

## Transcription

### Q1 2023 Financial Results of Karooooo.

Karooooo Ltd (NASDAQ:[KARO](#)) Q1 2023 Earnings Conference Call July 28, 2022 8:00 AM ET

#### Company Participants

Zak Calisto - Founder, CEO & Director

Richard Schubert – Group Chief Operating Officer

#### Conference Call Participants

##### Richard Schubert

Good Day. I would like to welcome everyone to the Karooooo Quarter 1 FY '23 earnings presentation.

I'm Richard Schubert, the Group Chief Operating Officer.

Karooooo Management would like to advise all investors to review this disclaimer. Karooooo, which is listed on the NASDAQ under the ticker KARO, has three operational entities that we will review – Carzuka, Cartrack and Karooooo Logistics.

Mobility is core to all on-the-ground operations and we are thinking beyond connected vehicles and equipment by providing a full platform to manage all on-the-ground operations. Our mission is to establish the leading on-the-ground operations cloud platform.

We solve problems by digitally transforming businesses. Our fleet management platform manages safety and visibility operations for our customers. Field worker management is helping SMEs like plumbers and ground servicing companies deliver. Logistics and delivery platforms help supermarkets and pharmacies with their on-time supply chain operations, while Carzuka is providing a safe and easy-to-use vehicle buying and selling platform. We are seeing a growing demand from small to large businesses to add operational efficiencies to their organization.

##### *Karooooo investment highlights that drive shareholder value*

We are at the early stage of a large and growing addressable market where mobility with IoT is key to improving operational efficiencies. There are large expansion options across 23 countries by tapping into the untapped network effect. Our decade long track record shows strong customer acquisition even in challenging markets with a robust and consistent business model.

We have a long-term track record with a robust balance sheet and revenue generation with disciplined capital allocation and a strong cash position despite allocating cash for future growth. Our track record has positioned us well for accelerated growth, with strong operating profits and unit economics while our founder-led culture focuses on agile innovation.

We are at the early stage of a large and long-term growth opportunity. We strongly believe that mobility is core to all on-the-ground operational improvements, which represent over 40% of the global GDP. This offers us a massive opportunity within South Africa where nearly one in 10 vehicles is managed by Karooooo. While post COVID, we see all markets opening up with customers adopting the Karooooo platform. The focus in Asia and Europe now is to grow and deliver more operational value to our customers. The scale of Karooooo's data is vast and growing, and we are fully aware of the untapped network effect of our platform.

Carzuka and Karooooo Logistics are both a direct result of our network effect, and both are solutions we believe we'll see a large success in as we continue to scale them. There are many opportunities that remain ripe for us to disrupt at this point in time. We are able to analyze our data to understand what our customers need, and are adding many verticals to our platform to capitalize our network effect and continue to add growing value to our customers' operations.

Our robust and consistently profitable business model supports over 90,000 commercial customers with a compounded annual growth rate of 17%, which translates to just over USD 182 million. Karooooo wins by providing a fully inclusive end-to-end IoT cloud platform that's easy for our customers to use.

It's continually updated and seamlessly integrates with customers third party ERP solutions. Our expanding distribution network ensures we service customers within the shortest possible lead times.

We understand our customers day-to-day challenges and our on-the-ground cloud platform solves these issues and gives them a high ROI. Our fully vertically integrated business model means we have a larger staff count, but provides a full control of all aspects of the business. Our established infrastructure gives us the human resources to scale with a proven track record to achieve strong growth. Karooooo is an agile and entrepreneurial culture that has proven to be resilient in challenging times. I will now hand over to Zak to present our Q1 financial numbers.

## **Zak Calisto**

Thank you, Richard.

We had a really good Q1 in terms of our financial metrics. We had record earnings and also had record cash generation from operating activities.

Our earnings per share was up by 42% at ZAR 4.96. If we normalize that and we take Q1 of FY '22 and remove the IPO costs, then our earnings per share adjusted would be 27%, which is extremely healthy.

Our profit for the period has gone up from ZAR 108 million to ZAR 156 million - up by 44%. And our cash generated from operating activities is up from ZAR 273 million to a record ZAR 319 million. All of this allowed us to declare the USD 0.60 dividend in April this year. Our business model remains resilient and highly cash generative.

Karooooo continues to grow at scale. Obviously, this is well supported by its high customer retention rate. If we look at this quarter's results, our revenue is at ZAR 801 million, up 28% on last year.

Operating profit at ZAR 217 million, which was our record operating profit - 29% up on last year and adjusted EBITDA at ZAR 354 million up 29% compared to last year's first quarter.

We have very strong unit economics and we have robust operating margins. We've consistently beaten the rule of 40, we have a strong balance sheet with a very strong cash position.

We ended off Q1 with a very strong cash position bolstered by a strong free cash flow generated notwithstanding investment for future growth. We ended up with ZAR 854 million on hand. This was obviously supported by Cartrack's debtors' days, which is now at 33 days compared to 34 days in the same quarter last year. We have a strong balance sheet and ample capacity to fund growth.

We generated from operating activities ZAR 319 million – up 17% compared to last year. We invested ZAR 162 million in operating activities, which is 37% more than last year. And our free cash flows at ZAR 157 million – 2% up on last year's first quarter.

We have strong revenue generation, strong earnings growth and strong cash flow. We are focused on increasing Karoo's presence across industries and geographies. As you can see from the slide, we have a substantial amount of large enterprise customers. Our focus is clearly to service small-to-large enterprise customers and we will continue to allocate capital to acquire more customers. We are reporting our performance by business segment, broken up into Cartrack, Carzuka and Karoo Logistics. I think all three entities have performed well. Our total revenue was up by ZAR 801 million.

Our revenue growth was 28%, operating profit ZAR 217 million, operating profit growth at 29%, adjusted EBITDA at ZAR 354 million, adjusted EBITDA growth at 29% and our adjusted EBITDA margin at 44%.

In Cartrack, we grew our revenue by 16% to ZAR 724 million. We grew our operating profit by 29% to ZAR 220 million – a record operating profit. And our adjusted EBITDA growth was 28% up to ZAR 357 million in EBITDA. Our adjusted EBITDA was at 49%, which is very much in line with our outlook for the year and very strong metrics.

With Carzuka, we grew revenue from ZAR 2 million last year to ZAR 50 million. And if you compare it to Q4 of the last financial year, from ZAR 32 million to ZAR 15 million, we are gaining really good growth and traction at delivering a lot of value for our existing customers.

Our operating profits remains negative at ZAR 4 million and our adjusted EBITDA also negative at ZAR 3 million.

On Karoo Logistics, we're also gaining good momentum if you compare it to quarter on quarter. We are now at ZAR 28 million compared to approximately ZAR 24 million in Q4 of last year.

Our operating profit is just under ZAR 1 million, so we're gaining traction to break-even and to become profitable, with our adjusted EBITDA positive at just under ZAR 1 million.

So, all segments are getting good traction and we continue to build our businesses Cartrack, Carzuka and Karoo Logistics.

We will now focus on Cartrack, our main business and the underlying asset to our business and the asset that creates all the value in terms of data for our business.

And as you can see, our subscription revenue growth was 17% compared to the same quarter last year, with revenue growth up 16%. And now we remain with a very high amount of our subscription revenue being a percentage of the total revenue - 98% in this quarter compared to 97% of last year. What is important is that Cartrack's outlook for 2023 remains unchanged.

We have a track record of well over 10 years of being able to execute, we see that on our subscriber growth, on our subscription revenue graph and on our profitability. We finished the quarter off with 1,543,000 subscribers. Our subscription revenue is at an all-time high of ZAR 707 million, and our operating profit also at all time high of ZAR 221 million. We continue with our strong financial discipline and our ability to scale in varying market conditions.

In this quarter, we saw customers being very cautious with the looming inflation. We also saw that the floods in South Africa and KwaZulu-Natal affected our subscriber base. And we only did 16,800 net subscribers by June this year, and certainly we have seen the same momentum in July. Just in June, we did more than 18,000 net subscribers. And we believe by Q2 this year, we'll restore our momentum.

We've continued to expand our business in all geographies. We saw subscribers up 11% in South Africa, clearly affected by the net subscribers of Q1 which has now been restored in Q2. We've seen good momentum as I said previously in Asia, where we're up 25%. And we're certainly hoping to increase that as we allocate more resources into driving growth in Asia. In Europe, we certainly want to allocate more resources as we grew our subscriber base by 15%. And in Africa other, we're gaining good momentum where we're up 11% on subscribers.

Cartrack has attractive unit economics. Our low cost of acquiring a customer allows for our LTV to CAC to be over nine times. If we look at our Cartrack subscription revenue gross profit margin, that is at 72% compared to 72% the same quarter last year, and Cartrack's operating profit up 31% compared to last year the same time at 27%.

We are well-positioned to materially increase our investment for growth. We will now discuss Cartrack's robust operating metrics.

Our research and development is 6% of our subscription revenue and our long term goal has been 4 to 6%. Sales and marketing is 13%, and we certainly will be allocating more capital to sales and marketing and over the long term we will be between 17 and 19%. Our general and administration as a percentage of subscription revenue is at 21% and as we get the economies of scale, we believe we'll bring that down to 12 to 16%.

Our adjusted EBITDA margin as a percentage of subscription revenue is 50% and our long term is between 50 and 55%. Cartrack's outlook for 2023 remains unchanged - number of subscribers is between 1.7 and 1.9 million, Cartrack's subscription revenue is between ZAR 2.95 and ZAR 3.1 million and Cartrack's adjusted EBITDA margin between 45 and 50%.

We had a very solid start to Q2, in June alone we added net subscribers of over 18,000 subscribers. We have one slide to summarize the revenue, of Carzuka and Karooooo Logistics. It is certainly gaining momentum.

We're very happy with the progress that we're making. As you can see from the slide, we had in Q4 ZAR 32 million and now we have ZAR 50 million in Carzuka revenue. In Karooooo Logistics, we had ZAR 24 million and its now at ZAR 28 million.

So we can see quarter on quarter, how we're growing.

I want to thank everybody for listening and attending our presentation. And I will now open up to questions.

Also, to remind everyone that wants to ask questions, please just to type the questions in the Q and A box.

### **Question-and-Answer Session**

**Question: Parker Lane, Stifel**

What are the assumptions around the growth of Carzuka and Karooooo Logistics in FY '23 and how should we think about the impact that the broader macro slowdown could have on these businesses?

**A – Zak Calisto**

We don't really know the effects of the new macro environment. However, we certainly believe that Carzuka will continue to grow quarter on quarter and I believe we will get strong growth.

By looking at the numbers, we are already very happy with June's numbers for both Carzuka and Karooooo Logistics. Karooooo Logistics onboarded some very large enterprise customers that we are busy rolling out.

So, the revenue you see today in Q1 is not the full revenue of all those customers. And I believe by Q3 and Q4, you will see the revenue of the existing.

Clearly, we will also be onboarding these newer and larger customers to be able to do all the integrations into their back office, into their warehouses and into their stock and this takes a bit of time.

It also takes a bit of time to roll out all their stores to be operational on our platform. I'm expecting to continue growing Carzuka and Karooooo Logistics and I'm certainly also expecting Cartrack to meet the outlook that we've given to the market.

**Question: Willow Miller, William Blair**

How is the European region performing versus your expectations?

**A – Zak Calisto**

I think coming out of Covid, we certainly want to grow our business. We've had four months of post-Covid, and we've had more staff taking off sick due to Covid in the last four or five months than we have had during the two years of the pandemic.

However, we are certainly going to start employing in Europe. It's summer now in Europe, but I think by October or November this year we'll start getting traction. It's certainly our focus for us to start growing Europe as fast as possible, and the same thing goes for Asia.

**Question: Willow Miller, William Blair**

Are you seeing any signs of a softer macro? Any differences by region?

**A – Zak Calisto**

Well, we certainly saw what I believe to be a response to the macro environment in South Africa, specifically in quarter one, but by quarter two I think that softness would have eroded because of the value we add in good times or bad times.

I believe our offering is good, both to save money and increase productivity. So overall, I think these macro-economic changes don't necessarily affect us negatively.

**Question: Parker Lane, Stifel**

When you look at your headcount expansion plans for the year, are you placing a greater emphasis on APAC or EMEA expansion?

**A – Zak Calisto**

I think our focus is in both, but clearly the biggest opportunity for us is APAC. Given that we are coming off a very low base and have basically been in pause for the last two years, I certainly believe that we will see faster growth in APAC than in Europe, Middle East and Africa.

**Question: John Messina, Raymond James**

Gross margins improved 4.3% sequentially in Q1, while it seems like there is a bit of a seasonal trend in Q1, how should we think about the pace of gross margin expansion throughout FY '23?

**A – Zak Calisto**

I don't have the exact detail in front of me, so I'm going to answer in broad terms. I think we've traditionally had gross profit margins in this sort of region between 70-72% and at times there are funds that can come through and affect our gross profit margins.

So, I'm expecting gross profit margins to be very in line with Q1.

**Question: John Messina, Raymond James**

We were really impressed with not only the growth out of Carzuka and Picup, but also the improvement in profitability. While it is a smaller overall component of the company, how should we think about the profitability ramp and the longer-term profitability profile of those businesses?

**A – Zak Calisto**

We've traditionally had a very disciplined way in which we allocate capital. Fundamentally, we like to grow our businesses organically and in a disciplined way. Sometimes we might even be a bit too prudent, and that could even slow down our growth. But I certainly believe that Carzuka and Karooooo Logistics will be profitable businesses by FY '24. Right now, the losses we are incurring and considering the scale and growth percentage we're getting, I think it's quite healthy.

**Question: Rudi van Niekerk, Desert Lion**

Can you please talk about input cost inflation, and how you view the future trajectory of ARPU and whether you will be able to protect margins?

**A – Zak Calisto**

It's a complex question. And the reality is, what we are charging today and what we were charging over 10 years ago is very much the same ARPU. Traditionally, we've just relied on economies of scale.

Having said that, in Q1 we did test the upselling of certain verticals on our platform that we traditionally just give to our customers for free. And that was very encouraging, the uptake in that but we do not want to change our philosophy which is to create more value for the same amount of money and rather to rely on economies of scale to continue having similar margins to what we have today.

I believe the opportunity is large, and I believe that we can grow. And with our growth, we will get the benefit of economies of scale which will offset any inflation pressures provided obviously these pressures are not too aggressive. We also don't want to have a knee jerk reaction to fuel price increases, because that's potentially one of the biggest catalysts into the inflation. We could see the petrol price by Q3 or Q4 drop by 80%, you know we've seen this this before. So, we don't want to have a knee jerk reaction where we start aggressively trying to increase pricing for our customers.

**Question: Drikus Greyling, Daily Investor News**

Largest subscription growth is from Asia, Middle East and Europe. Where do you see the biggest opportunities for growth in the region? And how does this compare to South Africa?

**A – Zak Calisto**

South Africa is the home country where we started the business. And we at this point in time, have got about 10% of all vehicles on the road that are on our cloud. We are certainly open to growing South Africa, and I believe South Africa still has got a lot of potential opportunity for further growth. Clearly, we certainly believe that Asia has got the biggest opportunity where we are also coming off a low base. The last two years have been very disruptive and we weren't really able to trade. We certainly are going to allocate capital and resources to grow Asia, and the same thing can go for Europe.

I certainly believe the biggest opportunity for us in the long term is the growth that we will get out of Asia and Europe.

**Question: Phumelele Mapekula, Mergence**

How many units did Carzuka sell in Q1 2023 vs Q4 2022?

**A – Zak Calisto**

I haven't got the number in front of me, but we are selling used vehicles from our customers and we're creating value for our customers by giving them the best price possible in order to sell the vehicles. And the best way to work it out is just to divide it by ZAR 100 000, because that's approximately the average vehicle we sell in the average price that would give you your answer with good proximity.

**Question: Rendani Magalela, Effectus Capital Management**

By when do you expect Carzuka and Karooooo logistics to breakeven considering the current growth momentum?

**A – Zak Calisto**

As I said before, we expect that by FY '24. I also don't want to promise anything, but I certainly believe by FY '24 both would be profitable.

**Question: Meta**

Does Karooooo Logistics own vehicles?

**A – Zak Calisto**

No, it does not. It's simply a software platform that does integrations and obviously it's very much linked into the Cartrack platform. We're busy merging the technologies. What Karooooo does is do integrations into customers' warehouses, stores and dispatch systems and help our customers with their own fleet to be able to outsource into professional courier companies to transport intercity cargo when they don't have sufficient resources to deal with the demand. They can also tap into third party crowd-sourced drivers. So, it's really just a software platform, there is no hardware involved.

**Question: Patrick O Leary, Fleetwatch**

In terms of Africa, do you see the Africa Free Trade Agreement as an opportunity for growth in terms of tracking vehicles?

**A – Zak Calisto**

Quite frankly, Patrick, I'm not very familiar with the Africa free trade agreement. But I think there's opportunity, whether there's an agreement or no agreement, I think the opportunity remains.

**Question: Hristo Georgiev, Resolute Software**

Given the inflation pressures around the world, have you been thinking over price increases of your offerings?

**A – Zak Calisto**

I think I've covered that.

**Question: Sandile Magagula, Umthombo Wealth**

At which pace are you looking to grow the total subscribers once the environment has fully normalized? Can you hit 30% at one stage, 2024/25 financial year? What explains the high cash conversion rates at KRO and do you see this holding up going forward?

**A – Zak Calisto**

It's very difficult for me to commit to any increase. What I am committing to is to allocate capital, to continue to recruit, to continue to train and continue to build.



And obviously we would love to be well over 30%, but I can't commit to that. We certainly have got a strong track record that we believe can get us over the 30%.

**Question: Roy Campbell, Morgan Stanley**

Is the strong Q1 earnings, EBITDA margin and cash flow a function of lower or slower growth in the subscriber base in Q1? And so, as growth picks up in Q2 and further out, we should expect lower margins and cash flows?

**A – Zak Calisto**

In essence, the answer to that is yes. However, what we also saw and what really talks to customer acquisition, is we still had very good sales but clearly not as we expected because that was dampened by the cautiousness of our customers with the looming inflation and the impact of the Kwazulu-Natal floods.

But what we did see also affecting us was the amount of customers that started defaulting payments, and a lot of it I believe was still very much related to customers that in the last two years have been under a lot of stress.

So, I believe what we obviously trying to achieve is growth, subscription revenue growth of more than 17%. But I believe, unless we go over 20%, subscription revenue growth and the margins will be very much in line with Q1.

**Question: Drikus Greyling, Daily Investor News**

Who are your biggest competitors in Asia, Europe?

**A – Zak Calisto**

Asia is a very fragmented market. We've got lots of competitors and what we found is that most of them are local competitors. They haven't really got that much of a sophisticated offering, but over time, I believe they will improve it. And what we have found is that very few European or South African companies have been able to go to Asia, and be able to acquire customers, own the customers, and be able to operate with the local cultures in a local environment.

So traditionally, what other European or South African or American peers have tried to do is a license agreement, and with very low ARPU's. We are going the route where we own the customer.

I'm a great believer that for the long-term investment, it is really for us to have that relationship with the final customer.

**Question: Khanh Ho**

In your expectation, how significant are Carzuka and Picup's contribution to your overall revenue in the next 2-3 years?

**A – Zak Calisto**

I think both of them. We certainly believe that Carzuka's revenue has obviously got much lower gross profit margins. So, the revenue in Carzuka could easily be much bigger than Cartrack with much smaller margins.

So, while the revenue of Carzuka could certainly reach much higher levels than Cartrack, the profitability will take some time to get there.

Picup's contribution, we're hoping to merge the two platforms over the next year or two. The way we see Karooooo Logistics, it just complements all the verticals that we've currently got on the Cartrack platform to help our customers with their operations. So obviously, it's a very strategic investment. It allows us to have a more complete offering to all our customers.

**END**

We thank you all for all the questions. And thank you very much once again for attending our presentation. Thank you.