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Verisk Analytics, Inc. (VRSK)

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Sherale and I will be your conference operator today. At this time, I would like to welcome everyone to the Verisk Analytics Q2 2019 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] .

Ms. Brodbar, you may begin your conference.

Stacey Brodbar

Head of Investor Relations, Verisk Analytics, Inc.

Thank you Sherale and good morning to everyone. We appreciate you joining us today for a discussion of our Second Quarter 2019 Financial Results. Today's call will be led by Scott Stephenson, Chairman, President and Chief Executive Officer, who will provide a brief overview of our business. Lisa Bonalle Hannan, President of Verisk Financial Services, will then provide an update on our Financial Services segment. Lastly, Lee Shavel, Chief Financial Officer, will highlight some key points about our financial performance. Mark Anquillare, Chief Operating Officer, will join the team for Q&A.

The earnings release referenced on this call as well as the associated 10-Q can be found in the Investors section of our website. www.verisk.com. The earnings release has been attached to an 8-K that has been furnished to the SEC. A replay of this call will be available for 30 days on our website and by dial-in. Finally, as set forth in more detail in today's earnings release, I will remind everyone that today's call may include forward-looking statements about Verisk's future performance. Actual performance could differ materially from what is suggested by our comments today. Information about the factors that could affect future performance is contained in our recent SEC filings.

Now I'll turn the call over to Scott.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Thanks, Stacey. Good morning everyone. I'm pleased to report that Verisk delivered another strong quarter, marked by a solid 7.2% organic constant currency revenue growth, which remains the most important measure of the health of our organization. Moreover, our growth was driven by continued broad based strength in our Insurance segment as well as marked improvement in our Financial Services segment.

At Verisk, it is our people that drive innovation, provide a great customer experience, and are critical to delivering our consistent and solid financial results. As such, we are keenly focused on maintaining an environment that attracts and retains the best talent through strong recruitment, leading talent development programs and management training efforts which ultimately result in highly engaged employees. I'm pleased to share that employment engagement at Verisk is on an upward trend, improving 2 percentage points from 2018. At the same time, we have maintained retention of our top performers at over 92% in each of the last three years in what is a very competitive labor market for our kind of talent.

From a recruiting perspective, this summer, we are hosting our largest class of interns ever with 119 interns across all our business units who can serve as a pipeline for permanent hires. On the training and development

front, we are investing in our future by hiring talent earlier in the talent pipeline and training them ourselves instead of competing for experienced talent.

As such, we have expanded our global Data Science Excellence Program, which is an internal four-plus-year rotational training program for data scientists with a Masters in Data Science or Data Analytics. We have also extended training programs for talent in key areas including cloud architecture and artificial intelligence.

We have enhanced our management training programs to include offerings for first-line managers as well as experienced leaders and have expanded our online education offerings in data science and analytics in connection with leading universities, such as Johns Hopkins and University of Michigan.

Lastly, as part of our global talent optimization strategy, during the second quarter, we opened a new office in Krakow, Poland. This office focuses on data science and analytics talent and we are seeing early success building out this team and have a strong pipeline of talent interested in joining Verisk. On the client engagement front, in June we hosted Verisk Vision in London, our client conference tailored to the London and European markets. We hosted approximately 300 attendees for a daylong event that focused on the ongoing transformation in the insurance landscape and covered areas including risk, claims and InsurTech such as cyber risk, artificial intelligence, anti-fraud analytics and digital transformation.

The event also featured the Verisk Innovation Lab, which showcased product demos featuring new technologies and industry applications which incorporate cutting-edge fields such as social media, image forensics, security and surveillance, aerial imagery and entity resolution. The event not only solidifies our position as an InsurTech thought leader, but it also strengthens our position as a key technology and data partner for the London and European insurance companies.

On the innovation front, we're seeing great success in gaining market share in personal lines due to strong sales of our LightSpeed suite of products. LightSpeed helps our insurance customers compete in the digital age as it utilizes innovative, data-forward advanced analytics that enable insurers to provide a fully bindable quote on just three simple pieces of information.

This addresses our customers' dual needs to both increase the velocity and efficiency of their operations by increasing the precision of their underwriting analytic. The result is more profitable conversion rates for our customers. Personal auto automation has led the way in this growth, quickly followed by personal property and small commercial.

At Wood Mackenzie, we continue to be encouraged by the early results of our data analytic platform called Lens. We have a strong pipeline of interest and continue to sign up new subscriptions with major oil companies, independents and global investment banks. Additionally, we are seeing solid double-digit growth in both visits and unique users to the platform.

We continue to work in partnership with our customers to deliver an offering that is unique in the marketplace, one that is scalable, dynamic and integrated into their workflows. We plan to add the next module of global upstream valuations to the Lens platform by year-end 2019 which we think will be very well received by the market.

And in Financial Services, we're seeing great success with our Merchant Analytics platform which Lisa will talk to you about in more detail. Finally, we continue to be engaged on the strategic acquisition front with a focus on finding high return on invested capital transactions that leverage our scale, existing resource and deep domain expertise. We recently announced the acquisition of Keystone aerial surveys. Keystone is a leading aerial survey

company with operations that cover the entire United States. Keystone will become part of Geomni and it demonstrates our commitment to becoming a leader in aerial imagery, property analytics and geospatial data solutions. The addition of Keystone will accelerate our nationwide imagery coverage effort and improve our refresh rate as we strive to bring our customers the most innovative and technologically superior geospatial solutions.

And now I'll turn the call over to Lisa to provide some insights on our Financial Services segment.

Lisa Bonalle Hannan

President, Verisk Financial, Verisk Analysts, Inc.

Thank you, Scott. I'm excited to have the opportunity to provide you with an update on Verisk Financial Services, our business unit built through the combination of the legacy Argus platform with acquisitions that added capabilities and expanded our solution set. Now that I've been in the role of President, Verisk Financial for just over a year, it's a great time to discuss the progress we've made over the past 12 months, provide an update on our key strategic initiatives and share our vision for the future.

To start, I think it's important to take a step back to better understand where Verisk Financial Services is in our evolution and where we're headed. At the start of 2017, the Financial Services segment of Verisk consisted of the Argus business, which is a data-contributory consortia business, working with the leading banks and payment companies around the globe, including the top 30 credit card issuers in North America, the UK and Australia.

Argus offers our customers unique solutions, such as tracking and measurement of over \$2 trillion worth of consumer spending annually, as well as industry benchmarking and portfolio profitability analytics. Throughout 2017, we made several business acquisitions that aligned from a strategic and financial perspective and added capabilities to our existing services.

In early 2018, we dedicated significant attention to integrating the acquired companies from an operating perspective and we began creating a unified go-to-market presence under the Verisk financial brand. In May of 2018, the management team went through a comprehensive strategic analysis of each of our solutions within Verisk Financial. We examined critically and dispassionately what Verisk Financial is doing well and where we could improve. Based on this analysis, we developed an integrated strategic plan for the business.

The first change, which many of you recall from our December Investor Day, was to align our go-to-market strategy around four solution sets. The first of these is portfolio management solutions, our legacy consortia-based products which provide industry benchmarking and portfolio profitability analysis for credit cards, payments and retail banking customers around the globe.

Second is credit risk and fraud management solutions, our portfolio of bankruptcy and merchant acquirer risk solutions and our new suite of fraud solutions for our banking clients. The third is spend analytics and marketing solutions, which encompasses our cards' marketing models, consumer and merchants' insights and media measurement solutions and finally enterprise data management solutions, comprised of our global regulatory reporting platform, and client-specific data management, MIS and data advisory solutions.

I'm happy to report that one year in, we're seeing the benefits of this solution-based orientation beginning to pay off. There is momentum in each of our solution sets, with particularly strong performance from our media measurement, merchant analytics and portfolio management solutions during the first half of the year. And while enterprise data management is a newer and developing business for Verisk, which tends to have more quarter to

quarter variability, we are experiencing sequentially improving trends with the introduction of some of our key strategic initiatives in that area.

In addition to reorienting our business, we've also implemented a number of operational improvements, including strengthening and reorganizing our sales team around the four solution sets for a more comprehensive and holistic go-to-market sales strategy and implementing Lean/Six Sigma and process automation. These changes have already created significant benefits to our business. For example, our process improvements for portfolio and benchmark reporting have led to a 35% reduction in processing time each month and the automation of report summarization module alone for benchmarking led to a labor savings of 200 hours per month, allowing us to free up resources for new product development efforts.

We believe that the investment in time to improve our operations ultimately creates a better environment for our innovation and growth. As we brought several smaller businesses together with our Argus platform, we've also made some key strategic decisions. We have rationalized head count and updated our client pricing structure for our enterprise data management offerings based in India; we have reduced our reliance on business opportunities that led to onetime short-term revenues in favor of longer-term subscription-based risk; and most recently, we sold our Verisk retail loss prevention business as it was no longer a fit within our new Verisk Financial Strategic roadmap.

Collectively, these decisions have led to a stronger, more aligned, Verisk Financial Services unit that is better positioned for future growth. As we look forward, we're ready to embark on the next phase of our business transformation. In addition to our relentless commitment to continuously improving our customer experience and our existing solutions, we are focused on long-term strategic growth, which is underpinned by the key strategic initiatives that we shared during our Investor Day. These include introducing our next-generation benchmarking platform, expanding our spend analytics solutions globally, building our fraud solutions, beginning with the fraud consortia in Mexico, advancing our cloud migration and developing a global regulatory analytic platform as part of our enterprise data management solutions. All of these initiatives are underway, meeting key milestones and beginning to deliver.

Of particular note, we are getting extremely strong market interest in the Mexico cards fraud consortia, which will deliver our first new consortia dataset since 2016 when we launched the Australian card study and the global regulatory platform as regulators around the globe embrace a data-driven approach to oversight. Our experience working with the OCC, the Fed and the CFPD in the U.S. as well as our work for the Lloyd's syndicates in the UK uniquely position us to meet the needs of both regulators and their regulated entities.

In addition to Verisk's financial strategic initiatives, we're also accelerating our cross-Verisk collaboration, working with our colleagues in the Insurance segment. We are currently working with our partners in Underwriting & rating on enhancing lead generation and market prospecting as well as working with our colleagues in Claims to collaborate on enhanced fraud solutions.

In summary, I'm proud of our team and the progress we've made over the past year as we have synthesized a series of acquisitions to create Verisk Financial Services, a single, cohesive operating unit. We have made tangible progress fusing long-term vision with near-term operating execution. Our bias is to action with the understanding that a world-class business isn't created overnight, but is instead the sum total of numerous incremental changes and consistent execution over time.

We are confident in our long-term growth potential and look forward to sharing additional progress updates with you in the future.

With that, let me turn the call over to Lee to cover our financial results.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

Thanks, Lisa. First, I would like to bring to everyone's attention that we've posted a quarterly earnings presentation that is available on our website. Presentation provides background, data trends and analysis to support our conversation today.

Moving to the financial results for the quarter. On a consolidated and a GAAP basis, revenue grew 8.5% to \$653 million, net income decreased 2% to \$150 million, while diluted GAAP EPS declined 1.1% to \$0.90 per share for the second quarter 2019. As we previewed on last quarter's earnings call, both GAAP net income and diluted GAAP EPS were negatively impacted by the acceleration of \$6 million in stock-based compensation in the quarter. Let us now focus our quarterly discussion on our organic constant currency results for all year-over-year growth rates and to eliminate the impact of currency fluctuations, recent acquisitions for which we don't have full year-over-year comparisons, non-operating acquisition-related costs including earn-outs, dispositions and nonrecurring items. We believe these are the best measures to evaluate the health of our overall business and are the metrics we use in our own compensation plans.

On an organic constant currency basis, Verisk delivered revenue growth of 7.2% in the second quarter of 2019, reflecting organic growth across all three segments and delivering on our long-term target of 7% growth. Growth was led by our Insurance segment and we also delivered improving trends in Financial Services.

Organic constant currency adjusted EBITDA growth was 5.2% and was 7.3% after normalizing for the accelerated expensing of stock-based compensation. Total adjusted EBITDA margin for the quarter was 46.6%, down from the 47.9% in the prior year, primarily the result of the acceleration of stock-based compensation, which decreased margins by approximately 1%. This total adjusted EBITDA margin includes both organic and inorganic revenue and EBITDA.

Acquisitions decreased total adjusted EBITDA margin by approximately 20 basis points in the period. The headwind from the acceleration of stock-based compensation is also reflected in the individual segment results as these costs have been allocated based on revenue contribution to Verisk.

On that note, let's turn to our segment results on an organic constant currency basis. As you see in the press release, Insurance reported 7.8% revenue growth, while adjusted EBITDA increased 5.1%. Within our Underwriting & rating business, growth was balanced across personal lines and commercial lines. We saw healthy growth in our industry standard insurance programs, property-specific underwriting and catastrophe modeling solutions revenue.

We are seeing strong uptake of our new innovative solutions including LightSpeed Auto as our new data-forward products are designed to meet the needs of our insurance customers for quicker, more efficient and easier-to-use solutions.

Within Claims, the strong growth was driven by solid performance in claims analytics, repair cost estimating and remote imagery solutions. This was offset in part by modest weakness in workers' compensation claim resolution services. Total adjusted EBITDA margin declined 140 basis points to 53% from 54.4% in the prior year period.

Energy and Specialized Markets delivered revenue growth of 5.5% for the quarter. Strong sales of market and cost intelligence solutions drove the growth. We also had positive contributions from core research and our environmental health and safety business. This was offset in part by softness in our consulting services related to strong performance from last year.

Adjusted EBITDA increased 3.7%, reflecting ongoing investments in breakout opportunities like Lens and our chemicals, subsurface and power and renewables breakouts.

Total adjusted EBITDA margin declined to 29.9% from 31.8%. The largest factor in that margin decline was a non-operational foreign currency translation loss. Excluding this item, margin in the segment would have been flat. Financial Services revenue increased 6.1% in the quarter, led by solid growth in portfolio management and spend-informed marketing solutions revenues. As Lisa mentioned earlier, these improving results reflect the impact of the strategy that we implemented in 2018 to transition Verisk Financial Services from a top-down orientation to a bottoms-up approach with an emphasis on steady growth.

We expect that investors will continue to see more clearly the long-term growth potential of this segment over time as we continue to make progress with the transition. Adjusted EBITDA increased 11.9% and total adjusted EBITDA margin increased to 31.9% from 30.3%. Strong focus on expense management as well as leverage from the revenue growth drove the margin expansion.

Reported interest expense was \$31 million in the quarter, down 4.7% from the prior year quarter due to the net repayments of our revolving credit facility. Total reported debt was \$2.5 billion at June 30, 2019, down from \$2.7 billion at year-end 2018 and our leverage at the end of the second quarter was 2.1 times.

Our consolidated cash and cash equivalents were \$153 million at June 30, 2019. Our reported effective tax rate was 19.7% for the quarter compared to 17% in the prior year quarter, primarily due to a lower level of option exercises. We maintain our estimate of our effective tax rate in the full year 2019 to be between 19% and 21%.

Adjusted net income was \$184 million and diluted adjusted EPS was \$1.10 for the second quarter, up 4.1% and 4.8% respectively. After normalizing for the impact of the incremental stock-based compensation, diluted adjusted EPS would have grown 8.6%. This increase reflects organic growth in the business, contributions from acquisitions, a decrease in interest expense and lower share count. The benefits were partially offset by an increase in depreciation and amortization expense and a higher effective tax rate.

Net cash provided by operating activities was \$200 million for the quarter, down 3.4% from the prior year. Net cash provided by operating activities was \$566 million, year-to-date up 6% from the prior year.

Capital expenditures were \$47 million for the quarter, down 16.4% from the prior year. CapEx represented 7.2% of total revenue, reflecting the expected decline in capital intensity as the result of reduced capital spending on the Geomni initiative following its initial ramp-up. We continue to expect capital expenditures to be in the range of \$220 million to \$240 million for 2019. Free cash flow was \$153 million for the quarter, an increase of 1.5% from the prior year. Free cash flow was \$474 million year-to-date, an increase of 9.1% from the prior year.

During the second quarter, we returned \$91 million in capital to shareholders through share repurchases and dividends. We repurchased approximately 361,000 shares at a weighted average price of \$138.32 for a total cost of \$50 million. At June 30, 2019, we had \$303 million remaining under our share repurchase authorization. In addition, we initiated a new \$75 million accelerated share repurchase to be executed in the third quarter.

On June 28, 2019, we paid a cash dividend of \$0.25 per common share and on July 24, 2019, our board of directors approved a cash dividend of \$0.25 per share of common stock payable on September 30, 2019, for shareholders of record on September 13, 2019.

We are excited about the opportunities to invest in our business and continue to manage capital prudently through internal investment, strategic acquisitions and the return of capital to shareholders through dividends and share repurchases. We remain confident that we have the financial strength and capital structure to support investment for the long term.

We appreciate all the support and interest in Verisk. In order to make time for questions from the large number of analysts covering the stock, we ask that you please limit yourself to one question. I'll ask the operator to open the line for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] . You do have a question from Toni Kaplan.

Toni M. Kaplan

Analyst, Morgan Stanley & Co. LLC

Q

Thank you. Good morning. Just taking a step back, you've had margin contraction in insurance for the past 10 quarters and you've been investing and experiencing an impact from dilutive acquisitions. But at some point, perhaps we could see that reverse and so just given operating leverage of the business overall, I guess at what point do you think that we could start to see some margin leverage in Insurance specifically? Thank you.

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

So Toni, thanks for the question. I think we've been focused on the year-over-year results. And so when we look at this quarter's year-over-year performance from a margin standpoint, I think it's important to understand that if you take the timing – compensation timing impact of about 1%, the margin in the second quarter of 53% would have been 54% versus 54.4% in the prior-year period. And so that certainly is – I think we would describe as flattish and at the same time, recognizing that we have been making some significant investments in Geomni and telematics that have been accelerated as we've ramped up, in particular, Geomni. And so we are making those investments with the expectation that those will be contributing to our margin improvement over time as we reach scale in those businesses. So I think it's the financial dimension and I'll turn it over to Mark to provide some additional color here.

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

I'll echo the investment we're making. I think the thing that I always like to emphasize is that inside investment, what we have seen is our top line organically growing quicker, which means our bottom line EBITDA cash flow is growing quicker. So I think that's been successful. We have been disciplined in the way we spend, invest. And I think there is scale clearly in the business as we take on pretty big investment in something like aerial imagery and IoT. So I just wanted to provide a little bit of color that I think we've had quite a bit of success in the growth side of things.

Toni M. Kaplan
Analyst, Morgan Stanley & Co. LLC

Q

Excellent. Thank you.

Operator: Your next question comes from Manav Patnaik.

Manav Patnaik
Analyst, Barclays Capital, Inc.

Q

Yeah, hi, good morning. I guess since you have Lisa on the call, maybe I can just ask on the Argus comments, and I think there was a comment about updating the pricing structure to more subscription-based revenue and that might have been specific to the EDM business based in India. So I was wondering if you could just elaborate on that with some context on how much of Argus today is subscription and are there any other areas there that you could see similar pricing structure updates?

Lisa Bonalle Hannan
President, Verisk Financial, Verisk Analysts, Inc.

A

Sure. There were two things. The first is that as we've begun integrating the companies that we acquired, the business that we acquired in India, we did go through a rigorous review of all of their solutions and the pricing for those solutions relative to our investment in those solutions. Based on that, we have updated our pricing structure for solutions based out of India. Those are primarily subscription-based solutions. In addition, across all of the Argus business, we have also been changing and shifting our mix towards more subscription-based and product-driven solutions as opposed to one-time implementations or initial development revenue upfront and more heavily weighted in the current year. As we implement some of our data analytics solutions, the enterprise data management solutions, we're now orienting those to more of a longer term subscription base as wells. So in all of the things that we're doing, we're looking for longer-term subscription-based revenue. Today, the percentage of revenue that's subscription-based is over 65%, close to 70%. We continue to move that up.

Operator: Your next question comes from Tim McHugh.

Timothy McHugh
Analyst, William Blair & Co. LLC

Q

Yes, thanks. Just wondered on LightSpeed, you highlighted that this quarter. So can you talk about how customers are adopting that? And is that displacing prior methods of kind of underwriting and acquiring customers or is it being used as an incremental? And then I think recently you talked about taking Sequel to the U.S., which I believe is a new initiative. So I guess talk about the plans and how aggressively you're pursuing that. Thanks.

Mark V. Anquillare
Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

Great. Thanks, Tim. This is Mark. So let me first talk a little about LightSpeed. Inside of the insurance process, there has typically been a two-step process. First, you provide a quote and then people run what are typically all the reports and gather the information. There's a [ph] clause there before they bind (28:56) the policy. So what we have attempted to do inside of our ecosystem is create a very automated approach so they can flow this business. That's a term of art. It can be completely automated, more accurate, more efficient and we're bringing all the data needs upfront. We call it our data-forward strategy.

So that represents kind of a different way of go-to-market. You can actually provide a quote, bind it all in one. Just as an example, you talk about digital engagement, on the personal auto front, on the car insurance, about 33% of all quotes you get online change after people do that work. So very poor experience. And what we've done is we've taken things like motor vehicle reports, loss histories, prior losses, prior coverage, all the things about the driver and brought that upfront and that has been adopted, well accepted and we have had nice success on the insurance front.

That kind of moves across auto to homeowners and even into small commercial. That is our theme and that's where we're headed. I'm going to now flip over to the question on Sequel. Just to remind everybody Sequel's solution set, which is for the most part all of the [ph] software-to-service policy, starting from the upfront to NIM (30:15), underwriting, onto claims, all of that very much a industry standard inside the London insurance market, primarily around things that what I'll refer to as ISO and most of Verisk hasn't been as focused on the [ph] non-admin (30:35) market, meaning the specialty lines, the really complex risks.

What we have attempted to do is use some of that technology in some of our products here, but more importantly what you saw in the press release is for specialty or complex insurance risks, we are going to bring Sequel to the United States. We seem to have quite a bit of interest. We are leveraging the teams in place, both on the claims side and on the ISO side or the underwriting side, and I think we're very optimistic that inside that niche specialty market, we have a solution that can win today and we're optimistic.

Timothy McHugh
Analyst, William Blair & Co. LLC

Q

Thank you.

Operator: Your next question comes from Andrew Steinerman.

Andrew Charles Steinerman
Analyst, JPMorgan Securities LLC

Q

Hi, it's Andrew. Could you give us a sense how your Energy clients are doing as they're increasing spend with WoodMac, which areas of interest is increasing with those Energy clients? And also you mentioned cost intelligence with Energy. I assume that's around PowerAdvocate and could you give a sense of how PowerAdvocate is doing and evolving within Verisk.

Scott G. Stephenson
Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yes. So, Scott here and in reverse order. The PowerAdvocate suite is doing well. The traditional customer set for PowerAdvocate has been utilities. A lot of the motion in the business has been taking the same kind of solution into the oil and gas space, which is one of those places where PowerAdvocate is advantaged by being tied to the business [indiscernible] (32:12) substantial footprint we've already got in the oil and gas space.

And then over on the traditional WoodMac side in the oil and gas space, basically there is a lot of interest in what the Lens platform provides, which is essentially more real-time and more integrated into the customer workflows and so it's essentially doing what we thought it would do, which is positioning our content even more deeply in the customer workflows and that's the direction of travel, basically, as the United States has sort of been differentially adding to the global supply curve, the U.S. environment is one where you're making operating decisions all the time as opposed to the traditional offshore decadal kind of investment cycle. And so the need for real-time, the need for more benchmarked kinds of data just goes up and that's exactly what we've been positioning for.

So, one of the leading metrics there is the rate of adoption of Lens among the oil and gas companies, both the integrated global as well as the more pure-play E&P companies and we're very happy with what's happening there.

Andrew Charles Steinerman
Analyst, JPMorgan Securities LLC

Q

Great. Thanks, Scott.

Operator: [Operator Instructions] . Your next question comes from Gary Bisbee.

Gary E. Bisbee
Analyst, Bank of America Merrill Lynch

Q

Yeah, hi, good morning. Thanks for the detailed rundown on the Financial Services business. It sounds like you're making a lot of progress there. I guess the key question is how do those changes impact how we should think about the medium or longer term growth potential of the business and maybe also profitability?

Historically, before the recent couple years of challenges, I think there was clear discussion on this being the fastest growth or growing above the corporate average. Is that a reasonable and sustainable target at some point in the future based on the progress you're doing? Thank you.

Lee M. Shavel
Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

A

Thank you, Gary. This is Lee. So we, for all three of our segments, our expectation that all of them have the ability to meet or exceed our long-term targeted 7% organic constant currency growth rate, as well as to realize the operating leverage and achieve EBITDA faster than that.

And so I think one of the challenges for investors which we certainly empathized with is that given some of the large contracts and contract transitions in the business, made it difficult to see the underlying growth within the business, and so we wanted to focus on really developing the bottoms-up approach to the business that Lisa described in each of the four solutions areas.

And I think in those more traditional, in the kind of the foundational benchmarking areas, those are probably mid-single digits growth elements and the fraud bankruptcy, enterprise data management, marketing spend analytics, are newer, higher growth businesses that we think contribute to achieving that 7% growth.

So no change in terms of our expectations of what the Financial Services business can achieve and can contribute to our overall growth rate. But there has been a shift in making sure that we're delivering that on a more sustainable and granular basis and that investors have greater clarity on that growth, which certainly I think – we think this quarter is a clear step in that direction.

Gary E. Bisbee
Analyst, Bank of America Merrill Lynch

Q

Thank you.

Operator: Your next question comes from Joseph Foresi.

Joseph Foresi

Analyst, Cantor Fitzgerald Securities

Q

Hi. I was wondering if you could talk about Geomni and some of the potential contribution to revenues and the CapEx that you put in there and what stage that's in. Thanks.

Mark V. Anquillare

Chief Operating Officer & Executive Vice President, Verisk Analytics, Inc.

A

This is Mark. Let me try to address that. So the opportunity with Geomni is very much focused on first ensuring that we have coverage, frequent refresh of those images, and with that, that library of information, our first step was really to address the claims-focused solutions in the insurance space. So literally by using those advanced pictures and some advanced analytics, we can get measurements and do repair cost estimates for the claims departments from the sky. They then use maybe some desktop adjusting, but for the most part, a majority of that is done in a very automated fashion, saving a very significant cost to the insurers as well as it's safer and more accurate.

We have opportunities to bring that into underwriting as well as the world of cat modeling. But I want to highlight, though, that as much as our first use case was insurance, there's probably and there is bigger opportunities outside of the insurance space. So we have partnered up with some folks that are doing construction. We're doing work in the solar space. We're doing work across various verticals where that imagery and those exact measurements are very helpful. And Geomni is contributing nicely to that claims category inside of our growth rates for insurance.

So it continues to be investment-oriented. Keystone accelerates that investment for us because it replaces what we have to buy in the form of sensors, meaning big cameras as well as the planes. Keystone has it. They have operations. They have pilots. So this will accelerate our path to strength there.

Joseph Foresi

Analyst, Cantor Fitzgerald Securities

Q

Thank you.

Operator: Your next question comes from Andrew Jeffrey.

Andrew Jeffrey

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Hi. Good morning. Thanks for taking the question. I wonder, and I'm thinking about LightSpeed, but broadly across your business, can you talk about the extent to which InsurTech maybe is driving some of your growth and how structural that is and whether as you look out of the market today, that's a potential growth acceleration driver over the next year or two?

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yeah, Scott here. It has two effects on our business. So one is if you think of InsurTech as a category of digitally enabled innovations, this is one of the things that actually our customers in all of our segments are looking for. They themselves are trying to transform their businesses, making use of digital methods and so here we are with our particular solution sets. They are rotating their budgets in the direction of making use of modern methods, so that's just a fundamentally constructive factor across everything we do basically.

But in addition to that, when people refer to InsurTech, partly what they're talking about are new companies that are basically using digital methods fundamentally to change the distribution of insurance, the sourcing of insurance customers presenting the insurance product to the end user. And so these are some of the companies that get celebrated as start-ups, that are – sort of kind of present a new face to the insurance consuming world.

We've done very well with those companies as customers. So here they are, they're inventing a new insurance company and we find that they just – that they have voted with their feet and basically want to use our industry standard solutions so that they have the benefit of efficiency, fighting fraud in effective ways.

One of the big issues you have when you emerge as an insurance company is you don't have a lot of experience and so how are you going to anticipate where your losses are going to be and at what level? That's one of the things that our solutions just give you right out of the box.

So it's really gratifying to see how many of them come our way when they form and then all of a sudden – and I had the chance to visit with the CEO – even recently with the CEOs of some of these highly celebrated emergent insurance companies and they just – they really, really like being a partner with Verisk.

Andrew Jeffrey

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thanks.

Operator: Your next question comes from Jeff Meuler.

Jeffrey P. Meuler

Analyst, Robert W. Baird & Co., Inc.

Q

Yes. Thanks. Scott, I was just hoping you could extend your earlier comments around kind of human capital and the opening of the Krakow office. You relatively, I guess recently acquired WoodMac and one of the points on the acquisition was expanding your global office footprint, but I know data nationalism always top of mind. So just roughly what percentage of your data and analytics and tech head count or innovation head count is in the United States or more expensive labor markets today? Like how big is this long term opportunity as a margin enhancement for you? Thank you.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Yeah, so the first thing that motivates us on this is access to talent. That's the thing that this is really about. So the reason we like Krakow so much is as we expand our business in Europe, especially Continental Europe, having high quality, technically deep people who also will get steeped in the verticals that we serve, having them right there to interact more easily with our customers is a really, really nice feature here.

And I'm glad you picked up on the point I was making about talent because that really is the wellspring for our company. And there's no question that everybody – we have about 9,000 associates at Verisk now. Everybody really counts. There are some of the technical disciplines that are the ones that are particularly in demand. I ticked off a few of those. So being able to make cloud architectures that are secure and really work, sort of data science as in the transformation of the data. There's also a big data engineering dimension always to what it is we do.

And so there's no question that over the last couple of years, as we have built those communities of people around Verisk, differentially the additions have been overseas between what we do in Continental Europe, both in Spain and in – now in Poland. We have added quite a few people in India.

And so as a percentage of the additions to the team that we've made, they're coming more not in the United States than in the United States of late. Of course, we're building both sides, but relatively it's even more overseas. I don't see that changing. And it is constructive from a cost point of view as well, but to me that's just a marker, actually, of supply and demand. And we're just trying to make sure that we are in as many places as, A, we intend to serve, and B, can provide great talent.

And the last thing I'll just emphasize again is the develop ourselves mentality that we have here. We feel very rewarded for having gone in a direction that I think by degrees at least is a little bit different than what some other companies do because several years ago we recognized if we're just going to count on our ability to go into the market and hire already experienced people, we're essentially saying we're going to let somebody else solve our challenge, the talent challenge.

And we said well, no, we can do better than that, and so we've just gone very early into the talent pipeline and we have felt very rewarded for doing that.

Jeffrey P. Meuler

Analyst, Robert W. Baird & Co., Inc.

Q

Got it. Thank you.

Operator: [Operator Instructions] Your next question comes from Bill Warmington.

William A. Warmington

Analyst, Wells Fargo Securities LLC

Q

Good morning, everyone.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

Good morning.

William A. Warmington

Analyst, Wells Fargo Securities LLC

Q

So the acquisition of Keystone last week brought to the front the question of how much coverage of the U.S. do you have now and is that enough because you've been – I know you've been talking about going into Japan and Asia, so in that context, I want to see how much is left to go in the U.S.? And then as you look out internationally, is this going to be the beginning of a new investment cycle in geospatial for Asia and how much you think it will be and how long do you think it will take?

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

A

So Mark, you may want to add to this, but I'll just kick off. So in the United States, we are approaching what we would consider full coverage. Now, you have to understand coverage as both the square miles that you are

imaging, but also the frequency with which you are imaging them. And so with respect to being able to reach all of the important corners of the United States, we are very, very close to being there.

With respect to the frequency of the refresh, that may always be something of a moving target. These data sets are not commodities and one of the ways that you make them to have the quality of not being a commodity is the freshness of the data. So we will always be taking account of customer needs and competition in order to determine how frequently are we refreshing the images. So when you think about coverage, you have to think about both of those.

With respect to overseas markets, we actually already do do some of this work in other places and basically the methods that we developed, the ability of the team to automatically interpret the image sets, that works everywhere. So as we build out our franchise generally and insurance is one of the killer apps for remote imagery. As we build out the insurance franchise globally, I think it's very clear we will want to come in behind with these methods. But it will – we've still got plenty of room to run in the United States and then we will sort of build it I think organically and consistently with the rate that our insurance franchise grows outside of the United States.

William A. Warmington

Analyst, Wells Fargo Securities LLC

Q

Thank you.

Operator: Your next question comes from George Tong.

George K. Tong

Analyst, Goldman Sachs & Co. LLC

Q

Hi. Thanks. Good morning. Historically, enterprise data management and fraud solutions were the two underperforming areas within Financial Services. This quarter, all solution sets within Financial Services saw sequential improvement. Can you elaborate on the relative performance here and specific initiatives you'd call out that should drive continued acceleration in revenue growth in this segment?

Lisa Bonalle Hannan

President, Verisk Financial, Verisk Analysts, Inc.

A

So it's true, all of the segments saw sequential improvement. The enterprise data management sector is the sector that will continue to be lumpy and have variability on a quarter-over-quarter basis. Those contracts are very long-term contracts, often delivered through RFPs, and so the sales cycle is very long and they also – some of them end. Some of the work that we've done on more of a client-by-client bespoke enterprise data management solution basis ends. So it's really about building a book of business there and getting to a level of sustainability that allows us to meet that level of consistent performance as we see contracts end and new contracts begin within a quarter and quarter to quarter.

Continued improvement in that sector, that is a sector that we're looking to grow over the long term and we'll continue to see lumpiness on a quarterly basis over the short term, but we do hear and continue to feel that the market is receptive to the solutions we're offering. Most particularly, we are hearing good reception to the global regulatory reporting platform.

Regulators around the globe are changing the way they do their oversight. They are creating, they are leveraging deep and rich granular data to do that work and we believe we're uniquely positioned to serve in the financial sector there.

Operator: And your next...

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Operator? Go ahead.

A

Operator: And your next question comes from Ashish Sabadra.

Ashish Sabadra

Analyst, Deutsche Bank Securities, Inc.

Thanks for taking my question. Just a quick two-part question on the Energy side. Any color on the softness in the consulting services? Is that mostly difficult comps? And then just where are we in terms of investments for the breakout opportunity? Which inning are we, and when can we start to see margin expansion in that segment? Thanks.

Q

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Yeah, so, go ahead, Lee.

A

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

Ashish, I may just want to get clarity around the second part of the question, I had a little difficult time hearing you. So on the first element in terms of the consulting revenue, some of it was a function of a very strong second quarter in 2018. We also saw among some of the large national oil companies some political transitions that delayed some of the revenue that we had anticipated in the quarter. We do not think that that was a revenue at risk, but simply a delay of some of that revenue. And then with regard to margin, if that was the question and the impact of the breakouts on the margin for Energy and Specialized Markets, Ashish, was that the thrust of your question?

A

Ashish Sabadra

Analyst, Deutsche Bank Securities, Inc.

Yes, yes, yes, that's right. Thanks.

Q

Lee M. Shavel

Chief Financial Officer & Executive Vice President, Verisk Analytics, Inc.

Yeah. So thanks for raising that. Within Energy and Specialized Markets, I think it's important to note that in this second quarter that a large part of the decline in the revenue, in fact the largest single element was an FX gain adjustment, which reduced margin by approximately 2%. That's a function of the dollar-pound exchange rate and valuation of our net current assets that influence that.

A

And so that would, absent that impact, which fluctuates from quarter to quarter, we would have had a higher margin. In addition, that margin also bears approximately the 1% impact of the timing from a compensation standpoint. So absent those two non-operational elements, it reflects the operating leverage and the margin

expansion that we are experiencing in the core business, while at the same time investing in new initiatives like Lens and the breakout areas like subsurface, power and renewables, and those elements.

And so I think we feel very good, this – the quarter, the numbers are distorted by that compensation timing issue and the FX, but overall from a pure operating standpoint, we actually saw margin expansion. And if I may, I want to emphasize this dynamic, to go back to Toni's question around the insurance side, in each of our businesses putting aside the FX impact as well as the timing issue, all of our insurance businesses saw an expansion in their operating margin.

And so that's the underlying operating leverage that drives our margin up and then we are deliberately making decisions from an investment standpoint with the breakouts in terms of how much of that do we want to spend down with an overall objective of increasing that margin over time and that's – we think that's a very healthy dynamic. It's important for continuing investment, but it's also important to understand that absent that investment, we are seeing that operating leverage and that margin expansion improve as we grow. It's just that when you look at the net number, there are various nonoperational impacts and investment impacts that are affecting that. Hopefully that addresses your question.

Ashish Sabadra

Analyst, Deutsche Bank Securities, Inc.



Yes. Thanks. Thanks for the color, Lee.

Operator: There are no further questions at this time.

Scott G. Stephenson

Chairman, President & Chief Executive Officer, Verisk Analytics, Inc.

Okay. Well, thank you everybody for joining us. We've scheduled a number of follow-ups with you. Look forward to that. Thanks for your interest and talk to you soon. Have a great day.

Operator: Thank you all. This does conclude today's conference call. You may all disconnect.

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