CLPS Incorporation

(NASDAQ: CLPS)

Fourth Quarter and Fiscal Year 2018 Earnings Conference Call

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CORPORATE PARTICIPANTS

Rose Zu, *ICR Investor Relations*

Raymond Lin, *Chief Exescutive Officer*

Tian van Acken, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Gregg Hammerman, *Larky*

PRESENTATION

Operator:

Hello everyone and welcome to the Fourth Quarter and Fiscal Year 2018 Earnings Conference Call for CLPS Incorporated. Today's conference is being recorded.

At this time, I would like to turn the call over to Ms. Rose Zu from ICR for opening remarks and introductions. Please go ahead.

Rose Zu:

Thank you, Operator. Hello everyone and thank you for joining us on today's call. CLPS Incorporated announced its fourth quarter and fiscal year 2018 financial results yesterday after U.S. markets closed. An earnings release is now available on the Company's IR website at ir.clpsglobal.com.

Today we will hear from CLPS' CEO, Mr. Raymond Lim, who will start off the call with a review of recent Company developments and operating results, followed by the Company's CFO, Ms. Tian van Acken, who will address financial results in more detail. Following Management's prepared remarks, we will conduct a Q&A session.

Please remember that our discussions today may include forward-looking statements that involve a number of risks, uncertainties and other factors that could cause actual results to differ materially from the forward-looking statements. In that respect, I would like to read the following disclaimer applicable to such statements.

Please note that the discussion today contains forward-looking statements within the meaning of the Safe Harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Investors can identify these forward-looking statements by words or phrases such as may, will, expect, anticipate, aims, estimates, intends, plans, believes, potential, continue, is, are likely to, or other similar expressions. Among other things, statements that are not historical facts, including statements about CLPS' beliefs and expectations, the business outlook, and quotations from Management in this announcement as well as CLPS' strategic and operational plans are or contain forward-looking statements. Forward-looking statements involve known or unknown risks and uncertainties.

A number of factors could cause actual results to differ materially from those contained in any forward-looking statement, including but not limited to the following: the Company's ability to complete and successfully integrate various acquisitions into its business and operations, to decrease costs, to improve margins and to increase profits, and to leverage the target client base to expand the Company's market and geographical reach, the Company's potential inability to successfully manage completed, proposed or future transactions, the Company's ability to capitalize on and include InfoGain's performance into its own financial performance and results, the Company's ability to manage expenditures relating to research, development, and implementation of the Company's products and services and risks that such products may not be developed successfully or approved for commercial use, infringement of the Company's technology or the assertion that the Company's technology infringes the rights of other parties, potential for significant adverse changes in PRC government regulations, changes in tax laws and regulations, fluctuations in exchange rates, concentration of a substantial portion of the Company's revenues among a few customers, volatility in the market price of the Company's common stock, the Company's future issuance of non-equity compensation under its equity incentive plans, changes in key personnel, changes in currency exchange rates, growth through acquisitions including the ability to commercialize technology acquired through, and other factors referred to in the Company's annual report on Form 20-F for the year ended June 30, 2018, and other materials filed with the Securities and Exchange Commission. The Company undertakes no obligation to update forward-looking statements to reflect subsequent occurring events or circumstances or changes in its expectations, except as may be required by law.

It is now my pleasure to introduce CLPS Incorporated's CEO, Mr. Raymond Lin. Please go ahead.

Raymond Lin:

Thank you, Rose. Hello everyone and welcome to the CLPS' fourth quarter and fiscal year 2018 earnings call. We were pleased to conclude our fiscal year 2018 with solid results. Revenue from our IT consulting services helped drive our fourth quarter and fiscal year revenue growth by over 50% as compared to the respective period in the prior year.

Following our growth plan to increase revenues from existing clients and to win new clients, we enjoyed a sizeable increase in our fiscal year 2018 revenue due to our close relationship with existing clients and addition of over 20 global corporate clients, located domestically and overseas, to our client list. This pace of growth was in line with our expectation of strong market demand for highly skilled professionals, business IT solutions, and cost effective operations on a global scale.

In recent years, the economic change in China has encouraged a quicker level of activity across the financial service sector. Frequent and high stakes transitions require a higher level of technical support to conduct day-to-day operations. Given rising staff costs and the difficulties of hiring and training professional IT teams, an increasing number of banking, finance and insurance companies, either based in China or operations in China, turn to professional services providers like CLPS for customized IT solutions and consulting services.

According to an ITC report, the market size of China's banking IT solution industry in 2017 grew by 22.5% to an estimated value of over 5 billion compared with 2015. To capitalize on this trend, we've concentrated on horizontal expansion. Our ability to provide a scalable IT solution and our employees' rich technical knowledge helped us secure additional projects with existing clients and bring new clients. We strengthened our growth potential in IT staffing by successfully completing the acquisition and integration of Judge China, a growing IT and engineering talent solutions provider in China. We also continued to deliver thousands of training hours to our employees through our industry-leading talent creation program and talent development program.

Following our IPO recently, in working on the next chapter of our growth, we expect to enhance our horizontal expansion by focusing on geographic expansion. We have already started implementing this strategy with the acquisition of the Singapore-based IT service and consulting firm, InfoGain, in August of this year. We believe that InfoGain, a company that is also focused on the banking and financial industry, can help accelerate our overseas expansion across Southeast Asia and further expand our reach to other high potential regions. Also during 2018, we established a U.S. office and are actively looking for a general manager to lead its development.

In addition to horizontal expansion, our next chapter of growth will include vertical deepening of our product and service offerings. We believe that the ability to provide advanced technology will always be a prerequisite for the successful IT solution and consulting services provider. With our deep relationships with our clients, we believe that we are well positioned to understand their needs. To supplement our existing solutions, we will develop applications of emerging technologies like Big Data, process automation, Blockchain and the cloud.

In the year ahead, we will remain focused on the integrity of our service and products, committed to our employees' growth, and open exciting growth opportunities with our (inaudible) through our strategic alliance and acquisitions, thus we will grow horizontally and vertically. We will expand our global footprint and market share, creating future value for our shareholders.

This concludes my prepared remarks. I will now turn the call to Ms. Tian, our CFO to review the fourth quarter and fiscal year 2018 financial results. Ms. Tian, go ahead, please.

Tian van Acken:

Thank you. Thank you, Raymond, and hello everyone. I will briefly review our fourth quarter 2018 results first, followed by our full year results and our balance sheet. Please note that unless stated otherwise, all numbers are presented in the U.S. dollar terms.

Revenue in the fourth quarter of 2018 increased by $4.7 million or 51.1% to $13.9 million from $9.2 million in the same quarter of 2017. This increase was primarily attributable to the increase of revenue in IT consulting services. Revenue from IT consulting services increased by $4.7 million or 54.3% to $13.3 million or 96.1% of total revenue, from $8.6 million or 94.1% of total revenue for the same quarter of 2017. This increase was primarily due to the increasing demand for IT consulting services from banks and other financial institutions. For the three months ended June 30, 2018 and 2017, 46.9% and 52.6% of IT consulting service revenue were from international banks respectively.

Revenue from customized IT solution services decreased by $0.04 million or 6.9% to $0.06 million from $0.5 million in the fourth quarter of 2017. The year-over-year decrease in IT solution services was primarily due to the fact that some of our projects were and remain in progress and have not been completed as of yet, and therefore we have not recognized the revenue from such projects.

During the fourth quarter of 2018, revenue from other services increased by $0.03 million to $0.07 million over the fourth quarter of 2017. The-year-over year increase in other services was mainly due to the increasing demand from our customers in the fourth quarter of 2018.

Cost of revenue was $9 million compared with $5.2 million for the same quarter of 2017. Gross profit was $4.8 million, an increase of 22.7% from $3.9 million for the same period of last year. Gross margin decreased to 34.9% from 43% in the prior year period. The decrease was primarily due to the lower gross margin for new projects.

Selling and marketing expenses increased by $0.1 million or 24.9% year-over-year to $0.6 million. The increase was primarily due to the expansion of the pre-sales and marketing teams in Shanghai, Dalian in China to support operations. Research and development expenses increased by $1 million or 102.4% year-over-year to $2 million. The increase was attributable to an increase in the number of research projects and research employee headcount. General and administrative expenses increased by $0.1 million or 5.4% year-over-year to $1.7 million. The increase was primarily due to growth of staff in support sectors.

Operating income in the fourth quarter of 2018 was $0.5 million compared to $0.8 million in the prior year period. Operating margin was 3.4% for the quarter compared to 8.8% in the prior year period. Net income decreased by $0.2 million or 16.5% year-over-year to $0.8 million. Net income attributable to shareholders for the three months ended June 30, 2018 was $0.7 million, or $0.06 per basic and diluted share, compared with net income attributable to shareholders of $0.8 million or $0.07 per basic and diluted share in the prior year period.

Now, let's turn to our fiscal year 2018 financial performance.

Revenues were $48.9 million, an increase of $17.6 million or 56% from $31.4 million in fiscal 2017. The growth of revenue in fiscal 2018 was mainly due to the increase in revenue from IT consulting services. Revenue from IT consulting services increased by $18 million or 61.8% to $47.2 million, and accounted for 96.4% of total revenue, compared with $29.1 million or 92.9% of total revenue in fiscal 2017. The increase was primarily due to the increasing demand for IT consulting services from banks and other financial institutions. For fiscal 2018 and 2017, 46.8% and 54% of our IT consulting services revenue was from international banks respectively. In fiscal 2018, we strengthened our expertise in the financial industry to leverage our existing industry knowledge and grow our customer base of local Chinese financial institutions.

Revenue from customized IT solution services decreased by $0.2 million or 11.5% to $1.6 million for fiscal 2018 from $1.8 million for fiscal 2017. The year-over-year decrease in IT solution services was primarily due to some of ongoing projects for which we have not recognized the revenue. Revenue from other services was $0.08 million in fiscal 2018.

Cost of revenue was $31.3 million in 2018, an increase of $12.6 million or 67.5% from $18.7 million in 2017, which is generally in line with the growth of revenue. As a percentage of revenue, our cost of revenue was 63.9% and 59.5% for fiscal 2018 and 2017 respectively.

Gross profit increased by $5 million or 39.2% to $17.7 million from $12.7 million in fiscal 2017. Gross margin decreased to 36.1% from 40.5%. The decrease was mainly due to the lower gross margin for the new projects.

Selling and marketing expenses in 2018 increased by $1 million or 84.5% year-over-year to $2.2 million. The increase was primarily attributable to the expansion of the pre-sales and marketing teams in Shanghai and Dalian in China. Research and development expenses in 2018 increased by $3.6 million or 85.2% year-over-year to $7.8 million. The increase was attributable to an increase in the number of research projects and research employee headcount. General and administrative expenses in 2018 were $5.9 million, an increase of $0.2 million or 4% year-over-year. The increase was primarily due to the growth of staff in support sectors.

Operating income in 2018 was $1.7 million, an increase of $0.1 million or 7.5% from $1.6 million in 2017. Operating margin was 3.5% for the year ended June 30, 2018 compared to 5.1% for the prior year period. Net income increased by $0.5 million or 22.2% to $2.7

million in fiscal 2018 from $2.2 million in fiscal 2017. The increase in net income was in line with increased gross profit. Net income attributable to shareholders in fiscal 2018 was $2.4 million or $0.21 per basic and diluted share, compared with net income attributable to shareholders of $2.2 million or $0.18 per basic and diluted share in fiscal 2017.

For the year ended June 30, 2018 and June 30, 2017, our weighted average number of ordinary shares used in computing basic earnings per ordinary share was 11,517,123 and 11,290,000 respectively. For the year ended June 30, 2018, our weighted average number of ordinary shares used in computing diluted earnings per ordinary share was 11,636,367 shares.

Let's turn to our balance sheet. As of June 30, 2018, our cash and cash equivalents was $9.7 million compared with $4.8 million as of June 30, 2017.

Guidance and business outlook for 2019. For fiscal year 2019, we expect absent material acquisitions or non-recurring transactions total sales growth in the range of approximately 30% to 35%, and a net income growth in the range of approximately 30% to 35% as compared with the 2018 financial results. The foregoing guidance includes estimated 2019 financial results of the InfoGain acquisition, an equity in which we acquired an 80% equity stake in August 2018. In addition, this guidance necessarily assumes no significant adverse price change during fiscal year 2019. This forecast reflects our current and preliminary views, which are subject to change and subject to risks and uncertainties, including but not limited to potential accounting adjustments attributable to the InfoGain acquisition, as well as risks and uncertainties identified in our public filings.

This concludes our prepared remarks for today. Operator, we are now ready to take some questions.

Operator:

Thank you. Ladies and gentlemen, if you wish to ask a question at this time, please signal by pressing star, one on your telephone keypad. Please ensure the mute function on your telephone is switched off to allow your signal to reach our equipment. Again, please press star, one to ask a question.

Again, that is star, one to ask a question.

We will now take a question from Gregg Hammerman from Larky. Please go ahead.

Gregg Hammerman:

Hi, good morning. Thank you for taking this question. I'm curious if you could talk a little bit more about plans for expansion into North America and other regions of the world.

Tian van Acken:

Sure. In 2018—in August 2018, we were able to successfully acquire InfoGain in Singapore. Now, this will enable us to be able to set a foot in Southeast Asia and continue to be able expand to neighborhood countries, for example in Thailand, Malaysia, Indonesia, and so on and so forth. Now, we are opening an office in America, in the U.S. We plan to hire a general manager by the end of this year. The reason for the U.S. expansion is that we do have clients currently (inaudible) in the west coast. eBay, PayPal and Facebook are our current existing clients, so we are planning to service these existing clients at the same time and be able to expand in North America.

I hope this answers your question.

Gregg Hammerman:

It does. Thank you very much.

Tian van Acken:

Sure. Thank you.

Operator:

Again ladies and gentlemen, if you wish to ask a question, please press star, one on your telephone keypad.

There are currently no more questions queued. I will now turn the call back to Mr. Raymond Lin for closing remarks.

Raymond Lin:

Hi. This concludes our fourth quarter and fiscal year 2018 earnings call. Thank you for your participation. We look forward to updating you on the progress of our business in the next six months. Thank you and have a good day for those who are based in U.S., and have a good night for those who are based in mainland China and Hong Kong. Thank you.

Tian van Acken:

Thank you.

Operator:

Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.