SEB Reports Results for Second Quarter, 2018

written by Raj Shah | July 31, 2018
July 30, 2018 (Source) – ***Conference Call Scheduled Wednesday, August 1, 2018, 11:00AM EST***

Smart Employee Benefits Inc. ("SEB" or the "Company") (TSXV: SEB) today reported its financial results for the three and six-month periods ending May 31, 2018.

States John McKimm, President/CEO of Smart Employee Benefits Inc., "Consolidated results for Gross Margin, EBITDA and Adjusted EBITDA for the second quarter, 2018 showed steady improvement, year over year from 2017 and 2016 fiscal years; however, they were short of our forecasts for 2018. Trailing 12-month comparisons also showed improvement with revenue of $107.5 million. Gross Margin of $30.1 million and EBITDA of $2.6 million. While revenue was only up $1.3 million, Gross Margin was up $3.2 million and EBITDA up $2.0 million versus November 30, 2017.

- **The Technology Division ("TD") EBITDA** has been relatively stable with modest growth for the past three years. TD contracts (Backlog, Option Years, Evergreen) wins and renewals remain healthy and continue to replace revenue with modest growth. Cost structures are well in hand, however, the utilization of the employee bench in select entities has shown modest weakness. Typically, the fourth quarter in the TD picks up any weakness in the first half. In 2017, Q4 represented over 33% of results.
- **Corporate Costs** on a cash basis have declined. The issuance of options added over $400,000 of non-cash expenses to corporate.

- **The Benefits Division** has shown steady improvement. Revenues are growing, gross margins are strong, 19 client contracts (representing over 120,000 employees) that have matured since April 2017 have been renewed. Many have included the opportunity for enhanced services provided by one or more of SEB's new FlexPlus modules. SEB has also decommissioned 3 of the 7 software platforms which were acquired from Aon, transitioning the clients to the "FlexPlus" environment. Additional platforms will be decommissioned by year end, which contributes to significant cost savings. SEB's Benefit Processing Solutions have all been moved to Microsoft Azure, SEB's cloud solution of choice, which allows SEB to launch its "FlexPlus" platform globally to Channel Partners. SEB also announced during the quarter the launch of its Voluntary Benefits Platform which supports the introduction of the first 5 Voluntary Benefit Solutions. The first sales of these solutions will be September 2018 though January 2019, during the first annual enrolment period. The Voluntary Benefits Products add significant value to SEB clients and their employees in a very cost-effective manner. The SEB Voluntary Benefits Platform allows employees to buy benefit solutions in minutes, not days and weeks. SEB's revenue participation is annuity, from the sales of these solutions."

McKimm goes on to state, "SEB has invested heavily in its Benefits Processing Solutions over the past number of years. This has penalized consolidated EBITDA. In 2017, SEB gained serious traction in its Benefits Processing division with the Aon transaction. Today we have over 50 name brand clients representing over 330,000 employees and over $1 Billion of premium. SEB's Benefit Processing solutions are in the market and proven. Our Flex Plus platform is capable of managing Flex, Traditional and Multi-Employer environments and has 16 modules, all operating in “One Processing Environment”. This is a unique competitive advantage for SEB to provide leading edge, cost effective, user friendly solutions to our clients and their plan members. The tens of millions of dollars SEB has invested in our “One Processing Environment” solutions, combined with our “Channel Partner” go to market model, now has major traction in the Canadian marketplace. Our results continue to show steady improvement and our cost structure is highly scalable with substantial profit margin growth with every new dollar of revenue”.

SEB’s business is “Managed Services”. This business falls into two categories – Technology Division and Benefit Division. In both divisions, our employees and contractors automate and manage business processes for clients using SEB’s proprietary technologies and technologies of SEB’s partners. Our focus is providing total outsourcing solutions on multi-year contracts. A summary of the progress SEB has made in the first half includes:

1. Technology Division (“TD”) – Stable, Consistent Performance

	a.	**Contracts** – We have won and renewed over $150 Million of Contracts since November 2017. Approximately 65% are renewals and the remainder are new. The contracts in this division (Backlog, Option Year, Evergreen) total over $400 Million.
	b.	**Revenue** – Revenue for Q2/18 and the first half of fiscal 2018, totaled $24.6 Million and $47.6 Million, respectively. This compares with $48.8 Million in the first half, 2017 and $49.1 Million in 2016 for the same periods. Revenue was up approximately $1.54 Million in Q2/18 over Q1/18.

	c.	**Gross Margin ("GM")** – GM for Q2/18 and the first half fiscal 2018, totaled $8.8 Million and $8.7 Million, respectively. This compares with $5.2 Million and $8.9 Million in 2017 and $4.5 Million and $8.6 Million in 2016, for the same periods. GM was up approximately $0.86 Million in Q2/18 over Q1/18.
	d.	**Adjusted EBITDA ("AEBITDA")** – AEBITDA for Q2/18 and the first half of fiscal 2018, totaled was $2.12 Million and $3.24 Million respectively. This compares with $1.67 Million and $2.62 Million in 2017 and $1.94 Million and $3.45 Million in 2016 for the same periods. AEBITDA was up approximately $1.0 Million in Q2/18 over Q2/17.
	e.	**EBITDA** – For Q2/18 and the first half of fiscal 2018, totaled $2.11 Million and $3.23 Million, respectively. This compares with $1.08 Million and $1.68 Million in 2017 and $1.70 Million and $3.20 Million In 2016, for the same time periods. EBITDA was up approximately $1.0 Million in Q2/18 versus Q1/18.
	f.	**Expectations** – Q2/18 showed significant improvement in EBITDA over Q1/18 and over Q2/17. The first half also showed improvement over the same periods. However, our budgets for the first half of fiscal 2018 were higher than our results. While EBITDA margins improved, revenue and gross margin fell short of budgets, between 5% and 10%. The primary reasons are several months delay in the start date of new contracts and a lower utilization of our employee bench in select entities than anticipated. We do expect to recover a portion of this shortfall in the fourth quarter, which is typically our strongest quarter. The fourth quarter represented (on a consolidated basis), over 33% of our results in fiscal 2017. The TD business remains a strong consistent performer, year over year.

2. Benefits Division ("BD")

	a.	**Revenue** – SEB’s BD had solid revenue growth in the first half, fiscal 2018, reaching $6.67 Million versus $2.72 Million the previous year and $0.38 Million in fiscal 2016. Revenue for Q2/18 versus Q2/17 and Q2/16 was $3.37 Million vs $2.26 Million and $0.39 Million, respectively. We expect continued growth in the second half of fiscal 2018, which is typically the strongest half.
	b.	**Gross Margin (“GM”)** – The BD is largely an employee base versus the TD which has a much larger contingent of contractors. As such, the GMs are very high at over 90% of revenue. The BD is very scalable with operational capacity within this infrastructure that supports exponential revenue growth with minimal increases in fixed costs. GM grew to $3.195 Million in Q2/18 up from $2.103 Million and $0.197 Million is Q2/17 and Q2/16, respectively. Continued growth is forecast for the second half of fiscal 2018. Q1/18 GM was approximately $3.158 million.
	c.	**Adjusted EBITDA** – Adjusted EBITDA was a negative $0.185 Million for Q2/18 and a negative $0.437 Million, for the first half, versus a negative $0.558 Million for 2017 and a negative $0.825 Million in 2016 for the same half year period. The second half of fiscal 2018 is expected to be positive.
	d.	**EBITDA** – EBITDA was a negative $0.598 Million in the first half 2018 versus a negative $1.778 Million and a negative $0.825 Million for the same period in 2017 and 2016, respectively. Q2/18 EBITDA was a negative $0.346 million and a negative $0.252 million in Q1/18.

	e.	**Expectations** – The Aon acquired business is growing and cash flow positive as a result of significant infrastructure cost savings and new client wins. The drag on cash flow in the BD during the first half is largely due to the costs of transitioning clients to FlexPlus from old platforms, decommissioning old platforms, bringing on new clients and the investment in new modules introduced to our “FlexPlus” suite of solutions. The additional drag on cash flow has been the cost of introducing and maintaining the 16 FlexPlus modules, a number of which are just beginning to generate revenue. These modules add over 20 revenue models and are expected to generate significant revenue opportunities in 2019 and beyond.	
	f.	**Progress in First Half, 2018** – The BD made substantial progress in the first half of fiscal 2018. Fiscal 2017 was dedicated to the acquisition and integration of the Aon administration business where SEB acquired over 265,000 plan members and 48 corporate clients. This progress includes:	
		–	**Contract Renewals (News Release of July 16, 2018)** – SEB renewed 19 (over 12,000 plan members) of the 48 clients acquired from Aon where the contracts came up for renewal since April, 2017. All contracts were renewed for multi-year periods. Today, SEB administers benefits for over 50 of Canada’s corporate elite, with contract backlog estimated to exceed $75.0 Million representing over 330,000 employees and over $1.0 Billion pf premium.

		–	**Voluntary Benefits (News Release July 23, 2018) –** SEB digital Ecosystem integrates with insurers and third-party environments (including marketing and underwriting) and manages the end to end business processes for selling and administering Voluntary Benefits. It allows clients to purchase a Voluntary Benefit in minutes versus days and weeks. The Voluntary Benefit Partnerships currently in place include:
			• **Vengo Workperks** – programs include instant access to over 2,200 perks from brand name and local vendors. Employees can save $1000 every year on a multitude of goods and services. • **Virtual HealthCare (Equinox)** – programs include online access to doctors, nurses and other medical practitioners for services, including renewing prescriptions. • **Insurance Solutions** – Include three insurance products (Critical Illness and Term Life) being launched in September 2018.
			Voluntary Benefits is forecast to be a significant growth area for SEB's BD, starting in the fourth quarter of 2018 and continuing into 2019 and beyond. SEB has invested significantly in this platform over the past several years. The revenue model for SEB is a share of the revenue from the purchase of the solutions. Currently, SEB is working with partners to introduce another 6 plus new Voluntary Benefits by the end of 2019.

		–	**Azure, SEB’s Cloud Solution of Choice (News Release July 16, 2018)** – SEB’s BD processing solutions have global application. Our “go to market” business model is “Channel Partnerships”. SEB has deployed its solutions in Microsoft Azure as its global cloud solution. This is a critical competitive advantage in SEB deploying its “FlexPlus” processing solutions, quickly and cost effectively to its Channel partners both in Canada and globally.

3. Corporate Division (“CD”)

CD is a cost centre which includes audit fees, valuation fees, director’s fees, public company costs, financing costs, etc. Cash Costs improved during this quarter, year over year. The costs for Q2/18 were $1.086 Million of which approximately $0.425 Million of these costs are non-cash allowances for options granted during the quarter. Actual cash costs for Q2/18 were approximately $0.661 Million, an improvement of over $0.302 Million from the same quarter in 2017.

4. Trailing Twelve Months (“TTM”) Comparisons

($000s)	**May 31/18 (TTM)**			**Nov 30/17 (FY)**			**Nov 30/16 (FY)**	
Revenue	$	107,546		$	106,283		$	97,228
Gross Margin		30,132			26,951			17,210
Adjusted EBITDA		2,373			3,022			2,080
EBITDA	$	2,550		$	554		$	(504)

	a.	**Revenue**, on a TTM basis, increased over the fiscal years 2017 and 2016 by $1.3M and $10.3M, respectively. At a minimum, the $1.3M increase in the May 31, 2018 TTM is expected to prevail quarterly throughout the year.

	b.	**Gross Margins** for the TTMs are $30.0M vs $27.0M for fiscal 2017 and $17.2M for fiscal 2016. SEB has a very scalable fixed cost structure and has reached the point where over 60 percent of the growth in gross margin dollars are forecast to go to EBITDA.
	c.	**Adjusted EBITDA** for the TTM was $2.4M vs $3.0M for fiscal 2017 and $2.1M for fiscal 2016. Continued growth is expected during the year.
	d.	**EBITDA** for the TTM grew to $2.6M from $554K in fiscal 2017 and a loss of $504K in fiscal 2016. The primary differences between Adjusted EBITDA and EBITDA are one-time and non-cash costs (i.e. share based compensation). In 2017, one-time costs included the costs of transitioning the Aon infrastructure from Aon to SEB. In the TTM ended May 31, 2018, one-time costs include a decommissioning investment whereby a number of the former Aon clients were transitioned to our Flex Plus platform, leading to the redundant platforms being decommissioned.

ACCOUNTS RECEIVABLE FUNDING – On July 26, 2018, SEB Administrative Services Inc. ("SEB Admin") closed a financing arrangement whereby SEB Admin arranged a $2 million-dollar accounts receivable financing for its over 90-day account receivables from a consortium of existing shareholders. The initial term is for a period of six months, with an option to renew for a further six months. The costs are consistent with account receivable factoring facilities. The delayed collection of accounts receivable in SEB Admin is related to the complicated billing arrangements whereby SEB bills the client indirectly through the Aon infrastructure. Currently approximately 50% of billings are directly to clients. By the fiscal year end over 95% of billing is expected to be direct to clients and the outstanding SEB Admin accounts receivable should be reduced by over $1.5 Million. Security for the funding is provided by the assets of SEB Admin, subject to any existing security held by SEB’s Schedule A Bank Lender.

QUARTERLY CONFERENCE CALL DETAILS

Date/Time: Wednesday, August 1, 2018 at 11:00 AM ET.
Canada & USA Toll Free Dial In: 1-800-319-4610
Toronto Toll Dial In: 1-416-915-3239
Callers should dial in 5-10 minutes prior to the scheduled start time and simply ask to join the call.

Webcast Link: access at http://services.choruscall.ca/links/sebq220180801.html	
Conference Call Replay Numbers:	
Canada & USA Toll Free:	1-855-669-9658
Code:	2526 followed by the # sign
Replay Duration: Available for one week until end of day August 8, 2018.	

ABOUT SEB

SEB is a Business Process Automation and Outsourcing Technology Company providing software, solutions and services to a national and global client base. SEB has a specialty growth focus in cloud enabled SaaS processing solutions for managing employer and government sponsored benefit plans on a BPO (Business Processing Outsourcing) business model, globally. This is a major growth focus, SEB currently serves corporate and government clients across Canada and internationally. Over 80% of SEB’s revenues derive from government, insurance and healthcare organizations. SEB’s technology infrastructure of over 800 multi-certified technical professionals, across Canada and globally, is a critical competitive advantage in supporting the implementation and management of SEB’s Benefits Processing

Solutions into client environments. SEB's Benefits Processing Solutions can be game changing for SEB clients. SEB currently administers over $1B of Premiums for more than 50 of Canada's corporate elite companies, representing over 330,000 plan members. SEB's revenues are over $100M with contracts (backlog, evergreen, option year) valued at over $500M.

The core expertise of SEB is utilizing its employees and contractors to automate and manage business processes utilizing SEB proprietary software solutions combined with solutions of third parties through joint ventures and partnerships. SEB's client acquisition model in benefits processing is "Channel Partnerships" where SEB processing solutions both improve cost structures and enable new revenue models for Channel Partners and clients. All SEB solutions are cloud enabled and can be delivered on a SaaS platform. SEB solutions turn cost centers to profit centers for our Benefits Processing Channel Partners.

For further information about SEB, please visit [www.seb-inc.com.](http://www.seb-inc.com)

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All figures are in Canadian dollars unless otherwise stated.