Neopost's CFO. I'm together with Geoffrey Godet, Neopost's CEO; and Gaële Le Men, Neopost's Investor Relations Officer. Let me first comment on our financial figures and then we will give you the floor for Q&A session.

If you have registered through our webcast modules, you should have access to our slide presentation. Otherwise, the slides are also available from the Finance section of our website.

So, let's move directly to slide number 3. As you know, we are currently involved in a big strategic review. Our new strategic plan will be presented on the 23rd of January. During this transition year, however, we remain fully focused on operating our current business portfolio in the most effective way. And as you can see on this chart, we achieved another relatively good performance this quarter. Our total sales were up 0.8% to €265 million. We had no scope effect this quarter.

As opposed to the first two quarters, we benefited from a positive currency effect of 0.6% and more importantly, we recorded a small organic growth of plus 0.2%. In a nutshell, this is thanks to the double-digit organic growth achieved by our Communications & Shipping businesses unit as a whole.

In the meantime, Mail Solutions declined organically by minus 4%, that is to say, at the high end of the historical range that we had experienced over the past few years. We are obviously quite pleased with this achievement, but this is not changing our trajectory for the full year. Indeed, we are confirming all the indications that we gave earlier.

If you can now switch to slide 4. Slide number 4 provides a good overview of the breakdown of the organic growth per business unit. SME Solutions came at minus 1.7%. I remind you that SME Solutions includes Mail Solutions, Graphics, as well as Digital Communications and Shipping Solutions dedicated to our SME client base.

Enterprise Digital Solutions is back to double-digit growth increasing by 12%. And Neopost Shipping increased by 12.6%. The combination of double-digit growth both in Enterprise Digital Solutions and in Shipping has more than offset the decline in SME Solutions. This is how we achieved another positive organic sales growth in Q3 at plus 0.2%.

I now hand over to Geoffrey for a more detailed review of our Q3 sales performance per business unit. You can turn to slide number 5.

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## Geoffrey Godet

*Chief Executive Officer, Neopost SA*

Thank you, Jean-François. Good afternoon, everyone. Happy to be with you. So, let's start the business review with Enterprise Digital Solutions division on slide number 5.

As you know, Enterprise Digital Solutions represent around 13% of the group total sales. As you could see on this chart, the third quarter confirmed that we had been back on track since the beginning of the year. Indeed, we have seen some continuous progress after the poor performance achieved last year for the second semester in particular, in Q3 and Q4. And therefore, our organic growth in the third quarter has reached 12%.

Let's now move to slide number 6. The bulk of the Enterprise Digital Solutions division is Customer Communications Management software, what we call CCM. As you know, we have engaged at the beginning of the year a process that consists in refining our commercial approach. We started to introduce a more phased approach to license sales to avoid laying the difficulty of selling large software deals up-front.

We also made management changes, several of them, with the new Head of North America appointed at the beginning of the year, and more recently, a new Head of our Northern Europe region appointed a few months ago. We continue to adapt our sales force to address new vertical industries like healthcare, on top of financial services and insurance verticals, and this process is still ongoing.

So, CCM recorded a 15% organic growth in the third quarter. We are not overoptimistic about our performance, because we benefited from an easy base of comparison in the third quarter. Nevertheless, our efforts has started to pay off. We didn't sell any large deal in in Q3 and since the beginning of the year, but we signed several mid-sized deals. Among them, for instance, we signed a couple of healthcare clients in the U.S. recently in the third quarter. These deals contributed to achieve growth in new license sales this quarter of the first time this year. On top of this, as our customer base has continued to increase, we enjoyed a sound growth in recurring revenues, that is to say, in revenues related to maintenance and services.

So, to conclude the review of Enterprise Digital Solutions division, a short comment on data quality. Data quality represented a smaller part of this business unit, as you know, and it continued to decline, although, at a lower pace with the organic growth of minus 1%.

So, in conclusion, overall, Enterprise Digital Solutions increased organically by 9% in the first nine months of the year and we continue to expect organic growth to reach, as mentioned before, a high-single digit for the full-year 2018.

We can now move to slide number 7. So, let's talk about our Shipping division. Shipping – Neopost Shipping division represents around 6% of our total sales. And as you could see on the chart, our historical performance has proved rather volatile from one quarter to another. This is a direct reflection of the mix between the various business that make our Shipping division. And these businesses include, as you know, some pure hardware sales businesses like the automated packing system, our CVP-500, the parcel lockers business which generates a high level of recurring revenue, and a wide variety of software businesses.

Let's now move to slide number 8. So, as expected, the third quarter, our Q3 organic growth was lower than the first two quarters and reached 13%, almost. This is however reflecting different trends. Packcity revenues were up 120% organically versus the last quarter last year – sorry, the third quarter last year. This is mainly due to the recurring revenue generated by install base of parcel lockers in Japan.

As anticipated, the revenue of lockers being installed has gone down to around roughly 80 new lockers per month this quarter, but we had the full impact of the sharp increase of our installed base over the last 15 months. Thanks to our partnership with Yamato, this installed base in Japan has gone up from 600 lockers at the end of July 2017, as a reminder, to 3,400 lockers at the end of October 2018. We also benefited from the delivery of a few parcel lockers to Australia Post in Australia, as well as a few more lockers delivered in France and in the U.S. this quarter.

Regarding the CVP-500, our fit-to-size packing system. We sold two new machines in the third quarter, which is the same number as in the third quarter last year. Having said that, the revenues were however slightly down compared to the third quarter last year.

In parallel with our revenues from shipping software went further down in the third quarter, almost an 8% organic decrease this quarter. As a reminder, shipping software is a mix bag of various products, such as ProShip in the U.S., track-and-trace softwares, RFID Solutions, Temando, et cetera. Some of these legacy software are being gradually phased out as we explained before and this explains the decline in revenue in this segment.

Overall, we continue to expect shipping to grow organically double-digit for the full year 2018; though, at a really much lower pace than in the first nine months of the year. The organic growth in the first nine months stands at 18.5% currently.

Let's move to SME Solutions on slide number 9. SME Solutions was around 81% of the total group sales. As you can see on this chart, we expand our effort to grow this business outside the Mail Solutions. The overall performance of this business unit remains strongly correlated with that of Mail Solutions. The historical trend in the organic structural decline in Mail Solutions stands in the range of minus 4% to minus 6% on a yearly basis. It does however fluctuate from one quarter to another.

So, after the surprisingly good second quarter, at minus 2.8%, we did minus 4% in Q3; and that is to say, in the high-end of the historical range. Within our SME non-mail related business, consistent growth in Digital Communications, Software and Shipping Solutions has been mitigated for some time now by the decline in graphic activities.

I'll now turn to slide number 10. So, Mail Solutions continued to represent the bulk of our SME division. As I said, after the surprisingly good second quarter at minus 2.8%, Mail Solutions decreased organically by 4% in the third quarter. North America continues to be more resilient and achieved a much lower decline compared to Europe. In Europe, the Mail Solutions continued to decrease in a similar pace than in previous quarters, with some difference from one country to another.

Over the first nine months of the year, the organic decline in Mail Solutions stand at close to 4%. We remain however very cautious for the end of the year. We should end up the year within the historical range of minus 4% to minus 6%.

Now, in Graphics. I'll remind you that we lost a large contract in Australia in the third quarter last year. This has accelerated the decline of this business over the last four quarters. In the third quarter this year, the decline was much lower at minus 3%.

Moving to Digital Communications and Shipping Solutions, dedicated to our SME client base, continued to do well. It achieved another strong performance in Q3 with a 21% organic growth compared to the third quarter last year. This good performance is due in particular to the continued success of our Customer Communications Management software as well as our De-materialize Electronic Mail Solutions.

In the first nine months of the year, SME Solutions recorded a 2% organic decline. Over the full year, the growth in Digital Communications and Shipping Solutions will not offset the decline in Mail Solutions and in Graphics for this division. We obviously continue to expect an organic decrease in SME Solutions as a whole.

So, this ends our business review per division. I now hand the floor back to Jean-François and we can move to slide 11.

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## Jean-François Labadie

*Chief Financial & Legal Officer, Neopost SA*

Thank you, Geoffrey. Just a few more comments on my side. Slide 11 gives you a quick overview of our performance third quarter this year; minus 2.1% in Q1, plus 1.2% in Q2 and plus 0.2% in Q3. This added to a virtually flat organic growth over the first nine months at minus 0.2% as you can see on the next slide. We are now on slide number 12.

First nine months sales are down 3.5% to €792 million. This is essentially due to currency effect even if the currency impact turned positive in Q3. We can now switch to slide number 13.

We are seeing here the nine months sales breakdown. First, per activity, Communications & Shipping Solutions all together grew organically by 9.5% and now represent 30% of total sales. Second, by revenue type, you can see that recurring revenue has grown further and now represents 71% of total sales. Last, by geography, North America is organically up by 1.6% and now represents almost as much as Europe.

Let me finish with the slide number 14. To remind you, our confirmed indications for the full year. We are still expecting a slight organic decrease for the full year. Revenue indications per division are as follows. We still expect Enterprise Digital Solutions to grow at high-single digit. Neopost Shipping will grow at double-digit, but well below our nine months 2018 performance. The growth in parcel locker business will continue in Q4, but at a lower pace. I also remind you that we have placed four automated packing systems in Q4 2017 and we might not be able to place as many in Q4 2018.

And finally, we will continue to experience a further decline in shipping software. As for SME Solutions revenue. We maintain our view that Mail Solutions should continue to follow the historical trend within the range of minus 4% to minus 6%. Digital Communications and Shipping Solutions dedicated to SME will continue to grow at double-digit. And lastly, we expect further decline coming from our graphic business.

Finally, we also confirm that the group EBIT margin for the full year should be above 17%. The Enterprise Digital Solutions will generate a higher margin in H2 than in H1. Thanks to a good control over our operating expenses, the SME division should produce a similar level of EBIT margin in H2 as in H1. The Shipping division's EBIT margin should remain at the same negative level in H2 as in H1. In addition, I'll remind you that we expect an increase in innovation expenses in H2 compared to H1. In the meantime, we confirm that we are expecting a high generation of operating cash flow.

This ends the review of our Q3 performance. Before moving to the Q&A, Geoffrey, you wanted to make a couple of additional comments?

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## Geoffrey Godet

*Chief Executive Officer, Neopost SA*

Yes. Thank you, Jean-François. I just wanted to remind everyone that we recently made a few changes regarding Neopost governance. At the board level, the board has decided to merge the Appointments Committee and the Remuneration Committee on the one hand, and to create a Strategy and Corporate Responsibility Committee on the other hand.

At the leadership team level, we also made a few changes. We created a new position of Chief Strategic Initiatives Officer, a position which is filled by Brandon Batt. Henri Dura, the former Head of Enterprise Digital Solutions has moved to another newly created function of Chief Strategic Marketing, Product, Technology, and Supply Chain Officer. Dennis LeStrange, the Head of our SME Solutions division is due to leave in January. This was a long-planned departure. Consequently, I have decided to take direct responsibility for both the Enterprise Digital Solutions and the SME Solutions divisions.

These views reflect our commitment to conduct an ongoing assessment of our strategy on the one hand, as well as to have a more integrated approach across the group. I will obviously tell you more about our future organization during our Capital Market Day in January.

Thank you for your time. And we are now ready to answer any of your question, Jean-François and I.

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## QUESTION AND ANSWER SECTION

**Operator:** [Operator Instructions] Okay. We do have a question coming through from the line of Martin Boeris calling from Exane. Please go ahead.

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Martin Boeris

*Analyst, Exane SA*

Yes. Good evening. I have two questions, one on Quadient and one on the CVP-500. So, first on Quadient. Would you say your good performance this quarter is mainly owing to a favorable base effect or are you seeing more structural business improvement here? And second, you reported two new CVP-500 sales. Could you tell us if they are repeat orders and what's the profile of clients? Thank you.

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Geoffrey Godet

*Chief Executive Officer, Neopost SA*

So two questions actually on Quadient. I will confirm that yes, we did had a lower comparison, an easier one. As you know, our Q3 last year was flat, and we did take that into account. That being said, and that I also shared with you along the way this year, we are making constant change to our businesses in terms of the sales approach in particular. And I explained that we should expect some continuous improvement, which means that there will be no big deals, and that we could see the progress that we are making quarter after quarter and it will take several quarters to pay off.

And in Q3, we have continued to see some improvements compared to Q2 and compared to Q1 in our sales performance. So, on the CVP-500, we sold two in the UK to the same customer. It's a new customer. It's not a repeat order, but it's a customer who are dealing with logistic activity for the retail.

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Martin Boeris

*Analyst, Exane SA*

Okay. Very clear. Thank you.

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Geoffrey Godet

*Chief Executive Officer, Neopost SA*

Welcome.

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**Operator:** We currently have no further questions coming through. [Operator Instructions] We have another question coming through from the line of Nicholas Tabor, calling from MainFirst Bank. Please go ahead.

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Q

Nicolas Tabor

*Analyst, MainFirst AG (France)*

Good afternoon. Thank you for holding this call, answering our questions. I have a few questions. So first, on Graphic Solutions, do you think we're still at risk of further strong decline or should it stabilize through this kind of organic decline level?

Then, if we look at Packcity, so Q3 was more or less in line with Q2. You said we have more revenue from rents. Should we expect Q4 to be in line as well or should it be down compared to Q2 and Q3 in terms of organic growth?

And then, sorry, I didn't quite hear you. Could you say again what's the new pace of installation in Q3 for Packcity? And can you repeat again the latest change in management at the Head of EDS? Thank you very much.

A

Geoffrey Godet

*Chief Executive Officer, Neopost SA*

Okay. So, for the Graphics, the main difference from the last few quarters is actually the comparison basis, since we lost a large contract in Australia in Q3 2017. So, this is why, we see a difference in the pace of the decline. That being said, the Graphics have been a declining activity to us for quite some time. So, we continue to expect some decline, but yes, at a much lower pace. So, that was for the Graphics.

On Quadiant, just bringing different order. The latest change in Quadiant is the Head of Quadiant. Henri Dura is now taking a group function to oversee strategic marketing, products, supply chain and R&D across the group, and this will cover Quadiant, as well as the SME division and the Shipping division.

Below that, we have made some changes in the sales organization constantly during the year, some of the one that we shared together was the Head of North America and that was now – I believe we shared that in Q2. And now, more recently, in Q3, we've made also a change in the Head of Sales for the Northern Region in Europe. So, those are the three changes that I referenced during this call.

For Packcity, yes, I do confirm that we did throw install an average in Q3 80 lockers in Japan per month. And then, as it relates to the growth rate that we anticipate in Q4, yes, we do anticipate that it will continue to be lower growth in Q4 compared to Q3 and the rest of the year.

Q

Nicolas Tabor

*Analyst, MainFirst AG (France)*

And could you also confirm one thing to me? So, you said that we'll get an update on January in terms of your position at EDS and SME. But will you consider this, your position, I mean, CEO position for these two segments to be able to stay merged that with only one person responsible for the two? Or then would you still see it as two different seats in the organization?



Geoffrey Godet

*Chief Executive Officer, Neopost SA*

This is an answer that we'd be very happy to be able to respond to you on January 23, because obviously, the organization should be in line with the new announcement that we have on the strategy.

A

Nicolas Tabor

*Analyst, MainFirst AG (France)*

Okay. Thank you very much. That's all I have for now.

Q

Geoffrey Godet

*Chief Executive Officer, Neopost SA*

Thank you, Nicolas. Sorry, I'm not able to give you more details on this one.

A

**Operator:** We currently have no questions coming through. [Operator Instructions] Okay. We have no questions coming through on the line. So, I shall hand you back over to your host.

A

Yeah. So, on my side, on the webcast, I have two questions. The first one relates to the CVP-500. So two machines were sold in Q3 is the same number as in Q3 last year. But still there is a decline of 7% in the revenue, so, why is that? Is it due to pricing pressure?

Geoffrey Godet

*Chief Executive Officer, Neopost SA*

So, we're keeping the same amount of machines from quarter to another. As you could imagine, we do have some price differences from one region to another, but we're talking about a very small amount in absolute value. So, we don't consider that to be meaningful, we could have done one way or the other. It's the same number of machines from one quarter to the other. The percentage of decline is not relevant.

A

Yeah, I have a second question, it's relating to the Mail Solution business. So, the question is, how the installed base of machines developed in 2018 versus last year, is it an increase or a decrease in the installed base of franking machines?

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**Geoffrey Godet**

*Chief Executive Officer, Neopost SA*

So, I do not believe we share numbers and the numbers of installed based from one quarter to another one. This is on the other hand, it is of close interest for me. So, I'll be happy to be able to give more input on our customer base at the capital market day. But this being said, I will just point out in the quarter that our recurring revenue has been increasing for the mail business this quarter. Well, I hope I had answered your question as well.

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Yeah. Courtney, do you have more questions on your side?

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**Operator:** We still have no questions coming through.

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**Geoffrey Godet**

*Chief Executive Officer, Neopost SA*

Okay. So, it think that should conclude our quarterly sales call. Thank you everybody for attending and I hope we addressed your questions. Thank you.

**Unverified Participant**

And we'll meet on the 23rd of January in Paris, I hope. So, you will receive the details of the invitation in due time. Thank you for being with us tonight. Bye-bye.

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**Jean-François Labadie**

*Chief Financial & Legal Officer, Neopost SA*

Thank you. Bye-bye.

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**Geoffrey Godet**

*Chief Executive Officer, Neopost SA*

Thank you. Bye-bye.

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**Operator:** Thank you for joining today's call. You may now disconnect you handsets.

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