Bankrate, Inc.

SECOND QUARTER 2016 EARNINGS CALL TRANSCRIPT
August 4, 2016 – 5:00 p.m. EDT

Katie Yates, VP, Corporate Communications

Thanks, operator. Good afternoon, everyone, and thank you for joining us for Bankrate Inc.'s second quarter 2016 earnings call. Here with me in our NY Office is the company's President and CEO, Ken Esterow and our Senior Vice President and Chief Financial Officer, Steve Barnhart.

Let me briefly review the call's format. First, Ken and Steve will deliver brief prepared remarks. Following their remarks, the lines will be open for Ken and Steve to take some questions.

We remind you that some of the statements made in this conference call, including those regarding the Company's future prospects, growth, future revenue & profitability, and our ability to successfully implement strategic initiatives, constitute forward looking statements. These forward looking statements reflect our current views with respect to future events and financial performance, but are not guarantees of future performance and are subject to numerous uncertainties and risks relating to the Company's operations and business environment, which may cause the Company's actual results in future periods to be materially different from those contemplated in such Forward Looking Statements.

While we cannot anticipate all of these uncertainties and risks, we have identified some important factors currently known to us in the press release that preceded this discussion, and we encourage you to read our reports filed with the SEC, including the discussion under "Cautionary Statement Concerning Forward-Looking Statements" and "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2015, as updated in our Quarterly Reports on Form 10-Q, which are available on the SEC's website.

A reconciliation of certain of the non-GAAP measures referenced in this call can be found in the back of the press release with the financial statements. We also posted a presentation with supplementary information and metrics on Bankrate's investor relations website at investor.bankrate.com.

So with that, I will turn the call over to Bankrate's President and CEO, Ken Esterow.

Ken Esterow, President & CEO

Thanks, Katie. Good afternoon everyone and thanks for joining.

As we announced this afternoon in our earnings release, for Q2 2016, Bankrate generated revenue of $98.3 million, up 10% over the second quarter 2015, exceeding guidance. Our second quarter adjusted EBITDA of $22.6 million also exceeded our guidance. The quarter's results demonstrate that not only are we able to drive top-line revenue growth and achieve our strategic objectives, but also that we can successfully rebuild towards adjusted EBITDA growth. On June 17th, we closed the previously announced NextAdvisor acquisition.

Steve will cover the quarter's financial results in more detail. So I'll move right into our business performance:

For our flagship Credit Cards segment, we accomplished what we set out to do in the quarter in terms of diversifying our consumer demand for credit cards beyond natural search, with additional focus on paid marketing across social, display and direct response TV. Further, there has been much less volatility in terms of organic consumer inquiries than in the first quarter, which is encouraging.

We continue to make strong progress in our Cards business, driving ROI-positive investments in paid marketing to reach more in-market consumers. In the quarter, our Cards segment posted its highest revenue EVER. Needless to say, we're pleased with our continued cards leadership position and evidence that the strategy is working!

As you may recall from last quarter, we outlined our strategy to restore Cards to EBITDA growth. We are no longer content to simply wait for consumers searching for credit cards to find us organically, but we are instead controlling our fate. We're well down the path to building a virtuous circle in Cards where our leading site authority, conversion and monetization enables us to drive profitable revenue growth through investments in paid marketing. In turn, these paid marketing investments create higher consumer awareness and engagement for Cards, improving our site authority, reinforcing our brand and supporting our organic foundation.

These online marketing efforts are leveraging advanced analytics to use first, second and third party data to optimize SEM, programmatic display and social media campaigns. Also, NextAdvisor started using their leading content marketing capabilities on Creditcards.com in addition to their core NextAdvisor business.

Our direct response television efforts also increased, with roughly $1m in media spend for the quarter. The good news is that our initial results show that we are indeed able to use offline media to drive significantly higher offer click volume and break through some of the brand clutter in the category. Over the coming quarters, we will continue to refine our approach, including our creative and media mix.

On the issuer front, we're providing innovative solutions. For example, we're working with a bank to present a targeted card offer if the Creditcards.com visitor is also identified as an existing customer of that bank. We're seeing meaningfully increased conversion while meeting the bank's objectives to improve customer cross-sell.

The macro environment for credit card marketing remains strong, with issuers continuing to shift budget to digital channels and competing for consumer demand. Two large issuers highlighted a post-recession high for new credit cards issued in the quarter. And the two largest global payment networks reported a combined 9% YOY growth in US card purchase volume in the quarter. Investors should keep in mind the target addressable market for credit card marketing is very large and expanding. We estimate that we have less than 2% share of the roughly 60m or more new general purpose credit cards issued every year, and strong secular trends continue in our favor.

Moving to our Banking segment -- our turn-around efforts here remain mid-cycle as we are not yet seeing the expected improvements in financial performance. On the positive side, we drove accelerating performance in mortgages throughout the quarter with our value-based pricing efforts. Mortgage revenue grew 48% versus the second quarter of 2015. And this growth was consistently strong through the quarter, even before the tailwind of higher refinancing demand post Brexit.

However, the success and traction we've generated with our mortgage value-based pricing has not yet been replicated with deposits.

With deposit rates hovering at near all-time lows and excess bank reserves of $2 trillion, there continues to be simply much less demand from banks to advertise deposits almost irrespective of advertising cost. Moreover, the same uncertainty which drove mortgage rates to near all-time lows helped many banks to exceed their deposit funding goals without their planned advertising expenditures. Our near term outlook is that this headwind for deposit advertising continues for both consumer inquiry and display revenue, but longer term advertiser demand for deposits would return when rates rise.

We've a dual-pronged approach to mitigate the downturn in display revenue that we've discussed on previous calls. First, our own recently deployed programmatic ad technology is gaining traction. In the quarter, we generated almost $1m in programmatic display, up 49% from Q1 2016 sequentially. We're actively securing more programmatic advertisers -- by the way, e-marketer notes that more than 2/3 of display advertising is now bought programmatically – we're integrating our ad technology into more ad-exchanges, and locking in key private market-place deals with a variety of financial services advertisers to yield up on our most valuable inventory. Second, we continue to focus on high-value integrated sponsorships such as the one we introduced in the quarter with Veterans United for VA mortgages. This 'barbell' of high value, high consumer intent, but lower volume sponsorships combined with high volume, lower CPM programmatically sold ads is where our display business is heading.

Within our Senior Care segment, revenue was up 5% YOY versus the prior year quarter. Our Caring sales team is adding communities to our network at a healthy clip. At the end of Q2 2016, we have more than 5,300 participating communities, up roughly 20% YOY from the second quarter of 2015. We also moved forward with our in-home care and financial services offerings. Over time, we expect this cross-selling of in-home care and senior care financing to increase the value and monetization of Caring consumer inquiries.

Let me now turn the call over to Steve who will cover our financial results:

Steve Barnhart – Bankrate, Inc. - CFO

Thanks.

As Ken said earlier, Bankrate reported record Q2 revenue of $98.3 million, up 10% versus the prior year. Adjusted EBITDA of $22.6 million was 28% lower vs. the prior year; however, it exceeded the guidance of $20-$22 million that we provided in May.

Two items in the quarter caused us to report a $41 million GAAP net loss. The first is a $25 million non-cash impairment charge to goodwill on our Banking segment, which I will discuss shortly. The second item is a $20 million charge to reserve for a previously announced pending legal settlement, approximately 70% of which is expected to be reimbursed by our insurance coverage.

Moving on to our operating business, in our credit card segment we posted revenue of $69.7 million, up 24% year-over-year. Revenue growth was driven by a 38% increase in consumer inquiry revenue from our owned and operated properties as our strategy of increasing investment in paid marketing to drive traffic continued in Q2.

We've discussed the decline in card affiliate revenues on our earnings calls over the past several quarters. Certain third party affiliates moved to direct links with issuers or other networks in 2015, and as a result, Affiliate Revenues in Q2 2016 were down 5% versus the prior year quarter. We believe we have now overlapped the movement of affiliates in 2015, and it should not impact our rate of revenue growth going forward. In any case, as we have communicated on past calls, Card Affiliate Revenue is low margin, and has little bottom line impact.

Credit Cards Adjusted EBITDA of $24.7 million was 4% lower than prior year, while Adjusted EBITDA margins were about 10.6 percentage points lower. Consistent with the trends we discussed on last quarter's call, lower margins can be attributed to: 1) a higher mix of revenue generated through paid marketing; and 2) increased investment in technology and product, which will have a longer term return. To give you a sense of the revenue mix shift toward paid marketing, the percentage of consumer inquiries from paid marketing in Q2 2016 doubled over the prior year level. We expect the paid marketing revenue mix to continue increasing as we further ramp our investment in paid marketing and have a full quarter of benefit from NextAdvisor in our financials.

Because the Next Advisor acquisition closed late in the quarter, on June 17th, Next Advisor had limited impact on Credit Cards results.

In the banking segment, total revenue of $23.2 million was 14% lower vs. the prior year quarter. Consumer inquiry revenue totaled $15.4 million in Q2, down 5%, driven by lower deposit advertiser demand. Mortgage revenues, on the other hand, grew 48% YOY on 75% higher consumer inquiries, benefiting from the value-based pricing initiative that we implemented in Q3 of last year. We are also implementing these strategies in the deposit vertical, but as Ken said, the macro bank deposit/interest rate environment remains challenging.

Display and other revenue of $7.8 million in Q2 was down 27% compared to the prior year, driven in large part by the same weak demand from deposit advertisers. Many of our largest deposit CPC advertisers supplement their rate table participation with display advertising, and the same factors that caused them to reduce their CPC spending also caused them to reduce their display ad spending.

Adjusted EBITDA for the Banking segment in Q2 was $4.8 million, down 48% from Q2 2015. The decline in adjusted EBITDA was mainly due to lower revenue. The performance of the Banking segment in Q2 caused us to review our Banking segment goodwill, and we recorded a $25 million non-cash impairment charge in the quarter.

Our Senior Care business generated revenue of $6 million during the second quarter. Adjusted EBITDA was half a million dollars, with the segment approximately break-even for the first half of the year.

In our Corporate segment, which includes Quizzle, expenses before costs associated with governmental investigations and related matters, and excluding depreciation, amortization and stock-based compensation, were $7.4 million in the second quarter, up $3.7 million dollars versus the prior year. The largest portion of the increase in corporate costs stemmed from investments in finance personnel and systems. We expect the level of Corporate costs to lower a bit in Q3 and Q4 as projects are completed.

Operating cash flow for the second quarter was approximately $18 million. There was approximately $12 million of operating cash usage due to the portion of the $75 million NextAdvisor purchase price that was put into escrow. We also had $2.6 million in capital expenditures as we continue to invest in product and technology. We ended the quarter with nearly $122 million in cash.

Ken Esterow, Bankrate, Inc. - President & CEO

Before turning to updated guidance, I'd like to thank my senior business leaders, Chris, Scott, and Karen and their teams, who have responded to RATE's challenges with terrific focus, intensity and teamwork. We have changed and built more in the past 6-9 months than perhaps any time in the company's history, certainly since Bankrate went public again in 2011. Our mission of helping consumers to master life's financial journey and being the best source of high-value customers for providers remains the same.

Turning to guidance -- we are particularly encouraged by the trends in our Card business offset, in part, by the aforementioned challenges in banking.

Including NextAdvisor in our guidance, for Q3 2016, we're expecting revenues of $110-$116 million with adjusted EBITDA of $23-$25 million. For the full year 2016, we're expecting revenues of $419-$430 million and adjusted EBITDA of $99-$103 million.

In closing, we're intensely focused on creating value for shareholders -- not only by driving consistent top-line revenue growth, but also by re-building RATE towards profitability growth, growth that we believe will kick in in Q4 2016.

With that – let's turn the call over for questions

Questions & Answers

Operator - -

A. (Operator Instructions) John Campbell, Stephens, Inc.

John Campbell - Stephens, Inc. - Analyst

Q. Hey guys, good afternoon. Congrats on a great quarter. So on the Card segment; it looks like the revenue per inquiry, that's accelerating pretty nicely. Just curious about what you guys have implied in guidance. I know that competition in the issuer space seems to be running at full throttle. Are you guys assuming that it maybe flattens out towards the end of the year or are you expecting continued acceleration there?

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. I'm sorry, you cut out half with your question, I'm sorry. Can you repeat, sometime in middle of the year?

John Campbell - Stephens, Inc. - Analyst

Q. Sure. So, the question is on the revenue per inquiry, it's picking up pretty nicely in the Card segment. It seems like competition is pretty rampant and pretty much running at full throttle in the industry. So, I was wondering if you guys are factoring in continued acceleration in that revenue per inquiry or is that going to cool off towards the end of the year.

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. So, I think there are two things that go into our revenue per inquiry. One is the mix of our business, the pieces that come from organic, paid, and the different components of paid and there is going to be mix element that factors in with the NextAdvisor acquisition as well that operates at different EPCs or CPAs than core Credit Cards and our guidance reflects all those impacts.

In terms of the competitive environment, based on our results and based on what we're seeing for the back half of the year, we feel really good about where we stand. We're really happy to have the NextAdvisor team onboard. They're working with the Cards team. I was on Bloomberg today, and you'll see a content marketing piece, at least I saw it two hours ago that showed both CreditCards.com and NextAdvisor and we're really excited about bringing those two elements together.

So I'm not going to speak specifically to competitors. We're focused on what we do well, ramping our business, growing revenue. In the issuer environment, pricing is a function of issuer demand, and I think everyone knows we run a monthly auction with respect to our highest demanded categories across our platform and through the issuers and the issuer demand that sets pricing. And to-date, that has been favorable certainly over the last two years, and based on the external environment we're seeing, we're bullish on that continuing through the back half of the year.

John Campbell - Stephens, Inc. - Analyst

Q. And then just a quick question, on the insurance business sell that you guys did a couple months ago, can you remind us the $25 million payout, is that -- I guess, remind us on the timing of that payout, and then what that is exactly contingent upon?

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. Yes, I'll let Steve take that one.

Steve Barnhart – Bankrate, Inc. - CFO

A. Yes, John, so it was, and after some cash adjustments had netted out, a little bit lower than $25 million, I can't remember the exact number, maybe $22 million, something more $22 million-ish, but it paid out at two years but that was contingent upon their ability to do so at that time based on their financing arrangements or could convert into a note. So those were the dynamics on that.

John Campbell - Stephens, Inc. - Analyst

Q. Okay. And then just housekeeping, how many buybacks in the quarter and then where do we stand with the current authorization?

Steve Barnhart – Bankrate, Inc. - CFO

A. We finished the $50 million buyback in the quarter.

John Campbell - Stephens, Inc. - Analyst

Q. Okay. And then, any plans on future authorizations?

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. We don't have anything to announce today, no.

Operator - -

A. Laura Martin, Needham & Co.

Laura Martin - Needham & Co. - Analyst

Q. I'd love an update, Ken, on myBankrate. We haven't talked about that in a while. I was just wondering what's going on there. And then, it feels to me like there is a lot of pricing pressure in Banking. We are talking about the programmatic and so I'm real interested in what -- is that programmatic putting downward pressure on your prices?

Just like when we moved to variable pricing, one of the reasons they were losing share is because we didn't have variable pricing. So by definition, variable pricing lowered price points. So could you talk about the pricing pressure in the business by segment? I'd be really interested in that. Thanks.

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. Sure, great. On the myBankrate and our goal to establish an ongoing relationship with our massive audience, we provided an update last quarter, we're around 3 million consumers across Banking with myBankrate and My.CreditCards and Wallaby. The focus in the second quarter really was about ramping our card spend and card marketing efforts and getting Banking on track in some of the core elements.

With the site redesigned for banking, which is rolling out in the second half, I think the first element is about to be launched. We'll start weaving in a lot more than myBankrate offerings, same thing with My.CreditCards. We think it's an important long-term opportunity for us and yields additional monetization and reduces ongoing cost of customer acquisition as people consider other financial products.

On the advertising pricing side, let me break it down into two pieces. When we talk about value-based pricing, that's really in our rate tables. So when we have consumers specifically looking for mortgage rates or deposit rates or auto loan rates and that's where we've moved from one size fits all, every click costs the same, that was 12 months ago, to calibrating our pricing based on the value of that click to the advertiser, the source of traffic, the time of day, the value of the request, loan size, FICO score et cetera.

And in mortgages we had a lot of success with that. Our units of volumes were up 75% in the quarter, overall revenue was up 48%. We think that was a great trade and on the deposit side, we're not seeing the price elasticity from deposit advertisers. So as we've tested different price points and tried to sync up with what our deposit advertisers are seeing in terms of their conversion funnel and accounts being opened. There is less advertiser demand at even lower price points.

When I talk about programmatic, it's really in our display environment, display has typically been-- if you go back a couple of years, about a third of our revenue, we had a very traditional way of selling display advertising, looking for insertion orders for fixed advertising units. We also sold a little bit of sponsorships from time to time.

The display advertising market has really pivoted to programmatic, advertisers are looking for audience. They're looking to re-target existing customers, technology and analytics allows doing them at scale efficiently, which has put downward pressure on our effective CPMs. So what I mention on the call is we're bifurcating our display approach, we've got a group of really terrific sales people focused on high-valued sponsorships that work with advertisers to focus on their brand and weaving in their content and their offering into the Bankrate experience.

If you go to the site today, Veterans United is probably the best example of that. We've done others in previous quarters with advertisers. And then the programmatic stack, it's really using this real-time marketplace and making sure that our inventory is available in as many exchanges as it make sense and that with certain endemic advertisers, the highly valuable financial services providers that we've set up the appropriate backstops and thresholds to make sure that the yield that we're providing to the advertisers is commensurate with the value we're providing to them.

And we've made a lot of progress in Q2. We stood up our programmatic stack for the first time, I think, in Q4 of 2015. That part of our business continues to accelerate, but I think it's fair to say our display revenue will be challenged for the foreseeable futures, just given the macro trends.

Operator - -

A. (Operator Instructions) Andrew Jeffery, SunTrust.

Andrew Jeffrey - SunTrust - Analyst

Q. Steve, can you just help us a little bit with NextAdvisor in terms of what you expect the revenue and EBITDA contribution to be in the back half of the year?

Steve Barnhart – Bankrate, Inc. - CFO

A. Andrew, we have reflected the NextAdvisor impact in the guidance and it is partially offset by some of the weakness we're seeing in Banking since we gave guidance back in May. But in terms of breaking it out balance of the year, we have already begun to run content marketing, NextAdvisor has already begun to running content marketing for the benefit of CreditCards.com and we don't want to go down the path of trying to isolate NextAdvisor for external discussions when a lot of their work really is mingled with CreditCard.com.

So if they're shifting ad inventory from use on one side to the other, we want them to be indifferent and we'd like to be indifferent as well. So other than disclosure requirements we have to meet, we'll present one Credit Card segment which will include NextAdvisor.

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. I think it's fair to say, if you were to look at what they did last year -- for the back half of the year, circa $25 million in revenue; $25 million to $30 million in revenue and call it $8 million or so, $7 million to $8 million of EBITDA adjusted down for a one time card offer they had from the issuer that allowed them to ramp up marketing in a six to eight week period. So, I think it's fair to say, we expect to do as well as that if not better, but going forward as you've said, we're not going to break it out and are become increasingly more difficult to break it out, just because of how close we can try to work the businesses together.

Andrew Jeffrey - SunTrust - Analyst

Q. Okay, that's fair enough. So, I guess going out a little bit of a different way, from a different angle. The guidance certainly implies a fairly steep ramp in the fourth quarter. It would appear to me, just looking at my model preliminarily, in both revenue and EBITDA. I assume that's coming from Credit Card. Should we anticipate a real nice lift in margin, despite what would apparently be a ramp in paid marketing? Am I thinking about that the right way and what would drive it, if I am?

Steve Barnhart – Bankrate, Inc. - CFO

A. Andrew, if you look at the factors why the second half is stronger than the first half, we do have normal second half seasonality and a lot of that is in the cards business that supports a higher second half versus the first half and then you've obviously got NextAdvisor coming and supporting the second half versus the first half. So those are the two big things that in terms of total EBITDA contribution, adjusted EBITDA contribution that elevates the second half.

Andrew Jeffrey - SunTrust - Analyst

Q. Just seems like fourth quarter is stronger than third. I guess I'm focused in on the way that breaks out.

Steve Barnhart – Bankrate, Inc. - CFO

A. Well I think, yes, if you're looking at and particularly if you're looking at it year-over-year, you got to remember the last year's fourth quarter was not a traditional seasonality. Typically we've got a good Q3 and a bit of a stronger Q4 last year with the items that hit in both banking with deposits and cards, Q4 actually stepped down from Q3, which is not normal and not the relationship we would typically expect.

Andrew Jeffrey - SunTrust - Analyst

Q. Okay. So, I guess and we can dig in a little more offline. But when I think about the segment profitability in the back half, would you expect Banking to improve a little bit? Ken, it sounds like perhaps you're taking some cost actions and so forth, so maybe a little more balanced contribution from Banking in the second half of the year?

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. Yes, I think, the low point on Banking, we're certainly looking at the second quarter and not necessary, it's not going to be cost driven. It's really about improved revenue performance as some of our initiatives take hold. And on the card side, as we think about these businesses, inclusive of NextAdvisor, getting to a normalized EBITDA run rate of plus-30% with some puts and takes over time, but that's how we're thinking about it.

Andrew Jeffrey - SunTrust - Analyst

Q. And then, from a business model perspective and then I'll jump off. You mentioned the efficacy you think you can bring to bear from NextAdvisor, and its marketing strategies and --

has differentiated from what Bankrate was able to standalone. Do you see any evidence of that virtuous cycle yet in Credit Cards?

Kenneth Esterow – Bankrate, Inc. – President & CEO

A. Yes even before NextAdvisor, we highlighted on the first quarter call, as we're ramping this up, we were staring at a pretty big dived as the ecosystem change for us relative to natural search and the cards marketing team down in Austin has done a terrific job in ramping up spend, proving out positive ROI.

Now, the margin profile, obviously it's different for paid and organic and we've got tracking tools in place to follow the consumer from the time they see an ad whether it's display or SEM or social, and how they behave, whether they come back? If they come back, whether they convert? We're using tools that allow us to track cross channel, cross device.

You have to triangulate a bit, but we're confident that our ramp in paid marketing spend in the second quarter was ROI positive, contribution margin positive. On the direct response television, I'd say right now, it's about a push, based on our tracking. In terms of contribution margin positive, but as we refine our media message, and our buying strategy, we're absolutely confident that we can turn that ROI positive.

We're still teething into it from an earnings perspective, but we're really focused on and second quarter has proved that we can move the needle, that our creative worked and drove response in terms of additional business to CreditCards.com, additional direct type visits of people who saw the ad and did something, including typing in CreditCards.com, and that's really encouraging.

Operator - -

A. I'm showing no further questions. I would now like to turn the call back over to Kenneth Esterow for any further remarks.

Kenneth Esterow – Bankrate, Inc. - President & CEO

A. Thanks, operator. Thanks everyone for joining today's call. We look forward to updating everyone next quarter and enjoy the rest of your summer. We'll talk to you soon.

Operator - -

A. Ladies and gentlemen, thank you for participating in today's conference. You may all disconnect. Everyone have a great day.