



Pivotree Inc.

The Frictionless Commerce Company

To our shareholders, employees and customers - Q3 2022

Thanks to the efforts of all of our Pivoters around the world we delivered another strong quarter, beating consensus estimates on all key measures from revenue and gross margin to EBITDA as well as delivering another record quarter of bookings. There are a few items worth digging into a little deeper to make sure our results are understood. As the team started shifting their focus to balance growth and profitability, we announced early in October that we had started streamlining some of our corporate operations to gain additional efficiencies and drive more responsibility into each business unit (BU). Starting this quarter I am reducing the length of my quarterly updates and will provide a more comprehensive annual update.

Operating Results:

Revenue remained strong at \$24.6 million with record bookings of \$19.2 million in the quarter (slightly edging out our previous record in Q1). We delivered 8.5% organic growth vs. Q3 2021 and 54% total growth versus a year ago. Our year to date revenues of \$75.5 million have us on pace to break \$100 million by the end of the fiscal year. We are benefitting from a strong US dollar in both revenue and bookings with more than 85% of revenues US dollar based. Our recurring revenues were up modestly versus the last few quarters coming in closer to 45% of total revenues in Q3. It is common for us to see MRR lifts in Q3 and Q4 during the ramp up to the holiday season. Our average quarterly bookings pace in 2021 was ~\$11 million (\$9.3 million before acquisitions). We are currently pacing to \$17 million in bookings per quarter this year which is a 54% increase from 2021. We have a strong pipeline carrying into Q4 and we remain optimistic that we will continue to maintain our average bookings pace. Some of the organizational changes we made this past quarter were to put more of the product development initiatives closer to the customers in the business units and free more investment dollars to accelerate product development efforts. Growing our product and recurring revenue business remains a priority and we will continue tweaking activities to drive the results we are looking for. Since the first quarter of this year we saw a 50% increase in penetration of managed services (MS) within our professional services (PS) customers. We are now tracking roughly one third of our PS customers, consuming MS.

Consistent gross profit growth +55% vs. Q3 2022 combined with tighter control on opex and a positive FX benefit helped to bring Q3's adjusted EBITDA in at **-\$425k** which is a significant improvement vs prior year and beats consensus estimates. We completed restructuring efforts in Q3 and combined with continued cost savings efforts we expect to see \$1 million per quarter of savings in 2023. This resulted in a one time restructuring charge which reduced EBITDA to **-\$1.8 million**. You can expect to see some of those savings start in Q4. In my Q2 CEO letter, I described the normalized Q2 adjusted EBITDA as being closer to **-\$1 million**, so Q3's **-\$425k** represents real progress on the plan.

Millions \$	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022
Total Revenue	\$16.2	\$16.5	\$15.0	\$14.3	\$16.0	\$22.2	\$24.5	\$26.5	\$24.6
Y over Y growth	6%	3%	-6%	-4%	-1%	34%	63%	84%	54%
Annualized Rev./ Share		\$2.68	\$2.43	\$2.31	\$2.54	\$3.51	\$3.87	\$3.97	\$3.70
Shares Outstanding at Quarter End (millions)		24.7	24.7	24.8	25.2	25.3	25.3	26.6	26.6
Gross profit/share		\$1.32	\$1.09	\$1.01	\$1.13	\$1.54	\$1.65	\$1.79	\$1.66
Adjusted EBITDA	\$0.9	\$1.0	-\$0.9	-\$1.6	-\$1.0	\$0	\$0.2	-\$0.1	-\$0.4

Organizational Changes

Our teams in India have an expression they use regularly - Jugaad. In short, this is about doing more with less. It is about less structured innovation in centralized R&D teams and more organic innovation born out of necessity. The rationale for continuing to grow our professional services business goes beyond the simple fact that it is profitable. We gain client intimacy and awareness of their biggest challenges and when we empower our teams we find practical and efficient innovation in these challenges. The biggest change we made this quarter was to break up the Digital Solutions group and move key product development initiatives into the business unit with the most relevant client opportunities to leverage the products.

Our leading indicators were telling us we needed more consumer driven insights into the use cases that would drive product road maps and those customer insights would be easier to access through the business units taking greater responsibility for the product development initiatives. We reduced the number of product initiatives into fewer discrete products with plans to invest more dollars into the ones that appear to have the greatest potential like our Data-as-a-Service solution (DIVE & Natalie). We also moved Pivotree Connect, which is our integration platform, into the Data BU and we have already seen early benefits coming from that move in additional new use cases driven from real customer experience as well as active implementations already under way. Our Pivotree Warehouse Management Solution (WMS) has made significant progress in converting to a modernized application. We want to invest more dollars to accelerate the completion of its migration path to a software-as-a-service, cloud first, headless WMS solution.

Our three business units are maturing well which also enabled this change. Commerce remains our largest BU with the highest percentage of recurring revenue, primarily managed services. This has been a transition year for Commerce as they have successfully ramped up pipeline in the next generation platforms and we expect this pipeline to translate into stronger bookings in 2023. A number of major projects have been approved by clients but are only getting budget released in 2023.

Our Data team has quickly scaled up and is expected to grow significantly again in 2023. This team has a complete management leadership structure, strong partnerships, excellent bookings and pipeline and will benefit greatly from the investments they are making in automation tools. The Data BU has taken over direct responsibility from the Digital Solutions team to accelerate development of our Natalie and DIVE applications and are already embedding them in our service offerings with PS engagements today.

Our Supply Chain team has delivered consistent results since we acquired them. We have helped to build out the management team by shifting senior leaders from other teams into this group. This is our smallest BU today but represents some of the greatest growth potential as our clients see supply chain as their greatest challenge to improving profitability. We are also shifting more investment dollars into converting our WMS solution to a more modern architecture and SaaS platform. This is a feature rich, proven application supporting some of the biggest and most complex warehouse systems in the world and we are in the process of modernizing it and expanding the market reach into the mid market. In my recent trip to meet with our India based teams I was impressed with the progress this team is making having already converted 20% of the core functionality to the new microservice format. The 20% of completed micro-services actually represents more than 20% of the most valuable "baseline" features that are core to any WMS solution.

The changes we made were about driving practical innovation through employees closer to our client challenges and making more capital available to invest in our most promising products that are now embedded in the business units. We have to do better with the rate of progress in our product development initiatives so we are reducing the number of products we are going to invest in over the next 12-18 months, but we are going to spend more aggressively to ensure our most promising products succeed.

August 2022

Acquisitions

We continue to build a healthy pipeline of targets and have taken opportunities to the LOI stage but have not successfully closed any deals to this point. While I expected to see the gap close between public and private valuations, it has not closed as much as I had expected by now. There are a number of key growth areas we have been focused on and I would like to get something closed, but as I have maintained since the time of our IPO, we will only close deals that meet our collective requirements of consistent growth, gross margins above 40%, positive cash flow, helps to accelerate a key strategic growth effort and meets our IRR hurdles using reasonable assumptions. It may take another quarter or two for the private valuations to come more in line with what our deal parameters can justify and in that time I hope our own valuation will become more in line with our peer group to expand the pool of potentially accretive deals we can do.

Measuring Success

In the short term our critical success measure is crossing over to EBITDA positive and ultimately operationally cash flow positive. We expect positive adjusted EBITDA in Q4 and to begin delivering operational cash flow in 2023. Longer term success will be measured in material operational gains in revenue and gross profit per employee and the same measures per share will demonstrate efficient capital allocation. There is the potential for great leverage through increased penetration of our software solutions in all of our services. I expect these changes to be more noticeable in annual reviews versus quarterly.

Summary

Q3 was another solid quarter of consistent execution and performance. The strong bookings and pipeline additions suggest our marketplace continues to benefit from long term tailwinds despite the macroeconomic headwinds we have all been reading a lot about. Since Q1/Q2 we have been taking measured steps to get better control of our destiny by relying on our own ability to produce cash. We took more significant steps in Q3 which will lead to \$1 million per quarter of savings in Fiscal Year 2023 and free up cash which we will be investing in our key product development initiatives as well as building capacity for more acquisitions.

Bill Di Nardo
Chief Executive Officer