



Redbubble Limited Investor Update - following Appendix 4C release Conference Call Transcript

Date: 22 July 2016

People: Martin Hosking CEO and Chris Nunn CFO

Martin Hosking, CEO

Hello. I'm Martin Hosking. I'm the CEO and cofounder of Redbubble and this is Redbubble's first ever investor call. So I'm delighted to welcome you all. I first note that it's a little bit unusual to do a call on the release of Appendix 4C quarterly cash flows. Our rationale for doing so is that it coincides with the end of our financial year and this is also the first indication of our results since Redbubble's IPO in May. In this context, we've decided to make a more expansive 4C announcement, inclusive of an investor presentation and hence an investor call also makes sense. I should point out that these numbers are unaudited. You'll find the investor presentation has been released to the market and you'll find that along with the Appendix 4C and you may refer to that - either for questions or during my comments or Chris' comments. The full year financial - full year preliminary Appendix 4E, along with the audited results will be released to the market in the customary manner on 25 August.

I'm delighted to provide the first indication of our results. Redbubble has had a strong year and is tracking above the forecast provided at the time of the IPO. Redbubble is a global marketplace that is scaling rapidly towards profitability. At this time, there are 438,000 artists in the marketplace and 10.2 million images. 2.2 million customers bought from the marketplace during financial year 2016. We are seeing strong scaling of the business over the course of the year. Over the year as a whole, gross transaction value, GTV, which is a measure of our total sales through the marketplace, was up 62% year-on-year. Operating expenditure growth was growing at a much slower rate and, looking at the last quarter, was up 16.4% year-on-year. Scaling is occurring ahead of forecasts, with an EBITDA loss of \$1.5 million better than expected. Margins remain strong. In the last quarter, we're at 36.5%, which was up 5.1% from the prior comparable quarter. Redbubble's CFO, Chris Nunn, will provide a little more context on the financials. I wanted to just highlight some of the underlying drivers.

Most importantly, the marketplace turnover has remained the primary driver of growth for Redbubble. Customer numbers grew at 54% year-on-year and selling artists at 62%. Visits were up 43%. The more artists Redbubble attracts, the more customers it attracts to the marketplace and the more visits that occur as a result. Secondly, as Redbubble grows, it continues to attract a high number of repeat purchasers and visitors. GTV from repeat visits was up 76% year-on-year versus the overall GTV growth of 62%. Finally, our customer acquisition costs remain low. Over the year as a whole, 68.5% of GTV came from free sources and 31.5% from paid, with the paid being profitable on first purchase. We expect paid to contribute about one-third of all GTV going forward. I would note that no forecast is ever going to be perfect. We had not accounted for Brexit, the fall in the pound and some other factors that impacted results at the end of June. While these may have had an impact in the short term, we are not changing our forecast and assumptions for FY2017 as provided in the prospectus.



As a company, we continue to work on those things that most enhance the marketplace dynamics. Six areas in particular contributing to growth and I'll go through each these briefly.

1. Firstly, search and traffic. Here, we are focused on improving search relevance, adding categories and providing more targeted feeds for Google and Facebook. These activities bring in new and repeat visits from both organic and paid channels. Secondly, we're adding products and we're improving the supply chain.
2. In the first half of the year, we have launched six new products and we continue to localise fulfilment. These activities improve the customer experience, attract new customers from new products and attract artists with new offerings. We expect to continue to launch new products at a steady rate.
3. Thirdly, the shopping experience: we're continuing to improve the ease and convenience of shopping on Redbubble. This is particularly important for improving conversion and also creating a compelling experience to bring in - bring back customers. I'm sure many of you are familiar with the Redbubble website and would have - familiar with these improvements. There are some examples of it in the deck.
4. New geographies: the German language site launched in March and the French in June. Spanish is due to launch shortly. These activities bring in both new and existing customers by making Redbubble available in their native languages.
5. Fifthly, engagement. We are building our personalisation and the capability for artists and customers to our collections. These activities are particularly designed for repeating customers.
6. Finally, native mobile. I note that currently more than 50% of Redbubble visitors come from mobile sources and our mobile responsive site will continue to be the main means of serving them. We are, in addition, developing a mobile app with different functionality, which is under development.

I just want to turn to some of the major factors at play with Redbubble. Redbubble is establishing global market leadership, delivering scalable growth and increasing profitability. This comes from major forces at play.

Firstly, we operate in a huge and growing global consumer market, demanding more personalised and relevant products. This will drive long-term sustainable growth for Redbubble.

Secondly, there are strong network effects from more artists and consumers, as well as a vast content library. These provide barriers to entry and also drive low customer acquisition costs and give us visibility into future sales. I would note that most future sales from Redbubble will come from artists and content that already exists on the site.

Thirdly, we have outsourced print-on-demand. As a result, we carry no inventory, have a positive cash cycle and sustainable margins. The Investor Presentation, which you have access to, provides more details on these themes, which I have briefly introduced. Before handing over to Chris, I just want to note that two business days following the announcement of our full year calendar results on 25 August, the escrow for some shareholders will be released. We've not been approached by shareholders about selling shares at this time. As we get closer to the release time, we will discuss with our financial advisors whether there is sufficient demand to establish a share sale facility. I will now hand over to Chris to discuss the financials.

Chris Nunn, CFO:

Thanks, Martin. If I could look firstly at the full year financial highlights, then move to the 4C, concluding with a brief look at the analysis of the two halves of FY16 and the last two quarters in particular, the detail of which is provided in the accompanying investor update, slide 7 and 8. I should point out that whilst we do not expect there to be significant variances, as Martin has said, all financial figures in the 4C and our presentation remain unaudited at this time. Redbubble has had a strong year and finished FY2016 meeting or exceeding its reportable financial IPO forecast numbers. Despite a small miss on gross transaction value, GTV, by 0.4%, revenue was marginally higher at \$114.6 million, versus our forecast of \$114.5 million. The GTV and revenue relationship can vary period to period due to timing of shipping, with GTV recorded on date of sale and revenue recognised on date of order shipment.



The relative value of taxes collected, dependent on both customer and fulfiller location, and the artist's own selected margin. The timing of shipping aspect, in particular, affected the quarter 3 and quarter 4 relativity, which I'll talk to later.

Gross profit was \$39 million versus our forecast of \$38.5 million. Importantly, this also represents a higher gross margin than forecast at 34% of revenue versus 33.8%, principally due to negotiated fulfiller arrangements, but also improved pricing on some products. Operating expenses for the year, excluding the one-off impact of IPO costs that have to be charged to the income statement, as they relate to the secondary element of the offer, were 3% or \$1.6 million lower than forecast, as costs, especially employment costs, were controlled, even as revenue growth was maintained. Hence, the resultant EBITDA loss and net cash outflows were better than forecast. Looking at the 4C itself, I would like to highlight some numbers to aid investors' understanding of Redbubble's financial model. The item Receipts From Customers, item 1.1, is a proxy for GTV, although is gross of later refunds, fraudulent transactions and credit card chargebacks, typically between 1.5% and 2%. These refunds, et cetera, are reflected in Other Working Capital, item 1.2(h) as a cash outflow.

Fulfiller Expenses, item 1.2(f), are the equivalent of costs of goods sold, but, of course, on a cash basis. They reflect product, printing, shipping and transaction costs. Allowing for the natural timing differences between cash flows and their impact on the income statement, the 4C cash flows represented here aligned well with our operating performance, over the year and in the fourth quarter. I would like to take this opportunity, however, to point out to investors that the seasonality of the Redbubble business can affect our quarterly cash flows, particularly for the December quarter, in which Thanksgiving and Christmas sales are included in receipts from customers and the March quarter, in which much of the payments to suppliers associated with the December quarter sales are included in fulfiller expenses. I will readdress that business characteristic in detail, when those statements are released.

Turning now to the more detailed period-by-period analysis set out in the accompanying investor update. The seasonality of the Redbubble business just mentioned is clearly shown when GTV and revenue in the first half of FY16 are compared with the second half. The December quarter typically represents around one-third of Redbubble's sales in GTV. There was a further anomaly affecting the spread between third quarter and fourth quarter revenue, as a result of a backlog of orders around Christmas, which deferred what might have been second quarter revenue to the third quarter. This had the effect of inflating third quarter revenue relative to the fourth quarter. Relativity of GTV therefore is more reflective of the growth between those two quarters. Gross profit margins show an upward trend from FY15 and across FY16, as we benefit from improved fulfiller pricing and opportunities taken to increase some product prices. Overall, it is pleasing to see the operating expenses are beginning to reflect the ability of the business to benefit from scale as it grows its top line.

I look forward to discussing our audited full year results in more detail with release of the Appendix 4E on 25 August.

At that point, I think we can throw it open to questions.

Ivor Rees: (Morgans Financial, Analyst) Good morning, Martin and Chris and the rest of the Redbubble team. Thank you very much. My first question will relate to the fulfiller - renegotiation of your fulfillers' agreements and the second one will be in relation to pricing and products. The first question on the renegotiated fulfiller arrangements, did you have the full benefit of that throughout the quarter or was there only a partial benefit from those new terms in relation to fulfillers? And the second question there, was there also some benefit from the change in mix in products in terms of pricing?

Martin Hosking: Thank you, Ivor. I might take a bit of it and then perhaps Chris. In relation to the fulfiller negotiations, we only had a partial benefit during the quarter, but I will note that that's very much an ongoing part of the business. Redbubble right now has 13 fulfillers and we tend to negotiate those contracts on a relatively rolling



basis and those prices on a rolling basis. So we only saw partial impact during the quarter and we'll continue to negotiate those contracts, particularly as our volume increases over time. In relation to your second question, I think what you're probably pointing to is the improved margin overall. Yes, we were pleased with the margins overall. Redbubble has managed to increase margins as a consequence of improved pricing and improved terms with fulfillers. That is also an ongoing part of the business.

Chris Nunn: You hit the nail on the head, Martin. The fulfiller negotiations are ongoing; every one we talk to regularly. As for the margins and the product mix, I don't think there's been a significant change in that really to affect GP *per se*.

Martin Hosking: It's also worth noting that as we bring on new products, typically they come in at solid margins.

Ivor Rees: (Morgans Financial, Analyst) So just reading between the lines there, I mean, the biggest selling item that you have in terms of the product is the t-shirt top, that area there. So can I take it that you've had sort of, on average, about 2% price increase in t-shirts over that period?

Martin Hosking: I'm not sure whether we can do it as an average. We have changed prices by jurisdiction and I couldn't give you that number at this stage, Ivor. We can take that one and address it in the context of the full year Appendix 4E announcement.

Chris Nunn: Yes. I couldn't add any further. It is a little bit about an overall mix between geographies and products, so I can't provide any precision on that, Ivor.

Ivor Rees: (Morgans Financial, Analyst) Great. Thanks.

Conor O'Prey: (Canaccord, Analyst) Good morning, gentlemen. Just a quick question on - you talked about not changing the guidance in the forecast for 2017. Just wondered, in the context of some of the fairly hefty currency moves you've seen since the Brexit vote, to what extent you had to take that into account, when you were sort of thinking about 2017.

Chris Nunn: Yes, look, Conor, you're right. FX will affect our floating currency numbers obviously. We've seen a significant movement clearly in the pound and more recently in the euro. That will affect the numbers. At this point in time, we're three weeks into the year. I've never been able to predict FX rates. So at this point, I'm not going to change anything, but clearly if we had a continued depression in those currencies, which looks likely, we'll just provide some sense to the analyses in our 4E announcement, if we get more sense of how long that will go.

Martin Hosking: I think it is worth noting, as well, though, because of the extreme diversified geographic mix of Redbubble, one specific currency is probably less important than the overall weight of the Australian dollar in the market. So we do have exposure not only to the pound, but also obviously to the euro, the Canadian dollar and the US dollar being the primary other currencies. So at this stage, we don't have a basis to - for revising based upon what's happened in that one currency there, namely the pound.

Chris Nunn: Yes. That's a good point, Martin. But what I should also say, Conor, is that in the prospectus we provided FX sensitivity.

Conor O'Prey: (Canaccord, Analyst) Yep.

Chris Nunn: ...related to FY17. Yet, the top line gets affected by currency movements, but when you work your way through the P&L to the bottom line, you have costs in those currencies too. So you get - you get a bit of a natural hedge which we've tried to reflect in that sensitivity. So that would always be a reference point.

Conor O'Prey: (Canaccord, Analyst) Yes. Okay. Thank you very much.



Ivor Rees: (Morgans Financial, Analyst) Sorry to hog proceedings, gentlemen, but if I can just ask another question. As part of the IPO process, in one of the presentations there, you listed a whole series of initiatives to improve revenue and also improve conversion rates throughout the year. I just wondered if you could give a sense on how all of those projects are going at the moment. Are they all pretty much tracking according to how you envisaged them tracking or no slippage in any of those projects?

Martin Hosking: Thanks, Ivor, and that's covered again on page 13 and 14 of the investor presentation. I briefly referred to it my notes. Inevitably, with a range of projects, there are risks and changes and variability on them. They are overall tracking to what we had expected and so we are - so those ones are outlined there. Probably the ones which people have had the most interest in are the launch of new products, so that is tracking to our expectation. We had indicated that we're going to be launching more than 20 products this financial year. We did six products in the last half of the last financial year. We're expecting to continue to accelerate product launches. In relation to the geographies, the German website came in on expected timing. The French was slightly earlier than expected. The Spanish website is also now earlier than expected - it is right now in beta. So in relation to the products around the customer experience, yes, we've had solid improvements in search and the onsite experience with traffic. We've had good experience in the first efforts at personalisation and we're anticipating more improvements there.

In terms of the shopping experience, you'll see that there's a new mobile checkout experience which is outlined there. That has performed well. The mobile responsive website is also performing well, with mobile actually ahead of forecast versus the IPO prospectus and with our conversion there also performing well. Finally, in relation to engagement, we're continuing to attract new customers back through the emails which comes from that and a more personalised experience. So, yes, those initiatives overall are performing in line with what our expectations were and what we'd outlined in the prospectus.

Ivor Rees: (Morgans Financial, Analyst): Yes. And your conversion rate nicely improved in FY16 over FY15. Any reason why - that 1.87% is a nice figure for the full year. Any reason why you shouldn't be able to improve on that as FY17 progresses?

Martin Hosking: No reason at all, Ivor. This - the biggest impact on the conversion has been the migration from the desktop to the mobile. We have always had a strong mobile site but we will also need to get better with the mobile responsive website. So that's been an area of investment. We typically see as we enter Q1 and Q2 of the financial year, the next two quarters, the conversion rates go up and we would expect that the - over FY17, conversion to continue to improve without investment in those areas.

Ivor Rees: (Morgans Financial, Analyst): If I just may ask one last question: just in terms of the outlook for CapEx for FY17, no change in the outlook there?

Chris Nunn: No. No change, Ivor. Our basic expenses remain pretty much on track and the extent to which we capitalise those expenses will be expected to be the same.

Ivor Rees: (Morgans Financial, Analyst) Fantastic. Thanks very much.

Martin Hosking: Well, thank you very much, everyone. We're delighted to do this and delighted to share our results with you. I look forward to future calls as we share more information. The next one will be on 25 August where we provide the full year results Appendix 4E.

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