Fluent, Inc.

First Quarter 2022 Earnings Conference Call

May 9, 2022

CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Michael Graham, *Canaccord Genuity*

James Goss, *Barrington Research Associates*

PRESENTATION

Operator

Good afternoon. Thank you for attending the Fluent, Inc. Q1 2022 Earnings Call. My name is Matt and I will be your moderator for today's call.

I would now like to pass the conference over to our host, Dan Barsky with Fluent. Dan, please go ahead.

Dan Barsky

Good afternoon and welcome. Thank you for joining us to discuss our First Quarter 2022 Earnings Results. Joining me today on today's call are Fluent's CEO, Don Patrick; our CFO, Sugandha Khandelwal; and Ryan Schulke, our Co-Founder and Chief Strategy Officer. Our call will begin with comments from Don Patrick and Sugandha Khandelwal followed by a question-and-answer session.

I would like to remind you that today's call is being webcast live and recorded. A replay of the event will be available following the call on our website. To access the webcast, please visit our Investor Relations page on our website, www.fluentco.com.

Before we begin, I would like to advise listeners that certain information discussed by Management during this conference call will contain forward-looking statements which are covered by the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. Any forward-looking statements made during this call speak only as of the date hereof. Actual results could differ materially from those stated or implied by our forward-looking statements due to risks and uncertainties associated with the Company's business. These statements may be identified by words such as expects, plans, projects, could, will, may,

anticipate, believe, should, intend, estimate, and other words of similar meaning. The Company undertakes no obligation to update the information provided on this call. For a discussion of the risks and uncertainties associated with Fluent's business, we encourage you to review the Company's filings with the Securities and Exchange Commission, including the Company's most recent annual report on Form 10-K, and quarterly reports on Form 10-Q.

During the call, we will also present certain non-GAAP financial information relating to media margin, Adjusted EBITDA, and adjusted net income. Management evaluates the financial performance of our business on a variety of indicators, including media margin, Adjusted EBITDA, and adjusted net income. The definitions of these metrics and reconciliations to the most directly comparable GAAP financial measures are provided in the earnings release issued later today.

With that, I'm pleased to introduce Fluent's CEO, Don Patrick.

Don Patrick

Thank you, Dan, and good afternoon. Thanks to all you for joining our call today. I'm here together with Ryan Schulke, our Chief Strategy Officer, Chairman of the Board and Company Founder, and Sugandha Khandelwal, our Chief Financial Officer.

Our first quarter results are consistent with what we articulated in our 2021 year-end earnings release, and represent the continued progress we're making towards our long term strategic growth plan focused on building high quality digital experiences for consumers who are creating more effective, efficient and sustainable customer acquisition solution for marketers. We continue to invest in strategic platforms and we remain confident that as we establish Fluent's presence and gain market share, we'll also be able to expand our margin over time by way of our operational capabilities.

In Q1 2022, our financial results were as follows: revenue of $89.1 million represents 27% year-over-year growth and is a positive reflection of prioritizing our long term growth strategies. We continue to lean into opportunities where we can establish and leverage Fluent's brand credentials in the marketplace. Our media margin of $26 million is up 4% year-over-year at 29.1% of revenue. This reflects our ongoing strategic investments focused on expanding our media footprint. And Adjusted EBITDA of $4.8 million represents 5.3% of revenue.

As we've consistently stated throughout 2021, our strategic growth plan is focused squarely on consumers and the quality of their experience in a performance marketplace. We believe this consumer-centric strategy represents the winning road forward and provides us competitive advantage. Fluent inherent brand strength and a foundational principle of our business model is creating a more effective and sustainable customer acquisition solutions for our clients, while successfully positioning Fluent as a market leader in a rapidly evolving industry environment.

A strategic growth plan, along with our ferocious appetite to test and learn has validated two major hypotheses. First, delivering consumers more meaningful, quality grounded experiences has enabled Fluent to more frequently reengage them after their initial visits to our owned and operated media properties, all based on their needs and wants. In turn, we're enhancing consumer lifetime value for clients, as well as Fluent.

Second, as we connect a more engaged consumer to our clients' brand platform it enables us to more efficiently and effectively deliver against our clients' customer acquisition goals, while improving their ROI. In turn, our total alignment with consumers and clients is driving improved monetization across our Fluent performance marketplace, while enhancing our brand equity with clients.

We will continue to focus on revenue growth leaning into a variety of strategic growth initiatives that we believe are sustainable. As we continue to learn, evolve and scorecard our business initiatives, we also assess where we believe we have the competitive advantage, utilizing market share gain as a consumer validator of our longer term potential. We believe this is the road to strategic revenue growth and opens the door for expanding margins over time. So in the near term, our quarterly margin profile will reflect our strategic investments in growth.

As we consistently articulated, Fluent's competitive advantage is grounded in three strategic growth pillars: our media footprint; our platform and our performance marketplace. Strengthening our go-to-market capabilities with each individual pillar is our everyday mission. While Fluent is differentiated it is building out our preferred market, while determining a logical point of intersection across each strategic pillar, with an operation scale for growth, saw enhancing client performance here across functional team play. The end result is exceeding clients' performance expectations by way of delivering a more targeted and engaged consumer audience, which also increases client ROI.

In the past, we've discussed our media footprint and performance marketplace. Today, I'll spend a little bit more time on our platform and strategic relevance. Our platform at its highest level is a proprietary and integrated data, analytics and technology marketing solutions and capabilities. We previously outlined investments we made to expand and strengthen our marketing position. At the core is our first party data asset, which given the ongoing and well documented data privacy changes, is designed to provide a significant competitive advantage in delivering higher quality, interactions and value for consumers and clients within our performance marketplace.

Apple's move to enhanced consumer privacy on its devices and Google's announcement of 2023 being the year to end third party cookies, this is forcing marketers to take action shifting away from third party data. Data from outside sources can improve short term performance and marketing but, unlike first party data, can't explain the relationship with consumers in their path to purchase. The breadth and depth of Fluent's first party data gives us an important advantage that it offers the kind of insight that give us real control over our long term strategic growth plan.

The power of our first party data and our ability to gather and enable real time insights through analytics and technology is critical to driving meaningful, higher quality consumer engagements tied to measurable performance-based outcomes. When a new consumer visits the property within Fluent's digital media portfolio, we ask simple questions to determine individual interests, needs and preferences and then present relevant offers from our world class clients, ultimately creating a more meaningful and rewarding experience. When a consumer returns, they proactively enable us with their prior survey responses and performance marketplace experience, which allows us to utilize these key insights as the strategy of strength and relevancy and improve consumer engagement. In essence. increasing lifetime value. In this manner the consumer wins as does our roster of clients.

As you can see, our platform is foundational, and we believe it's a clear competitive advantage that differentiates us in the industry. Our platform efficiently and effectively connects our media footprint with our performance marketplace. In turn, we've established Fluent capability that solves the marketing (inaudible) every advertiser chases, delivering the right offer at the right time to the right consumer and in real time with the convenience of automation. Over time, as our media footprint and performance marketplace strengthen and expand, our platform is strategically positioned to drive long term value to consumers and our clients, which represents the key revenue and margin path to our operating business units.

Given the strategic value data plays within our ecosystem, we recently completed our Q1 data evaluation with Truthset, who measures data accuracy in several popular demographic attributes and provide scoring against their current cohort of data providers. Across 19 top tier data providers including Acxiom,

Epsilon, B12 (phon) and Data Axle, Fluent ranked number one for accuracy and more attributes than any other data provider except one. The accuracy of our first party data is a reflection of higher quality consumer experiences in the Fluent marketplace and further enhances our relationship with them, while enabling us to competitively leverage relevant strategic insights with our clients.

In Q1, we were also encouraged by our continued progress with our other two strategic growth pillars: our media footprint and our performance marketplace. We're actively expanding our media footprint via strategic growth initiatives that extend and reach into new media channels, where we can provide more relevant content and offers to consumers and our clients. This leaves us strategically and financially motivated as we explore longer term growth opportunities that a larger Fluent media footprint will create, while we concurrently extend our reach into new media channels. We'll discuss this further as we learn more.

Relative to our performance marketplace, our key strategic growth initiatives continue to primarily be driven by building out Fluent sales solutions, and separately, our CRM capabilities, both of which are grounded in higher quality consumer experiences. These strategic initiatives provide a significant marketplace and creating meaningful downstream experiences for consumers, while expanding our relationship with world class clients in key industry verticals.

Critically inherent to our strategic framework is that we're enhancing each consumer's lifetime value. More to follow here in subsequent quarters.

In closing, we remain fixated on our well defined pillars and we will continue leaning into strategically compelling 2022 revenue opportunities where we believe we have a differentiated position and significant consumer runway. Earning market share where we can leverage our consumer-centric core and execute via our operation capabilities will be the key driver of our longer term growth agenda.

These are the strategic bets we are constantly making, prudently investing as we launch and establish our longer term path in a growing marketplace. In parallel, we'll manage the business mix across our investment profiles with a clear goal of expanding Fluent business margins as we scale and establish a competitive advantage.

Overall, we believe our 2022 financial results will show revenue growth returning at or above industry growth rates and require priority number one. We are then shifting our sights on sequential margin improvement as we scale.

And with that, I'll turn to Sugandha to provide more details on our financial results.

Sugandha Khandelwal

Thank you, Don, and good afternoon to everyone. We are pleased with strong first quarter results and continued momentum in the business as we execute on the fundamentals and progress with our strategy.

(Inaudible) first party data assets and strong advertiser relationships have put us in a great competitive position. The Q1 results builds on the momentum that we saw as we closed 2021 in terms of progress against both our strategic and operational priorities. In the first quarter, Fluent generated $89.1 million of revenue, up 27% year-over-year, and above the guidance that we provided in the previous earnings call. This growth was driven by three primary areas.

Firstly, we saw significant strength in our core rewards business, driven by expanding our media footprint in both the U.S. and international markets. Rewards is the largest piece of the Fluent business and our portfolio includes websites in the U.S., U.K., Canada, Australia, as well as the mobile app. Millions of

consumers visit our rewarded (phon) properties everyday to discover products and offers while earning rewards and we are encouraged by the strong top line growth from our rewarded properties.

And the second area of growth in the first quarter was our internal CRM capability, primarily emails and SMS, which enables us to reengage consumers who have already registered on our own media properties and enhance their overall lifetime value.

Lastly, Fluent sales solutions remains a strategic priority for us and continues to be a key growth driver. Through this live agent capability, we are now able to drive new demand across different industry verticals and high (inaudible) categories, (inaudible) the use of contracted call center personnel.

As a part of the traffic quality initiative, (inaudible) strategic and deliberate approach and building high quality targeted media traffic by reducing the volume of lower quality traffic. While we are conscious (inaudible) quality will reduce our traffic volume, we are pleased. But a monetization increase almost 50% in Q1 as compared to the same quarter last year, that supported the strong double digit revenue growth.

Our media margin in Q1 was $26 million, up 4% year-over-year and representing 29.1% of revenue. For context, we spent nearly $63 million on paid media in the quarter, our largest cost component. In the course of deploying the media spend, we found success with new promotional campaigns, which expanded our addressable audience and new means of cross-promoting our program across Fluent's own media properties.

On the last earnings call, we noted the opportunity to drive high quality traffic from variable (phon) platform, albeit at margin levels below the affiliate side of our media mix. While we expect this mix shift to digital media platform to continue in the near future, we remain confident in our ability to optimize our spend level and ultimately drive higher profitability over time.

Our operating expenses on a GAAP basis for Q1, comprising sales and marketing, product development and G&A, grew in aggregate by $1.6 million or 8.8% year-over-year to $19.7 million. Within that mix, sales and marketing increased by $900,000, driven largely by an increase in business travel, events and in-person meetings. Our product development expense increased by $1.1 million, reflecting continued investments that we made in our technology and analytics platform, as well as development of new ad based media properties expanding beyond our traditional focus on (inaudible) media properties.

Lastly, our G&A expense came down by $400,000. The decrease was mainly a result of an accrued expense for put call consideration related to the Winopoly acquisition during the first quarter of 2021 that did not exist in the first quarter of this year. This G&A expense is offset partially by increased litigation cost and certain acquisition related costs. On March 31, 2022 we reached a settlement with the New York State Department of Taxation and Finance regarding sales (inaudible) of $1.65 million. The amount was paid to the tax department on April 1, 2022. Our accrual increased from $823,000 in the fourth quarter of 2021 to $1.65 million, resulting in an incremental expense of $827,000 in Q1.

Finally, on profitability, our Adjusted EBITDA for the first quarter was $4.8 million, representing 5.3% of revenue and up 0.5% year-over-year. This is higher than the outlook we provided at our last earnings call and it's driven largely by the benefit we saw on media margins. Moving forward, we will continue to focus on driving revenue growth and market share gains, while maintaining a disciplined approach to overall operating expenses, turning (phon) revenue down to the bottom line.

Our interest expense declined by $600,000 year-over-year, benefiting from the lower cost of debt under our new credit facility. In Q1, we continue to be a non-cash federal taxpayer, due to the availability of NOLs.

We reported GAAP net loss of $2 million in the quarter and adjusted net income, a non-GAAP measure, of $1.1 million. As a reminder, our non-GAAP metrics are reconciled in the earnings release and our 10-Q filings.

Turning to the balance sheet, we ended the quarter with $29 million of cash and cash equivalents. This represents a decrease of 12% year-over-year. Working capital, defined as current assets minus current liabilities, ended the quarter at $46.6 million, up 1.7% year-over-year. Total debt, as reflected on the balance sheet, ended the quarter at $47 million. Again, we are pleased with the first quarter results and feel good about the underlying strength of our business.

Our leadership team has a number of exciting strategic initiatives currently underway that will allow us to differentiate ourselves and enhance Fluent's value proposition and generate a strong revenue and earnings profile.

Thank you for your time. We are glad to take questions now.

Operator

The first question is from Michael Graham with Canaccord. Your line is now open.

Michael Graham

Thanks a lot. And hey, everyone. Thanks for all the good information on the call there. I wanted to ask a couple of questions, if I could. The first one is just, it seems like on your traffic quality initiative, it seems like you're still getting some good benefits from that. Can you just maybe provide a little context on, like where you think we are there in terms of the evolution of that footprint? And then I have one other one.

Don Patrick

Thanks, Michael. Thanks for the question. The TQI is something that we're over a year into and it originally started around the traffic and around the quality of that. It is something that we originally thought was going to be a project for about a year and then we move on from that. Actually, we've seen such strong benefits from it in our business that at this point its embedded into our core operating principles. And the quality of the traffic is paying dividends, both with our clients from an ROI perspective and is equally important in our monetization side.

So we continue to work with the partners aggressively to continue to improve their quality so we can drive better results for our clients and better results for us. So I feel good about where we are from a foundational perspective, but there's still a lot of opportunity around the monetization side that we think we can play into.

Michael Graham

Great. Thanks, Don. That makes sense. I also just wanted to ask about CTV more broadly and such a dynamic area, and I just want to kind of get some updates from you in terms of, like how it's going? How it's impacting kind of your business model going forward?

Don Patrick

Michael, I'll turn over to Ryan who's been leading that effort for us. So thanks for the question.

Ryan Schulke

Yes, Michael, in terms of channel expansion, connected TV and other mediums where we can go out and utilize our first party data and everything that comes with that strength is very, very attractive to us. TV is a new format for us where we're testing and learning as we go here, but seeing some really interesting performance trends as we start to apply some of the best practices driven approaches from the digital world into places like connected TV and start to learn more on the creative side how that will influence things.

So it's still very new, but exciting for us, exciting for our partners. This type of traffic is coming in at a different quality profile. We're seeing different types of behavioral trends just with somebody that's coming off of these new types of mediums that we're testing into. So it certainly is something we're optimistic about growing as we roll on here.

Michael Graham

All right. Awesome. Thanks, Ryan. And I'll go back in the queue guys. Thank you.

Don Patrick

Thanks, Michael.

Operator

Thank you. The next question is from Jim Goss with Barrington Research. Your line is now open.

James Goss

Okay. Thanks. I've got a couple. First, it seems that the initiative involves sort of reducing the number of overall clients to favor quality over quantity. If that's the correct assumption, please tell me that? And is there a way to scale just how many points of contact you have right now relative to how many you did have and where that would be headed?

Don Patrick

Thanks, Jim. So you're asking about reducing the number of clients. It's clients and not consumers, is that your question's about?

James Goss

Yes. Well, the consumer—the ones you are targeting, not the business clients, but the individuals you are targeting.

Don Patrick

Yes. It's a great—it's a good question, Jim. Thanks. There's multiple pieces to answer here so I'll sort of walk through a couple. First is, as we've talked about before there's when the consumer first comes onto our properties, and then it's how long and the lifetime value that we have in terms of our relationship with them. So one of the things that we've been talking about now for a little over year is all our CRM efforts and our ability to build the consumer journey and extend that in a much longer time period than it is traditionally been at Fluent. So although there might be less overall consumers coming in, the number of consumers that are on our properties every single day has continued to increase.

The second big thing is, we've talked about in terms of just when they're on our websites and they're on our digital properties how many interactions are we having with them, and what can we do with those interactions with our first party data? So, we have millions of site interactions per day, we have hundreds and thousands of campaigns interactions per day and we use that data to make it more relevant for the consumer and obviously drive better ROI for our clients. So it's more about the quality and the lifetime value that's been extended.

The second piece I'd answer Jim is, we've been extending our, what I'll call, our media footprint and our pillar. And that is, it's not only on sort of the traditional web-based properties, but we've been expanding internationally, we've been expanding with mobile apps, we've been expanding with other properties like jobs and expanding that also allows us to continue to drive the consumers and the amount that we have in and also the interactions that we have with them.

James Goss

Okay. And are you looking to sort of maintain more of a continuous—continuing relationship with these clients? And how do you effectively make that happen?

Don Patrick

Absolutely. We are looking to maintain and continue to leverage that over a longer time period. That is defined by the engagement that we have with the consumers and the value that they're getting out of it. So a key piece of our fundamental business proposition is that, when the consumers come onto to our digital properties, how relevant is that and how engaging is that to the needs and wants at that time when they're on our property. So the way we sort of measure that is around how often they're coming back, what their monetization, what verticals they are interested in and the length of time in which we are able to work with them, whether it's thirty days, sixty days, three years, five years, that's the measurements that we're looking at now, Jim.

James Goss

Okay. Last thing for me. You made the comment about accuracy of first party data. And I was just wondering how is that measured in back home?

Don Patrick

The example we gave in the earnings release is a third party evaluation company called Truthset. They do it quarterly and they pull cohorts together, they volunteer people, they ask data providers to come in and they independently value, independently rank the data providers based on the data that comes in, how accurate it is based on external sources. So it's independent. And as I said, we ranked first in more categories than everyone else except one. And the names we are going against are very longstanding data providers that have been in this business for a real long time. So I think it tells you the power that as they come onto to our properties of declared data, its first party and the relevancy of us being able to use that to provide meaningful experiences to them allows them to continue to interact with us and give more insight into what they like to see and what they like to be engaged with.

James Goss

Okay. Thank you very much. Appreciate it.

Don Patrick

Thanks Jim.

Operator

Thank you for your question. There are currently no further questions registered. The next question is a follow up from Michael Graham. Your line is now open.

Michael Graham

Yes. Thanks. I just wanted to slip in one more. You mentioned your sales capabilities, and kind of expanding those, and I just wonder if you could put any kind of framework around the magnitude of that effort and what it looks like over the next year or so?

Don Patrick

Sure. Thanks, Michael. We continue to see strong growth in the Fluent Sale Solutions Group and the Q1 was certainly another very strong quarter for us. The way we talked about it last time is that we really lean heavily into the health vertical. And then in Q1 we got into the life insurance. And then right now, we're really spinning up our third vertical, which is around auto. The one big difference that we talked about is our competitors then take a sales approach to the business. They look at the demand and they say how do I get the supply for it. We're taking a very consumer-centric approach here. We look at the audiences and we look at our consumers on our digital properties. And they would say, how can we build the right audience and connect them to the world class brand?

So we will not be the biggest, but we certainly think our quality and our consumer experience would be the best. So we did grow double digits, we continue to look to have double digit growth on the top end side throughout 2022 and it's going to be mostly around building out the new verticals, getting the marketplace right and continuing to drive that value within those core verticals. So you'll see another vertical in Q3. And as we continue to test and learn, you'll see another one in Q4. So we're being very methodical on how we grow those out.

Michael Graham

All right. Thanks a lot Don.

Don Patrick

Thanks, Michael.

Operator

Thank you for your question. There are no additional questions waiting at this time. So I will pass the conference over to the Management team for closing remarks.

Don Patrick

I want to thank everyone for joining us today. The earnings release will be out shortly. And thank you very much for your support and your questions.

Operator

That concludes the Fluent, Inc. Q1 2022 Earnings call. Thank you for your participation. You may now disconnect your lines.