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RSSS - Q2 2015 Research Solutions Inc Earnings Call

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Alan Urban *Research Solutions Inc. - CFO*

CONFERENCE CALL PARTICIPANTS

Dennis Worth - *Analyst*

Juan Molta *B. Riley & Company - Analyst*

PRESENTATION

Operator

Good afternoon. Welcome to Research Solutions fiscal second quarter 2015 results conference call. My name is Amanda, and I will be your operator today.

Joining us for today's presentation is Research Solutions' President and CEO, Peter Derycz; and CFO, Alan Urban.

Following their remarks, we will open up the call for your questions.

Then before we conclude today's call, I'll provide the necessary cautions regarding the forward-looking statements made by management during this call, as well as information about the Company's use of non-GAAP financial information.

I would like to remind everyone that this call will be recorded and made available for replay via a link in the Investors section of the Company's website.

Now, I would like to turn the call over to Research Solutions' Chief Executive Officer, Mr. Peter Derycz. Sir, please proceed.

Peter Derycz - *Research Solutions Inc. - Chairman, President, CEO*

Thank you, operator. And thank you all for joining us today for our fiscal second quarter 2015 earnings conference call. We really appreciate you taking the time to learn more about our recent performance and outlook.

I'm going to start this call with some highlights about the second quarter as compared to the year-ago quarter. Revenue generated by Article Galaxy, our flagship product for accessing scientific, technical and medical information, increased 19% to \$5.1 million.

The number of Article Galaxy transactions increased 22% during the quarter to 138,736, with our active customer accounts up 21% to 732.

Article Galaxy gross profit was up 34% to \$1.3 million, with gross profit as a percentage of revenue up 280 basis points to a record 25%. These results helped increase our overall adjusted EBITDA by 136% to \$112,000. Alan will drill into our numbers in a bit more detail. But, first, I'd like to address what has been driving these positive results with Article Galaxy.

Despite the typical seasonality that occurs in our fiscal second quarter, when revenues dip sequentially due to lower customer activity during the holiday season, our revenue per Article Galaxy customer held steady from the prior quarter. In fact, the second quarter marks our ninth consecutive quarter of double-digit revenue growth with Article Galaxy.

For those less familiar, Article Galaxy is used primarily to help research-driven organization obtain access to key must-have scientific literature to support their research, regulatory and intellectual property efforts in a way that fit their internal workflows.



Our customers come from a broad spectrum of industries, from pharmaceutical, biotechnology, food and chemicals, to aerospace, engineering, electronics, semiconductor, automotive, environmental protection and legal. Increasingly, our customers are also represented by academia.

Through Article Galaxy, these customers receive broad access to key information resources on a robust platform that can integrate with their own internal networks, systems and workflows 24 hours a day, 365 days a year. Article Galaxy also creates tremendous efficiencies and cost savings that can be measured and tracked.

As our result over the last several quarters have demonstrated, Article Galaxy has achieved steady growth via rapid customer adoption. Our customers learn about Article Galaxy through our sales and marketing efforts, but more importantly via word of mouth. One satisfied customer just brings on another.

Our 732 active accounts come from all over the world. And by active accounts, we mean accounts that spend money with us every single month. Through these accounts, we serve tens of thousands of end-users.

Our technology breakthroughs with Article Galaxy have also been attracting new interest. Earlier in this quarter, we launched the Article Galaxy Widget, which has received rave reviews. Information industry analytics firm, Outsell, called it, the ultimate sophistication. And there were tweets, like the one from an end-user named, Chris Ventursia, who said, this is officially awesome, how to make searching peer-reviewed literature world easier.

The overwhelming feedback that's positive, come from the fact that Article Galaxy Widget seamlessly connect to any website to Article Galaxy with a single click. Given unique tools like the Widget and a whole host of other technology we have developed, when it comes to scientific information, Article Galaxy has become the hub that connects discovery with delivery.

In fact, connecting discovery with delivery is one of the key elements of Article Galaxy. This paired with our sophisticated end-user authentication transaction management reporting and 24/7 best-in-class customer support, all makes for something that is indeed officially awesome.

Are we excited about Article Galaxy's progress? You bet we are, and it's only getting better. We've only scratched the surface of what's possible and along with guidance from our customers, we will relentlessly continue with our planned improvements to this very unique and valuable platform.

As I mentioned earlier, in the second quarter we realized an expansion in our Article Galaxy gross profit as a percentage of revenue, which increased 280 basis points to a record 25%. Since this improvement was primarily due to reduced production expenses, resulting from greater efficiencies as well as decreased content acquisition cost, due to greater economies of scale, we expect this percentage to be sustained or improved even as we advance into traditionally stronger revenue quarters.

Increased focus by our sales force to build upon their success in the corporate sector and address the much larger and mostly untapped academic market was also a key driver for citing new customers in fiscal Q2. Moreover, our customer acquisition efforts continue to realize a 90% closing rate, when our solution is evaluated against our competitors.

We are also beginning to see positive momentum from the ongoing promotion we announced at the beginning of last December to encourage faculty and student users of ILLiad's popular library resource sharing management software to install our document delivery browser plug-in.

From an operational perspective, we made several enhancements to our Article Galaxy platform that improved the speed and convenience for customers procuring STM content. We believe these new features will also help us secure new customers in the academic market. The academic market for STM subscription and syndication services is important, since we estimate it represents a \$4.5 billion addressable market opportunity for us as compared to about \$500 million for the corporate sector.

Now, I would like to turn the call over to our CFO, Alan Urban, who will take us through the financial details for the fiscal second quarter. Alan?



Alan Urban - *Research Solutions Inc. - CFO*

Thank you, Peter, and welcome, everyone. Earlier today we issued a press release with our results for the fiscal second quarter ended December 31, 2014. A copy of this release is available in the Investors section of our website, at researchsolutions.com.

In addition, you can also find archived past quarterly earnings calls, press releases and SEC filings there.

Our total revenue for the quarter was \$7.9 million. That's an increase of 7% compared to the same quarter last year. The increase is primarily attributable to increased orders resulting from the acquisition of new customers for Article Galaxy, our digital cloud-based software-as-a-service solution.

Article Galaxy, which accounts for approximately two-thirds of revenue now, saw \$5.1 million in revenue for the quarter, an increase of 19% compared to the same quarter last year. The increase was primarily due to increased orders resulting from the acquisition of new customers.

Single-article delivery services generate nearly all of the revenue attributable to the Article Galaxy journal article platform. Even though single-article delivery services are charged on a transactional basis, customer order volume tends to be consistent from month-to-month in part due to consistent orders of our largest customers that require the implementation of our services into their workflow.

Article Galaxy transactions increased 22% to roughly 138,000 during the quarter compared to roughly 114,000 in the same quarter last year. Also, active customer accounts increased 21% to 732 in the quarter versus 603 in the same quarter last year.

Total gross profit was \$1.5 million for the quarter. That's an increase of 15% compared to the same quarter last year. Total gross profit as a percentage of revenue was up by 1.2 points for the quarter compared to the same quarter last year, from 17.8% to 19%.

Again, the increase was primarily due to slightly reduced production expenses and decreased content acquisition costs.

Gross profit from Article Galaxy, which accounts for approximately 84% of gross profit, was \$1.3 million for the quarter, an increase of 34% compared to the same quarter last year. Gross profit as a percentage of revenue from Article Galaxy was up by 2.7 points for the quarter compared to the same quarter last year, from 22.2% to 25%.

Total operating expenses were \$1.6 million for the quarter, a decrease of almost \$200,000 or 11% compared to the same quarter last year. The decrease was primarily due to a decrease in professional service fees.

Our net loss from continuing operations for the fiscal second quarter improved to a net loss of \$94,000 or a loss of \$0.01 per diluted share compared to a net loss of \$467,000 or a net loss of \$0.03 per diluted share for the same quarter last year.

Also, adjusted EBITDA increased 136% to \$112,000 for the quarter compared to adjusted EBITDA loss of \$312,000 for the same quarter last year. This represents a \$425,000 improvement in adjusted EBITDA.

Adjusted EBITDA is defined as net income or loss plus interest expense, other income or expenses, provision for income taxes, depreciation and amortization, stock-based compensation, income or loss from discontinued operations, and other potential adjustments that may arise.

We use the non-GAAP measure of adjusted EBITDA, because we believe that it provides useful information in comparing our performance across multiple periods on a consistent basis by excluding items that we believe are not indicative of our core operating performance.

At the end of the fiscal second quarter, we had cash and cash equivalents of approximately \$1.8 million compared to approximately \$1.9 million at the end of June 30, 2014. This decrease is primarily attributable to cash used in discontinued operations.

We believe that our current cash resources, borrowing availability under our existing line of credit and expected cash flow from operations will be sufficient to sustain operations for the next 12 months and beyond. As of the fiscal second quarter, there were no outstanding borrowings under the companies revolving line of credit with Silicon Valley Bank.

The amount of the line is the lesser of \$4 million or 80% of eligible accounts receivables, which equaled approximately \$2.25 million at December 31, 2014.

In addition, our balance sheet remains very clean with cash and prepaid expenses comprising nearly all of our assets and accounts payable and accrued expenses representing nearly all of our liabilities. We have no long-term debt and no long-term liabilities.

This completes my financial summary. Peter?

Peter Derycz - *Research Solutions Inc. - Chairman, President, CEO*

Thank you, Alan. Over the last quarter, we have made significant progress executing on strategic initiatives that are designed to drive growth and shareholder value. As we now pass the halfway point in our third fiscal quarter, we see Article Galaxy continuing its upper trajectory, with new customer wins and increased usage by existing customers producing double-digit revenue growth. In fact, we saw 16% growth in January Article Galaxy revenue compared to the same year-ago month.

We also began Q3 with a new customer that is one of the largest pharmaceutical companies in the world. With this new win, our client base now includes over half of the top 20 pharmaceutical companies in terms of global sales in 2014. We expect to realize revenue from this new major customer in the third quarter.

Our performance in Q3 is also being supported by the official launch of the Article Galaxy Widget in January. The Article Galaxy Widget accelerates scientific discovery by simplifying lowest cost access to research articles indexed by popular search tools and STM databases. Customers who are using the widget to conduct their online research are experiencing a new level of ease, access and affordability.

As mentioned earlier, these benefits were recognized by the information industry analytics firm, Outsell, which in a recent report elicited Leonardo Da Vinci's famous maxim to describe the Article Galaxy Widget: simplicity is the ultimate sophistication.

Outsell stated in their initial feedback from the market was overwhelmingly positive and that our Article Galaxy Widget follows their ideal zero-clicks away model for procuring scientific, technical and medical research information.

Outsell also pointed out that given the possibility of shrinking information budgets, particularly for government or small research organizations, some feel that in a couple of years the best solution we'll be working with a Document Delivery Service like Reprints Desk.

Outsell said that in the case of our Article Galaxy Widget, rather than clicking through myriad article titles to determine accessibility, users know immediately what their options are and can select, acquire and download articles in a single click. And for time-constrained researchers, as Outsell puts it, this is a dream come true.

Now, as we progress through the end of the year, we expect our digital solutions to continue supplanting our legacy print business, as we further penetrate both the corporate and academic markets with Article Galaxy. By doing so, we anticipate eventually fully realizing the leverage in our new business model, where we see a 2x increase in Article Galaxy revenue, resulting in a 5x increase in adjusted EBITDA.

Now, with that, we're ready to open the call for your questions. Operator?



QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

We do have a question from the line of [Dennis Worth].

Dennis Worth -- Analyst

I wanted to ask, so from the simplistic standing-back perception, I see that the accretion has all been within the same 21%, 22%, right. And so when everything jumps forward at the same pace essentially it make me worry for the earlier customers, whether they are just at a steady sales rate or how do you get them to accrete along with? Because it looks like all of this is new business is what's adding. It's not like all the business is accreting. I guess that's my question. Am I getting this wrong?

Peter Derycz - Research Solutions Inc. - Chairman, President, CEO

Well, there's a two parts to that. On the existing customer base, we have some customers that are increasing, as they grow. We have a lot of biotech companies that grow, and the pharma companies, and so on.

And we have other customers that aren't doing so well, that probably will decrease. So I think on that side there's probably ups and downs depending on the customer and their research health, I guess.

The other thing is it takes a while -- when we add a new customer, it takes a while for the new customer to, let's say, implement our solution company-wide or worldwide, it depends on how they're doing it.

So I think the customer acquisition rate will always be higher than, let's say, the growth rate, because the new customers added -- our new customers, right, they're just rolling out our solution, connecting on our tools to their internet and so on. So there is a bit of a lag between percentage in customer growth versus percentage in revenue growth.

Dennis Worth -- Analyst

I am jus wondering, if those initial sign-ups, are they just kind of stagnating, or what efforts can be made to make sure that the older customers are not getting too settled in their studying studying patterns?

Peter Derycz - Research Solutions Inc. - Chairman, President, CEO

Yes, there's two ways. One way to do that is to do basically internal marketing with our customers. So when we launch our platform inside their company, we help them market internally. And so, let's say, we land a law firm in one city, we want to make sure that the other cities from that same law firm are also using us as well, right. So there is a little more selling going on after our customer's been added.

And we are also launching new tools and make new enhancements available to the product and the service, and those are upsell opportunities. So that's another area where we can go internally to our existing customer base with more value and more of an upsell.

I'd like to add to that that, let's say, we've had virtually zero churn win our top customers, so all of our largest customers, top-20 to 40 accounts, virtually no churn. So I think on the large accounts people are staying, sticking with us. And if there is any smaller entity is going out of business, things like that, we'll see some drop in revenue, but typically we see pretty good stickiness.



Operator

Our next question comes from Ian Corydon with B. Riley & Company.

Juan Molta - *B. Riley & Company - Analyst*

This is Juan Molta on for Ian with B. Riley. And I had the same questions that the gentleman before me had. In addition to that I wanted to know if you guys could comment on the platform subscription fee that you guys have talked about.

Peter Derycz - *Research Solutions Inc. - Chairman, President, CEO*

So Article Galaxy has evolved over time, start out being just a very small part of our revenue, when it was sort of, I guess, early day system. But as Article Galaxy has evolved and value has been added, a new modules and features have been added to it, we've actually been able to charge for as a software-as-a-solution as a platform.

And we're in our first year or so of that, but that's growing, its part of our future, and definitely what we will be focusing on going forward. There is definitely a software platform sale as part of this whole mix and those gross margins tend to be, as you can expect, a hell of a lot higher than what we do now.

Juan Molta - *B. Riley & Company - Analyst*

And then any comments as to when you can provide, when you think you'll start providing formal guidance?

Peter Derycz - *Research Solutions Inc. - Chairman, President, CEO*

No comment to that point, at this point in time.

Operator

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

Peter Derycz - *Research Solutions Inc. - Chairman, President, CEO*

All right. Well, thanks to everyone for joining us on our call today. And if we haven't been able to answer any of your questions on this call, yes, please feel free to contact us or our Investor Relations firm, Liolios Group, who would be happy to answer them. We look forward to speaking with you soon and look forward to another great quarter. Thank you so much.

Operator

Before we conclude today's call, I would like to provide Research Solutions' Safe Harbor statement that includes important cautions regarding forward-looking statements made during this call, as well as a statement regarding the Company's use of non-GAAP financial information. Examples of forward-looking statements on this call include statements related to our new strategic focus, product verticals, anticipated revenue, and profitability.

Such matters involve risk and uncertainties that may cause actual results to differ materially, including the following: changes in economic conditions, general competitive factors, acceptance of the Company's products in the market, the Company's success in obtaining new customers, the Company's success in technology and product development, the Company's ability to execute its business model and strategic plans, the Company's successes in integrating acquired entities and assets, and all the risks and related information described from time to time in the Company's filings with the SEC, including financial statements and related information contained in the Company's Annual Report on Form 10-K and interim quarterly reports on Form 10-Q. The Company assumes no obligation to update the cautionary information in this presentation.

Today's presentation also includes financial measures defined as non-GAAP financial measures by the SEC.

The presentation of this financial information is not intended to be considered in isolation or as a substitute for the financial information prepared and presented in accordance with generally accepted accounting principles accepted in the U.S., otherwise referred to as GAAP.

Please refer to a more detailed discussion about the Company's use of non-GAAP measures and a reconciliation to nearest GAAP measures in today's earnings press release, which is available on the Company's website at www.researchsolutions.com.

Finally, I would like to remind everyone that a recording of today's call will be available for replay immediately after the call and through February 24, 2015. Please refer to today's press release for dial-in instruction.

Thank you for joining us today for our presentation. You may now disconnect.

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