CORPORATE PARTICIPANTS

Bill Wood
President and Chief Executive Officer

Sujeet Kini
Chief Financial Officer

Jennifer Smith
Capital Markets Communication, LodeRock Advisors Inc.

CONFERENCE CALL PARTICIPANTS

Gavin Fairweather
Cormark Securities

Parth Shah
Canaccord Genuity

Adam Wilk
Greystone Capital Management

Amr Ezzat
Industrial Alliance

PRESENTATION

Operator

Good morning, ladies and gentlemen. Welcome to the Sylogist Q2 2023 Earnings Call.

I would now like to turn the meeting over to Ms. Jennifer Smith of LodeRock Advisors. Please go ahead, Ms. Smith.

Jennifer Smith, Capital Markets Communication, LodeRock Advisors Inc.

Thank you, Patrick, and good morning.

Joining me today to discuss Sylogist's Q2 Fiscal 2023 results are Bill Wood, Sylogist's President and Chief Executive Officer, and Sujeet Kini, Chief Financial Officer.

This call is being recorded live at 10:30 a.m. Eastern Time on August 10, 2023.

Our Q2 press release, MD&A, financial statements and accompanying notes have all been issued and are available for download on SEDAR+.

Please note that some of the statements made on the call may be forward-looking. Actual events or results may differ materially from those expressed or implied, and Sylogist disclaims any intent or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

The complete Safe Harbour statement is available in both our MD&A and press release, as well as on sylogist.com. We encourage our investors to read it in its entirety.

We are reporting our financial results in accordance with international financial reporting standards, or IFRS. As before, we will also discuss non-GAAP performance measures, which should be viewed as supplemental. The MD&A contains definitions of each one used in our reporting.

All of the dollar figures expressed on this call are in Canadian, unless otherwise noted.

I'll turn it over to Bill first for opening remarks, then Sujeet will review our Q2 financial performance, after which Bill will conclude with scripted remarks with an outlook on our business and markets, at which time we will open it up for questions.

With that, I'll hand it over to Bill.

Bill Wood, President and Chief Executive Officer

Thank you, Jen and good morning, everyone.

As most of you already know, Sylogist is a software-as-a-service, or a SaaS company, that provides mission-critical solution to over 2,000 customers worldwide, primarily in three public sector verticals: education, non-profit, and government.

We help mid to upmarket public sector organizations more effectively fulfill their mandates with flexible, advanced SaaS solutions that address their unique needs. Our platforms scale, deliver clear ROI, and provide user-friendly and highly secure technology to our customers.

We delivered another quarter of strong profitable organic growth in Q2. The results we achieved were due to a talented, dedicated workforce, industry best, 100 percent SaaS solutions, a customer-centric mindset, and a data-driven culture to measure and adjust the execution of our strategy.

With our continued momentum, our total revenue reached a new record of $16.6 million in the quarter. That's a year-over-year organic growth rate of 21 percent, or 18 percent on a constant currency basis. Reoccurring revenue was strong in Q2 at $9.7 million, up

8 percent year-over-year, and this was led by our SaaS subscription revenues, which were up 9 percent year-over-year.

As this organic growth is supported by a solid foundation of profitability, as evidenced by a Q2 EBITDA margin of 26 percent, in short, we continued to execute our profitable growth plan effectively, culminating in an overall posture of 47 against our rule-of-40 benchmark, or 44 on a constant currency basis.

New bookings in Q2 were $6.1 million. We're very pleased with the quarter's booking achievement, given the typically slower seasonal deal contracting period of Q2, when the public sector is consumed with fiscal year-end close activities and awaiting new budgets to become available July 1st.

Before handing it over to Sujeet to review our Q2 numbers in more detail, I'd like to draw your attention to a couple important points and provide an update on our key initiatives that we expect will continue to make positive contributions to our top and bottom lines in future quarters.

First, the strategic R&D and go-to-market investments we've made are unquestionably driving our strong organic growth results. Our marketing and sales motions are creating high-quality ideal customer profile, or ICP leads, and our win rate in Q2 was stronger than at any time since I've joined the Company.

I also want to point out that our spend on R&D has largely plateaued and that our marketing and sales investments remain sub-10 percent of total revenue, underpinning the effectiveness of the investments we're making to deliver the impressive profitable organic growth that we've achieved over the last three quarters.

Additionally, as I've highlighted over the last couple of quarters, building out a high-performing partner channel has been a top priority as a means to increase our awareness and expand our sales and delivery capacity in a leveraged manner. To that end, partner-led bookings increased 3x in Q2, an indicator that our strategy is taking hold and beginning to pay dividends.

Secondly, I want to share a quick update with respect to the non-profit, government, and education markets. As expected, the SylogistMission pillar of our strategy has driven the majority of the organic growth we've seen to-date. Our thesis to offer an industry-first, 100 percent SaaS, fully integrated, Microsoft-based fundraising and finance solution is driving an uptick in combined ERP and CRM opportunities.

The SylogistMission platform gives us the flexibility to sell to the customers' pain point and then pull through the rest of our platform once they see the benefits it represents, and come to value us as a trusted partner in their success.

I also want to highlight that Microsoft-originated leads are being funnelled our way in an increasingly material manner, which is a very good sign in terms of our expanding strategic relationship with Microsoft and their partner ecosystem.

Our SylogistGov beta customers will be transitioned to our new Gov platform in early Q4. Realities were such that we decided to push their cutover to SylogistGov out approximately 60 days from the originally planned date due to the customers' limited bandwidth during their fiscal year-end close.

Feedback from users has been exceptionally positive and they're looking forward to cutting over to the new SylogistGov platform very soon. We expect these early successes will act as a catalyst for the next wave of new and existing customers to move forward with SylogistGov in the first half of '24.

Also on the SylogistGov front, we are now weeks away from another state going live on our Gov, fully SaaS, victim notification solution. This is noteworthy because it positions us well to win additional, large, multiyear contracts in other states going forward.

On the SylogistEd side, following the successful lift and shift of our software platform from Oklahoma to North Carolina, and a top 10 school district in North Carolina having gone live on SylogistEd right on schedule, we are seeing several other districts leaning in to follow suit. I see us as very well-positioned to accelerate in North Carolina over the next 12 months, and elsewhere in the back half of '24.

As I've said before, we're just getting started in the SylogistGov and SylogistEd markets, and the value creation opportunity we see ahead is large, very large.

I'd like to now turn things over to Sujeet to go through our Q2 financial performance in more detail. Sujeet?

Sujeet Kini, Chief Financial Officer

Thank you, Bill.

It's been a busy and exciting two months since I joined Sylogist. I've had my head down, wrapping up on my understanding of Sylogist's business and operating model, reviewing the metrics, we discuss and disclose, and listening to feedback from the Street.

In June of this year, I had the unique pleasure, along with Bill and the rest of our Management team, of speaking with many of our investors and analysts at our Investor Day. I look forward to continuing this outreach and increasing Sylogist's profile across the financial community.

Looking at our business through the highlights of this quarter's financial performance. Q2 has demonstrated again the successful execution of our profitable growth plan. Revenue was $16.7 million, up $2.9 million or 21 percent relative to Q2 2022, and 18 percent on a constant currency basis.

Recurring revenue grew 8 percent, driven by increases in both SaaS subscription revenue and maintenance and support revenues. The increase in Saas revenue was driven by growth in SylogistMission, including implementations and uplift through our SaaS offerings, and strategic growth in our SylogistEd and SylogistGov offerings. The increase in maintenance and support revenues was driven primarily by SylogistService and SylogistMission.

Project services revenue grew by 44 percent, primarily due to customer upgrades and new implementations in SylogistMission. I will point out here that project services revenue attached to our software was at 64 percent, up significantly from 59 percent at the end of Q1 2023.

Our backlog continues to be strong, at $28.9 million, compared to $28.1 million in Q1 '23. Our gross profit margin was 61 percent compared to 60 percent last quarter.

Total Opex was 36 percent in revenue, the same as last quarter. We continue to make investments in our Sales and Marketing teams, with a focus on go-to-market initiatives, including partner-related expansion and enhancement of spending on sales and marketing related events.

Adjusted EBITDA was $4.2 million, resulting in an Adjusted EBITDA margin of 25.7 percent, up from 24.1 percent in Q1 '23. We believe these results demonstrate our strategic ability to continue investing in our business, while at the same time growing in a sustainable way.

Through the combination of an improving EBITDA profile, visibility on our backlog of future revenues, and increased confidence in achieving organic revenue growth in the mid-teens, we expect to see operating leverage and efficiencies of scale by mid-2024.

At the end of Q2, we had $9.8 million in cash, which is in line with the seasonality of our business and our customer renewal cycle. We maintain a strong and disciplined balance sheet, with debt holding steady at $21.2 million.

We will continue to allocate capital in a measured and thoughtful way, and that is through its highest and best use including buying back our stock when advantageous to our shareholders.

With that, I will hand the call back to Bill for some final thoughts. Back to you, Bill.

Bill Wood, President and Chief Executive Officer

Thanks, Sujeet.

In closing, it's said that three data points make a trend. To that end, Sylogist has now posted three consecutive quarters of strong, profitable growth. As a result of the strategic investments we've made, a pivot to a customer-first orientation in everything we do, an unwavering commitment to delivering nothing less than industry-best, highly secure, 100 percent SaaS offerings, and impressively strong execution over the last two years, we've effectively gone from a Company that was backsliding in terms of organic growth, to neutral, to slightly positive, to now, a third quarter of 20 percent organic growth, all while keeping EBITDA margins in the mid-20 percent range.

The scaffolding to support continued profitable growth is in place and we're just hitting our stride. With each passing quarter, we are increasingly better positioned to continue seizing opportunities and to growing both organically and inorganically through strategic acquisitions that make sense and don't necessarily dilute our focus away from the high ROIC organic growth opportunities that we've teed up.

Above all else, the successes we're achieving are a result of having the most experienced, incredibly talented and dedicated Management team in the business. They are the reason the transformation that's taken place over the last two years has happened, and for the material value creation upside headwind.

Delivering results that reflect our commitment to profitable organic growth, disciplined capital allocation, strong self-funding capability, and a rule-of-40+ posture, combined with expanding well-regarded analysts providing third party research coverage and by ratings, we look forward to a strengthening share price that better reflects the results we're delivering and the strong value creation opportunity ahead of us.

I want to end by again personally thanking our customers for their confidence in us, our shareholders for their support, our Board of Directors for their trust and guidance, and every team member at Sylogist for their incredible commitment and energy. I'm extremely proud to represent you every day.

Jen, let's go to the questions, as time allows.

QUESTION AND ANSWER SESSION

Operator

Thank you. (Operator Instructions)

The first question is from Gavin Fairweather from Cormark. Please go ahead.

Gavin Fairweather, Cormark Securities

Oh, hey, good morning. Congrats on the quarter. I just wanted to start out on the recurring revenue line; kind of flat sequentially, although I understand some of the seasonality around the budget cycle.

I guess the question is, what are you hearing from your customers on the availability of budget for the year ahead? What are the spending priorities on their end? Then, what is your pipeline telling you around your ability to accelerate recurring revenue growth?

Bill Wood, President and Chief Executive Officer

Hi, Gavin, good morning. We're not seeing any pullback relative to what we're hearing from prospective customers and customers. The number of RFPs that are being made available in the markets, as well as our positioning in those, is strengthening. Budgets overall, we're feeling very good about their dollars being targeted towards the digital transformational that I talked about previously, and queuing those up for the '24 and '25 year.

That's really reflected in the strength of our pipeline. It's strong or stronger than it's been since I joined, and the blend of deals, in terms of our core focus areas, which is midmarket and upmarket, are perfectly aligned with what we've been trying to do. I think those will matriculate effectively here over the coming quarters.

Gavin Fairweather, Cormark Securities

That's great. Then maybe just on the partner channel, appreciate the commentary in terms of the number of partner-influenced deals. Maybe if you can just speak to where we are in the process of building up that partner channel, how you're attacking partner enablement now, just in general of how that ecosystem is developing?

Bill Wood, President and Chief Executive Officer

Yes. Overall, I give a lot of credit to the team overall in terms of what they've been able to do to identify the kind of partners that we feel are a good fit with us and have roots and relationships in the markets we're looking to expand on and into.

What we have been doing, and I kind of shared this a little bit at Investor Day, is we have developed and refined our own playbook and implementation playbook relative to what we're asking them to spin up on. That is being done by them shadowing us over these first few deals, in combination, so that they understand what our voice is, what our priorities are, and the ability for us to represent our software with them in front of the customer.

The building blocks for the early customers we feel are—for the early partners, are in place, and we see many others that are now knocking on our door with interest out of the Microsoft ecosystem and beyond, to be able to now want to lean in and get access to the availability to represent our solution. We think the foundation that we've laid, the motions that we've put in place that are repeatable, the ability to now have three more resources aligned with the partner channel in terms of sales engineers, relationship managers, to make sure that they have the information that they need to be successful. Then, the ability to, in the near-term, have a dedicated implementation specialist aligned with them that can bring in the appropriate resources to make sure that we're successful.

Gavin Fairweather, Cormark Securities

Okay, great to hear. Then on margins, nice to see the margins bounce back this quarter. Thinking about the commentary that was provided by Sujeet there, should we think about progressive expansion over the back half of the year, or do you really see that reacceleration in operating leverage kicking in, in '24 as you turn on more of these customers in your pipeline now?

Bill Wood, President and Chief Executive Officer

Sujeet, would you like to take that?

Sujeet Kini, Chief Financial Officer

Yes. Sorry, Bill, did you want me to take that?

Bill Wood, President and Chief Executive Officer

Yes, please.

Sujeet Kini, Chief Financial Officer

Yes. Hi, Gavin. Yes. Our general sense is more that the benefits from an operating leverage perspective, as well as gaining the efficiencies of scale where we see more going into 2024, and I mean in a mid-2024, that's our general sense in terms of the efficiencies kicking in.

Gavin Fairweather, Cormark Securities

Okay, I'll re-queue. Thank you.

Operator

Thank you.

The next question is from Parth Shah from Canaccord Genuity. Please go ahead.

Parth Shah, Canaccord Genuity

Hi, good morning and thank you for taking my questions. Nice quarter.

I want to dig a little bit deeper into the pipeline and try and understand to get a sense about how recurring revenue with professional services is trending. Any other colour you can provide there on Mission versus Gov, the mix there? Any colour there would be helpful.

Bill Wood, President and Chief Executive Officer

Yes, I think, Parth, good morning and thank you for joining the call and your question.

We're very pleased with where we are in terms of the project services attachment rate continuing to increase, as we highlighted on this call, to now 64 percent of the overall project services revenue is tied to RFPs. A we mentioned in the prepared remarks, that's a very clear leading indicator of, then the SaaS revenue, which takes a full 12 months to then blossom. The idea of what we're doing in terms of our implementation now, there's an obvious lag at the SaaS provider to be able to get the fulsomeness. If we were selling licenses, it would've all showed up and we would've been able to more clearly associate that dollars with the services, but the indications that we're seeing is a very strong pipeline in terms of our professional services.

The backlog continues to not just grow in a dizzying manner. We need resources, and we've built up to be able to deliver on the backlog that we have. But project services right now are very much tied to the blossoming of our subscription revenue that will come over the next 12 months.

Parth Shah, Canaccord Genuity

That's helpful. Then, maybe a little bit more about, you had mentioned higher win rates. How much of that is RFPs versus greenfield opportunities? I'm guessing there's a bit of comparative displacement there, but any information that you would like to share there?

Bill Wood, President and Chief Executive Officer

We have very few deals that aren't RFP related, Parth. To that end, these are competitive situations. We feel we now are very well-positioned in terms of our full SaaS posture. The integration of our platform and the desirability of Microsoft in our three primary markets, it is turning in our favour, as I mentioned, in terms of the number of Microsoft-originated leads being handed to us, or them walking us into opportunities that they've been nurturing at a much higher rate than we've seen since I joined two-plus years ago.

To that end, I think that's a very good telltale in terms of our overall effectiveness of our marketing strategy driving ICP leads; not just celebrating leads overall, but are they good fits for us, is our messaging right, are the right kind of people knocking on our door and becoming aware of us? I think all those things are going on now at a much higher clip than we've seen in the past.

Parth Shah, Canaccord Genuity

Got it. Then just one last one for me, the North Carolina expansion, any update there? You did mention a few new school districts, but where do you see North Carolina heading, maybe more towards Oklahoma or majority market share there or gradual progress? Thank you.

Bill Wood, President and Chief Executive Officer

Yes, overall, we have solid market share in North Carolina. As some who have been with the story for some time, they were in the process of exiting and going to some other solutions that have been anointed by the state. Well, that's now all been unwound, and to that end, we feel very solid about not only transitioning our existing customer base, but growing new market share in the state of North Carolina because of the, I guess, the credibility that we've earned, as I've said.

We wanted to take it slow there. We wanted to make sure that our successes were clear, and really did not replicate the struggles that a couple of our competitors have faced in that state. That is to our benefit, as now, the state has kind of pulled back on anointing any particular vendor. Actually, we are in very good relationship with the state and with key stakeholders in the state to be able to accelerate now on the back of the new customer that we just lit up on time.

Parth Shah, Canaccord Genuity

Great, thank you and congrats on the quarter. I'll pass the line.

Operator

Thank you.

The next question is from Adam Wilk from Greystone Capital Management. Please go ahead.

Adam Wilk, Greystone Capital Management

Hi, good morning. Thanks for taking my questions—or question, just one for me.

I appreciate the commentary surrounding the opportunity in education. It kind of answers my original question, but wanted to maybe try to drill down on that a little bit more.

Can you maybe quantify the opportunity set at this stage or provide a little more colour on kind of how those talks with various states unfold? Based on the channel checks I've done, it seems like there's pretty significant opportunity, as you mentioned, both in terms of whitespace but also given the struggles of some of your competitors.

I'm wondering if there's—again, the ability, on your end, to quantify that opportunity set or maybe talk about some of the dynamics surrounding how you get your foot in the door or expand your existing customer base over time?

Bill Wood, President and Chief Executive Officer

Hey, good morning, Adam. It's a good question, and one that I'll add a little colour on to the degree that I can.

Our ability to lift and shift from the Oklahoma dominance into another state, we did thoughtfully and actually in a more expansive way than if we were just trying to get to North Carolina well. By that I mean, we took out all the hard wiring that was Oklahoma-specific when we lifted and shifted the code into North Carolina, so that it is now relatively state-agnostic. By that I mean, it's all toggle switches and setup information that, depending on state requirements, reporting requirements, so on and so forth, we now have the ability, without material R&D investment as we made going from Oklahoma to North Carolina, to be able to now have a platform that we can take elsewhere.

I feel very good about how we're positioned. We wanted to prove it out in another state first; not only the software, but our ability to deliver this kind of relationship. That is, a lot of these states have enjoyed with their legacy provider, us being one of them, really, where others that have come in and tried to offer a shiny new object have really struggled, because the idea of delivery, ongoing service relationship with those customers in various states has been weak. It's been something that's created opportunity for us.

Going forward, we already have some customer density in a few other states as a result of our legacy software that exists there. We already have outposts; not nearly to the density of North Carolina, but we have already built a moat around those customers. We expect to build bridges now to those states, and others in that state, where we've assessed the opportunity in those respective states and feel those to be material.

We do have our sights set on two to three additional states in '24 where we'll look to penetrate beyond just North Carolina.

Adam Wilk, Greystone Capital Management

Okay, great, that's helpful. Then as a follow-up, are the education markets similar to other public sector areas where the environment is similarly collegial, or how do you guys look at that, the opportunity across states?

Bill Wood, President and Chief Executive Officer

I think there's always the willingness to share, I think, school districts, by the nature of what they do, as kind of a public and national forum, if you will, of wider state idiosyncrasies. There is an overall initiative at the federal level to make sure that students are learning well and effectively.

To that end, I think that within a state, it's extraordinarily collegial, even maybe more so than states and the non-profit space. It's very much one leads to three, leads to seven, leads to nine. They largely, I think as most of you know, once they are on a new platform and feel that the vendor is providing this kind of relationship and service and partnership that they're looking for, they stay for quite a long time in terms of the stickiness. I'm now talking years. We're sometimes talking decades.

To that end, we feel good about being able to effectively leverage our very high NPS within the Ed space, as it sits right now. It's off the charts, in terms of the relationships and the trust that our customers have with us as being a partner. We think that'll play for us very well as we go forward.

Adam Wilk, Greystone Capital Management

Okay, great. Yes, no, also appreciate the high win rates comment earlier as well, that's great to hear. That's it for me. Great job this quarter and keep up the good work. Thanks.

Bill Wood, President and Chief Executive Officer

Thanks, Adam.

Operator

Thank you. (Operator Instructions)

The next question is from Amr Ezzat from Industrial Alliance. Please go ahead.

Amr Ezzat, Industrial Alliance

Good morning, Bill. Good morning, Sujeet. Thanks for taking my question.

One follow-up on your comments, Bill, in your prepared remarks on R&D spend. Did you say we should expect them to decrease, or are they plateauing?

Bill Wood, President and Chief Executive Officer

Yes, good morning, Amr. Thanks for coming in and joining.

Yes, I used the term at this point, plateauing. I still think there is quarters ahead where we see our R&D and what we want to get done, but we don't see those on the rise and we do see a point in time, as Sujeet has indicated and I did at Investor Day, where we expect those will start to decline as a percentage of overall revenue and leverage that we talked about in '24 starting to materialize.

Amr Ezzat, Industrial Alliance

Fantastic. Decreasing as a percentage of revenues, then the dollar amounts might be the same, is what I understand?

Sujeet Kini, Chief Financial Officer

Yes. Amr, I'll quickly jump in there. That is overall an accurate assessment. In terms of R&D, the one thing I will point out this quarter is we had an element of a true-up on account of additional capital projects identified. There was, if you will, a bit of a trough from an R&D expense perspective, so it will level off going into next quarter. But, the overall sense we have from an R&D perspective is, as a percentage of revenues, it will move downwards.

Amr Ezzat, Industrial Alliance

Okay. Then I've got one that might be tougher for you.

Sujeet Kini, Chief Financial Officer

Mm-hmm.

Amr Ezzat, Industrial Alliance

Appreciate the EBITDA uptick quarter-to-quarter, but if I'm implying correctly, your capitalized software development costs are the highest I've ever seen them, \$1.2 million in the quarter versus last quarter's \$700,000.

I'd like to try to get a sense of what is happening there. How should we expect your capitalized software development costs to evolve over time?

Sujeet Kini, Chief Financial Officer

Right. Maybe if I break it up a little bit; Capex as a percentage of revenue in the coming quarter is around 5 percent. These are trending in the 8 percent to 9 percent in prior quarters. As far as the impact of cap dev, the cap dev credit, product development as a percentage of revenues was in the 12 percent range.

Going forward, our expectation is that the 5 percent that you saw in the current quarter, which I indicated was on account of a true-up relating to additional projects identified, that 5 percent will continue probably in the 7 percent to 8 percent range. It will tick up, or it will go up relative to the 5 percent in the current quarter, but we see it not going up to the levels that we saw at that 9 percent range, if that helps.

Amr Ezzat, Industrial Alliance

Okay. Sorry, so the true-up happens on the expense portion of the R&D as opposed to the capitalized portion?

Sujeet Kini, Chief Financial Officer

Correct, yes. The true-up happens, so essentially R&D costs prior to the application of the cap dev credits, were in the 12 percent range.

Amr Ezzat, Industrial Alliance

Right.

Sujeet Kini, Chief Financial Officer

Basically, there was a true-up on account of additional projects identified. Some of that true-up related back to projects that were started in Q1, and so we did that true-up.

Amr Ezzat, Industrial Alliance

Okay. Maybe we could discuss that offline as well. Appreciate the colour. I'll pass the line.

Operator

Thank you.

There are no further questions at this time. I would like to turn the meeting back over to Mr. Wood.

Bill Wood, President and Chief Executive Officer

I just want to thank you all for your continuing interest and support of our efforts here at Sylogist. We're very excited about the opportunities we see ahead and sincerely appreciate the support, and growing support, for what we're executing on here at the Company. Have a great day. Bye for now.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time, and we thank you for your participation.
