

OneSpan Inc. (Q1 2025)
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Corporate Speakers:

- Joe Maxa; OneSpan Inc.; Vice President of Investor Relations
- Victor Limongelli; OneSpan Inc.; Chief Executive Officer
- Jorge Martell; OneSpan Inc.; Chief Financial Officer

Participants:

- Catharine Trebnick; Rosenblatt; Analyst
- Trevor Rambo; BTIG; Analyst
- Anja Soderstrom; Sidoti; Analyst
- Rudy Kessinger; D.A. Davidson; Analyst

PRESENTATION

Operator^ Good day. Thank you for standing by. Welcome to the Q1 2025 OneSpan Earnings Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your first speaker today Joe Maxa, Vice President of Investor Relations. Please go ahead.

Joe Maxa^ Thank you, Operator. Hello, everyone. Thank you for joining the OneSpan first quarter 2025 earnings conference call. This call is being webcast and can be accessed on the Investor Relations section of OneSpan's website at investors.onespan.com. Joining me on the call today is Victor Limongelli, our Chief Executive Officer, and Jorge Martell our Chief Financial Officer.

This afternoon after market close, OneSpan issued a press release announcing results for our first quarter 2025. To access a copy of the press release and other investor information, please visit our website. Following our prepared comments today we will open the call for questions.

Please note that statements made during this conference call that relate to future plans, events or performance including the outlook for full year 2025 and other long-term financial targets are forward-looking statements. These statements involve risks and uncertainties and are based on current assumptions. Consequently, actual results could differ materially from the expectations expressed in these forward-looking statements.

I direct your attention to today's press release and the company's filing with the U.S. Securities and Exchange Commission for a discussion of such risks and uncertainties. Also note that certain financial measures that may be discussed on this call are expressed on a non-GAAP basis and have been adjusted from a related GAAP financial measure. We have provided an explanation for and reconciliations of these non-GAAP financial

measures to the most directly comparable GAAP financial measures in the earnings press release and in the investor presentation available on our website.

In addition, please note that all growth rates discussed on this call refer to a year-over-year basis, unless otherwise indicated. The date of this conference call is May 1, 2025. Any forward-looking statements and related assumptions are made as of this date. Except as required by law, we undertake no obligation to update these statements as a result of new information or future events or for any other reason.

I will now turn the call over to Victor.

Victor Limongelli^ Thank you, Joe. Thank you, everyone, for joining us today for our first quarter earnings call. I'm very pleased that we reported another strong quarter, driven by the great work and discipline of the team in continuing to optimize our cost structure as well as a more favorable revenue mix as compared to last year. We achieved record high adjusted EBITDA of \$23 million, which was nearly 15% higher than last year's first quarter record of \$20 million. Our adjusted EBITDA reached a record high 36% of revenue.

First quarter 2025 ARR grew 9%, in line with the growth rate implied by the midpoint of our full year 2025 guidance. Q1 subscription revenue also grew 9%, and was driven by demand for our software authentication, app shielding and e-signature solutions. As expected, total revenue declined slightly in the first quarter. The growth in subscription revenue was primarily offset by the following three trends that we've discussed on prior calls.

First, banks in EMEA and to a lesser extent in APAC over the past few years have been adopting mobile-first policies with respect to consumer banking authentication. This has resulted in lower hardware revenues in recent quarters. When a customer transitions to our software solutions from hardware, all else equal, we see lower revenue in the short run, although the gross margin profile of our software offerings is obviously better than is the case with hardware.

Second, in 2024, we transitioned certain legacy perpetual maintenance contracts to term-based subscriptions, which had the effect of lowering maintenance revenue in Q1 2025 compared to the prior year period. Third, headwinds related to sunsetted products was \$1.4 million in the quarter. We expect a similar headwind in the second quarter, and a total of approximately \$1 million spread over the second half of 2025 and then minimal headwinds in 2026.

I'll now provide additional commentary specific to each business unit. In Security, subscription revenue grew 7% and included headwinds from sunsetted products of approximately 3 percentage points. In general, growth in Security subscription revenue is primarily driven by expansion contracts with our existing global security customers including many of the world's largest banks. Regarding our on-time renewal rate, it slipped by a few percentage points in the first quarter, primarily due to two seven-figure

renewal contracts that were expected to close at the end of March. One of the contracts actually expanded to three years from one year and has closed in early Q2. The other contract is also expected to close this quarter.

More broadly in our Security business, our customers and their clients utilize our industry leading anti-fraud solutions that are designed to mitigate even the most advanced account takeover and other hacking attempts. Given our strong customer base and leading position in the authentication market, combined with the increasing sophistication of account takeover attacks, we believe we have a unique opportunity to continue innovating to deliver additional value-added solutions.

In other words, we believe that we can further help our customers solve their emerging authentication and security challenges. In Digital Agreements, Q1 subscription revenue grew 13%. Growth in subscription revenue was primarily driven by expansion contracts and to a lesser extent, new logos. Both business units were again nicely profitable at the segment level, with Security continuing to be very profitable.

We believe we are well positioned to achieve our stated goals for both business units to deliver growth and strong profitability. As we focus on the future, we will remain committed to operational excellence and on driving efficient revenue growth to help ensure we achieve our profitability commitments. Before turning the call over to Jorge, I want to briefly highlight our robust cash generation and the dividend we paid during the quarter. We generated \$29 million in cash from operations and ended the quarter with \$105 million in cash on hand.

During the quarter, we paid a \$0.12 per share dividend, totaling approximately \$4.6 million. It was the first quarterly dividend paid as part of the company's recurring quarterly dividend program. The Board approved our second \$0.12 per share dividend to be paid in the current quarter and plans to continue operating with a balanced capital allocation strategy, weighing potential increases in the capital return to shareholders as well as organic investments in the business and targeted M&A.

With that, I will turn the call over to Jorge.

Jorge Martell^ Thank you, Victor. And good afternoon, everyone. I'm pleased that we reported another strong quarter. However I'm particularly pleased with our strong cash generation and record adjusted EBITDA. We generated more than \$29 million in cash from operations and adjusted EBITDA was \$23 million. ARR grew 9% to \$168.4 million, and our net retention rate or NRR was 107%. ARR and NRR primarily benefited from customer expansion contracts and ARR, to a lesser extent, also benefited from new customers. First quarter 2025 revenue was \$63.4 million, or 2% less than last year's Q1. Digital Agreements' revenue grew 9% and Security Solutions' revenue declined 5%, in line with expectations. We continue to focus on driving subscription revenue growth, which grew 9% in the quarter, led by 13% growth in Digital Agreements and 7% growth in Security.

First quarter gross margin was 74% compared to 73% in the prior year quarter. The slight increase in gross margin was primarily driven by favorable product mix and improved operational efficiencies in both business units as compared to last year. First quarter GAAP operating income was \$17.2 million compared to \$14.1 million in the first quarter of last year. The increase in operating income is primarily attributed to a higher gross margin, lower operating expenses due to the cost savings initiatives we executed in 2024 and lower restructuring costs. GAAP net income per share was \$0.37 in the first quarter of 2025 compared to \$0.35 in the same period last year.

For non-GAAP reporting purposes, I'd like to call your attention to changes we made this quarter. Given the significant growth in our profitability in 2024 and to provide better consistency across interim reporting periods in 2025 and beyond, we have used a forecasted long-term projected non-GAAP tax rate of 20% for the purpose of determining our non-GAAP net income and non-GAAP net income per share.

We're also now including employer payroll taxes related to employee stock-based awards with our long-term incentive compensation expense in our non-GAAP reconciliation tables and have adjusted prior period amounts to reflect both of these changes. Please refer to our Q1 earnings release and the investor presentation that can be found on our Investor Relations website for additional details regarding these changes. Non-GAAP earnings per share, which excludes long-term incentive compensation and related payroll taxes, amortization, restructuring charges and other non-recurring items and the impact of tax adjustments was \$0.45 in the first quarter of 2025 compared to \$0.39 in the first quarter of 2024.

First quarter adjusted EBITDA and adjusted EBITDA margin was \$23 million and 36.4%, both of which were new records for us compared to \$20.2 million and 31.2% in the same period of last year, respectively.

Turning to our Security Solutions business unit. ARR grew 7% year-over-year in the first quarter to \$107 million. First quarter Security revenue declined 5% to \$47.7 million. Growth in subscription revenue was offset by headwinds from sunsetted products, the expected decline in hardware and the expected decline in maintenance and support and professional services as we transition to SaaS and term software licenses over time. Security subscription revenue increased 7% to \$28.1 million.

Growth in subscription revenue was primarily driven by expansion of licenses from existing customers for our software-based authentication and app shielding products, partially offset by the sunseting of our legacy deal flow solution. Q1 2025 gross margin was 76% as compared to 74% in the first quarter of 2024. The increase in margin is primarily attributable to favorable product and customer mix. Security segment operating income was \$24.2 million compared to \$25.9 million in last year's first quarter, primarily due to lower revenue and gross profit. Security segment operating margin was 51% in both periods.

Now turning to Digital Agreements. ARR grew 12% to \$61 million. Revenue grew 9% to \$15.7 million. The increase in revenue was primarily driven by new contracts and expansion of renewal contracts, partially offset by a reduction in maintenance revenue related to the sunsetting of our on-premise e-signature product. Headwinds related to sunsetted products impacted revenue growth by about 4percentage points. Subscription revenue grew 13% to \$15.5 million. Maintenance and support revenue was negligible in the quarter as compared to \$0.5 million in Q1 of last year. The year-over-year decline is attributed to the sunsetting of our on-premise e-signature solution.

First quarter gross margin was 70% as compared to 69% in the prior year quarter. The increase in margin was primarily driven by higher SaaS revenue and improved operating leverage, partially offset by lower maintenance revenue due to the transition to SaaS licenses. Segment operating income was \$3.4 million, or 22% of revenue as compared to an operating loss of \$0.3 million, or negative 2% of revenue in the first quarter of last year. The year-over-year improvement in performance was driven by increased revenue and gross profit, and a decrease in operating expenses due to lower headcount.

Now turning to our balance sheet. We ended the first quarter of 2025 with \$105.2 million in cash and cash equivalents compared to \$83.2 million at the end of 2024. Due in part to the seasonality of our collections with the first quarter being typically the strongest of the year, we generated \$29.4 million in cash from operations during the quarter as compared to \$27 million in the first quarter of last year.

We have no long-term debt. Geographically, our revenue mix by region in the first quarter of 2025 was consistent with the first quarter of last year. EMEA accounted for 49%. The Americas accounted for 33%, and Asia Pacific accounted for 18% of revenue, respectively, in each period. Moving to our financial outlook and modeling notes.

Though we are, of course pleased with our Q1 performance and continue to expect double-digit subscription revenue growth for the full year of 2025, we are monitoring the potential impact of tariffs and foreign currency. A single-digit percentage of our hardware revenue has potential tariff exposure. Thus, based on the tariffs currently announced, we estimate that we could see up to \$1 million of incremental tariff-related costs for the full year 2025. The timing of customer orders could also be impacted by the tariffs.

In addition, significant changes in foreign currency rates could affect our results. That said, given the confidence we have in our core business, at this time we are affirming our previously issued guidance. More specifically, we expect revenue to be in the range of \$245 million to \$251 million. ARR to end the year in the range of \$180 million to \$186 million, and adjusted EBITDA to be in the range of \$72 million to \$76 million.

For additional modeling points, I'd like to remind you that due to the secular industry shift from hardware to mobile authentication, we expect Q2 2025 hardware revenue to be in a similar range as compared to the prior three quarters.

For the full year 2025, we believe our strong focus on operational excellence will enable us to achieve another year of strong profitability and cash generation and enable us to continue returning capital to shareholders via quarterly cash dividends and potentially other methods as part of a balanced capital allocation strategy.

That concludes my remarks. I'll turn the call back over to Victor.

Victor Limongelli^ Thanks, Jorge. To recap, we had a strong quarter, and I'm very proud of the OneSpan team's performance. Beyond the first quarter, however we know that we have more work to do in order to deliver an excellent year. We are committed to delivering value to our customers and to returning value to our shareholders by growing revenue efficiently and profitably. We will continue to focus on driving towards achieving a Rule of 40 performance level.

Jorge and I will now be happy to take your questions.

QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) Our first question comes from the line of Catharine Trebnick of Rosenblatt.

Catharine Trebnick^ On your tariff, on the hardware piece, how much of the revenue is - do you expect to be from Europe? Because you really have only recently really took on marketing towards the U.S. bank. So I'd just kind of like to piece parse that a little bit more, if you don't mind.

Victor Limongelli^ Yes. Catharine, this is Victor. So the -- as you noted, the U.S. exposure is pretty small for us. And as Jorge mentioned, at the currently announced tariff rates, the expense impact, even if they stayed in effect through the rest of the year, and we had the same orders as last year would be pretty small.

Europe is our biggest market for hardware. Jorge, I don't know if you have the specific numbers at hand, but it's definitely an important market for us. But we haven't seen any -- at least to date, any tariff impact in Europe from other markets. We do produce some of the hardware in Europe as well. We have a production line in -- within the EU, although most of the production is in Asia.

Jorge Martell^ Yes. I don't have the number off hand, Catharine. But yes, I think it's obviously meaningful. EMEA is the largest region that we record revenue from hardware, I would venture and say it's probably over 50%. But to Vic's point, it is not subject to tariffs or the incremental tariffs or the tariff -- changes in any tariffs in 2025 so far from China to the EU.

Operator^ Our next question comes from the line of Trevor Rambo of BTIG.

Trevor Rambo^ This is Trevor on for Gray Powell. So just two from my side. One, you talked about the two large deals slipping out of Q1 into Q2. Could you quantify the impact of those deals on ARR? And can you touch a bit more on what you saw in general in the quarter in terms of customer buying behavior compared to your expectations?

Victor Limongelli^ You handle the first one, I'll take the second.

Jorge Martell^ Yes. So to quantify, so really, when you think about the ARR impact, so you have to think about -- because it's on the subscription -- it's on the security subscription, Trevor, really have to think about the start date of that contract, right? We talked about on-time renewals. When we measure on-time renewals, we measure them based on the expiration. So these two contracts, the expiration was the end of the quarter Q1, but the start date was April 1, Trevor. And so, they didn't have an impact on Q2 -- on Q1 ARR. But -- and so, just to differentiate between the on-time renewals, right, versus the ARR impact. I just want to clarify that for you.

Victor Limongelli^ Trevor, yes, just to take your second question was how have we seen buyers act so far in 2025? Is that the gist of the question?

Trevor Rambo^ Yes. You got it.

Victor Limongelli^ So we've been -- obviously there's a lot going on in the world, but we've been pleased so far through the first four months of the year. We had -- obviously we don't report bookings per se, but we had a good bookings Q1 and Q2 looks solid as well. A little hard to say how things will shake out later in the year, but we've been happy with the sales team's performance so far this year. It's probably one of the upsides maybe that we have relatively less exposure to the U.S. market on the security side compared to some others, but we've been doing well so far this year on a bookings perspective.

Trevor Rambo^ Great. That makes a lot of sense. I appreciate the color. Then maybe my second one on the guide. So can you touch on the guidance and what you're seeing in terms of what's giving you confidence in keeping that outlook unchanged despite a lot of the macro uncertainty we're seeing right now? Because we've seen a few companies previously report and take some of their expectations down. So I'm just curious as to what you're seeing specifically in your business that's driving that level of confidence to keep the guide unchanged.

Victor Limongelli^ Yes. Thanks, Trevor. I think what I just alluded to, we've had a good year -- I mean year, four months. We've had a good start to the year in terms of booking - - in terms of the levels that we're booking versus our plan. So we feel like we're on track so far. It is fuzzier, of course the later you go. That's always the case, but especially this year because things are, depending on the news cycle, have been changing quite a bit. So it gets a little harder to predict a Q4 per se. But so far, so good is the way we feel, and that's why we maintained the guidance that we had.

Operator^ Our next question comes from the line of Anja Soderstrom of Sidoti.

Anja Soderstrom^ Congrats on the nice progress here. I'm curious with the adjusted EBITDA margin being so strong in the first quarter. Why wouldn't we expect it to be better for the full year? And was there anything in particular that impacted it in the first quarter?

Jorge Martell^ Yes. Thanks for the question, Anja. So like I mentioned in the prepared remarks, Q1 tends to be the strongest from a revenue mix and that flow -- higher software versus hardware. So that flows all the way to the bottom line. When you look at our remaining year, I think the remainder of the year, Q2 is going to look more like last year's Q2.

Obviously the mix is going to shift. We talked about the headwinds on the hardware business. So although we have obviously a tough compare to last year, I mentioned the revenue for hardware should be more in line with the last three quarters kind of the average there. But nonetheless, still software revenue will come down naturally. So that's why the mix is going to change a little bit, driving, obviously the adjusted EBITDA margin down. So that should behave that way and then gradually increasing just naturally seasonally speaking, if you look at our Q3, second half of last year, software tends to grow a little bit. So that's why you see that similar dynamic playing this year, Anja. So you're going to have, I would say just taking a step back, similar seasonality for the remainder of the year compared to last year. Therefore, it's going to rebalance for the full year.

Anja Soderstrom^ Okay. That was helpful. And how much of your revenue is derived from outside of the U.S.?

Victor Limongelli^ On the security side, it's almost 90% on the security side of the business, upper 80s. The DA business has kind of flipped the other way around, at least for North America, let's say North America versus the rest of the world. Jorge, I don't know if you have the numbers handy for DA.

Jorge Martell^ No. I don't have the exact numbers, but that is directionally right, Victor. It is pretty much a little bit of the opposite between the DA business and the Security Solutions business, Anja. I think you can probably do the math based on the percentages that Victor mentioned.

Anja Soderstrom^ Okay. So you should start to benefit from the weakening dollar then.

Jorge Martell^ Yes. It's interesting. Obviously the -- with the new administration and some of the policies on tariffs and things like that, we saw in Q1, a tough, right? I think we didn't call it out too much, but we did see a little bit of a headwind from an FX perspective. In Q2, we're seeing, obviously euro to USD being more in the \$1.13, \$1.14-ish range. So that should benefit us going into. But we're cautious about FX, Anja. There's a lot of things in play with the trade policies, the GDP, the Fed just issued and just recently, the economic projection was updated, pointing to a lower economy --

weaker economy rather, higher inflation, just things like that. So we're cautious about it. So so far, it should have some tailwinds, but we're constantly monitoring, Anja.

Anja Soderstrom^ Okay. It seems like most of your growth has come from expansion of existing contracts. What are you doing in terms of trying to get new logos?

Victor Limongelli^ Well Anja, it varies between the two business units. On the DA side, we have proportionately more effort on lead generation in sort of online lead generation and pursuing them that way. It's a little bit different in security when you're selling to big banks, and they tend to be larger deals. So it's not so much of a pipeline from leads, but more trying to have meetings with individual banks face-to-face. So it's a little bit more of a classic field sales team approach, as well as cultivating channel partners that have relationships with these financial institutions that we may not have. So both of those efforts we pursue on the security side.

Anja Soderstrom^ Okay. And just one last follow-up on the macro environment here. It seems like you haven't really seen a slowdown or your customers having a little bit of a wait-and-see approach to what's going on. Have I understood that correctly or --

Victor Limongelli^ Yes. I think that's fair. I mean the first quarter business was good versus our plan. April has been good. There's certainly a lot of noise. So we have our eye on it, and it's hard to say how things shake out in the latter half of the year. You were right, directionally, the weakening dollar would help us. It's really -- just to be clear, I just want to clarify this. We do business in a lot of parts of the world, but the exchange rate that matters for us is euro-dollar because we -- most of our revenues in dollars and then a minority of it is in euros.

So -- and it also -- although it helps on the revenue side, it increases our cost because we have a significant employee base over in Europe. So we have expenses in euros as well. So the weakening dollar would help overall. We try not to get too hung up on exchange rates, whether we were hurt a little bit like in Q1 or helped a little bit in Q2, unless they're really extreme. We're just trying to kind of execute as best we can and not hang our hats on exchange rates, if that makes sense.

Operator^ (Operator Instructions) Our next question comes from the line of Rudy Kessinger of D.A. Davidson.

Rudy Kessinger^ So just what are the net new ARR expectations for the year? You only had \$700,000 of net new in the first quarter. Midpoint of guidance, I think implies another \$14.5 million over the next three quarters. I know last year was pretty lumpy, weak in Q1, massive Q2. How should we expect the new bookings and net new ARR to flow through the year?

Jorge Martell^ Yes. Thanks for the question, Rudy. So listen, I think when you take a step back, Q1 was aligned to plan. So we grew 9% ARR, which was again midpoint of our guide. I think what you would expect in Q2, just because of the situation you

mentioned, we had a really, really strong Q2 as a result of a couple of large 7-figure deals -- dollar deals that we closed, particularly on the DA side. We had, I remember one on the security side. So that compare is going to be tough and challenging. So I would expect ARR growth to be more in the mid- to low single digits and then gradually increasing for the remaining for the second half of the year, Q3 and Q4 to be back in line with the midpoint guide, Rudy.

Rudy Kessinger^ Got it. That's helpful. Then secondly, you got a little over \$100 million in cash now. You're going to generate a lot of cash this year even above and beyond the dividend if you don't increase it. I heard you mention maybe targeted M&A in the prepared remarks. Just how are you thinking about capital allocation? Should we be expecting maybe another buyback, Dutch auction? Or you're more likely going to lean into the M&A side? And if so, what kind of areas -- what are you looking to add via M&A, I guess?

Victor Limongelli^ So let me take a stab at that. I think the Board is going to look at potentially other -- obviously the institutional dividend was a big thing for us this year and over the course of the year would be -- if it stays at the same level for the full year, it would be close to \$20 million return to shareholders. The Board will also look at other means of returning cash to shareholders, whether they be buybacks in the open market or a Dutch tender approach.

Then on the M&A side, to answer your question directly, we're much more likely, I think although not exclusively, much more likely to do a deal on the security side of the business to expand our capabilities because we do have a -- we have a very broad and deep customer base on the security side, 60 of the world's 100 largest banks.

So if we can deliver more value to them through an acquisition that we can add to our product portfolio, we see that as a way to efficiently grow the business. So that would be what we would be looking at. It's likely, Rudy, that, that is, at least in 2025 to be on the more modest size. We're unlikely to do a giant deal, just to clarify this. That's why we said targeted M&A.

Operator^ Thank you. I am showing no further questions at this time. I would now like to turn it back to Joe Maxa for closing remarks.

Joe Maxa^ Thank you, everyone. We look forward to sharing our results with you again next quarter. Have a great day.

Operator^ Thank you for your participation in today's conference. This does conclude the program. You may now disconnect.