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Deluxe Corp. (DLX)

Q2 2024 Earnings Call

CORPORATE PARTICIPANTS

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Charles Strauzer

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by, and welcome to the Deluxe Quarterly Earnings Conference Call. All participants are currently in a listen-only mode. And today's call is being recorded.

At this time, I would like to turn the conference over to your host, Vice President of Strategy and Investor Relations, Brian Anderson. Please go ahead.

Brian Anderson

Vice President, Strategy & Investor Relations, Deluxe Corp.

Thank you, operator, and welcome to the Deluxe second quarter 2024 earnings call. Joining me on today's call are Barry McCarthy, our President and Chief Executive Officer; and Chip Zint, our Chief Financial Officer. At the end of today's prepared remarks, we will take questions.

Before we begin and as seen on the current slide, I'd like to remind everyone that comments made today regarding management's intentions, projections, financial estimates, and expectations about the company's future strategy or performance are forward-looking in nature, as defined in the Private Securities Litigation Reform Act of 1995.

Additional information about factors that may cause actual results to differ from projections is set forth in the press release we furnished this afternoon in our Form 10-K for the year ended December 31, 2023, and our other company SEC filings.

On the call today, we will discuss non-GAAP financial measures, including comparable adjusted revenue, adjusted and comparable adjusted EBITDA and EBITDA margin, adjusted and comparable adjusted EPS, and free cash flow.

In our press release, today's presentation and our filings with the SEC, you'll find additional disclosures regarding the non-GAAP measures, including reconciliation of these measures to the most comparable measures under U.S. GAAP. Within the materials, we are also providing reconciliations of GAAP EPS to comparable adjusted EPS, which may assist with your modeling.

And with that, I'll turn it over to Barry.

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

Thanks, Brian, and good evening, everyone. I'm pleased to report our second quarter results, reflecting sustained earnings momentum across the enterprise, including continued year-over-year improvement to both comparable adjusted EBITDA dollars and rate, which improved 80 basis points to 19% during the period.

We also continued to deliver strong operating cash flows, reflecting expected sequential growth versus our first quarter results, and a very robust year-to-date improvement versus the first half of 2023. These results are reflective of our continuing strong execution across core capital allocation priorities and initiatives of our North Star operating plan.

These efforts are accelerating the growth of these key profitability metrics and further demonstrate our ability to consistently expand earnings faster than revenue.

During the quarter, we continued to deliver strong revenue results across both the Data Solutions and Merchant Services segments, in particular, reflecting year-to-date growth rates through the first half of 2024 at 13% and 8%, respectively, which I'll cover a bit more in a few moments.

Accompanying this growth, we also experienced some ongoing revenue headwinds across the B2B payments segment, as well as expected secular declines within the Print portfolio. Based on these trends and our updated outlook, today, we're pleased to reaffirm our full-year guidance ranges for earnings and free cash flow, for modestly adjusting our revenue range, given some lingering macro uncertainty over the balance of the year.

Importantly, each of our operating segments has continued to maintain strong year-to-date adjusted EBITDA margins, in line with both the operating leverage demonstrated in our total enterprise results and North Star objectives.

Now, prior to reviewing our second quarter enterprise and segment highlights in a bit more detail, I'd like to provide a couple of additional comments on the broader macro environment and our North Star progress. As we discussed previously, Deluxe monitors trends around both small business sentiment and consumer discretionary spending, as well as the interest rate environment.

We review many sources of data, including from the card brands, Federal Reserve and other economic forecast providers, as well as our own proprietary data. These trends impact multiple areas of our portfolio. While our year-to-date performance reflected a generally stable economic environment, there remains some signs of continued pressure on the average consumer.

In our Merchant segment, we have seen some elevated trends towards non-discretionary spend compared with discretionary spend, and in certain market articles, we have seen flattening of same-store sales. Similarly, demand from some short cycle discretionary promo products has also softened.

As a result of these data points and lingering macro uncertainty within the balance of your economic forecasts, we believe our revenue performance may trend to the low end of our original full-year guidance range, leading to our adjustments today. In line with our Northstar execution to-date, we remain confident that our profitability outlook remains solidly within our reaffirmed guidance range, inclusive of free cash flow generation.

Shifting now to North Star progress. The enterprise continues to execute well against both cost optimization and revenue enhancing initiatives spanning the wholistic North Star multiyear execution plan. As a reminder, our North Star goal remains to unlock \$80 million of incremental adjusted EBITDA, and \$100 million of annualized incremental free cash flow, both by 2026.

Consistent with my update following the first quarter, we continue to make meaningful progress across all 12 North Star work streams shown here. Initiatives comprising roughly two-thirds of our goal are moving through the execution phase. Benefit realization will be reflected over both the back half of this year and throughout 2025, as execution progresses.

What are the simplest ways to see our North Star progress, you'll see the continued decline in corporate segment expense as a percent of total company revenue. Since we began the program, we've improved that metric by roughly 100 basis points. We're also pleased to advise that our more complex work streams planned to begin later in our process are now fully in flight, along with each of the workstreams shown toward the top of the chart.

One notable Q2 example of execution within the marketing effectiveness workstream was the consolidation of all six brands acquired as part of First American into one unified brand, Deluxe Merchant Services. This will improve our marketing efficiency and performance.

Additionally, this brand consolidation will further leverage and simplify our One Deluxe go-to-market success in driving cross-sell. Even before the brand consolidation, the One Deluxe model has been helping drive merchant growth, as evidenced by the segments performance, which has materially improved since the acquisition in June of 2021.

Now to provide some additional details about our second quarter performance. As a reminder, and consistent with our prior calls, today, in my comments, I'll be discussing comparable adjusted results for the quarter and year-to-date periods, which we believe best reflect our ongoing business performance. Chip will review both our reported consolidated and comparable adjusted results to provide additional perspective.

For the second quarter, net of business exits, revenue was \$535 million, which reflected a decline of 3% year-over-year. As I noted during my introductory comments, this top line result was just a bit below our overall plan for the first half of the year. The specific period included both expected softness and B2B, and the promotional portion of Print, in addition to some prior year comparable timing impacts in the data segment.

Despite some of these top line challenges, total adjusted EBITDA dollars increased 1.6% from the second quarter of 2023 to \$102 million, continuing to reflect robust operating leverage at the enterprise level, as I noted in my opening comments. Adjusted EBITDA margins finished the quarter at 19%, reflecting continuation of the Q1 year-over-year expansion dynamics and growing by 80 basis points versus the prior year.

On a year-to-date basis, comparable adjusted EBITDA margins have expanded by 90 basis points, while free cash flow improved by more than \$26 million from the year-to-date 2023 figure. We remain particularly pleased with these adjusted EBITDA and cash flow results, further demonstrating our progress against North Star.

Moving on to some segment highlights, beginning with Merchant Services. For the second quarter, Merchant Segment revenue grew 7.7%, while adjusted EBITDA dollars grew 11%, and margins continued to improve, expanding by 60 basis points from the second quarter of 2023, accompanying the continued strong revenue trajectory.

The merchant business continues to benefit from both core processing volume as well as new customer wins across our omnichannel solutions, offered both via our direct and independent family resources, and our expanding network of FI, and integrated software vendors or ISV partners.

Shifting to results within the B2B Payments segment, we saw year-over-year declines of 8% for B2B revenue, consistent with the overall first quarter trajectory. We continue to expect material improvement in our B2B growth rate over the second half of the year.

As we've shared on our previous calls, we're transitioning this business toward a recurring Software-as-a-Service or SaaS model, thereby reducing our dependency on one-time non-recurring revenue. We also experienced a bit of base volume softness across the lockbox space. The year-to-date impact has been less revenue, but a 60 basis point increase in margins.

Over the past three quarters, we've also signed four major new lockbox clients, all of which will go live over the course of the second half, expected to contribute more than \$20 million in annualized recurring revenue, offsetting secular declines. The combination of these wins and the growing pipeline for our new products, gives us confidence in the expected revenue trajectory rebound ahead.

Moving now to Data Solutions, which continued to deliver strong results during the second quarter. You will recall this business has quarter-to-quarter lumpiness based on the timing of customer planned marketing spend. We see the best view of Data's growth trajectory remains through a multi-quarter lens.

During the second quarter, the core data-driven marketing or DDM business lapped a very tough revenue comp from 2023, resulting in a 3.2% decline for the specific period. Year-to-date, revenue growth for Data was 13% to the first six months of this year, highlighting strong demand for FI and non-FI customers.

This growth is helping to deliver strong margin expansion and we remain confident the segment will deliver full-year mid-to-high single-digit growth, in line with our anticipated longer-term expectations.

Shifting finally to our Print segment. This business experienced a revenue decline of 4.8% during the second quarter to \$309 million, while adjusted EBITDA margins held at 30%, in line with our longer-term outlook for the combined Print portfolio. To be very clear, legacy check performed well with most of the softness occurring in the short cycle, discretionary promo business.

On a year-to-date basis, legacy check revenues remained strong at \$358 million, reflecting a 2% decline from the prior-year six-month period. Promo revenue softness was a bit more than expected, but roughly in line with our forecasted trajectory, as we continue to focus on higher margin printed offerings, which are more impacted by macro market trends. Overall, we continue to manage the print portfolio to maximize cash flow through operating efficiencies, pricing actions and responsible investments.

To summarize, our overall second quarter results, and particularly, our earnings expansion, demonstrate our continued transformation and Northstar progress. While much work remains to fully execute against our second half goals and targets, our consistent and sustained pace of progress creates even greater confidence in our

bright future, as a payments and data company. We remain diligently focused on our multiyear capital allocation priorities, building from our first half progress.

Finally, before I pass over to Chip, I want to acknowledge and thank all of my fellow Deluxers, the continuing dedication to our customers and to the delivery of our innovative product and service offerings remains the critical enabler toward our realization of the second quarter and year-to-date results.

With that, I'll turn it over to Chip.

Chip Zint

Chief Financial Officer & Senior Vice President, Deluxe Corp.

Thank you, Barry, and good evening, everyone. As Barry noted in his opening, we were pleased with our second quarter progress, particularly our year-to-date free cash flow generation and our continued year-over-year comparable adjusted EBITDA and EPS growth during the period.

As customary, I'll begin today with a bit of additional color around our consolidated highlights for the period, before moving on to the segment results, our balance sheet and cash flow progress, and our full-year 2024 guidance. For the quarter, on a reported basis, we posted total revenue of \$538 million, down 5.9% inclusive of the impact of our prior-year exits, while declining 3% year-over-year on a comparable adjusted basis.

We have now fully lapped the divestiture of our North American web hosting business, and expect the impacts of exits to be lower in the back half of the year, as we finish transitioning the payroll business.

We reported GAAP net income of \$20.5 million or \$0.46 per share for the period, improving from \$16.4 million or \$0.37 per share in the second quarter of 2023. This increase was driven by improved operating results, including both lower SG&A and restructuring-related expense.

Comparable adjusted EBITDA was \$101.8 million, up 1.6% versus the second quarter of last year. Comparable adjusted EBITDA margins were 19%, improving 80 basis points versus the second quarter of 2023, as Barry noted. Q2 comparable adjusted diluted EPS came in at \$0.85, improving from \$0.81 in 2023, primarily driven by the operating income drivers previously noted.

Now turning to our operating segment details, beginning with the Merchant Services business. The Merchant business grew second quarter revenue by 7.7% year-over-year to \$98.5 million, reflecting strong year-to-date performance.

Segment adjusted EBITDA finished at \$19.2 million, improving \$1.9 million or 11% versus the prior year, with margins expanding 60 basis points to finish at 19.5%, mainly driven by the continued strong growth of revenue and resulting operating cost leverage across the expanding platform.

The Merchant business continued to benefit from new merchant adds, and their presence spanning a diversified set of category verticals. Merchant remains well-positioned to deliver our mid-to-high single-digit revenue growth and low-20% adjusted EBITDA long-term outlook.

As we've noted, potential second half moderation of macro level spending trends and our Q4 lapping of the large mid-market FI partner conversion previously discussed, are likely to result in some back half easing of growth rates versus the year-to-date levels.

Moving to B2B Payments, for the second quarter, B2B segment revenues finished at \$70.2 million, sequentially improving from the first quarter, but down from \$76.3 million during 2023. Overall, remittance volumes were slightly below expectations, with revenues declining roughly 4% during the quarter, while the balance of the B2B offerings continued to lap some prior year non-recurring sales from 2023, resulting in an overall 8% decline year-over-year.

In line with some of the year-over-year revenue headwinds within the segment, adjusted EBITDA declined 7.9% from 2023 to finish at \$14 million, while margins remained flat at 19.9%. As Barry noted, year-to-date, adjusted EBITDA margins of 19.5% reflected an overall 60 basis points improvement versus the first half of 2023, as we sustained our focus on operational efficiencies during the transition of this operating segment toward an increasingly SaaS-based set of product offerings.

Based on these year-to-date results, we now anticipate a full-year low-single-digit revenue decline rate for this segment, which is included in our updated revenue guidance. We remain confident that adjusted EBITDA margin should improve to the low-to-mid 20% range over time.

Moving on to Data Solutions, this segment continued its strong performance inclusive of the very challenging prior-year revenue comp during the second quarter. Data revenues finished at \$57.4 million for the quarter, reflecting a modest year-over-year decline of 3.2% versus the same period of 2023, lapping very strong prior-year deposit seeking campaign activity amongst core FI partners, which we discussed during both the second and third quarters of 2023.

Adjusted EBITDA finished at \$15.8 million, reflecting a very strong 17.9% growth versus Q2 of the prior year. While adjusted EBITDA margins expanded 490 basis points to 27.5% on both an improved mix of DDM campaign activity and continued operating expense efficiency across the business.

The continued strong performance of this segment reinforces our mid-to-high single-digit longer-term growth expectations for the full-year 2024 horizon. We also maintained strong confidence in the long-term low-to-mid 20% adjusted EBITDA rate guidance for this segment.

Turning now to our Print businesses. Print segment second quarter revenues were \$308.8 million, declining 4.8% on a year-over-year basis. This decline was largely in line with our secular decline expectations, especially given the deployment of our ERP upgrade during the first half of last year, and the resulting shift of some revenues from the first to second quarter comparable figure.

Legacy check product revenue declined 3.8% during the quarter, with promo revenues driving the balance of the full segment decline rate. Adjusted EBITDA for the quarter finished at \$93.9 million, remaining at 30.4% of revenue, in line with our longer-term low-30s target, but a 190 basis points below the prior-year rate. Certain specific accounts receivable reserve adjustments during the quarter impacted margins for the period by approximately 140 basis points versus the prior year.

Legacy check margins remain consistent with our historical and previously communicated expectations during the period, inclusive of these adjustments. We would not anticipate this level of reserve adjustments to occur over the balance of 2024. We remain very focused on operating expense discipline and overall efficiency across cost of goods sold inputs within the Print segment in particular.

Consistent with our longer-term outlook for the balance of 2024, we continue to expect to see low-to-mid single-digit revenue declines across the Print segment, with adjusted EBITDA margins remaining in the low-30s, inclusive of the non-recurring Q2 items previously noted.

Turning now to our balance sheet and cash flow. We ended the second quarter with a net debt level of \$1.53 billion, remaining nearly flat to our 2023 year-end level of \$1.52 billion, while materially improved from the \$1.63 billion mark at the end of Q2 of 2023, and consistent with our ongoing commitment to debt reduction as a top capital allocation priority.

Our net debt to adjusted EBITDA ratio remain 3.7 times at the end of the quarter, flat on a sequential basis, while slightly increased from the 3.6 times ratio reported at year-end. As we've noted, our long-term strategic target remains approximately 3 times leverage and the second half typically reflects sequentially improving cash flow results, which tends to weigh improvements of our reported leverage ratios more heavily towards the balance of the year.

Free cash flow, defined as cash provided by operating activities, less capital expenditures, finished at \$17.6 million for the year-to-date period, improving by \$26.2 million from the negative results reported through the first half of 2023, driven by continued improved operating results, lower restructuring spend, and lower capital expenditures versus the prior year.

We remain very pleased with our overall operating cash flow generation during recent quarters and in our ability to continue our de-leveraging path consistent with our clear capital allocation priorities. As a brief additional update regarding our overall capital structure, I'll remind listeners, as we shared last quarter, that we entered into an accounts receivable securitization facility and utilized a draw down against the interest rate advantage capacity towards prepayments of the balance of our 2024 required quarterly amortization.

This 36-month agreement terminates in the first quarter of 2027, and has shifted \$80 million of maturities to the extended horizon beyond 2026, shown on the current slide. As Barry mentioned, we continue to actively monitor the broader interest rate environment, both as it relates to potential impacts to our operating trajectory, as well as exploration of options regarding our longer-term debt capital stack.

As shown here, our existing revolving credit and term loan facilities are just over three calendar quarters from current status, carrying June of 2026 maturities, while our 8% bonds mature in 2029. We continue to remain comfortable with our available liquidity levels, and we'll certainly provide additional updates on any capital structure or financing developments going forward.

Before turning to guidance, consistent with prior quarters, our board approved a regular quarterly dividend of \$0.30 per share on all outstanding shares. The dividend will be payable on September 3, 2024 to all shareholders of record as of market closing on August 19, 2024. As noted previously, we continue to make progress across our key North Star initiatives, forecasted realization of the implemented workstream impacts noted in Barry's comments are fully reflected within our 2024 guidance ranges.

As signaled during his introductory comments, our year-to-date revenue results, combined with remaining uncertainty around some of the economic outlook for the second half of the year, present a line of sight towards the low end of our original guidance, leading to the adjustment we are making to the expected revenue range.

With that, our full-year guidance figures are shown on the current slide keeping in mind all figures are approximate and reflect the impact of business exits over the past 12 months. Revenue of \$2.12 billion to \$2.16 billion, reflecting a decline of 1%, to positive 1% comparable adjusted growth versus 2023.

Adjusted EBITDA of \$400 million to \$420 million, reflecting between 2% and 7% comparable adjusted growth. Adjusted EPS of \$3.10 to \$3.40, reflecting 3% to 13% comparable adjusted growth and free cash flow of \$80 million to \$100 million.

Finally, to further assist with your modeling, our guidance assumes the following; interest expense of \$120 million to \$125 million and adjusted tax rate of 26%. Depreciation and amortization of \$160 million, of which acquisition amortization is approximately \$70 million, and average outstanding share count of 45 million shares and capital expenditures of approximately \$100 million.

This guidance remains subject to, among other things, prevailing macroeconomic conditions, as noted previously, including interest rates, labor supply issues, inflation and the impact of divestitures.

In summary, we remain pleased with our continued execution during the second quarter and our overall first half year-to-date results. Our ability to demonstrate sustaining year-over-year growth of adjusted EBITDA, EPS, and particularly, free cash flow despite areas of anticipated top line pressure during the quarter, are testament to our continued focus on both North Star execution and our clear long-term capital allocation priorities.

We remain confident that this diligent focus against core deliverables will continue to be reflected within our ongoing back half performance and look forward to providing additional updates as the year progresses. Operator, we are now ready to take questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question is from the line of Lance Vitanza with TD Cowen. Lance, your line is open. Lance, please check your phone and make sure you're not self-muted.

Lance Vitanza

Analyst, TD Cowen

Q

Hi. Can you hear me, guys, I'm so sorry. Sorry, I had the phone on mute. Thanks for taking the questions, guys. Barry, I had a question regarding the macro pressure for you, and then, hopefully there'll be time for me to get one more in for Chip, regarding guidance.

But Barry, I think you mentioned some surveys, maybe some government data series that you were looking at, but could you talk a little bit more about what exactly it is that you're seeing that's making you build in a little bit more pressure in the back half? And which segments are most exposed to that pressure?

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

A

Sure, Lance, we've got gotten word that there were -- this section was a little bit hard to hear. So just for everyone's benefit, I thought, I would reread the section of the prepared comments. And then I'm happy to take the question there and go any deeper as you'd like. But, what I was saying, and perhaps some people could hear

and some didn't, I said that as we've discussed previously, Deluxe monitors trends around on both small business sentiment and consumer discretionary spending, as well as the interest rate environment.

We review many sources of data, including from the card brands, Federal Reserve and other economic forecast providers, as well as our own proprietary data. These trends impact multiple areas of our portfolio. While our year-to-date performance reflected a generally stable economic environment, there are some signs of continued pressure on the average consumer.

In our Merchant segment, we've seen some elevated trends toward non-discretionary spend compared with discretionary spend, and in certain market verticals, we've seen flattening of same-store sales. Similarly, demand for some short cycle discretionary promo products has also softened.

As a result of these data points and lingering macro uncertainty with a balance of the economic forecasts, we believe our revenue performance may trend to the low end of our original full-year guidance, leading to our adjustment today. In line with our North Star execution to-date, we remain confident that our profitability outlook remains solidly within our reaffirmed guidance range, inclusive of free cash flow generation.

Lance Vitanza

Analyst, TD Cowen

Q

Great. And so, yeah, I think I did hear that. But, just to go a little bit deeper, I'm wondering, you called out Merchant in that -- in the prepared remarks. Is that -- does that mean to imply that that's where we should expect the bulk of the pressure? Or is it really going to be more broad-based throughout the enterprise?

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

A

Well, Lance, I think you saw it in our Q2 performance that our short cycle promo products were impacted and that we do see a little bit of pressure there in Merchant. And we think that it is -- the average consumer seems to be under a bit of stress. You can see the level of the balance between discretionary versus non-discretionary still is in favor of non-discretionary spending, which in some ways, is very good for our Merchant portfolio.

We have a large amount of our business there that is non-discretionary. People have to pay their taxes, they have to get their cars fixed, they have to pay fees throughout their community. So, we -- that part of our business is strong, but there are other pieces there that we're just signaling where we're seeing some flattening out of same-store sales, which we think may be a -- a bit of headwind in the back half.

But like we said, we feel confident about our profitability and we think that the revenue is going to be at the low end of our original guidance. But, we thought it was just prudent Lance, just prudence to make the modest adjustment that we did to be reflecting what that, that bit of consumer pressure we see.

Lance Vitanza

Analyst, TD Cowen

Q

Great. And then, just maybe on Merchant, the strength in Merchant revenue is up 8%. Is it possible to talk about how much of that growth came from cross-selling new Merchants versus increased volumes at existing Merchants? And then, just as a follow up to that, if you could remind me, sort of what's the lead time you're seeing on cross-selling merchant services? How long does it take from the initial contact to the time that you can actually generate revenues from a new merchant? Thanks.

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

A

There's a couple of great questions in there. So, let me start with the revenue growth that you're seeing there. We see good performance from our existing portfolio of customers. But to recall that we won a large, large piece of business that went live in the fourth quarter of last year, and that continues today to perform actually above our expectations.

So, a piece of the growth that you're seeing here is from that significant win. But, even, we feel solid about the base business and its performance on our ability to win merchants in the broad marketplace.

And your question is about, if we win an individual merchant, how quickly we can get that merchant boarded and live? And any individual merchant could take a couple of days to be longer, depending on the complexity of their system.

If you think about a big deal like the one that went live in the fourth quarter of last year, which was a bank referral relationship and reboarding their entire portfolio of merchants on our platform, that can be a pretty long cycle, as you would imagine, if you're moving a large amount of volume with a, ultimately executing a flip of the switch to move that volume to us.

The last thing you're making about -- the question you had about cross-selling, we are really pleased, one of the fundamental theses of the acquisition announced more than three years ago, was that we could help the Merchant business grow faster inside our four walls because of our ability to offer leads from across the portfolio, as well as the strength of our brand, our trusted nature, with financial institutions, with small businesses, et cetera.

And that's really played out. And just for perspective, Lance, we can board merchants in cases as fast as two hours, if we have gotten the merchant meet certain criteria. And that's, of course, obviously for certain types of merchants. But, we're very pleased with the progress of that business. We think it's obviously a standout in the portfolio and the fundamental thesis of what we're doing with First American, and for the acquisition, we think is proving out quite well.

Operator: Your next question is from the line of Kartik Mehta with Northcoast Research.

Kartik Mehta

Analyst, Northcoast Research Partners LLC

Q

Good afternoon. Barry, just on the Merchant business, I'm wondering as you look throughout the quarter, is there a slowing start at a certain point in time? I guess, when did you start noticing maybe some weakness in the consumer and that impacting the Merchant business?

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

A

Part of what we've seen is some just generally unusual patterns, where the spending towards non-discretionary categories has been a bigger percentage of the pie versus discretionary. And we've seen that pattern before, but we started seeing it in the second quarter, and we're not particularly concerned about it. We're just noting that that does represent some stress for the average consumer. And we're flagging that today just as a caution.

Kartik Mehta

Analyst, Northcoast Research Partners LLC

And then in the check bid, sorry, Chip, I apologize.

Q

Chip Zint

Chief Financial Officer & Senior Vice President, Deluxe Corp.

Just adding, even despite those pressures, which as Barry indicated, we started to see, towards the mid to late part of the quarter, and it's been in line with all the things you would have read this week from other consumer-related releases, what I would just continue to point out is, we're still guiding kind of mid-to-high single-digit growth for that business this year.

A

So, still feel good about the year-to-date trends we've been on, the volumes we're seeing there, and of course, the long-term trajectory of the business. However long it started, however long it's going to last, we view this as a bit of a softening that a lot of people are going to be dealing with, and we don't view it as a longlasting pressure against our business that would change our strategies. So, we still feel good about the long-term growth trajectory of the Merchant business.

Kartik Mehta

Analyst, Northcoast Research Partners LLC

Fair. Just going to Print business on check, you've had some success winning market share. And I'm wondering, as you look over the next 12 months, maybe, obviously, if you can name opportunities every day, but you can't, maybe what the outlook is for your ability to gain market share in that business?

Q

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

So, it's hard to predict market share gains on any narrow window like the back half of the year. But I can tell you that we're really pleased that we continue to win far more than we would lose, what, in a competitive bid situation. And we like our chances of continuing to grow market share there.

A

And you'll recall, Kartik, we've even had periods where we were growing revenue in that part of the company space. So, we feel like that's still a great cash flowing business, and solid prospects to continue.

Chip Zint

Chief Financial Officer & Senior Vice President, Deluxe Corp.

And I guess, I'd just add, Kartik, along those lines, we of course can't predict market share takeaways. We're going to get, as Barry alluded. But I think one of the great things about Deluxe is given our reach of the 4,005 and the way we partner across the segment with those FI that we don't support them from a check perspective today.

A

We do have some on average typical commercial relationship with them, which gives us the ability to talk through these things and have it on our roadmap, and get a chance to play in it when the opportunity comes our way.

Kartik Mehta

Analyst, Northcoast Research Partners LLC

Sure. And then, just one last question, on the promo business, obviously, it seems like the economy is having a little bit of an impact on the business. Are you seeing any pricing pressure as a result, our competitors getting a little bit more aggressive because they're seeing the same trend or as pricing not been an issue up to this point?

Q

Chip Zint

Chief Financial Officer & Senior Vice President, Deluxe Corp.

A

Hey, this is Chip again. I think it's hard to directly address the pricing question. I don't believe we've seen a radical change. What I would remind you, though, is, as part of our North Star journey and one of the theses of going with this combined print entity, we've gotten focused on margin improvement and margin expansion, specifically to improve the cash flow.

So, we've mentioned it before. We've already gone a bit foot forward to try to think about the deals we do take, the price we're willing to take, and the margins we're willing to play in that promo space. So, I think you can think of it. Yes, there's a softening there with these short cycle promo activity, but there's also us being a little bit more discerning in terms of the type of deal we want to take.

And so, because of that, are we seeing a little bit of pricing change? It's hard to know, because we've just fundamentally shifted our focus a little bit there, Kartik.

Operator: Your next question is from the line of Charlie Strauzer with CJS Securities.

Charles Strauzer

Analyst, CJS Securities, Inc.

Q

Hi, good evening. This is Charlie. I just want to say thanks for taking my questions. And if you look at the results in Data, it clearly performed better than we had expected, especially given the strong Q1. Can you provide maybe a little bit more color on how we should think about the back half of the year beyond what Chip had laid out before?

Chip Zint

Chief Financial Officer & Senior Vice President, Deluxe Corp.

A

Yeah, thanks for acknowledging that, Charlie. You're right. As we indicated on the last call, we recommended averaging three quarters at that time to get the right trend. And given the lumpiness of the business and the timing of the campaigns, I would continue to update that perspective and say, now I think if you average the most recent four quarters, I think it continues to show you the right trend.

That will clearly imply, again, another softer data quarter because we're coming up against just another record comp. You may recall data had a fantastic Q2 a year-ago, and then, followed up with an even greater Q3. But again, if you roll these things forward, it continues to show on a rolling basis, very solid growth.

So, even though we don't guide quarters, my direction to you would be to look at the most recent four-quarter average from the third quarter of last year through to the second quarter we just reported. And I think that's a good indicator to what to expect for the third.

Charles Strauzer

Analyst, CJS Securities, Inc.

Q

Great. That's helpful. Thank you. And then looking at lockbox that, you know, Barry mentioned that, that's new customers that you're onboarding there, but maybe some more color behind that too?

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

A

Yeah, we continue to win market share here and it's because of the quality of our service footprint we have and where we process those payments. I think what we're particularly pleased about is that those wins represent sort of the, across the industry. They are regional banks all the way up to money center banks, and that they're in the queue to go live across the back half of the year.

And that's why we just have confidence that, and that part of the business over the long-term will continue to get share to help that business stay robust, as we're building and launching and selling, and implementing, our new products in B2B around receivables and payables, digital receivables and digital payables.

Chip Zint

Chief Financial Officer & Senior Vice President, Deluxe Corp.

A

And Charlie, just to add, I think lockbox is an area we're not talking enough about. You may recall a few years ago we went through some operational challenges there. It coincided with the rapid raise and labor rates for hourly workers, and we also had some systemic things we had to work on.

And so, you may recall over the last few years, we've been talking about the work we've done to improve the profitability, improve the operations, and that's included a lot of investments in our systems there, consolidating sites, getting new modern sites.

And I think it's all colliding in this moment in time where we now have very stable modern operations there that are performing very well. And it's met a point in the market where we have an opportunity to take share gains and we're capitalizing on that. And it's also super critical for us because that lockbox area becomes the gateway to migrate these transactions to our new receivables, R360 SaaS-based solution.

So, the strategies coming together, the teams performing great, the investments we've made over the last few years have put us in a really great position. And so, we're trying to go take market share. And as I said in the check conversation, this is a place where we have great relationships that can really leverage cross-sell and all of our bank partners to really take hold of that area. And we're going to continue to really make some really good progress there.

Charles Strauzer

Analyst, CJS Securities, Inc.

Q

Excellent, and staying on lockbox for a second. Do you think you can find more ways to expand margins there? Is it purely revenue, additional revenue or is it the things that you can do there to improve the margins?

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

A

I think we do believe that and we have made progress there as Chip has said, we have worked on our distribution footprint of how we receive payments, et cetera, and operating efficiencies throughout the organization. So, we do believe that that is an area where we have opportunity over time for margin expansion. We'll win market share. And then, Chip has already given you the message about how it's a strategically important for us as we build the other future businesses around B2B.

Operator: [Operator Instructions] Your next question is from the line of Marc Riddick with Sidoti.

Marc Riddick

Analyst, Sidoti & Co. LLC

Hey, good afternoon.

Q

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

Hi, Marc.

A

Marc Riddick

Analyst, Sidoti & Co. LLC

I wanted to sort of -- we covered quite a bit, so a lot of my questions have already been answered. But I wanted to circle back around to the commentary around the forces that led to the sort of pointing to the low portion of the revenue guide.

Q

I was wondering, and I appreciate you putting a finer point on a lot of the things that you guys are looking at, was there any one or two parts of those considerations that maybe helped greater weight or if not greater weight maybe were a little more surprising than you thought they would be? Or how should we think about maybe the bigger impact than others?

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

Yeah, Marc, I think it wasn't any one specific thing. I think what we're communicating is that there's just a bit of softness and a consumer demand for the consumer that's under a little bit of a little stress. We are not signaling major stress, we're just signaling there's a bit of softness there and that will guide us to the lower end of our range. And we're just trying to be prudent in sharing that with you at this point in time.

A

Marc Riddick

Analyst, Sidoti & Co. LLC

Okay, that's fair. And then, on a -- on a different track, I suppose, I was wondering if we could, I think in the prepared remarks, there were thoughts around where you were seeking out for interest for the year. Can you just sort of remind us maybe what your thoughts are around the potential of cuts and how that plays into your interest expense thoughts and the like? Thank you.

Q

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

Yeah, we -- thanks for the question, Marc. We aren't including any cuts in our forecast. And I will remind you that throughout the last two years, we've fixed 75% of our interest rate. So, any cut we'd have, while we'd welcome it, obviously, the whole market would welcome that, for what, that could help with the consumer and the economy, we wouldn't expect any unless that rates really start to come down by a few points.

A

It's not going to be material. So, a 25 basis point cut next month, as an example, would maybe help us save \$300,000 of interest cost the back half of the year. And it's not material, it's not meaningful. And that's because we're 75% fixed at this moment. I think, obviously, we're hopeful rates will continue to come down and that will be a big part of as we think about long-term debt financing structure and what we do in terms of setting the long-term policy around our fixed variable interest rate exposure.

Marc Riddick

Analyst, Sidoti & Co. LLC



Okay, great. That's very helpful. Thank you.

Operator: At this time, there are no further questions. I would now hand the call over to presenters for any closing remarks.

Barry C. McCarthy

President, Chief Executive Officer & Director, Deluxe Corp.

Thanks, Tinika. Before we conclude, I'd like to share that management will be participating virtually at the CL King's 22nd Annual Best Ideas Conference on September 16 during the quarter, for which, the webcast link will be posted to our Investor Relations website. Thank you again for joining us today and we look forward to speaking with you all again in November as we share our third quarter results.

Operator: This concludes today's call. Thank you for joining. You may now disconnect your lines.

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