



Investor Briefing - Appendix 4C, Quarterly Update and Reaffirming Guidance

26 April 2017

Start of Transcript

Paul Gordon: Good morning. This is Paul Gordon, Company Secretary for Redbubble Limited. Following the release this morning of Redbubble's quarterly cash flow report, Appendix 4C and press release. I will now hand over to Martin Hosking, CEO, and Chris Nunn, CFO, for an investor update and then question-and-answer session.

Martin Hosking: Thank you, Paul. It is Martin Hosking here. I am delighted to be announcing Redbubble's 4C results for the third quarter of financial year 2017. As has been our practice, we are also providing an unaudited P&L and some brief commentary on business performance and metrics.

Looking at the quarter and year as whole, Redbubble's business is showing a strong growth and defensible position that comes from developing a healthy and vibrant global marketplace. We have seen the operating leverage that we had expected from previous investments and which are a consequence of the healthy marketplace dynamics. Globally, consumers are turning to Redbubble to get products and enjoy a unique experience which they cannot get elsewhere and which cannot be replicated by the traditional online or offline retailers. This experience exists because of the vast breadth of content contributed by artists on Redbubble. In turn, these artists get access to customers through Redbubble which they otherwise could not get.

The health and sheer scale of the marketplace is evident in some basic numbers. 2.8 million customers have bought through the site year to date, and in the third quarter alone customers increased by 36% year-on-year. 200,000 artists year-to-date have sold through the website and in the third quarter the number of selling artists increased by 46%. To give another sense of the breadth of the site, there have been over 140 million visits year-to-date to Redbubble, and in the third quarter visits were up 33.2% year-on-year.

Behind these top-line numbers are compelling metrics, underscoring the robustness of the performance as prior investments deliver what had been expected. Most notably, we have seen strong growth from Redbubble's European language websites. Germany is up 83.6%, Spain is up almost 100% and France is up over 48%. This is despite 5.8% average deterioration in the euro. As we have previously remarked, continued low customer acquisitions mark the Redbubble business model and marketing is only 8.3% of total sales.

Indeed, during the quarter, we saw an improvement in customers coming from unpaid, i.e. free channels, and 58% of GTV, gross transaction value, was sourced from unpaid channels during the quarter. This is up from 56% in the December quarter, and there has been an improvement of 2% in the sources of unpaid free



sources of customers. We have also seen a strong mobile experience and for the first time during the quarter mobile visits were over 50% of total visits.

In the coming quarters, Redbubble will be continuing to invest in the fundamentals of this global marketplace, most notably to deliver a faster or personalised experience of an increasingly loyal and mobile customer and artist base, and at the same time we will be delivering maintaining margins and improving operating expenditure. Given the solid results and looking towards the forecast and with a slight improvement in our expected level of expenses, Redbubble reaffirms the guidance given in our January 4C update, and as outlined in the release.

Many of the headwinds recently faced by Redbubble are subsiding. Since 31 March the Australian dollar has weakened and if sustained, this will eliminate the foreign exchange headwind which has worked against Redbubble's top-line growth for the past 12 months. Margins are being maintained whilst growth in paid marketing and operating expenditures should continue to moderate on the back of the solid marketplace dynamics we have pointed. We expect the operating leverage of the business to be further demonstrated as we move through financial year 2018 and as Redbubble continues to demonstrate the power of the global marketplace serving a unique customer need.

Thank you, and I'll answer questions after Chris provides a little more detail on the financial metrics and numbers. Over to you, Chris.

Chris Nunn: Thanks, Martin and apologies to everyone in advance for my voice, which I'm losing. I'll attempt to keep it for the next five or 10 minutes. I should point out - Martin pointed out that we've included the profit and loss with our announcement, with our 4C release. I should point out at this point that has not been audited, so it will not be until the end of the financial year.

I'll look firstly at that quarterly and year-to-date result referred to in our release and then move briefly to the 4C, pointing out anything there that assists investors' and analysts' understanding of our past and projected cash flow.

GTV came in \$38.2 million for the third quarter representing growth of 35.3% on a constant currency basis over the corresponding period. This is a faster rate than we experienced in the first half of the year, pushing year-to-date GTV up to \$136.7 million and a growth of 32.4% on a constant currency basis.

The gross profit margin of 35.3% year-to-date has continued to strengthen relative to last year despite a slightly weaker third quarter. Redbubble received supplier rebate in the third quarter of FY16 as compensation for failure of one of our power supplies in December 2015. This artificially boosted the quarter's GP margin. The March quarter margin is typically weaker than trend, with an increase in refunds and returns from the holiday



season. We continue to improve product pricing and negotiate better pricing from fulfillers, generating higher product margins whilst returning some of that to customers through promotional strategies.

Paid acquisition costs are growing faster than GTV presently, with the reported transition to mobile visits. However, we saw some stabilisation, as Martin pointed out, in the ratio of unpaid to paid as the third quarter progressed. The cost to acquire a new customer is approximately \$4.80, whilst the initial purchase, I'll say the initial purchase of each new customer delivers on average a gross profit contribution of \$10.20. Gross profit after paid acquisition, referred to as GPAPA, is growing faster year-to-date than GTV growth at 25.8%; that is 36.1% on a constant currency basis. It is also growing faster than the year-to-date operating expenditure at 15.7%, 19.2% on a constant currency basis, showing the emerging operating leverage at current levels of growth investment. Redbubble's operating expenditure includes most of our significant investment in the fourth growth themes presented previously.

Turning briefly to the 4C, it shows our 31 March 2017 cash position is \$31.9 million. Investors and analysts are reminded that due to Redbubble's operating model, significant fulfilment expenses and various sales taxes accrued in the previous quarter's holiday season get paid out during the third quarter. Net operating cash flow for the year to date is negative \$2.4 million. The projected outflows for the next quarter presented in the Appendix 4C reflect our current guidance.

On the subject of guidance, we do expect a slight improvement in the level of operating expenses incurred in FY17 with the full-year outcome likely to be at the lower end of the range of \$44 million to \$45.5 million, please be advised, with a result a small improvement in the bottom-line range from \$5.8 to \$8 million before other non-cash expenses. A minor change there, otherwise we reaffirm that guidance.

Operator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. If you would like to ask a question, please press star-1 on your telephone and wait for your name to be announced. If you need to cancel that request, please press the pound or hash key. Once again, to ask a question it is star-1 on your telephone. Our first question comes from Owen Humphries from Canaccord. Please ask your question.

Owen Humphries: (Canaccord, Analyst) Good day, guys. Congratulations on the quarter, looks like you're seeing that reacceleration in that GTV growth, which is what I've been looking for. Just a couple of quick ones. One that's been quite topical in the market right now is from the 457 visas. Do you guys have any workers or programmers on that visa? Is there any impact on your business in that - on those changes in those initiatives?

Martin Hosking: Owen, it's Martin here. I'm not sure we can comment on detail on that. The workers - we do have people on the 457 visa program. They're in the technical capacity, which has been quarantined from the proposed changes, but we'd obviously want to see the detail of how it works out. We're not expecting any significant impact based upon what the information which has been provided to us so far.



Owen Humphries: (Canaccord, Analyst) Okay, no worries. Maybe just highlight on a couple of your growth initiatives for the next six months or nine months leading into calendar year '17. How many products do you guys now have in the platform and how many are you expecting to end the year on? I use an Android device and have you guys launched an app yet or are you planning to launch an Android app in the interim?

Martin Hosking: Yes. Thanks, Owen, I'll take that. In relation to the products right now, it's 64 products. Is that right, Chris? I think it's 64.

Chris Nunn: It's 64, yes.

Martin Hosking: 63 or 64. We're releasing products slightly at the lower end of expectations, primarily because we have found that work in other areas is delivered at a higher, greater value. Particularly, I would point to the experience which we have had on our European site. This is always a question of where do you devote your resources for maximum bang for the buck, and clearly the strong growth in Europe suggests that that's an area where we should be putting attention in addition, and so hence this has always been a relatively - we reassess where the resources go based upon what we are experiencing.

In relation to the mobile experience, as I've pointed out, the primary - and it will continue for some time - the primary mobile experience for Redbubble will be on the responsive website, which is obviously available on your mobile device regardless of what the mobile device is, and certainly when we talk to consumers, which we do on an incredibly regular basis, they indicate to us that it's a very strong mobile experience on their device.

We have released the iPhone app; that's only now rolling out more globally, and we expect that to accelerate during the course of the year as we get better at the mobile apps, the iPhone app will then - and assuming that's performing well, that would be when we'd be turning to the Android app. But I expect still for a number of years into the future the predominant way in which most Redbubble customers will be accessing Redbubble through the responsive website. The mobile app will only be for the most intensely engaged users. That said, having used the mobile app I am finding it really compelling, as are other consumers who are currently using it. It's certainly showing strong promise but I won't absolutely commit to when we'd launch an Android version at this time, Owen.

Owen Humphries: (Canaccord, Analyst) Okay, no worries. Thanks, Martin. Maybe just quickly can you just update myself and other investors on any changes in the competitive environment that you operate in, if that's possible?



Martin Hosking: Yes. I think it's one of the things which - we haven't seen any significant changes in the competitive environment, it does remain an incredibly challenging thing to launch any significant marketplace at any scale. As we've always pointed to, once established they just are very hard to shift. We have seen Amazon has had - and it's got their Amazon Merch program, all indications we have about that is it's being targeted primarily at the local sports club or people who want to create merchandising which follows from a name related to their particular initiatives, rather than being a competitive marketplace. Clearly they have the capacity, probably, to launch a marketplace, although there are marketplaces that have over the years have been - robustly withstood Amazon much more successfully than traditional e-tailers or retailers, just because they are very hard to dislodge a marketplace once it gets going.

In addition, it is worth pointing out that strong niche plays such as Redbubble, and as has proven in the offline world, also they have an inherent resilience, which means when people are looking for things which are distinctive, which speak to them, Redbubble is a likely place where they will go. When they want to buy toilet paper or books, they'll probably go to Amazon.

Owen Humphries: (Canaccord, Analyst) Great. Thanks, guys, well done.

Operator: The next question comes from Ivor Ries from Morgans Financial. Please ask your question.

Ivor Ries: (Morgans Financial, Analyst) Yes. Good morning to everyone. I would just like to throw a question to Chris Nunn if I could first on the conversion rates. Chris, could you give us the approximate split in conversion rates between desktop and mobile, thanks?

Chris Nunn: What I can tell you is the extent to which they both grew. I don't have the individual numbers in front of me, Ivor, but they both grew about 12% compared to the previous period, corresponding period. The combined growth is 7.5%. I can certainly get those numbers to you.

Ivor Ries: (Morgans Financial, Analyst) Right, okay.

Chris Nunn: The combined growth of 7.5%, and that's because of the mix between the two, but together they both grew about 12% relative to third quarter last year.

Ivor Ries: (Morgans Financial, Analyst) Yes. If you could get those numbers that would be great, that would be very useful. You've mentioned currency impact in the current quarter. Which currency pairs have moved mostly in your favour?



Chris Nunn: Well, if we look at the - in that quarter there wasn't - we still had a pretty significant headwind in that quarter. It's really in the last three or four weeks we've seen the pound has strengthened against - you've got to remember, this is against the Australian dollar a year ago.

Ivor Ries: (Morgans Financial, Analyst) Yes, of course.

Chris Nunn: So the US dollar is pretty much on par now with a year ago. The pound is around about 9% or 10% weaker than it was a year ago, but it has been 20%, up to 20% weaker. The euro is a little bit weaker but not much change.

Ivor Ries: (Morgans Financial, Analyst) Yes. So on a net-net basis in the current quarter if the current exchange rates remain in place you'll have only - I mean I think you're battling sort of an 8%, 9% currency headwind, is that right? So that'll moderate. It'll still be a headwind but it won't be as big as what it was?

Chris Nunn: Yes, I think 8% or 9% is about right in most of the last 12 months. I've been looking at it daily the last few weeks and it's been varying between 2% up and 2% down in the last few weeks. So let's say lie on a par, and I'm talking about a weighted mix with the US dollar being the significant weight, being 60%.

Ivor Ries: (Morgans Financial, Analyst) Yes. I just wonder if you could just give us a bit more colour about the iPhone app. What was the launch date on that, when did you launch that?

Martin Hosking: Yes, it was sort of in beta for quite a while, so I can't say exactly when it was more publicly available, I don't actually have that on the top of my head. Ivor, we're not yet reporting separately on the experience of the mobile, simply because it's price is still - you know, it's still experimental, we're still working out what the best experience is. As soon as we have any data which is worth noting, we will certainly get that to investors.

Analyst - Ivor: Yes. If I may ask one more question. Just in terms of your gross profit margin being just a little bit down relative to PCP, you mentioned earlier that in the previous year there was some sort of - there were some one-off factors there in the previous corresponding quarter. So I'm just wondering what are the factors that you're going to get to take that back to 35%?

Chris Nunn: Ivor, I'm confident enough to say we were running at better than 35% in March.

Ivor Ries: (Morgans Financial, Analyst) Right.



Chris Nunn: So the short-term hiccup, they had a comparison just thrown out by something that happened a year ago. I just wanted to make that clear so people didn't come to the conclusion you've just come to, but I didn't succeed obviously. But, yes, look I'm confident about the margins.

Ivor Ries: (Morgans Financial, Analyst) Great. Just looking at the reacceleration in the growth rate at the top line in traffic, is that due entirely to just greater investment in marketing, or is it due to a whole bunch of other things?

Martin Hosking: Chris, do you want to take that? No, it's not due to investment in marketing, it's primarily out of organic factors that are coming from a whole series of things.

Chris Nunn: Yes, I think it's about organic, or should we say unpaid. The very important metric started that mix between paid and unpaid. Clearly we want to get as much unpaid as possible and that's certainly improved in the quarter.

Ivor Ries: (Morgans Financial, Analyst) Yes, so there's no single factor you can identify that has given you that reacceleration in the growth rate.

Martin Hosking: No, there's no single factor. Obviously European growth has been strong, loyalty measures have been strong, strong performance of repeat customer remarketing through email which is another free source that's been strong. So I think it's a multitude of factors contributing. It just reflects the reality of the business. We invest in things and that's part of the operating expenditure and that then delivers that ongoing - that yields the growth.

Ivor Ries: (Morgans Financial, Analyst) Great, thanks, well done on a really great quarter.

Martin Hosking: Thank you.

Operator: Once again, ladies and gentlemen, if you would like to ask a question, please press star one on your telephone. If there are no further questions, I might hand back to yourself, Martin and Chris, thank you.

Martin Hosking: Look, thank you very much. That's all. Chris is available for a follow-up call if need be, otherwise thank you very much.



Chris Nunn: Yes, if Ivor of any investors wanted to call, I'm here to call. Martin's overseas at present, that's why the sound is different between him and me but I'm happy to take any calls today or tomorrow or anytime.

Operator: Thank you very much. Ladies and gentlemen, that does conclude our conference for today. Thank you very much for your attendance, you may all disconnect.

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