

Company Name: Onespan Inc. (OSPN)
Event: 23rd Annual Needham Growth Conference
Date: January 13, 2021

<<Vincent Kover, Analyst, Needham & Company>>

Good afternoon. And thank you for joining the 23rd Annual Needham Growth Conference. We're in the third day of conference. And I'm having the privilege of introducing you to Scott Clements. He's the CEO at Onespan. For everyone in the audience, we're going to hold a question-and-answer at the conclusion of Scott's presentation. Please feel free to utilize the text box in the upper right-hand corner of your screen to enter any questions throughout the presentation and of course at the end. Scott, the floor is yours.

<<Scott Clements, President and Chief Executive Officer>>

Vincent, thanks very much. Good afternoon, everyone. I hope you are all are well. I want to take just a few minutes here to give you an introduction and update to Onespan and what we're about and what we're up to. I do want to note here. I don't usually as a matter of course spend any time on the Safe Harbor slide, but just use it as a reminder that we are in our quiet period before we report our fourth quarter earnings. So that limits a little bit, what I can talk about with respect to Q4 and full year 2020 results.

So, OneSpan's focus as a company, our mission is to make a high value digital transactions secure, accessible easy and valuable, and to do that at a large scale, where we deployed to millions of a bank's customers all the time. And we touch 60%, of the world's top 100 global banks are our customers. And we have played a role, an important role, I think in reducing a \$15 billion of fraud losses over the last decade. We focus on peoples identities on the devices that they use and on the transactions they carry out on those devices, making sure that all of those elements of a digital interaction are secure.

This slide just gives you a little bit of a sense for, what it is we specifically do and actually do. The first thing, and the thing that we've been doing for many years, although we're doing it differently now than in the past, is to secure the login of known identities to prevent account takeover essentially most often in the banking space.

The second thing we do is, to secure the digital transaction data that flows between the end point and the center. And we do that through a transaction signing of fraud analysis and secure channel type technologies.

Then the third element is, to protect the applications, the mobile applications from a bank or another type of a company on the mobile device. So, we aren't so concerned with securing the device. We're more concerned with securing the mobile application on the device. And that's important because when banks deploy to millions of the customers, they're deploying to a very heterogeneous endpoint environment, lots of different types of mobile devices with different biometric interfaces, and all of that. And so we help them make sure that when they deploy that

application onto, or that application is deployed onto a mobile device that it is, wrapped and secure that we manage the communications in and out the biometric interfaces that get used on the different devices. We abstract that to simplify that task for the bank. And really try to do this in a transparent way.

More recently we'd begun to help identify, verify the identity of new customers, new users that are joining a bank or other institution as a customer. And to help, and this is really not a protect against new account opening fraud, which has been a pretty big issue over the last year. New account opening fraud has really skyrocketed because of people trying to launder money, that was taken from government unemployment programs, a PPP program things like that, there are lots of new accounts that are being opened and uses to launder money and so helping to prevent that is really a newer part of what we do. And we include in that process of digital channel account opening, not only the identity verification, but the workflow components, that e-signature dimension, so that a customer can complete the user agreement or contracts and do all of that really in the digital space without offline activity.

Typically in most of our security type solutions, is important to understand that there is going to be both an endpoint component and a server or a cloud side component. And that has always been the case even as a hardware authentication company in the past now is a mobile security, mobile authentication company. In all of those cases, there still will be some server-side component or cloud component now to really help manage these security communications authentication provisioning processes, so on and so forth. And I did mention briefly, we also have a growing, a rapidly growing e-signature business that is we acquired a few years ago. It's doing very well right now. We're seeing a lot of global expansion in e-signature as a standalone, but also in working with our security components either on a new account opening scenario or other types of use cases.

The value propositions that we deliver are really framed around reducing fraud, delivering these secure frictionless user experiences, kind of making sure they're not only frictionless and pleasant, but also highly secure all at the same time. And then also reducing costs and increasing agility for our customers, with some of our digitization related products. And then certainly last in this list, but not least in importance is, complying with regulation, banking as you all know is highly regulated around the world. The regulations vary around the world. We have the depth of knowledge and understanding to help those customers, deliver security and these other value propositions in a compliant manner.

If you look at the bottom here, this is really a little bit of a representation of the evolution of our business. It used to be that five, six and more years ago, we were primarily a company that sold hardware authentication devices. And the hardware authentication device actually (inaudible) on purpose created some friction in the user experience, in order to execute a one-time password or other type of authentication process. That was fine when customers logging into their bank account from their desktop maybe a few times a month, really was not a big deal to have some of that friction. But as we come to the modern day, and as we look ahead, people are accessing financial services and lots of different things on their mobile devices, multiple times a day or many times a day. And as that transaction volume goes up in the variety of transactions, becomes more diverse. The cost and the friction from security really has to go down and become overtime

almost invisible. And so that is one of the underlying drivers of the evolution of our business, away from hardware authentication and more towards a software-based digital cloud-based, authentication and security processes.

So, just a few words about our customer base. On the left you can see, many global banks that are very familiar. As I said, we have over 60% of the top 100 banks in the world are our customers. Most of those have been our customers for quite a long time. And we continue to grow, with those customers as well as adding new logos. Many of these banks are in the early phases of transition to cloud-based services, the cloud-based security offerings. And a big part of our investment over the past two, three years has been to move, more and more of our offering into a cloud format, so that we can move forward with these customers and deliver the increased agility lower costs, a higher service level that we can get, from a cloud-based rather than behind the firewall on premise type offerings.

We do participate in some other vertical spaces as well. You can see on the right here, government healthcare and enterprise. And enterprise, we're primarily focused on remote access type use cases, for example in the automobile company cases that you see here, we helped to secure the access to corporate resources, for dealers and service companies. And so on that are really heavily reliant on data and information from the auto manufacturer. We also do, as I mentioned earlier, a new account opening work with some of the large automobile companies, helping them to digitally qualify people and onboard people for a new car loans when people go to the dealer to buy a car.

In government and healthcare, these are newer areas for us. We have touched in these, one way or another for some years, but they are becoming more important to us as we think about diversifying our customer base. We're seeing a very good growth in government security and then and digital healthcare still a relatively small part of our business probably in the, mid-single digit type share, but showing some interesting growth. And these are areas where there isn't really an increasing demand for security, and a lot of opportunity for us to penetrate, I think more fully, then we have so far, with the products, essentially the products that we have today. So, these are areas where we're looking to really diversify our customer base, and we're going to obviously be very focused on financial services for a long time, but now that we've launched these numbers of new services over the last few years, we think we have significant opportunity to go toward these adjacencies.

So, when we look at the growth drivers of the business, we have a number of things that are happening here that I think are really important. The threat environment itself is very dynamic. And I think we've all heard about the recent solar winds hack, and the use of ADFS, to access network services and so on. And so these kinds of things are happening all the time. The entities that do these hacks are, of course, just like companies almost they have R&D budgets and employees and all of these kinds of things, because it can be quite profitable. So, these are very sophisticated actors that can attack corporations, banks, the state, so on and so forth. And so very often the initial access point before these kinds of attacks is through identity, through phishing attacks or through the use of stolen credentials and other things like that. So, we believe that the things that we've done for banks for a long time to really help, protect those environments can be

applied, in many areas going forward, so lots of opportunity not only in banking, but more broadly.

And I think, the other thing that's happening, I think is it banks and financial services, value chains are increasingly being disaggregated. I think we probably all know that from financial service or FinTech companies. And from a digital platform companies and from others. And so the competition for banks is increasingly revolving around the mobile, and digital user experience. And so they, banks to compete on that base, they have to deliver a high levels of security, but doing that in a way that is really transparent to the user or even in some cases additive to the user experience.

And so much of what we have done over the last few years, is to become able to deliver that security and that value that reflects a diverse threat environment. And so adapt the security to the situation at hand. There's also a lot of regulatory requirements, as I mentioned earlier about identity, particularly in Europe and Asia Pacific, that regulatory environment is extremely complex. And part of what we do is, help our customers survive in that increasingly complex regulatory environment.

And then just a word about the pandemic. It had the some of the effects of the pandemic caused us some challenges in the middle of 2020, and the third quarter in particular. This was really just related to the banks, our primary customers having to shift all of their employees to remote work, taking care of all the security requirements around that do some digitization of different processes and so on, really re-look at their budgets for the year. And do all these kinds of things that happened because of the pandemic that takes the attention away from some of our projects and some of the things that are high value, but maybe can wait for a little while.

And so we did see that happen, in the middle of the year. And, we are seeing that now reverse, I think as we go through the latter part of this year, lots of return to more normal customer conversations, more normal types of activity. So, we think that was a short-term effect of, some small number of quarters. But then when we really look at the long-term effects of the pandemic these are really going to be, I think, positives for our company. It has really encouraged banks to accelerate the transition to the cloud. More people are using the mobile channel, more than they ever have before. And many or most of those who have started to use the mobile channel more for the first time, say they will continue to do so, in the future. And then also, there it is really driving digitization demand, of different processes and activities and banking as well as many other verticals. And that has had a very positive impact, and even in the short term honorary signature business, but we think that will perpetuate also. So, I think the pandemic has really raised the importance of the digital channel and digital connection, and that's really what our business is all about.

You can see on the right, we do serve some significant markets in terms of their size. You add all these up, it's probably a \$15 to \$20 billion TAM, and these are showing a pretty good growth rates also, in the various areas. I think security and anti-fraud, growth rate is probably even a little better now than we show here, but really never in any case, big markets with good growth opportunity, that I think we're increasingly well positioned for.

So, let me illustrate a little bit, how the work that we've done over the last two, three years has expanded the opportunity set for Onespan. When I joined the company back in late 2015, we were really a predominantly, a two factor authentication hardware company. We did have some relatively simple server side authentication software, SDKs really. And then we began to build out a new set of capabilities around, mobile security, mobile application protection, using having on the phone device, the analogs of hardware authentication, but then going certainly well beyond that in terms of our mobile security capabilities, then we added the e-signature through acquisition in early 2016. And then over the last two years or so two, three years or so, we have really been building out a new set of cloud-based services, that are around as I've already described authentic identity verification, cloud-based authentication, risk analytics, and a few other things that we've developed and we're working on.

So, we've gone from being a company that really had essentially one thing to sell a lot of varieties of that one thing, but only one thing, to now we have a wide, a much wider array of things we can sell to our existing customers, as well as new customers. And we think the transition that our customers are going through toward the cloud, and towards a more mobile and digital engagement are really positive for our business. And today, if you look at our top 200 customers, virtually all of those customers use at least a two or three of these offerings, with the opportunity to do more.

And I think you can see that a little bit on this chart. This was what our product penetration looked like in our top 200 customers. First of all back in 2015, on the left, we had a penetration of about 98%, on hardware tokens. We were already in the early days of the mobile security business at that point in time you can see, almost half of those customers. And today over half of our top 200 customers use both hardware and a mobile security authentication products. So, when we look at sort of the end of the third quarter of 2020, there's a couple interesting things I'll point out here. Authentication software's still shows a pretty high penetration around 72%, but it is down from 2015.

And if you look all the way to the right here at the cloud security column that's really where the balance has gone. Now, you really could take that cloud security, a column and set it on top of authentication. So this indicates that we are beginning to get some good traction on our new cloud-based security products, over the last couple of years as we've launched them; but certainly, a lot of opportunity yet to be a part of the transition of our banking customers toward the cloud. Two factor hardware is still important about 80% of our top 200 customers still use our hardware authentication even as we see the shift over time towards more reliance on mobile security. And then e-signature is really a new addition in the right-hand chart there and about 22% of our top 200 customers, our e-signature customers as well, so significant opportunity to build upon that in our installed customer base.

So, we have been not only transforming the product line of the company, but really also the financial model and business model of the company back in 2015, 2016 timeframe to the degree that we sold software, we sold really as a perpetual license business. Over the last year or two, we have really begun working hard and to transition the company towards recurring revenue models in software and services.

Today, as of this year, we will be about 60% of our revenue will be from software and service business, and 40% or less are from hardware products. And we will see of that software and service revenue this year about 75% of that will be recurring and we expect by 2022 that north of 85% of that software and services revenue will be recurring. And the large majority of our revenues will be coming from software and services.

So, we've targeted a 25% to 30% ARR growth over the period 2020 to 2022. We are generally looking at about 120% net retention or a dollar base net expansion rate over that period. And we're seeing about that this year in 2020, I should say. And we expect to see it in 2021. And then we're targeting about as I said 85% of software and services to be recurring by 2022, that's an increase of our target by about 10 percentage points and you can see how that progression is we're working on the bottom of the chart.

So, a little picture for you the evolution of Onespan. This is, we're sort of midway on a multi-year transition for our company. We have been, I think, becoming an earnest, more of a software company for a pretty short time here, really only two or three years. We've made a lot of progress in that time, but we have a lot more than we want to do.

And I think it's important to remember when sort of looking at where we are on this process – this transition process that most of the other cloud and SaaS companies that we compare to ourselves to and then you compare us to have been at this game for well in excess of a decade in most cases, certainly, in terms of the public companies. And mostly, when I look at our peer group of about 20 cyber security software companies on average, they have been in the software business for 17 years.

So, we're making really great progress. We got a lot more that we want to do. You can see that over the 2018 and 2019, 2020, it was really about launching some of these new services in 2020 and 2021. We're really working to build out the core platform services that will help us to make these products more efficient, more unified in their user experience and their capabilities. Then at the same time, we're not starting to build out a digital ecosystem of partners, technology partners, and go-to-market partners that will help us really access a broader piece of the market more rapidly.

And then we're also really doing a lot of internal work to build out a digital ecosystem within the company that really will allow us to interact with our customers in a seamless digital manner over the course of 2018 through 2020. We replaced or added, basically every internal system that we have in finance and HR operations collaboration tools and so on.

We have a complete new IT infrastructure in the company. And now, we're building on that to link our products and our services to the inside of our company, so that we can gather that data have that information deliver at low cost, a high service level to our customers, and then really adding on more innovation. We've done a lot of work over the last few years; I would say to catch up from a technology point of view. Now, we're going to start to increase our emphasis on innovation and then expanding into these adjacencies that I talked about earlier.

So, let me give you a quick update on 2020, I'm sorry this is a little bit out of date just from the sense that these are based on numbers from the end of the third quarter. And of course, we'll update these when we report in the fourth quarter, but I think these give you a reasonable understanding of where we are and where we're going. So, ARR has been a really good story for us over the past few years seeing some pretty steady growth and we have targeted as I said, 25% to 30% ARR growth over this period, and we expect to be in that range certainly, in 2020 and then our dollar base net retention also is quite strong.

We have tremendous customer relationships and a lot of our products drive repeat business and repeat orders with those existing customers as well as through getting new customers. But you can see that based on this dollar net expansion rate, we have a real leg up in terms of our annual growth goals, just based on additional sales to existing customers before we even talk about new customers and new logos.

So, this is a nine-month year-to-date data here. And what you can see is that we overall, have had a decline in revenue from 2019 to 2020. The driver for that is really, the pretty significant decline in our hardware business that went from 52% last year of the total revenue down to 40% this year. And through that, we've continued to see growth in our recurring software offerings, but being really offset by some of that decline in hardware and then also some decline in other remaining perpetual license business, which by the end of 2021 will be pretty small. I mean, you can see on the right here really solid growth in recurring revenue contract bookings throughout this period, good growth in recurring revenue.

And then let's see we got to talk about the transition to recurring revenue creating a little bit of a headwind, but we're managing our way through that. And our – I think this is important, our software and services sales pipeline, the sales funnel in the course of 2020 has been quite strong. We've been seeing something in the order of 40% growth in our sales pipeline throughout this period, even as that pipeline slowed a little bit in terms of the flow through the pipeline, the size of the pipeline has continued to grow. So that gives us a lot of optimism about 2021 and the value of what we have to offer. And as we get through that as we've gotten through that period with the pandemic. We'll see we expect to see some solid results in the company.

So, a little more on the banking environment and the outlook. I think I've talked about most of these items on the left-hand side here. In 2021, we're optimistic, because there are projections for certainly increased technology and security spending by banks in 2021, being driven by worsening fraud losses and fraud attacks, the digitization and ID verification, the ability to onboard new customers through that digital channel are going to really be important drivers and we're going to be continuing to driving ARR growth. We do think the hardware decline will moderate. It will not be as fast in 2021 as we signed 2020, and we are active as I described in looking for and increasing our penetration in some of these new adjacency areas.

So, just a couple things to wrap up here. We have taken a great deal of effort over the last couple of years to really strengthen our Board. And that's not a reflection, any negative reflection on the Board that we have had for quite some time. It's really a reflection on the evolution of the business as we have shifted towards software and services and more towards cloud delivery of those services, as we look at acquisition opportunities to build our company, we really have

taken the opportunity to refresh that Board to add a highly-qualified and experienced people in the areas that matter. And you can see these names and read the backgrounds here. Marc Boroditsky is the CRO at Twilio; Naureen Hassan, who is responsible for Digital Banking at Morgan Stanley Wealth Management; Marianne Johnson, a tremendously deep technologist with a significant background in Financial Services and the Fraud area and Al Nietzel just joined us a longtime CFO of CDK Global and Marc Zenner, he has been on our Board for about a year and a half now with a really incredible background in Investment Banking as well as in academia related to financial matters.

So, this is in addition to the other Board members that we have. So, we feel really good about the strength, the diversity and the capability of this Board to help us move the company forward. So that's really the wrap up here. You can see some of the points reiterated here in a summary slide, but why don't we go ahead and shift over to the Q&A. Vincent?

<<Vincent Kover, Analyst, Needham & Company>>

Excellent, Scott, thank you so much for your presentation. Just a reminder to the audience, if you would like to submit a question, please do so by using the text box in the upper right hand corner. We did have a couple of come-in Scott, over the course of the presentation, a few around the competitive environment, specifically your thoughts on DocuSign and potentially grabbing market share. Floor is yours.

<<Scott Clements, President and Chief Executive Officer>>

Sure. Yes, I think when we compete in the e-signature space; we see DocuSign, we see the Adobe, we see HelloSign in the region – other regions of the world, there are some regional companies that we will run into. But I think the consistent competitor that we see is DocuSign and most of the situations that we participate in we've really optimized our product and our business to deal with integrated use cases that require significant security, a strong audit trail, white labeling of the product and that's been a strategy that has been pretty successful for us certainly over the course of 2020.

Through the first three quarters of 2020, we're seeing triple-digit growth in our sales and bookings for e-signature. And so we expect to have a continued and really strong result in 2021. And at the same time, we're extending the value proposition of our e-signature capabilities by adding a remote online notarization integration, stronger ID verification capabilities on the front end of e-signature processes and so on.

Now, DocuSign is really strong. They're a good competitor everywhere, but they are – the real heart of their strength is in their user generated space. This is where they sell their product to a small companies or law office or real estate agent et cetera, and they have a really strong self-service capability. They've added billing and other things like that to the offering and they're really strong, but we don't really – we have some of those capabilities, but we don't really try to compete with them in that space. We're really focused on banks, and healthcare and insurance and regulated industries that really value the differentiators that we have.

<<Vincent Kover, Analyst, Needham & Company>>

Excellent, Scott. Thank you. That segments nicely into the next question. With regards to client segmenting, is there a segment of the banking market that is most appealing regional versus global to you?

<<Scott Clements, President and Chief Executive Officer>>

I think that they are all appealing to us and we have over 2,000 banking customers around the world. We have 10,000 customers overall, but the bigger ones and the higher value ones are mostly in the banking space, and we have about 2,000 of those. And those go everything from the very largest top-tier banks in the U.S. and Europe, and Japan, and elsewhere Australia to all of the brand names that you know of are – the majority of those are – the significant majority of those are our customers. But we also do a lot of work with regional banks today. And then in smaller institutions, although we do that primarily through channel partners, that can take our solutions efficiently into those smaller tiers of customers.

In the mid-market space, that is a really important part of our future. Those are the – we think the bank customers that are going to have a higher propensity to value the fact that we can bring a complete portfolio of relevant security solutions to that customer, be able to deliver over time, a consistent user interface, a consistent set of underlying services around that power those applications. And so we develop and really fulfill, I think our vision around the platform and around the solution that mid-tier will, I think, take on increasing importance to us. And one of the other things that we're doing is really beginning to establish partnerships with core banking software platform providers and bring the security component to what they do, so that is another way, another channel, in which we can gain access to a broader range of those mid-tier and smaller institutions around the world.

<<Vincent Kover, Analyst, Needham & Company>>

Excellent. I have a question on market risks in particular, if you see any factors that would beat future growth?

<<Scott Clements, President and Chief Executive Officer>>

I think there are probably a couple of things I would touch on there that we pay a close attention to. Let me just say, first of all, in general, our – I don't think our problem or our challenges is a lack of opportunity. I think there's a tremendous amount of opportunity and we have an outstanding position banking financial services, but we can do much more, I think for those customers than we do today by organically and inorganically expanding the offering that we have just have long standing relationships with these institutions are qualified suppliers, security supplier to these institutions. These are things that are hard to get and are of high value.

I think a couple of challenges if we think, maybe, in terms of the competitive landscape for banks is really this, evolution of some non-traditional service providers, digital-only banks, other fin tech service providers that are carving out pieces of a traditional banking business.

I think we have to adapt to that and really find ways to access and deliver value to those new players in the financial services market and we have had some success with that already and doing business with the digital only banks that are emerging, just had, I know there's a webcast that we co-sponsored with Orange Money yesterday, I think it was we've provided the security for Orange Money, Romania for example, a new branch of that organization is digital only. And they found that our cloud delivery and the breadth of capabilities we have, have given them a high degree of security without an impact to their, really critical user experience. So, I think that's one thing that we have to really be aware of is that we can't just only serve the traditional customer.

We have to go out and access these new players in financial services. I think the second thing that bears probably watching is the evolution of digital identity schemes and that are being sponsored by government primarily in different parts of the world. Those are going to take some time to evolve, but we need to understand how those will work, how we can participate, how we can deliver added value around those digital identity offerings or capabilities that are being developed.

<<Vincent Kover, Analyst, Needham & Company>>

Excellent, Scott. Well, thank you so much for your time today. We're coming up at our time. If the audience does have any additional questions, please feel free to reach out to myself and my colleagues on the institutional equity sales team or your contact at Needham.

Scott, thank you, again. We hope everyone enjoys the final few days of the Needham Growth Conference and hope everyone has a lovely evening. Take care.

<<Scott Clements, President and Chief Executive Officer>>

Thanks, Vincent. Thanks, everyone.