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CORPORATE PARTICIPANTS

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Ryan L. Pape *XPEL Technologies Corp. - CEO, President & Director*

CONFERENCE CALL PARTICIPANTS

John Nesbett *Institutional Marketing Services, Inc. - Founder and President*

PRESENTATION

Operator

Greetings, and welcome to the XPEL, Inc. Year-End 2018 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, John Nesbett of IMS Investor Relations. Thank you. Mr. Nesbett, you may begin.

John Nesbett - *Institutional Marketing Services, Inc. - Founder and President*

Good morning, and welcome to our conference call to discuss XPEL's financial results for 2018. On the call today, Ryan Pape, XPEL's President and Chief Executive Officer; and Barry Wood, XPEL's Chief Financial Officer, will provide an overview of the business operations and review the company's financial results. Immediately after the prepared comments, we will take questions from our call participants.

I'd like to take a moment to read the safe harbor statement. During the course of this call, we'll make certain forward-looking statements regarding XPEL, Inc. and its business, which may include but not be limited to anticipated use of proceeds from capital transactions, expansion into new markets and execution of the company's growth strategy. Often but not always, forward-looking statements can be identified by the use of words such as plans, is expected, expects, scheduled, intends, contemplates, anticipates, believes, proposes or variations, including negative variations of such words and phrases, or state that certain actions, events or results may, could, would, might or will be taken, occur or be achieved. Such statements are based on the current expectations of the management of XPEL.

The forward-looking events and circumstances discussed in this call may not occur by certain specified dates or at all and could differ materially as a result of known and unknown risk factors and uncertainties affecting the company performance and acceptance of the company's products, economic factors, competition, the equity markets generally and other factors beyond the control of XPEL. Although XPEL has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that could cause actions, events or results to differ from those anticipated, estimated or intended. No forward-looking statement can be guaranteed.

Except as required by applicable securities laws, forward-looking statements speak only as of the date on which they were made, and XPEL undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

Okay. With that, I will now turn the call over to Ryan. Go ahead, Ryan.

Ryan L. Pape - *XPEL Technologies Corp. - CEO, President & Director*

Thanks, John, and good morning, everyone. Welcome to our year-end 2018 conference call as well. Today is a milestone day in the history of our company. As most of you know by now, we took the first step towards a U.S. listing with today's filing of the Form 10 with the SEC. Barry will walk you through more of the details on that and the related time lines later, but today's filing of the Form 10 effectively means that we've requested



to register our securities in the U.S. pursuant to the '34 Act. We also applied for a listing on Nasdaq Capital Market under the symbol XPEL. It's been a long time coming for the company, and I'm excited that we're finally here.

To become an SEC issuer, we're required to issue our financial statements in accordance with accounting principles generally accepted in the U.S. or U.S. GAAP. Prior to today's filing, financial statements previously issued by the company were stated in accordance with International Financial Reporting Standards, or IFRS. In layman's terms, we had to switch accounting standards in order to register our securities in the U.S. And that's obviously a lot of work, and congrats to our finance team for getting that done. So therefore, any numbers we talk to today relating to our results are now U.S. GAAP-based numbers.

With that, let's talk about what was clearly an outstanding year for XPEL. Our revenues for Q4 grew 33.1% to \$26.8 million, reflecting continued strong growth for the company. As we alluded to on previous calls, we expected our revenue growth to moderate as we went through last year and then in Q4. Given that, I was pleased with our Q4 performance. Revenues from China represented 26.1% of our total Q4 revenue, reflecting continued moderation of that mix. For the year, our revenues grew 63.3% to almost \$110 million. Growth was strong in most all of our regions.

In Q4, our European business growth rate was lower than earlier in the year, owing to the WLTP change in emission standards, which impacted a lot of the auto sector in Europe and accelerated some sales into Q3, which, in turn, negatively impacted Q4 as the industry attempted to get ahead of the new emissions deadlines. You can see this very evidently in aberrations in the car sales data out of Europe for Q3 into Q4, but that seems to have been a temporary phenomenon.

Our year-over-year growth in China was lower in Q4 than the preceding 3 quarters. This is largely because Q4 2017 is where our China growth kicked off, so the year-over-year comp is a tougher one. Our China revenue declined sequentially in 2018 from our peak around March or April as we were able to bring more product into the channel to catch up with demand. And as a result and considering our ending run rate for China in 2018, we will see China revenue decline significantly in Q1 of '19 from the prior year. This is a function of the timing of the acceleration of sales in China last year, some softness due to competitive factors in China and new products we've been developing for China that have been pushed to Q2.

Overall, we're still very bullish on China and working hard to keep up with changing needs from our customers and distributors in the channel in terms of product assortment, marketing support and the like. We would expect to see this effect moderate into the year as we move off our peak China sales from the prior year. As a result to this year-over-year comparison, our overall revenue will decline modestly in Q1 despite strong sales in our other regions.

I was also very pleased with our gross margin performance in 2018, which finished at 30.4%, reflecting nice results from our margin expansion initiatives, which we began in late 2017. Margin expansion remains the top focus for the company, and we're working hard to continue to make improvements in this area. And we'll be devoting even more time to it now that we have the U.S. GAAP transition complete.

SG&A expenses for the year represented 19.7% of total revenue. Obviously, there were some onetime costs in 2018 related to our transition to the U.S., and those will continue into the first quarter of '19. That being said, we continue to be diligent on striking the right balance between controlling expenses and investing in the business, as we've talked about.

EBITDA for the year finished at \$13 million versus \$3.6 million in 2017 driven by the combination of tremendous revenue growth, gross margin expansion and the operating leverage that creates. Net income for the year finished at \$8.7 million or \$0.32 per share.

I remain more confident than ever that our overall strategy, which centers around the notion of getting close to the customer, is the right strategy for our company. I think our 2018 results confirm this. As most of you know, our strategy centers around 4 key initiatives. First, we continue to search for and execute on global expansion opportunities where it makes sense. In addition to our operations in Canada, Mexico, the United Kingdom and the Netherlands, in 2018, we acquired our distributor in Taiwan, which critically established our first presence in Asia as all of Asia, including China, is going to be a growth driver for us going forward. This won't be our last presence in Asia as we execute on our strategy.



Secondly, we continue to enhance XPEL's global brand awareness, a more premium brand and well known in the automotive industry. We know that growing worldwide recognition of the brand will be leveraged to drive additional product sales. As an example, we recently launched our XPEL FUSION PLUS, a new ceramic coating, which nicely complements our paint protection film. FUSION PLUS is a hydrophobic self-cleaning coating that provides additional protection to paint protection film or on a vehicle's painted surfaces to enhance the gloss and make it easier to clean. This product also gives us and our dealers the ability to increase addressable gross revenue per vehicle. As the XPEL brand is well respected, the rollout of this product has been very well received. We're about a month in. It's a top-notch product, very complementary to our line. And as we expand the auto product line from paint protection to automotive window film, now with the ceramic coating, we'll be increasingly encouraging our dealers to adopt all of the products on the platform for the best customer experience and incentivizing them to do so.

Our third strategy centers around the continuation of our channel acquisition strategy. To that end, we acquired 3 installation facilities in Canada last year. We found that our ability to drive increased product revenue that's greatly improved when we have a presence in a given local market. We've had consistent success with this model, and we continue -- we expect to continue this strategy as we move through 2019, with several key opportunities currently under evaluation.

Finally, we continue to drive expansion of our nonautomotive product portfolio. As you may remember, in 2018, we acquired E-Shields Health, which facilitated the launch of a silver-infused antimicrobial protective film, XPEL RX, which has a number of potential uses for customers in different industries, including health care and foodservice and more. We're just now taking that product to market.

We also launched our commercial and residential solar and security film, XPEL VISION, last year. We'll be talking more about the VISION line and our plans for this product line as we go through the year, very excited about these new product opportunities for this -- for 2019.

And I think a year-over-year comparison of the ending balance sheet is a great way to sum up and highlight our success for last year. We were able to drive 63% top line growth while ending the year with more cash, flat AR, almost flat inventory, a reduction of \$3.4 million in accounts payable and over \$2 million reduction in debt. So that's an awesome operational performance.

As a fantastic year for XPEL, I'm very proud of the results and proud of our employees for the results we delivered to our shareholders but just as importantly to our customers. And we look forward to building on that success for 2019.

So with that, I will turn it over to Barry to review some of the transition we've done and more of the financials. Barry?

Barry R. Wood - XPEL Technologies Corp. - CFO

Thanks, Ryan, and good morning, everyone. Before I talk a little more on our results, I would like to walk you through our filing process leading up to today's announcement. As Ryan mentioned, we have filed a registration statement on Form 10 to register our securities in the U.S. pursuant to the 1934 Exchange Act, plus we're seeking to list our common stock on Nasdaq under the symbol XPEL. To be clear, this is not an S-1 filing as we do not need to raise capital at this time. As required by the '34 Act, the Form 10 necessitates inclusion of financial statements audited in accordance with U.S. GAAP. Because we're designated as an emerging growth company under the JOBS Act of 2012, we're only required to submit 2 years of audited financials in the Form 10. As most of you know, our previous financial statements were under IFRS. Given that, we had to go through an IFRS-to-U. S. GAAP conversion for our 2017 and 2018 financial statements. And once that was completed, our U.S.-based auditor, Baker Tilly, had to reaudit our U.S. GAAP-converted 2017 financial statements as well as audit our 2018 U.S. GAAP financial statements.

In addition, since we're currently still a Canadian reporting company, we requested and were granted an exemption by the Ontario Securities Commission, which allows us to file U.S. GAAP-based financial statements in Canada instead of the otherwise required IFRS-based financial statements. As a condition to granting this exemption request, the Ontario Securities Commission has required us to file U.S. GAAP-based 2018 interim or quarterly financial statements on SEDAR no later than April 30. This effectively means that we have to quarter-ize, if you will, our audited 2018 annual GAAP financial statements, meaning that our IFRS-to-U. S. GAAP adjustments, which were determined on an annual basis, need to be applied on a quarterly basis. This has been completed, but as an SEC issuer, our 2018 quarterly statements are required to be reviewed by our auditors since they will be used as comparatives to our 2019 quarterly financial statements. And as such, we cannot discuss detailed quarterly results beyond revenue until these reviews are complete.

As you would likely expect, there are differences in IFRS versus U.S. GAAP accounting standards. Consequently, we recorded various adjustments to convert to U.S. GAAP. One major difference is the way in which we account for our kit design costs. Under IFRS, we capitalize these costs and amortize them over their estimated useful life. Under U.S. GAAP, these costs are expensed as incurred, and I'll comment more on our U.S. GAAP results a bit later.

And as we mentioned earlier, our Form 10 was filed today. In general, Form 10s are automatically effective 60 days after the file date. We anticipate receiving comments from the SEC during this process, and we will address those comments as we receive them.

Assuming our Nasdaq application is approved, we cannot list on Nasdaq until all SEC comments are clear. There has been no decision yet regarding the TSX Venture listing's future. As Ryan mentioned, pursuing a U.S. listing has been a long time coming for our company, and we're very excited to enter this next chapter of our corporate life at XPEL.

Now let's take a more detailed look into our 2018 results. First, I'd like to point out that our income statement looks a little bit different than past presentations. Our revenue is broken out between product and service revenue in accordance with the U.S. reporting requirements. And as Ryan mentioned, total Q4 2018 revenue grew 33.1%, and our total 2018 annual revenue grew 63.3% to \$109.9 million. And geographically, we saw strong growth in almost all of our regions led by China where revenue almost tripled in 2018.

Product revenue grew 69.5% to \$95.5 million. And in the product revenue category, paint protection film grew 72.8% to \$85.5 million and represented 77.8% of our total revenue. Window film grew 43.2% and represented 6.7% of total revenue.

Total service revenue grew 31.5% to \$14 million. Our service revenue consists of access fees for our Design Access Program software, or DAP; cutbank credits revenue, which represents cut fees charged for the use of our DAP software; and installation labor revenue from the labor portion of installation sales at our company-owned installation centers; and then finally, training fee income, resulting primarily from fees charged for the attendance of our training classes.

While software and installation labor categories are fairly straightforward, I want to briefly walk you through our cutbank program. The essence of our cutbank program is to incent customers who use our DAP to purchase our film. Basically, if you're a DAP user and you buy our film, you only pay your monthly access fee. When you buy our film, we add the total square footage of film you purchase from us to your cutbank. Think of it just like your checking account at your bank. One square footage is added, you have the ability to cut patterns up to the square footage balance in your cutbank. If your bank goes to 0, you cannot cut any more patterns until you deposit more square footage into your bank, either by buying more film from us or purchasing cutbank credits.

Historically, we have offered to sell cutbank credits à la carte in certain circumstances. So all in all, up until now, this was fairly straightforward. But for those of you that follow U.S. GAAP-based companies, you've likely heard of a new revenue recognition standard known as ASC or Topic 606. I'm not going to go too deep into this, but 606 effectively required us to allocate a portion of our product revenue to service revenue for the estimated value of cutbank credits we added to customers' cutbank because they purchased our film. And under IFRS, this allocation was not made.

So back to service revenue results. Software revenue declined 9% due mainly to the restructuring of DAP access fees commensurate with the implementation of our cutbank program. Cutbank credits revenue increased a little under 50% due mainly to strong product sales. Installation labor grew 40.5% due mainly to continued strong demand in our company-owned installation centers. And as a side note, total installation revenue, combining product and labor, increased about 41%.

As Ryan mentioned, we were particularly pleased with our gross profit results for 2018, which the dollar has doubled from 2017, and our gross margin percentage finished at 30.4%. And again, just to reiterate, gross margin remains a top focus for the company as we move into 2019.

Our 2018 SG&A expenses grew 49.3% versus 2017 and represented 19.7% of total revenue. And you'll also notice the income statement presentation is a bit different in this category as well than in past because we are required to break out sales and marketing-related expenses from general and administrative expenses for U.S. reporting purposes. Sales and marketing expenses grew 37.5% due mainly to continued support of the ongoing growth of the business. 2018 general and administrative expenses grew 55.4% versus 2017 due mainly to increases in personnel, occupancy, IT



and travel-related costs to support the ongoing growth of the business as well as increases in professional fees due mainly to the ancillary costs related to the preparation and filing of our registration statement.

2018 EBITDA grew \$9.4 million to \$13.0 million, reflecting strong revenue and gross margin performance and related operating leverage. And EBITDA margin for 2018 closed at 11.9%.

As I mentioned earlier, one of the major changes from IFRS to U.S. GAAP is how we account for our kit design costs. Because we now expense these costs as incurred versus capitalizing and amortizing the costs over their estimated useful lives, the EBITDA -- our EBITDA calculation was impacted. Again, this is just a math exercise but just something to keep in mind going forward.

2018 net income grew \$7.7 million to \$8.7 million and represented 7.9% of total revenue. And EPS for 2018 closed at \$0.32 per share. 2018 cash flow from ops grew \$3.8 million to \$6.8 million. And as Ryan alluded to in his comments on our balance sheet, our financial position remains very strong, and we're effectively net debt 0 at 12/31/2018.

In summary, we were very pleased with our 2018 results. We accomplished a lot, and we look forward to continuing to execute as we move forward.

And with that, operator, we'll now open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of [Adam Goldstein], private investor.

Unidentified Participant

I just want to make sure I understood. Ryan, you said there will be a decline in revenue in the first quarter of 2019. Was that a decline in comparison to the first quarter of '18 or in comparison to Q4 of '18?

Ryan L. Pape - XPEL Technologies Corp. - CEO, President & Director

No, we're speaking year-over-year.

Unidentified Participant

Wow. So there'll be a year-over-year decline in revenue. That's the first time I think I've ever seen that.

Ryan L. Pape - XPEL Technologies Corp. - CEO, President & Director

Yes. Well, I mean we're -- we don't know the exact number. Obviously, we just finished March just a few days ago, which is our -- the biggest month of the first quarter typically seasonally. But when we're sort of normalizing our volume into China instead of sort of building volume and building product out in the channel as we did in the first half of last year and just sort of equalizing to demand coming off tripling the volume essentially last year as we did, that will have a very modest result and a very modest decline in revenue in the first quarter from the first quarter of 2018. And that's despite really strong performance elsewhere. So part of that is that obviously the growth in China on a year-over-year basis has moderated like we talked about in Q4, and it's just -- it was really exceptional last year, so we have a big comparison to make there.



Unidentified Participant

Okay. And one more -- my follow-up, I guess, is will there -- I noticed there's no more disclosure on net income based on geographic segment like there used to be. Did I just miss it? Or is that the case, that's no longer going to be disclosed?

Barry R. Wood - XPEL Technologies Corp. - CFO

That's correct, Adam. This is Barry. We are under U.S. GAAP. We effectively have one segment. So on a go-forward basis, that's the way we'll present.

Ryan L. Pape - XPEL Technologies Corp. - CEO, President & Director

Yes, and I would -- I'd add to that -- to Barry's remark there. So you will notice on the U.S. GAAP presentation, we have revenue by geography rather than a segment presentation in the IFRS financials. And I can tell you that while looking at the IFRS segment net income may seem particularly useful to us internally, that particular metric is not that useful because you've got transfer pricing mechanisms and sort of arbitrarily assign profit around the world. So while on the surface I think losing that sort of segment net income may be a loss, I don't think it's really as useful as it would seem. And instead, the geographic breakdown sort of mandated in the U.S. presentation, like we have now on a revenue basis, I think is actually more useful, in fact.

Operator

(Operator Instructions) Our next question comes from the line of [Jason Hirschman], a private investor.

Unidentified Participant

A great year, and congratulations on the pending uplisting to Nasdaq. I've got a question for you today. I was wondering perhaps if you can comment a little bit more on the opportunities that you see in 2019 and a little bit into the future in other areas of Asia Pacific, specifically Japan and Korea.

Ryan L. Pape - XPEL Technologies Corp. - CEO, President & Director

Sure, Jason. Yes, I think we've all talked extensively about the success in China over the past year and the growth, but I think it highlights a very good point, which is that, by any metric, many of these other markets in Asia correspondingly are substantially under-penetrated or underperforming as you see it. Japan is a particularly good example. I mean for the size of that economy, our sales there, relatively speaking, historically are very small. And so one of our areas of focus over the past 6 months really and leveraging our team in Taiwan has been Japan specifically. And so we have real high expectations for Japan, as an example, and other markets around Asia that we're able to spend more time and devote more local resources to. And all of these markets are different. China has a certain profile and a unique draw to the product and a unique way to go to market, and these other markets are -- they're different. And we have to sort of cater to them and have the right partners or distributors or direct presence. But you mentioned Japan. That's one that we are particularly focused on, among other points in the region.

Unidentified Participant

Just one follow-up question is that you've given some commentary on China for Q1 2019. Could you give a little more commentary perhaps on Continental Europe and how that's developing so far?



Ryan L. Pape - XPEL Technologies Corp. - CEO, President & Director

Yes. We've been pleased coming out of Q4. Like I mentioned, we've seen sort of growth rates decline there, sort of kind of watching how that's going to behave. Europe, we still see great opportunity. Our flow of customers in terms of new leads and new opportunities continues to be strong as ever, along with a lot of other unique projects. One of the things we're seeing there is Tesla, as an example, which we do very well in, in terms of our attachment rate to Teslas sold. Many of them are just now, on Model 3, just now reaching Europe for the first time. Shipments just started recently. So that's a net positive for us, along with all of our other initiatives there. So we're very bullish on Europe going forward, and I think we have a lot of opportunity there.

Operator

There are no further questions in the queue. I would like to hand the call back to management for closing comments.

Ryan L. Pape - XPEL Technologies Corp. - CEO, President & Director

I'd like to thank everybody for joining us today on our year-end call, and we look forward to speaking with you next time. Thank you.

Operator

Ladies and gentlemen, this does conclude today's teleconference. Thank you for your participation. You may disconnect your lines at this time, and have a wonderful day.

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