Q3 2023 Q&A Transcript

Introduction [Monica Webb, Vice President, Investor Relations]

Welcome to Tucows' question and answer dialogue for Q3 2023. Elliot Noss, President and Chief Executive Officer, will be responding to your questions. For your convenience, this audio file is also available as a transcript in the Investors section of our website, along with our Q3 2023 Financial Results and updated reports. I would also like to remind investors that if you would like to receive our quarterly reports and Q&A via email, please make the request to ir@tucows.com.

Please note that the following discussion may include forward-looking statements which are subject to risks and uncertainties that could cause actual results to differ materially. These risk factors are described in detail in the company's documents filed with the SEC, specifically the most recent reports on the Forms 10-Q and 10-K. The company urges you to read its security filings for a full description of the risk factors applicable to its business.

Today's commentary includes responses to questions submitted to us following the prerecorded management remarks regarding the quarter and outlook for the Company. We are grouping similar questions into categories that we feel are addressing common queries. If your questions reach a certain threshold or volume, we may ask you to schedule a call instead to ensure we can address the full body of your questions. And if you feel that the recorded questions and/or any direct email you may receive do not address the full meat of your questions, please let us know.

Go ahead, Elliot.

Opening Remarks [Elliot Noss, President and Chief Executive Officer]

Thank you, Monica. And welcome to our Q&A for our third quarter 2023 financial results.

First, we had a question on the 10-year runway of payments for Ting subscribers in the DISH contract. We have said a few times that the easiest way to model these payments was to impute a churn rate with no replacement. We note that in any subscription business, churn generally improves as a cohort ages. We also note that this "bet" we made by taking this approach to dealing with our MVNO subs has to be considered a win at this point. It also further reflects the strength of the Tucows-DISH relationship in that they accommodated an unconventional approach.

We had a related question for the TCX segment on our legacy Ting MVNO contractual obligations to Verizon. We have said many times: We priced this into the deal with DISH. And we are making lemonade out of lemons by using the Verizon mobile contract to reduce churn and attract new subscribers in Ting towns. We launched and are in the process of ramping up marketing for a $10/month unlimited product, which is THE best offering in the U.S. We will certainly be doing our best to use all of the commitment and more, turning a fallow asset into strategic marketing. There is not a material shortfall this year. Of course, you should expect us to budget conservatively as we provide ’24 guidance next quarter.

Given its strong performance this quarter, we had a couple questions about Wavelo. The first one was on the future of one-off and nonrecurring revenues that Wavelo incurs for professional services that typically involve creating features for new and generally larger customers. Because that work is driven by the timing of bringing on new customers, and the complexity of the features needed, that work and the associated revenues will be highly dependent on the Wavelo pipeline and will ebb and flow as we onboard new customers. So the amount of professional services and timing is difficult to predict, but we will scale when and as needed to deliver on new features and customizations. One other thing to note about our mix of recurring to one-time revenue is that it is well above industry norms because of our per-subscriber SaaS pricing model and go-to-market strategy of being customer centric in an industry that is obsessed with professional services revenues.

The second question was around our expectations for Wavelo’s profitability and EBITDA without further clients. We can maintain the level of profitability, but for business growth, we need new clients. And for new clients, we will need to invest in our go-to-market efforts. This is a balance all companies must strike.

We had a question about the impact of our Memphis partner market on short- to mid-term EBITDA. As always, the appeal of being a tenant on a network rather than the owner is the significantly reduced capital investment. With partner markets, the atomic unit—the cost of marketing and onboarding relative to long-term customer value—is the most important measure. Sometimes, that will also include installation cost depending on the specific partner deal. Of course, those costs are borne up front, and the revenue is collected over time, as with any other subscription business. And with the Memphis agreement with Blue Suede Networks, a Meridiam company, we have terms that are more cash-flow friendly for Ting in the short term while we’re investing in marketing and onboarding. That investment is expected to have a small negative impact on EBITDA through the next couple of years.

We had questions about Ting EBITDA more generally. First, I want to stress and remind you that the current EBITDA loss is associated with building the machine and loading the network.

In terms of when Ting will be profitable, I think the first, most important thing I can say is that a north of $40 million operating loss is not consistent with any of what I have been saying for the last couple of quarters. Without providing specifics—and of course we will provide guidance for 2024 as we usually do next quarter—we intend to address the size of the loss. This can be done operationally or structurally or both. We have been clear that we want to get to cash across all of our businesses. We have been clear that they are all performing strongly.

With Ting specifically, we have tried in our ongoing disclosure and in detail at our Investor Day in May to demonstrate that the business is profitable when looking at the atomic unit, when looking at it on a town level and when looking at it on the level of a fully run-out model. A lot of this work is available in the archives.

Providing further detail prior to announcing anything would compromise our ability to keep all our options open. We appreciate and understand how investors feel about an operating loss that big. We share their feelings. Most importantly, the coax-to-fiber transition in the U.S. presents a multigenerational business opportunity that matches our particular operating strengths to a T. And we need to pursue that opportunity in a way that is responsible. Being able to balance long-term growth with short-term profitability is a huge challenge for any CEO. It is particularly challenging with an opportunity this large and this capital intensive in this macro environment. We have tools at our disposal, and we intend to use them.

Thank you for listening to our Q&A and a reminder that if you feel that the recorded answers or any direct email you may receive do not address your question, please follow up with us at ir@tucows.com.

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