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Q1 2021 Collectors Universe Inc Earnings Call

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CORPORATE PARTICIPANTS

Joseph J. Orlando *Collectors Universe, Inc. - President, CEO & Director*
Joseph J. Wallace *Collectors Universe, Inc. - Senior VP & CFO*

CONFERENCE CALL PARTICIPANTS

Leanne Sievers

PRESENTATION

Operator

Good afternoon, everyone, and thank you for joining us to discuss Collectors Universe Fiscal 2021 First Quarter Earnings Conference Call. With us today from management are Joseph J. Orlando, President and Chief Executive Officer; and Joseph Wallace, Senior Vice President and Chief Financial Officer. Management will provide a brief overview of the quarter, and I open up the call to your questions.

Comments made during today's call may contain statements regarding the company's expectations about its future financial performance, including forecasts and statements concerning business trends and profitability that are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. The company's actual results in the future may differ, possibly materially, from those forecast in this call due to a number of risks and uncertainties. Certain of these risks and uncertainties, in addition to other risks, are more fully described in the company's filings with the Securities and Exchange Commission. These forward-looking statements are made only as of the date of today's conference call, and the company undertakes no obligation to update or revise these forward-looking statements whether as a result of new information, future events or otherwise.

With that, I'd like to turn the conference over to LeAnne Sievers of Shelton Group Investor Relations. Please go ahead.

Leanne Sievers

Thank you, and welcome to everyone who has joined us today to review our first quarter fiscal 2021 financial results.

I'd like to now turn the call over to Joe Orlando, President and CEO. Joe, please go ahead.

Joseph J. Orlando *Collectors Universe, Inc. - President, CEO & Director*

Thank you, LeAnne, and welcome, everyone, to today's conference call to review our first quarter fiscal 2021 financial results. I'll begin today's call by summarizing the results for Q1 and then provide some commentary on the outlook going into our second fiscal quarter.

I am pleased to report that Collectors Universe finished Q1 with record operating results. Total revenues in the first quarter were up 52% year-over-year to \$30.8 million from \$20.2 million in the same quarter a year ago, setting an all-time quarterly record for the company.

Our strong growth this quarter was led by our PSA trading card and autograph business, which was up 130% year-over-year. We were also pleased with the performance of our coin business, PCGS, which was up 4% over last year despite the headwinds in this business related to the pandemic.

Also highlighting our quarter was the achievement of record operating profit and cash flow. Operating income was \$7.8 million or 25% of revenue compared to \$4.6 million in the previous year. It is important to note that the first quarter operating profit included expenses related to professional and recruitment fees in the amount of \$2.2 million and higher noncash stock-based compensation expenses of \$0.9 million. Together, these expenses reduced operating margin by 10% in the quarter, further underscoring the significant leverage in our operating model.

In addition, our cash position increased by a record \$8.1 million sequentially to \$36.7 million, surpassing last quarter's record of \$6.4 million in Q4 of fiscal 2020. These results are a direct reflection of the diligent work by our team over the past few years to transform the business in a way that could enable the kind of growth we achieved in the first quarter of fiscal 2021. And while it's gratifying to deliver these results, it's even more exciting that we continue to see expanding opportunities ahead.

To support this growth, we recently announced the expansion of our existing facility in Southern California by an additional 63,000 square feet, which is directly adjacent to our current facility, thereby doubling our square footage to over 126,000. This new facility has recently been upgraded and includes space for training rooms that we can utilize for quickly onboarding new employees. This expansion will also allow our IT, customer service and marketing personnel to return to the office, while still being able to adhere to social distancing guidelines.

Due to the proximity of the newly acquired space, we will not experience any material workforce disruptions or downtime that is typically associated with moving to an off-site location. Our expansion into the new space will be staged over time to support our growing backlog of business while also providing ample room to integrate technology solutions in the future -- such as robotic automation -- and support our long-term vision for the company.

Now let's take a deeper look into the performance of each authentication and grading division. Beginning with our PSA and PSA/DNA services, a strong combination of increased throughput and improved pricing catapulted our trading card, autograph and memorabilia division to a new quarterly record of \$18.6 million, which represented 60% of total Collectors Universe revenue. This includes record quarterly output for the division as we shipped approximately 1.25 million total collectibles, surpassing the prior record of about 775,000 items set in Q2 of fiscal 2020.

The PSA ASP rose 40% year-over-year. Improved market conditions and the need for faster turnaround times from our customer base helped drive the ASP strength in the quarter, which resulted in better margins. As throughput increases, however, the average ASP in our PSA division could fluctuate due to changes in submission mix. The substantial demand for these services and the strength of the overall trading card market have not shown signs of letting up, which is why we continue to believe that our PSA division will be a material contributor to our future growth.

Now turning to PCGS. Our coin division grew year-over-year by 4% to \$11.5 million despite the previously reported headwinds the division has been facing due to the global pandemic. PCGS' recent response to those challenges included hosting smaller domestic events to combat the ongoing absence of major trade shows.

Looking at PCGS domestic, PCGS vintage was up 6% year-over-year to \$3.6 million in Q1 versus \$3.4 million in the prior year quarter. As expected, all major coin conventions scheduled in Q1 were canceled, including our own trade show in Long Beach, California. By hosting smaller coin trading events, PCGS was able to replace approximately 87% of the show grading revenue versus last year.

And as we have talked about on prior earnings calls, it is important to combine PCGS Vintage and Show revenue when evaluating performance ... since some coins can simply be rerouted to our Vintage service line or vice versa by the customer. When combined in this way, both revenue figures in Q1 of fiscal 2021 were virtually even with last year's first quarter. So PCGS' quick response to the changing environment helped stabilize this revenue stream despite the lack of traditional trade shows.

Turning to PCGS Bulk. This part of the business was up 10% year-over-year and finished Q1 with approximately \$3 million in service revenues compared to \$2.7 million in fiscal 2020.

In terms of PCGS International, this is where we saw the greatest impact from COVID overall, but we were pleased with our continued progress in China from a year-over-year perspective. Even though we were not able to host any on-site grading events or send additional PCGS personnel to Shanghai due to restricted travel, China revenue still rose 20% to approximately \$1.6 million compared to \$1.3 million in the same quarter a year ago. We have been increasing our operational capacity in China so that we are less reliant on U.S.-based staff, which helped contribute to our performance in the quarter.

We did see some weakness in our Hong Kong and Paris locations, which were down about \$270,000 on a combined basis from the prior year, mainly due to processing challenges from the pandemic.

With that, let me now turn the call over to Joe Wallace for a more detailed review of our financial performance in Q1. Joe?

Joseph J. Wallace *Collectors Universe, Inc. - Senior VP & CFO*

Thank you, Joe. I will now give a brief overview of the financial results for the first quarter of fiscal '21. Despite the COVID-19 challenges that continued to impact primarily our coin business in Q1, the company announced record operating results in the quarter.

In the first quarter, the company generated record quarterly revenues of \$30.8 million, earned operating income of \$7.8 million and net income of \$6.0 million or \$0.65 per share. This compares to quarterly revenues of \$20.2 million, operating income of \$4.6 million and net income of \$3.6 million or \$0.40 per share in the first quarter of fiscal '20.

Despite earning record operating income in the quarter, the operating results were impacted by higher G&A expenses discussed below. The total revenue increase of \$10.6 million or 52% in the quarter was driven by an increase of \$10.5 million in cards and autograph revenues, representing a growth rate of 130% in the quarter and a quarterly record for that business. The revenue increase was driven by increasing capacity, primarily personnel, which enabled us to ship more units in the quarter and earning higher average service fees from customers paying for faster turnaround times.

Although revenue growth for cards and autographs accelerated this quarter to 60% of total revenues, that business has achieved quarter-over-quarter of revenue growth in 40 of the last 41 quarters. U.S. coin revenues increased 5% to 0 -- excuse me, U.S. coin revenues increased 5% or \$0.5 million and China revenues increased 20% or \$0.3 million in the quarter despite the COVID-related challenges of canceled trade shows, uncertainty as to the U.S. Mint Production schedule and restrictions on international travel.

Combined, our cards and autographs and coin businesses represented about 98% of revenues for the quarter and reflects the continued importance of those 2 businesses to our overall financial performance. Cards and autographs finished the quarter with another record backlog and therefore, we plan on continuing to increase authentication grading capacity through adding personnel and utilizing the additional space that we have recently secured, which will allow us to support the continued growth of that business.

The second fiscal quarter is seasonally the slowest quarter of the year for coins. And we expect that trend to continue this year also.

With respect to our China business, which ended the quarter with a sizable backlog, we will continue increasing local capacity to offset the impact of travel restrictions between the U.S. and China, which we expect will result in progressive revenue growth in future quarters.

The gross profit margin was 63% in the quarter as compared to 60% in last year's first quarter. The higher gross profit margin was due to the higher ASP earned in the cards and autographs business. As previously disclosed, there can be ongoing variability in the gross profit margin due to the mix of revenues and the seasonality of our business. On a quarterly basis during the 3 years ended June '20, our gross profit margins vary between 53% and 62%. Our combined operating expenses represented 37% of revenues in both this year and last year's first quarter.

Selling and marketing expenses were 7% of revenues in the current first quarter versus 13% in last year's first quarter. The lower selling and marketing expense in dollars reflected lower trade show costs due to the cancellation of 2 of the largest shows of the year, the Nationals for cards and autographs and the ANA for coins, both due to the COVID-19. Those cost reductions were partially offset by higher business development and customer service costs primarily due to the growth of the cards and autographs business.

G&A expenses represented 30% of revenues in this year's first quarter as compared to 24% in last year's first quarter. The dollar increase in G&A expenses of \$4.4 million in the quarter included: (1), \$2.2 million of professional fees incurred in connection with the now settled activist issue and the recruitment of new board members; (2), higher noncash stock-based compensation expense of \$0.9 million; and (3) higher G&A payroll costs of about \$1 million, which was inclusive of higher incentive costs due to the improved performance of the business.

Together, the higher professional fees and noncash stock-based compensation costs represented about \$3.1 million or 10% of revenue. The resulting operating margins were 25% of revenues in this quarter as compared to 23% in last year's first quarter, which, when the \$3.1 million of higher G&A costs discussed above are taken into account demonstrates the improved operating leverage of the business.

Turning to our balance sheet. The company's cash position was \$36.7 million at September 30, '20, as compared to \$28.6 million at June '20 and \$21.3 million at September '19. Net cash generated for the quarter of \$8.1 million included cash generated from operating activities of \$11.7 million, partially offset by \$1.6 million of cash dividends paid to stockholders, \$1.6 million used for capital expenditures and capitalized software costs, \$0.2 million used to pay down the company's term loan and \$0.2 million used to pay withholding tax of invested shares.

As previously disclosed on October 1, 2020, we entered into a lease amendment with our landlord to lease additional space that doubles the space occupied at our operations and corporate headquarter facility. The updated lease will be accounted for as a lease modification under the accounting rules and will give rise to a higher right-of-use assets and related lease obligation, which will be reflected in our balance sheet when we announce our Q2 results.

Our cash dividend of \$0.175 per share for the second quarter of fiscal '21 will be paid on November 27 to stockholders of record on November 13.

In summary, our first quarter results further demonstrate our ability to ramp up increased capacity that quickly contributes to revenue generation. We finished Q1 with strong momentum, primarily in the cards and autographs business. And with the continued record backlog in that business, we intend to build on that momentum as we progress through fiscal '21.

With that, I'd like to thank you for your attention. Joe?

Joseph J. Orlando *Collectors Universe, Inc. - President, CEO & Director*

Thanks, Joe. Before we conclude and open the call to your questions, I would like to make a few final comments about the close of Q1 and the outlook going into our second fiscal quarter.

As we look to the coming quarter, the record backlog in the PSA division will help moderate any anticipated volatility in authentication and grading revenues, in what has typically been the seasonally slowest quarter of our fiscal year. We have visibility into this side of our business, which helps support our efforts to begin staging our capacity expansion efforts over the coming quarters.

Additionally, the outlook for PCGS remained solid but somewhat tempered due to the near-term obstacles that are present in the coin business, with the ongoing absence of major trade shows and restricted international travel. With a great start to the new fiscal year, we remain focused on the opportunity we have in front of us to grow the business.

To fully capitalize on that opportunity, we plan to continue investing in our operations in terms of personnel, capacity and technology. Some of these actions will bear fruit immediately as we showcased in the first quarter, while others will potentially be key contributors to the long-term evolution of our company.

As a reminder, our expectations going forward are subject to several factors outside our control such as the price of precious metals, the market for collectibles, fallout from the COVID-19 pandemic, the overall state of the economic climate, primarily in the U.S., and the possibility of changing international trade policies worldwide. Overall, we remain very encouraged by the record results achieved in Q1. The Collectors Universe management team and Board of Directors are both energized by the progress and aligned as we set our course for the future and focus on providing increasing returns to our shareholders.

Now I would like to open the call to any questions you may have.

Operator

(Operator Instructions) It appears we have no questions. I'll turn it back to you, Joe.

Joseph J. Orlando *Collectors Universe, Inc. - President, CEO & Director*

Thank you all for joining us today. One final comment. We plan to attend the Furey Research Hidden Gems Conference on November 19 and then the Needham Growth Conference the week of January 11. If you'd like to request a meeting, please reach out to the respective firm or you could also contact The Shelton Group to arrange a call with management. We look forward to providing an update on our business next quarter.

Operator, you may now disconnect.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.

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