

APPENDIX 4C REPORT AND HALF YEAR UPDATE

TRANSCRIPT OF CONFERENCE CALL

REDBUBBLE GROUP ACHIEVES POSITIVE OPERATING EBITDA DELIVERING RESULTS FROM STRATEGY WITH MEMBER GROWTH, IMPROVING MARGINS AND TEEPUBLIC ACCRETION

29 January 2019

Start of Transcript

Paul Gordon: Good morning all, this is Paul Gordon, Company Secretary for Redbubble. Welcome to this teleconference for Redbubble's second quarter results for financial year 2019 and first half year update. With me I have Redbubble's CEO, Barry Newstead and CFO, Chris Nunn. Redbubble released its second quarter results Appendix 4C to the market in an ASX announcement earlier this morning, along with a half year update. Barry and Chris will present before we open up the floor to questions. This presentation and Q&A session are being recorded.

Now before we start, I would like to call your attention to the safe harbour statement regarding forward-looking information in the ASX release accompanying the Redbubble results. That safe harbour statement also applies to this call and Q&A. Over to you, Barry.

Barry Newstead: Thank you, Paul. Happy new year, hope everyone had a good holiday season and wish you all a healthy and happy 2019. Today we are providing an update to the market on the results for July to December 2018, the first half of financial year 2019. The key information is in the ASX release, the 4C filing and the supporting presentation. We have updated our reports to reflect the integration of TeePublic into what we will refer to as the RB Group. Throughout the call we will talk mostly about RB Group metrics and where we refer to one or the other marketplaces, we will refer to Redbubble or TeePublic as relevant.

I'd like to kick off today's call by reiterating the strategic opportunity that motivates the RB Group. RB Group has been building leading global marketplaces for independent artists for close to 12 years and we are still in the early days of achieving the revolutionary potential of our platform. The retail commerce opportunity in front of us is an immense one, worth over \$250 billion. The huge potential market we are seeking to disrupt is central to our strategic decision making.

At the core, RB Group is creating a new kind of retail commerce for customers. The RB Group offers its customers personalised, creative adventures and delightful service for a range of quality products. This



experience is in contrast to the sea of bland, undifferentiated product options available from many other consumer retail businesses today.

Across both Redbubble and TeePublic, customers are going on creative adventures, leading to an often surprising treasure in the content discovered. This is how customers describe the experience whenever we interview them. They relish the human connection to independent artists who create truly unexpected content, which turns generic products into canvases for self-expression and meaningful gifting. How many retail experiences enable 279,000 selling artists the opportunity to shape the customer experience through their creativity and earn income from this?

Redbubble is an emotive brand experience, which has the potential for real stickiness. This will emerge fully as personalisation is rolled out in the customer experience and it is reflected in our marketing activities. It will take deep hold as artists and customers connect with each other on the human level. In addition, RB Group delivers delightful and consistent service across a wide array of apparel, home and lifestyle products. They're affordable and made-to-order geographically close to customers.

As we grow the supply model offers the potential to be as efficient as the best functioning retail supply chains, with a much smaller environmental footprint. Our partners are investing alongside us as we grow. There were 3.3 million customers who experienced what the RB Group has to offer over the past six months and an increasing number are members and/or repeat customers. In fact, repeat customer Revenue grew 36% year-on-year. The RB Group strategy is to deliver on the differentiated customer value proposition through creating a personalised member experience for customers. This is enabled by the marketplace flywheel and the network effects of market leadership.

In addition to the customer experience, the strategy aims to drive content growth from artist engagement, new products and content partnerships alongside fulfilment and operational scaling. We have seen traction in the content partnership space, having invested in content management and enforcement tools and building relationships with licence holders. We are now hosting 16 brands in our licensed fan art portfolio, including the initial launch of Cartoon Network partnerships over the past quarter. Whilst there are typically longer sales cycles and we remain in the early stages of a lot of opportunity, our fan art team is making good progress.

The momentum of the flywheel underpins RB Group's ability to solidify growth and profitability and extend our market leadership position. Over the past six months RB Group has delivered on three strategic and investment areas that support continued marketplace growth.

First, we have been building the core member experience on mobile web and via Redbubble's iOS app. This work has and will remain a priority. Over the past six months, Marketplace Revenue from members grew 113%, reaching 25% of total RB Group Marketplace Revenue. Active members grew 61% to 3.1 million. Members are a powerful accelerator to the marketplace beyond the sales value they generate. They provide valuable data signals and diversify Revenue away from paid and search channels. They are great brand ambassadors and help inspire the artist community and partners.

The second strategic area of focus is on realising the benefits of scale in the marketplace and extracting economies of scale across a number of operating areas: customer support, infrastructure costs and supply chain management as examples. We saw strengthening margins and maintained operating leverage across the Group in the last six months. On Redbubble, this has been achieved while improving customer net promoter score and reducing shipping time for customers.

Finally, with the acquisition of TeePublic, we solidified RB Group's leadership position in North America, accelerate the benefits of scale and enable highly aligned sister marketplaces to cross-pollinate learnings, whilst positioning towards different segments. TeePublic has already made valuable contribution to RB Group's financial performance, including insights used to enhance Redbubble's performance over the last quarter. The integration is progressing smoothly.

Before I hand over to Chris, I'd like to talk briefly about the financial performance of the business. Clearly the changes to Google search algorithm in October has been an external factor that slowed growth in the past quarter. The changes were in no way disastrous as year-on-year growth in the channel remains positive. While RB Group continues to diversify our channels of growth as it has done for several years, organic search remains an important source of traffic and customer acquisition.

As discussed in November, we have a number of areas where we have made improvements and several additional areas where work is ongoing. The exact timing of when the benefits will emerge remains uncertain, but as in the past, we are confident that RB Group's unique content and customer experience will again position us for success in organic search and we'll also continue to diversify our channels with a priority focus on membership, including app growth.

Over the past three months, the team has focused across the P&L to deliver the results you see today. We did not achieve the Revenue growth we had aspired to, but we focused on what we could control and showed the progress of this business in a range of areas by delivering profitable paid channel Revenue, excellent gross margins and disciplined control of the operating expense line. We remain on the strategic path with steely resolve to focus on generating value from our efforts and continue to invest in the major areas that will position Redbubble to capture the large market opportunity that is available as we invest in our differentiated customer experience and marketplace flywheel.

I will now pass on to Chris to speak more about the financial performance of RB Group and our expectations for the group in FY19. Chris.

Chris Nunn: Thank you Barry. As has been our practice, we have included with our 4C release for the December quarter an income statement for the quarter and the first half as a whole, down to the EBITDA level, comparing both with the corresponding periods last financial year. TeePublic has been included for the last two months of the second quarter and first half. Whilst we do not expect there to be significant variances, all financial figures in



this release remain subject to half year audit review. Final first half results will be released with the Appendix 4D in February.

In the supporting pack, we have also provided some new key operating metrics and, as Barry mentioned, they reflect a refreshed view of how RB Group is managed. Management believes they are more appropriate for tracking the company's strategy and its progress towards building a business of enduring value.

Management is pleased with the improving P&L delivered in the first half. We have been able to actively manage those elements we can control in a way that has and will continue to mitigate the effect of any ongoing organic search weakness. Gross profit margin in particular is strong and we see continuing upside that will enable us to balance margin improvements with growth objectives.

At the top line, RB Group Marketplace Revenue, formerly known as product and shipping Revenue, so not including artists' Revenue, was \$142.6 million for the first half, up 39.4%, that is up 31.4% on a constant currency basis. FX has been a significant factor this year so far with the US dollar in particular generally in the range of 6% to 10% stronger than the previous first half. This helps our Revenue line but does the opposite, of course, at the cost lines of COGS, paid marketing and operating expenses. For Redbubble, the net impact of FX on EBITDA has been a positive \$700,000 in the first half.

A strong first quarter FY2019 performance by Redbubble was followed by weaker Revenue growth in the second quarter due to the impact of the organic search sales weakness. TeePublic maintained strong growth across the first half. Group Revenue growth overall was supported by the strength and efficiency in paid channels on both platforms. As I will expand on below, the cost of paid Revenue continues to be efficient and very profitable.

In the accompanying investor deck at slide 8, we have shown the respective year-on-year Revenue growth rates of the two RB Group platforms. Both have been impacted by weaker organic search, although it is more pronounced in Redbubble's case. Over time we expect to merge financial metrics across the RB Group, although anticipate continuing to show Revenue growth by platform.

On that point, we have moved our disclosure away from GTV towards Revenue, which is a better indicator of Redbubble's top line financial performance. GTV has become increasingly distorted as a true measure of growth as we have progressively begun to collect sales taxes in more and more US states. From collecting only in California six months ago, we now collect in 23 states and even then, this is only half way to what we expect will be the ultimate position by the end of calendar year 2019. Whilst it is hard to isolate, our analysis suggests the impact of the sales tax impost on growth has been negligible. There is, in fact, some upside in that it further enhances the strong working capital advantage we generate from our model as we grow.

As I mentioned, gross margins strengthened across the RB Group (that is both brands, but Redbubble in particular), through the combination of strategic pricing work and the flow-through of fulfilment and shipping cost reduction that result from RB Group's supply chain strategy. The synergies to be extracted are a continuing



testament to the benefits of RB Group's increasing scale and the power of our market position. RB Group delivered gross profit of \$51.9 million in the first half of FY19, up 47.1% (up 38.5% on a constant currency basis). This contributed to gross profit margin of 36.4% based on Marketplace Revenue, which represents a 1.9 percentage point improvement on the gross profit margin for the first half of last financial year. Redbubble brand itself delivered 1.7 percentage points with the rest due to TeePublic's contribution of a higher underlying margin.

As I mentioned earlier, paid channels have been a significant driver of growth, particularly in the second quarter. The paid percentage contribution to GTV was 50%, up from around 43% in the first half of the last financial year, largely reflecting organic's weakness but also paid's strength. Throughout the challenging second quarter, management maintained a disciplined approach to sourcing sales from paid channels and did not ramp up expenditure at the expense of efficiency.

When measured as a percentage of Marketplace Revenue, RB Group's cost of acquisition continues to be low compared to other online marketplaces or platform peers in a similar stage of life to RB Group, even with the weaker unpaid growth. It was 10.4% of Marketplace Revenue in the first half, up 1.6 percentage points year-on-year. Redbubble's cost of acquisition remains constant at 10.9% across both sources. The Group delivered gross profit after paid acquisition of \$36.6 million in the first half, up 42.5% (up 34% on a constant currency basis). GPAPA outpaced both Revenue growth and more importantly, OpEx growth.

Cash operating expenses for the half were \$30.9 million, up 34.2% (28.1% on a constant currency basis). Operating leverage remains evident for the second quarter and first half despite the weaker Revenue. For the first half, Redbubble's operating expenses are running below the original budget, which was used to previously guide the expected growth rate, on a constant currency basis, as management has taken prudent action to control expenses growth in light of the weaker top line growth. This has been achieved despite capitalised development expenses being lower than forecast, with the resultant additional charge to the P&L and an unfavourable impact of FX. Furthermore, investment in automation and business process design in customer support has been absorbed and that will aid in slowing future volume based cost growth.

The Group delivered Operating EBITDA of \$5.6 million at a margin of 3.9% of Marketplace Revenue, an increase of 1.4 percentage points year-on-year. The Group generated free cash flow of \$25.6 million for the first half, up 41.4% from the \$18.1 million first half last year. The acquisition of TeePublic and associated costs have been excluded from the investing cash flows for that purpose. RB Group's cash balance at 31 December 2018 was \$58.8 million. The closing cash balance was enhanced by \$7.9 million, with \$57.2 million (after costs) raised for the acquisition of TeePublic in early November offset by the initial settlement payment of \$49.3 million (that is US\$35 million) at that time. The final instalment of US\$6 million is due in May 2020.

Redbubble and TeePublic are seasonal businesses don't forget, with the second quarter containing the significant holiday seasons. Much of the fulfilment expenses, artist margins and taxes associated with sales in November and December are not paid out until the March quarter. This seasonality is seen in the actual December 2018 quarter cash outflows and the forecast March 2019 quarter cash flows in the Appendix 4C.



Finally before I pass back to Barry, I want to reaffirm what we have previously indicated, by way of guidance. RB Group expects to generate a positive Operating EBITDA and cash flow results for FY19. Whilst organic search channel continues to show lower growth on both platforms, management has taken strong action on the levers it can control. GP margins are strong and the outlook remains good for further improvements on both platforms to give us the tactical flexibility on pricing.

We have remained disciplined on paid marketing spend efficiency with the increase in paid acquisition costs as a percentage of Marketplace Revenue due to the slowdown in organic and we have actively managed operating expenses, although FX has worked against us realising the full benefit in floating terms. Thank you and now back to Barry before we open for questions.

Barry Newstead: Thanks Chris. RB Group remains focussed on a strategy enhanced to differentiate customer experience and accelerate the marketplace flywheel. Looking at calendar year 2019, our priorities are as follows. Grow the base of customers and members through deeply personal and creative adventures, inspired experiences. Secondly, sustainably launch and sell products that artists want to design for and customers will love. Third, build deeper relationships with authentic artists by sustainably increasing their commercial success, which includes launching and expanding fan art partnerships with the world's leading fan art brands.

The teams across Redbubble and TeePublic are already delivering value in 2019. We are at the forefront of what is a revolution in retail commerce and positioned to be the leading global platform for independent artists and customers looking for creative adventures. With that, we'll now take your questions.

Question and Answer session:

Operator: Ladies and gentlemen we will now begin the question and answer session. If you wish to ask a question please press star one on your telephone and wait for your name to be announced. If you wish to cancel your request, please press the pound or hash key. Your first question comes from the line of Ivor Ries from Morgan Financial. Please ask your question.

Ivor Ries: (Morgan Financial, Analyst) Good morning Barry and good morning Chris. If I could ask the question about the overall underlying traffic growth rate we that is both organic and paid, that you experienced in that last quarter and whether we should assume that sort of growth rate going forward.

Chris Nunn: It is true to say currently that is the growth rate Ivor. Obviously, as Barry pointed out, our work is to grow particularly in the organic channels and to remain efficient in the paid channels.

Ivor Ries: (Morgan Financial, Analyst) Yes. I'm sorry. I haven't been able to go through all the documentation. So what was the true like for like growth rate?



Chris Nunn: Okay. The second quarter, it is on slide 8 of the deck. Second quarter growth rate Marketplace Revenue for Redbubble is 18%, 12% on a constant currency basis and for TeePublic 41% on a constant currency basis. But they sell all their stuff in US dollars. There is no variation between floating and fixed.

Ivor Ries: (Morgan Financial, Analyst) That is revenue. I'm just talking about traffic.

Chris Nunn: I don't have the information on traffic.

Ivor Ries: (Morgan Financial, Analyst) Okay, but I assume that there hasn't been any great change in the conversion rate, so your revenue growth rate will be roughly the same as traffic.

Chris Nunn: Yes. I can confirm the conversion rates are very consistent with last year, across the half year and the second quarter.

Ivor Ries: (Morgan Financial, Analyst) Right, okay and if I can ask a second question. You obviously exercise great restraint in terms of costs, in that in the last quarter of the year. Is it possible to run at this cost rate without choking off the growth initiatives that you need to put in place?

Barry Newstead: Look I think the main source of the operating expense discipline is really about us continuing to find ways to get more leverage in the model and benefitting from the economies of the scale, particularly in places like customer support and our infrastructure costs. We are confident, we more than believe that is sustainable - and we also believe that we are investing at a reasonable level.

Now clearly one can make an argument for greater investment, but I think we have made the decisions around trying to find the right balance. We really feel like, given where we are at, it is imperative for management and for all the people in Redbubble's building is to make sure we are delivering maximum value, maximum growth and impact from the work that we are doing today and in a sense that becomes permission space for our future work.

Ivor Ries: (Morgan Financial, Analyst) Yes if I may be so rude as to ask one more question before I get off the line. Just on your gross profit margin there, going up 2.5 percentage points, quite a big shift there and a surprise. Is that just simply improving fulfillment terms or is there some other element at work there?

Chris Nunn: Fulfiller, but included in fulfillment is the whole range of costs of goods sold. So it goes from product to shipping, even to transaction taxes. So it is work we do consistently on all three elements.

Barry Newstead: And as mentioned earlier - strategic pricing. So we continue to look for ways in which we optimise both the cost, but also our pricing model.

Chris Nunn: Yes, sorry. I was thinking - it is in both aspects, both product pricing and shipping pricing, as well as product costs and shipping costs. You're right. Thanks Barry.

Ivor Ries: (Morgan Financial, Analyst) Right and so can you maintain that going forward? Or is that just simply a function of the second half being a much better time of the year for margins?

Chris Nunn: Well, I think, as we said a year ago today or whenever it was, that we were hit a little bit by certain events that made last year's number a bit lower. But I'm very happy that this year's number is a reflection of where we can take it and we can improve on this, as I mentioned in my speaking notes.

Ivor Ries: (Morgan Financial, Analyst) Fantastic.

Barry Newstead: And I will just add to that - we start the New Year with a real focus (exactly where we were last year), with a real focus on getting value from our scale, in terms of on the cost side and also cross-pollinating learnings between the two marketplaces, in terms of places where we can add more margin. So I do think it continues to be a strategic priority to make sure that we are capturing the fair share of the gross profit margin in this business - for the RB Group.

Ivor Ries: (Morgan Financial, Analyst) Thanks Barry. Thanks Chris.

Operator: Your next question comes from the line of Grace Fulton from Goldman Sachs. Please ask your question.

Grace Fulton: (Goldman Sachs, Analyst) Hi guys. Thank you for taking my question, just a question around the organic growth through the quarter for Redbubble specifically. At the Thanksgiving result you said that it was down 3% and then in the documents today you said that there was minimal growth across the quarter. I assume that includes TeePublic. Could you just give an idea of how organic growth has tracked for Redbubble specifically?

Chris Nunn: I think we have actually specifically in the release at least excluded the TeePublic from the 'minimal growth', so 'minimal growth' is the number for Redbubble. That is on a constant currency basis. In actual dollar terms we are doing a little bit better than 'minimal' (if you know what 'minimal' means). So on a constant currency basis that is the measure on the RB Group. TeePublic remains strong.

Grace Fulton: (Goldman Sachs, Analyst) So Redbubble has returned to positive organic growth?

Chris Nunn: Yes.

Grace Fulton: (Goldman Sachs, Analyst) Okay, also could you just give us an update on your new product launches? i.e. when you expect them to come? and just through the focus on membership can we expect to see an Android app soon?

Barry Newstead: The Android app is the most popular question at the moment. I think we continue to actively look at the timing of launch of an Android app. It continues to be a question of timing. The aspiration is - I would like to go to Christmas 2019 with an Android app. So that's current in-plan. We just need to make sure that we consider the various investment opportunities quarter by quarter through the year. But that is the ambition. In terms of new product launches, that is a priority, as I noted a minute ago. I think we guided previously that the second quarter of the calendar year would be really the time where we start putting new products out. That is currently on our roadmap to do just that and to really re-establish again the importance of new products within the growth story of Redbubble. So through the rest of this calendar year you can expect to see us launching products.

Grace Fulton: (Goldman Sachs, Analyst) Okay, thank you.

Operator: Your next question comes from the line of Owen Humphries from Canaccord. Please ask your question.

Owen Humphries: (Canaccord, Analyst) Hey guys, just a question about looking forward. Obviously you are now going into earnings break even, either this year or next and just a question around the expectations to maybe just provide a bit of guidance to us in terms of how you plan to deploy that. As you go through cash flow breakeven are we expecting to have earnings or have the increased retained earnings or are we thinking about acquisitions? Or do we expect you guys to go hard at the marketing channel, given the accretive unit economics at hand? Just maybe just provide - I understand there is bit of deviation in the consensus going out a couple of years - maybe provide a bit of guidance about how you guys plan to deploy the excess capital that you guys generate.

Barry Newstead: I'd like to defer that one probably a quarter, maybe two quarters before we get into that. We are really focussed on the things we are focussed on at the moment and we are really focussed on demonstrating that indeed the guidance around getting the Operating EBITDA and cash flow positive position is indeed where we are getting to. Then I think we will probably be in a good position to have the conversation about our different options for deploying capital beyond that. Clearly our interests will always be around building a business of enduring value and looking to generate significant value for shareholders.

Owen Humphries: (Canaccord, Analyst) Okay, no worries. Thanks guys.

Operator: Once again, if you wish to ask a question please press star one on your telephone and wait for your name to be announced. Your next question comes from again from Ivor Ries from Morgan Financial. Please ask your question.

Ivor Ries: (Morgan Financial, Analyst) Oh yes, sorry for hogging the line guys. Barry, I think you mentioned in your presentation, you've got 16 brands now in the partnership portfolio and I just wondered at what point do you push the button on that portfolio and start marketing it more aggressively. Because I mean looking at the site at the moment, it is not obvious that you have those brands. So when do you plan to get more aggressive in promoting those partnerships?

Barry Newstead: Yes. A great question. Thank you. We feel that this is a major part of our future growth of Redbubble and this is adding a really powerful new dimension in terms of a content that could be available on Redbubble. So with that in mind, we are really making sure that we deliver the core aspects of that experience step by step and the things that we have been focussed on to this point are really about - first about convincing the partners that we are the right partner to work with in the space. I think we are starting to get some real traction with that. Second is getting artists to contribute content for the partnerships with - that we have signed, which I think we are making good progress. I think there's terrific art and artists are really getting excited about the partnerships as are the rightsholders that we are in partnership with.

So that is where we are at. The next step is really showing our ability to launch more of these partnerships more frequently and with that, will then come exactly what you just talked about, which is the increased marketing of these partnerships. Both are Redbubble's marketing activities, as well as collaborative marketing with the partners. So I think we are going to see that continue to evolve through 2019, but I would say that given the scale of the opportunity and how new these partnerships are, we are really making sure that we are building this with a very solid foundation underneath it. The last thing that we want to do is really push marketing really heavily and feel like we don't have the artist community in the right place or the rightsholder partnerships in the right place, or frankly our operational capability set up to really manage the volume. I mean each of those needs to be done really well and we to have that foundation so as it takes off, it doesn't sort of crumble underneath us.

So it is a really exciting area, really important, very much aligned with the Redbubble motto that we are bringing unique content to customers and having those independent artists really is a key intermediary there so we are excited about its potential, but we are staying patient.

Ivor Ries: (Morgan Financial, Analyst) Right, so it is more of a gradual phased rollout than a big bang.

Barry Newstead: Yes that is right. We will clearly, if we have the opportunity to, if we feel ready, we will turn the dial up pretty significantly.

Ivor Ries: (Morgan Financial, Analyst) Great, thank you.

Barry Newstead: Yes.

Operator: There is another follow up question from the line of Grace Fulton from Goldman Sachs. Please ask your question.

Grace Fulton: (Goldman Sachs, Analyst) Hi guys. Just in the release, you mentioned that one of the opportunities for revenue growth is pricing strategy work. Could you just elaborate on what you meant by that?

Barry Newstead: Yes, so we continue to look at - and we have for the last couple of years - we continue to look at what the right prices are for our products and actually for our shipping as well. So what we have been doing is experimenting with different prices, in some cases price reductions, in other cases price increases, to really find a sweet spot in terms of where are we in terms of Revenue and actually forget about Revenue - gross profit maximisation. So we continue to do work on that front, running experiments within the marketplace to determine where the optimums are - I think we made significant gains on that in the last half. We actually made really sustained gains from that over the last couple of years and so we are sustaining activity on that front and TeePublic is doing the same.

Chris Nunn: I should say Grace, that - I talked about in my speaking notes about practical flexibility. It is about that - in the end - it is getting GP dollars, as Barry says, not necessarily GP margin. So if the opportunity is there to reduce pricing which may affect the GP margin but significantly increase the GP dollars, then we take that kind of decision within that discussion.

Grace Fulton: (Goldman Sachs, Analyst) Okay, thank you.

Operator: Once again, if you wish to ask a question, please press star one on your telephone and wait for your name to be announced. Again, it is star one to ask a question. Ladies and gentlemen, it is star one to ask a question.

Barry Newstead: Looks like we are done. Well, thank you everybody for attending and for the questions that folks asked. We look forward to delivering on our plans for 2019 and again, I want to wish everybody a wonderful year ahead and we look forward to talking to you in April next quarterly update. Thanks everyone.

Operator: Ladies and gentlemen, that does conclude our conference for today. Thank you for participating. You may all disconnect.

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