01-Nov-2017

Acxiom Corp. (ACXM)

Q2 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon, ladies and gentlemen, and welcome to Acxiom Fiscal 2018 Second Quarter Earnings 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] As a reminder, this conference call is being recorded.

I would now like to turn the call over to your host, Ms. Lauren Dillard, Head of Investors Relations (sic) [Investor Relations] (00:40). Lauren Dillard, please proceed.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Thank you, operator. Good afternoon and welcome. Thank you for joining us to discuss our fiscal 2018 second quarter results. With me today are Scott Howe, our CEO; and Warren Jenson, our CFO. Today's press release and this call may contain forward-looking statements that are subject to risks and uncertainties that could cause actual results to differ materially. For a detailed description of these risks, please read the Risk Factors section of our public filings and the press release.

Acxiom undertakes no obligation to release publicly any revisions to any of our forward-looking statements. A copy of our press release and financial schedules, including any reconciliation to non-GAAP financial measures, is available at acxiom.com. Also, during the call today, we will be referring to the slide deck posted on our website.

At this time, I'll turn the call over to Scott.

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

Thanks to you, Lauren. Good afternoon, and thank you for joining us. I am pleased to report a solid second quarter, highlighted by top line growth, expanding margins, and continued innovation across the portfolio. Excluding divestitures and the impact of foreign exchange, total revenue was up 8%, driven by accelerating revenue growth of LiveRamp, which grew 58% during the quarter. International revenue was also up double digits. Beneath the top line, we delivered meaningful margin improvement, with total company gross margin up over 500 basis points, and operating income up 27%. LiveRamp posted record double-digit segment margin, and Marketing Services improved its bottom line by more than 400 basis points.

During my portion of the call today, I will update you on each of our businesses, and in that discussion, highlight some recent momentum that gives me confidence in the back half of the year.

First, Marketing Services. I'd like to revisit the four main goals we outlined in our last call for Marketing Services, and update you on our progress against each in Q2. Our number one goal in Marketing Services is to maintain and delight our current clients. This is key to defending our cash flows and growing existing relationships. During Q2, we closed all material contracts up for renewal, including a multiyear contract with a large financial services client and an expanded global deal with Harley-Davidson. We are now working with Harley-Davidson geographies, representing over 75% of the world's population to enable its customer acquisition and retention strategy.

In addition, we were recently recognized by Citibank with the Citi Supplier Award for our high levels of service and performance. Acxiom was the only supplier to win this award two years in a row, underscoring our commitment to delivering tangible results for our clients. As I mentioned at the last call, all our top 10 clients are under renewal through the remainder of this fiscal year, de-risking a large majority of our second half revenue.

A second goal is to add new logos to the Marketing Services client roster. During the quarter, we signed three new logo deals, most notably, a multiyear deal with GNC, a leading health and wellness retailer, to enable its omni-channel engagement strategy. I am encouraged by our recent momentum in signing new clients, and this will remain an area of focus for us in the back half of the year. Deals are progressing through the funnel as expected, and we have several large late-stage deals in the pipeline. Hitting just a handful of those puts the business in a much stronger position heading into next year.

A third goal for Marketing Services is to leverage its deep client relationships to catalyze its sister divisions. All three of the new logo wins I mentioned also included services provided by either Audience Solutions or Connectivity. For example, to power GNC's omni-channel engagement strategy, the recognition technology in Audience Solutions is a necessary and fundamental component of the underlying platform we provide.

A final and important goal for Marketing Services is to depend and grow its cash flows. Here, we did a very nice job during the quarter. Gross margin expanded nearly 400 basis points, and segment income was up 10%. In the U.S., Marketing Services segment income has grown in each, each of the last eight quarters, a testament to the team's ongoing efficiency and automation efforts. In summary, we continue to believe Marketing Services is a stable and healthy business. Our pipeline is sizable, and importantly, the number of late-stage, high-quality deals in the pipeline gives me confidence this business is poised to exit the year on a growth trajectory.

Now, moving on to Audience Solutions. Audience Solutions, despite a flat top line this quarter, continues to make progress against its key growth initiatives. On our last call, we talked about the transitioning revenue model at our largest publisher partner. Specifically, we said that our revenue sharing arrangement with this publisher would convert to a licensing fee quicker than we anticipated, creating the headwind this year. Although I have talked about this at length, I don't want to gloss over it today.

It will have a material effect on our growth rates, both this year and next. However, we have several other initiatives in place that we expect to kick in in the back half of the year to offset some of this decline. Digital data growth, our data being resold through indirect digital channels like publishers and platforms, was up over 30% in the quarter, excluding the large publisher to which I just referred. As publishers and platforms outside of the big-walled gardens look to compete with the targeting capabilities that Facebook and Google provide, people-based data must be a part of their strategy. We are well-positioned to enable this trend, and we continue to expect digital data usage to be a meaningful growth driver for us, despite the near-term headwinds.

During the quarter, we entered into a new global data partnership with IPG Mediabrands to help strengthen its data and analytics capabilities. Through this partnership, agencies across the IPG Mediabrands network will have access to our data to help power their people-based targeting efforts. This is IPG's largest data alliance to date, and spans 14 different markets.

We also recently announced the launch of a new joint offering with Amex Advance, a personalization services business within American Express, that predicts purchase intent across the U.S. consumer population. This joint solution combines spending insights from American Express's network with Acxiom's InfoBase data and first-party customer data in a privacy safe way to predict when consumers will be in market for a purchase.

Audience is created through the partnership, help marketers increase effectiveness by engaging consumers with relevant offers when they are most ready to buy. One of the newer growth initiatives inside of Audience Solutions is Global Data. We have largely completed our Global Data asset filled out with coverage across 62 countries and more than 65% of the world's connected population.

Going forward, we will add additional markets selectively. Our focus has shifted to activating these data assets in the digital ecosystem by connecting them to both global and local platforms and publishers. The IPG win is a strong validation of our global strategy, as is, the recent expansion of our PayPal relationship, which now spans 14 markets.

In summary, the challenges we face with a single large publisher are real, but we believe, unique to this single publisher. We have an experienced team pursuing a number of initiatives to reaccelerate our growth, that when we look at our segment guidance, we feel it is balanced.

Next, Connectivity. Connectivity had a milestone quarter. During the period, we achieved a $200 million revenue run rate, and posted record gross and segment margins. Bolstering these strong results is our continued innovation and commitment to building an open and common identity framework for the common good of everyone in the ecosystem.

A few highlights from the quarter. Segment revenue was approximately $52 million, up 58% year-over-year. We signed over 25 new logo deals, bringing our total direct client count to over 475. Notably, in the U.S., LiveRamp now works with five of the top six financial services companies, four of the top five retailers, four of the top five automotive companies, and all six of the top telecom providers. Our growth puts LiveRamp on pace [ph] with either (11:40) comparable best-in-class SaaS companies and we are pleased to have achieved it, while also meaningfully growing our bottom line.

We continue to build out our partner network and added several new integration partners in the second quarter. Also, we are broadening the use cases we offer to our clients. For example, during the quarter, we announced a new partnership with Yelp Local Audiences, allowing marketers to leverage Yelp location and search data to target very specific audience segments on third party sites.

In recent quarters, we've seen a lot of interesting second party data sharing use cases emerge. For example, IdentityLink enables brands or first-party data owners to share data for co-marketing purposes. One of our more sophisticated retail clients is leveraging this use case to run co-marketing campaigns with a major airline, and is sharing data with a credit card partner for better analytics.

In addition, through our Data Innovators program, we can enable two or more data owners to share data to create new and differentiated products in the data store. We continue to see very strong adoption of the Google Customer Match use case. In fact, with more than 120 brands leveraging their data for people-based search, Google Customer Match has quickly become a top destination for our clients.

Our ultimate goal is to build out the broadest and deepest coverage map of use cases in the ecosystem, and with more than 500 partners part of this ecosystem today, we are well on our way to achieving our goal. The average number of connections per customer remains between 10 and 11, which we feel good about. The number of recent new clients signed up for the Google Customer Match program has held the average roughly flat.

Just last week, we announced IdentityLink for agencies, marking the completion of our industry-wide IdentityLink rollout. Agencies play an important role in managing the development and execution of marketing strategies for their clients, and we now work with agencies from all six of the top holding companies, including powering full identity across three of them. IdentityLink for agencies allows agencies to scale people-based marketing capabilities across platforms and channels for their clients.

Specifically, this new offering enables agencies to: execute people-based planning, buying and measurement for any client regardless of their technology stack; better manage consumer reach and frequency across channels; and enrich people-based audiences with data from more than 120 unique data providers. Perhaps most importantly, this solution allows agencies to build innovative products and services for their clients on top of LiveRamp's deterministic identity resolution capabilities.

LiveRamp isn't an agency competitor. It is an agency catalyst. A year ago on this call, we shared an ambitious plan to build a standard for omni-channel identity resolution that everyone in the ecosystem could leverage – brands, agencies, technology providers, data owners, and publishers. With this launch, we have completed the first phase of this initiative. All key players can now leverage the industry's largest and most accurate open identity graph to power their people-based marketing efforts. Our focus going forward is ensuring data can move in any direction needed: offline to digital, digital to digital, and digital back to offline to create an omni-channel view of the consumer that can be activated seamlessly across any channel.

International. Before I conclude, I'd like to briefly touch on some of the progress we are making outside of the U.S. International, again, had a strong quarter with revenue up double digits for the second quarter in a row. We continue to make good progress growing our LiveRamp business in the UK and France. During the quarter, we landed several new onboarding clients, including the largest utility provider in France. We are also generating traction with Google Customer Match outside of the U.S., and are currently working with over 15 marketers across Europe to enable people-based search.

On our last call, we highlighted the launch of Connected Spaces in partnership with Adobe. This is early stage, but a great example of innovation, for example, a core client who's experiencing a 20% growth in loyalty program membership and a 23% increase in customer spending per visit since launching earlier this year. As more and more venues are trying to solve the customer experience challenge, we are seeing strong interest from a variety of other airports, malls, stadiums, resorts, and even entire cities for Connected Spaces.

Finally, in APAC, Acxiom China was recently selected by Alibaba Group to become a certified service vendor of Alibaba data bank, the data foundation for all marketing and advertising across Alibaba's ecosystem. Leveraging Acxiom, marketers and platforms can onboard their data into the data bank, merge their data with other sources, and build people-based segments that can be targeted across the scale and reach of Alibaba. We are seeing a lot of early interest in this capability and are currently working with nine brands, including seven new logos to power this use case.

In closing, we are pleased with our solid results in the second quarter. And I would like to thank our associates for their ongoing hard work and many contributions. While we have work to do in each of our divisions, I remain very confident in our business and the steps we are taking to generate even greater results for our clients and shareholders.

Thank you again for joining us today. We look forward to updating you on our continued progress in the quarters ahead. And with that, I will turn the call over to Warren.

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Thanks, Scott, and good afternoon, everyone. In my portion of the call today, I'll highlight our results and then conclude with our guidance. Next, Lauren will lead a question-and-answer session, in which Scott and I will address a few top-of-mind questions. Following this QA, we will open the call to your questions.

Q2 highlights. Please turn to slide 4. Our performance trend line is clear, Q2 is yet another positive proof point. Adjusted revenue was up 8%, Q2 was the eighth consecutive quarter in which revenue has increased by more than 5%. As a company, our gross margin again exceeded 50%. In fact, at 52%, it is up over 500 basis points. Our gross margin has been at or above 50% in each of the last four quarters. Operating income of $31 million was up 27%. On average over the last eight quarters, our operating income has increased 21%. Operating margin was 14%, up 250 basis points. On a trailing 12-month basis, our operating margin was 12%, up 160 basis points. Adjusted EBITDA improved 14% to $47 million, and our EBITDA margin was 21%, up 170 basis points. And free cash flow to equity on a trailing 12-month basis was $68 million, up from $39 million a year ago.

In the quarter, Marketing Services again posted meaningful margin improvements. Gross margin improved 390 basis points to 36%. Segment margin expanded over 400 basis points to 23%. Most importantly, we're pleased that this segment margin has improved in seven of the last eight quarters.

Next, please turn to slide 5. Connectivity is a best-in-class SaaS company. In Q2, our revenue run rate exceeded $200 million, revenue growth accelerated to 58%, gross margin surpassed 67%, and segment margin expanded to 11%. And lastly, our business is scaling beautifully. In the U.S., our gross margin was 71%, and our segment margin was a stellar 18%.

On slide 5, we have highlighted a few comparative metrics. Whether it's our margin structure, the number of $1 million clients, dollar-based net retention, or our revenue per head of approximately $400,000, make no mistake, the value of this asset is clear and is significant. And finally, we continue to return capital to our shareowners. In the quarter, we repurchased 860,000 shares for approximately $19.8 million. Since inception of our repurchase program, we have repurchased 17.7 million shares for approximately $306 million.

In summary, our performance continues to demonstrate a trend of continuous improvement and value creation. Next, Connectivity is performing beautifully, and as an asset, compares favorably to the best-in-class SaaS companies. And finally, we continue to walk the talk when it comes to balancing growth and reinvestment with a return of capital to our shareowners.

Before jumping into our guidance, let me mention that slide 6 through 12 highlight the detail of our quarterly performance. These charts are the same as we have consistently provided. Now, onto guidance.

Please turn to slide 13. As a reminder, our guidance excludes items, including non-cash stock compensation, purchased intangible asset amortization, restructuring charges, and separation costs. That said, we continue to expect total revenue of between $920 million and $930 million. Next, we are increasing our full-year adjusted EPS guidance. We now expect adjusted EPS to be in the range of $0.80 to $0.85, up from our prior guidance of roughly $0.80. We continue to expect that business separation activities will be completed by the end of fiscal Q3. However, we now expect our expenditures to be between $15 million and $20 million. And finally, we now expect CapEx to be roughly $60 million, down from our perilous guidance of $65 million. Slides 14 and 15 highlight our expected revenue phasing and other guidance assumptions.

With that, I will turn the call back to Lauren, following this QA, we will open the call to your questions.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Thanks, Warren. For those of you listening today, we thought we thought we might change it up a bit and proactively address a few top-of-mind questions. So let's begin with Audience Solutions. Warren, can you talk about the growth rate of Audience Solutions exclusive of the large digital publisher of which you spoke this past quarter?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Lauren, I'd be happy to. Let me start off by saying that as a matter of principle, we won't talk about the economics of any customer. That said, let me try to add some level of color. In the first half of this year, excluding this customer, our segment revenue was down as a result of timing, non-recurring revenue, and delayed bookings.

In the second half of this year, meaning in Q3 and Q4, we expect our revenue growth rate exclusive of this customer to rebound. So net for the year, we would expect our Audience Solutions revenue growth, again exclusive of this customer, to be up mid-single digits. By way of comparison, the comparable revenue growth metric in FY 2017 was roughly flat.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Warren, do you continue to expect revenue from this customer to fall off considerably in Q3?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Yes. We expect revenue associated with this customer to decline materially this quarter.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

So for the year, do you still believe Audience Solutions revenue will be up low to mid-single digits?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

We do. We continue to believe this is the right estimate. While revenues from this large customer will decline significantly, our Audience Solutions management team has been hard at work building new sources of revenue. Specifically, we're counting on growth from all other digital revenues, our Global Data initiative, and initiatives associated with other services.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Thanks. Scott, a question for you. When I look at the back half of the year, it seems that you've replaced highly certain revenue with expected revenue from largely and proven initiative, am I missing anything?

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

Well, Lauren, I think what you have to remember is the following. So first, we've been working with other digital publishers for years. So expense in growing our digital footprint is a natural extension of what we already do. Next, our other growth initiatives were kicked off well before this transition. These initiatives, like Global Data, also leverage our core capabilities. And finally, we have a highly skilled and experienced Audience Solutions management team that has consistently delivered. From that, I don't and we won't ever discount the risk, but the same time, we believe our guidance is very balanced.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Thanks. Just another question for you. What is the risk of other publishers transitioning to this new revenue model?

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

Well, I mean there's always risk. But that said, we don't believe there is another shoe to drop here. We don't have any other publishers that operate at this scale or with this level of sophistication. Stated differently, most publishers don't have the capability nor interest to manufacture high-quality data themselves. We believe there continues to be a large untapped opportunity for us to pursue.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Thanks. So switching gears now to Marketing Services. Scott, what gives you confidence in your second half outlook for Marketing Services, and when do we get back to flat or positive growth?

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

Yeah. So, long and short, it's our contracted and committed revenue. So in Q3, we've seen little risk in our forecast. And in Q4, what is not already contracted or committed is in line with historical norms. And also remember that the comps get much easier in Q4.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Great. So, a couple of questions on Connectivity then. One, Connectivity had an exceptional quarter, but your year-to-date performance implies a deceleration in the second half to get to your guidance. Anything we should be worried about here, or it's simply the law of large numbers?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Well, first of all, there is no new news here. We do expect lower grade growth rates in the second half. That said, let me be clear, this business is performing extremely well, and we have lots of positive things going on, but let me just name a few. First, this is a huge category and we are the industry leader. Next, our bookings remain strong, and we have best-in-class net retention rates. And finally, we continue to innovate and grow the business through things like data store, new use cases, and international expansion.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

So then let me ask the question a little bit differently. On past calls, you indicated that revenue growth in Connectivity would reaccelerate in FY 2018. Is this still the case?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Yes. We continue to expect revenue growth to accelerate for the year.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Great. A quick housekeeping item. Warren, how is your stock-based comp expense trending?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Let me ask everyone for a moment to turn to slide 20. When you look at this chart, keep in mind a few things. First, we continue to expect stock comp expense for the year to be roughly $65 million. Next and importantly, stock awards are critical component of our acquisition strategy. Roughly 40% of the $65 million is directly tied to acquisitions. As a percentage of revenue, our ongoing stock-based comp is well within industry norms.

Lauren Russi Dillard
Vice President of Investor Relations, Acxiom Corp.

Thanks. Switching gears to a top-of-mind topic, your separation effort. You raised your full-year estimates for separation spend. Why the increase and what do you hope to have accomplished by the end of Q3?

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

First, why the increase. Well, we are sprinting to the finish. As to your second question, as we've stated before, we are giving ourselves optionality. In other words, for any of our divisions, should a situation arise, such as a major partnership or combination, we have put ourselves in a position where we can act on that opportunity in a reasonable timeframe.

Lauren Russi Dillard

Vice President of Investor Relations, Acxiom Corp.

So you're saying this is it?

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Yes. This is it. Everyone should remember though, should an event or a transaction occur, there will be additional spend.

Lauren Russi Dillard

Vice President of Investor Relations, Acxiom Corp.

Thanks, guys. Well that's all I've got. We will now open the call to other questions. Operator?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from Brett Huff from Stephens. Brett, your line is open.

Brett Huff

Analyst, Stephens, Inc.

Q

Thank you and congrats on a really nice quarter on both legacy containing the pricing pressure, as well as the really nice Connectivity quarter, so congrats on that.

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Great. Thanks, Brett.

Scott E. Howe

President, Chief Executive Officer & Director, Acxiom Corp.

A

Thanks.

Brett Huff

Analyst, Stephens, Inc.

Q

Two questions for me. One, can you talk about match rates and just give us an update on that, and maybe also in so doing, can you talk about the variety of match rate, sort of data points that are out there? I think that is confusing the market, it certainly confuses us, number one. And then number two, can you talk a little bit about Google Customer Match as sort of a potential "killer app" that really gets a lot of new customers in the door? It seems like at a faster rate than maybe any other new launch that you've had. So, just give us thoughts on both of those, and thanks.

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.
A

Yeah. So, first off in terms of match rates, and these are ballpark kind of top of mind, Brett, as opposed to exact. I'd say, our web match rates are now north of 60%, and our mobile match rates, call it, 45% or above. And remember, these are deterministic match rates, and I think that's the important thing to remember in all the confusion. So, there are folks out there who claim to have higher match rates, but they're typically – what they're talking about is a probabilistic or sampled match rate, and we could do that, too. But we like to quote the numbers in the context of 100% statistical significant and accurate, meaning, you're not going to get any false positives.

And I should also note that the match rates that we experience vary significantly by client. So, if someone's using SmartReach, for example, which is the co-op of pooling different clients, PII together for only use and match rates, the number could be much higher in excess of 90%. Or if a client is sizable, and they have relationships with a vast majority of consumers, they're going to have a much higher match rate. And so, the numbers we quote are typical match rates, but then when we pool that with specific clients or the co-op data, it often can be much greater.

And I think – the second question you asked is about Google Customer Match. And yes, I mean, we do think it is a killer app. Clients embrace what works, and we publish some case studies that show that the lift from this, high double-digit percentage kind of lift, and given how big search spend is for most advertisers, it's not surprisingly something that they've been quick to adopt. We've now been in market with this for a little over a year. And I want to say, we have north of 120 Customer Match clients, and then also now launching it internationally as well. So I think that'll be a driver for us internationally.

That said, I think we got one more [ph] comment (35:10), and that is when we launch people-based programmatic, I think it's going to be another one of these killer apps, it's something we've been talking about for a couple quarters now. From where we sit today, it looks like that'll be a commercial launch in calendar Q1, and if we know that search is the largest element of most digital spends, we know that programmatic is right on par with it. And so together, those two applications comprise 70% on average of digital spend, and so the good news is coming soon. Advertisers will be able to personalize against both of those killer apps.

Brett Huff
Analyst, Stephens, Inc.
Q

Great. Thank you.

Operator: Your next question comes from Bill Warmington from Wells Fargo. Bill, your line's open.

Q

Hey, guys. This is [indiscernible] (36:05) on for Bill Warmington.

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Hey, [ph] Bill (36:07).

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

A

Hey, [ph] Bill (36:07).

Q

Hey. I have a few questions for you. Connectivity obviously had a very strong quarter, with 58% year-over-year growth. Could you rank the drivers of its performance by new customer contributions versus upselling existing customers?

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

A

Yeah, I could take that. Scott. It's still the majority of new clients. So we probably saw like a low double-digit percent increase in kind of what we call same-store, but as we've said before, that really hasn't been a huge focus for us, and when we go talk to our customers, which we do regularly, that quite frankly, the single biggest pain point that they express, that they'd like us to see us do more evangelization, more education around how do they expand their use cases. So that's something that going forward, over the next few years, we'll start to prioritize and will be an increased growth driver for us.

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Hey, [ph] Bill (37:12). One thing I could add on on that question to what Scott said is, the net retention that we spoke about during the call is over 110% year-over-year, and it actually has been at that level for each of the last eight quarters at LiveRamp. We went and we looked at best-in-class SaaS, and what you kind of find is that if you're over 100%, it's awfully good, if you're north of 110%, you're in some pretty darn good company. So, we're extremely pleased also with our customer net retention.

Q

Got you. And do you have an update for the SmartReach participant count?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

SmartReach participants today are right little bit over 100, right in that neighborhood with...

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

A

90 to 100.

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

...90 to 100 with a few less than – or less than half having implemented so far.

Q

Okay. And then Europe has been a strategic focus for you on Connectivity in particular, particularly the UK and France. I was wondering, what your thoughts are on the potential impact from that General Data Protection Regulation, which is slated for May of next year?

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

I'll give you my take from talking with a lot of customers throughout Europe. First of all, one of the things that we've made a point of is that we welcome GDPR. So what GDPR does is it represents harmonization. Secondly, from Acxiom standpoint, recognize that we've been dealing with privacy and the complexities of privacy for many, many years. So we believe that this plays right into our sweet spot. So at the end of the day, we know that our customers are looking for trusted partners to help them navigate the complexities of privacy, the complexities of GDPR. We believe we are exactly that partner. We also feel that whether it's in Europe or anywhere else for that matter, when people are thinking about how to utilize their data, how to monetize it, better use it for their customers, there's no better partner than Acxiom, and this is just another example of why.

Q

Got you. All right. That's it for me. Thanks, guys.

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Thank you.

Operator: Your next question comes from Dan Salmon from BMO Capital Markets. Dan, your line's open.

Q

Hi, everyone. This is [ph] William (39:44) on for Dan.

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

A

Hey, [ph] William (39:46).

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Hey, [ph] William (39:47).

Q

Hey. Two quick questions. I know on your fiscal 4Q 2017 call, you talked about potential expansion beyond this marketing, so obviously extremely early, but I was wondering if you could provide any updates there. And there's obviously the question on GDPR, a question on the rollout of iOS 11 in Apple's ITP, it's obviously impacting a bunch of other companies in the ecosystem. To what extent does that provide an opportunity for you guys to sort of sell data to those guys to help them track users across the web? Thank you.

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

A

Yeah. So on the first one, [ph] William (40:23), this is Scott, expansion beyond marketing, boy, if I could turn back the clock and take back those comments, quite frankly, I wish I could. And the reason being is that, I think what I talked about that, I laid these out as initiatives that we were going to pursue that we thought would be important to lock in the next 10 years of growth. And I got a lot of comments from investors worried that we were going to go do some crazy acquisition and overextend ourselves into new markets, which was not my intent at all.

Rather, as we go investigate these new markets, our plan is to expand into areas that are adjacent and build on capabilities that we already have. And these things will be fairly immaterial to our growth over the next 12 months, but potentially quite meaningful over the next three to five years. Over the last six months, we have explored some adjacent spaces, we've prioritized them. And we start to make some traction in some additional areas: government, healthcare, risk or authentication, but still so early that it's not all that useful to talk about in the call. Fairly minor in terms of investment that we're putting against it, and certainly minor in terms of revenue contribution. But the important thing is we're planting several [ph] seed streams (42:07), and we believe that some of them will hit and be fruitful for us over time. Your second question, remind me...

Q

On ITP.

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.

A

Yeah. So, I mean to be clear, we don't have the same kind of exposure to say Safari that others out there do. We don't use them as a match partner. And you know, we don't build our match network, we build it up, personal identifiers as opposed to solely cookie. In addition, we work with so many clients that are collecting first-party permissions and in many cases like SmartReach, they're giving us permission to federate those permissions, so all is said as we think about the impact of that, we think that we're largely insulated from it.

And in fact, the discussion around that, the industry attention on those issues and privacy, we feel is good for us, because it makes everybody in this space realize how important identity resolution is, and that's obviously something that we pride ourselves at being the market leader at.

Q

Perfect. Thanks a lot.

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.
A

Thank you.

Operator: [Operator Instructions] Your next question comes from Kip Paulson from Cantor Fitzgerald. Kip, your line's open.

Kip Paulson
Analyst, Cantor Fitzgerald Securities
Q

Hi. Thanks for taking the question. Just a couple for me. First, gross margins in the Connectivity business are impressive, and then I believe you guys mentioned 71% in the U.S. Do you think there's still room to move higher from here, or do you think that's kind of capped out, and you'll keep reinvesting in the business there? And then second, I believe you mentioned average use cases between 10 and 11, is this a case of new customers dragging down the average? How many use cases do your heaviest customers have? Thanks.

Warren C. Jenson
Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.
A

So, Kip, let me talk about gross margin. There will always be instances where we will invest, so I'm not going to predict that every quarter, we're going to be in the U.S. over 71% or 67% in total. But obviously, a very, very strong performance. I'd highlight a couple of things.

First of all, it does demonstrate the leverage of this business, because the business is scaling beautifully. The other two metrics that I'd ask everybody to really think about is an [ph] offer or a (44:49) contribution margin of 11% in the quarter in total, coupled with a contribution margin in the U.S. of 18%. One of the things that's going on right now is, we are moving into a period of rapid potential cash flow generation. So if you look at EBITDA for this segment, and you were to calculate our EBITDA run rate as of Q2, you'd see that it's about $35 million, which means you'd factor in some growth, and would anticipate that in the forward periods, throwing off some really pretty interesting cash flow.

So, now coming back specifically to your question, yes, over time, our target gross margin is over 75% in Connectivity. We're not predicting a timeframe by which we will be there, but the trend line is very clear and very positive for this business.

Scott E. Howe
President, Chief Executive Officer & Director, Acxiom Corp.
A

And I can handle the second question, which was about the use cases. So if we look at our very heaviest, I mean, we probably have a couple that are activating, call it, 30 roughly and that's not the exact number, but 30 roughly use cases, so those are our power users.

We think that gives us a lot of headroom. Our belief is that the average Fortune 500 marketer could activate between 300 to 500 different use cases. And so, it tells us that we're still very early stage here. And when I talk about use cases, I'm talking about every single digital publisher on the media plan, including both search and display, addressable television, addressable radio, call centers, site personalization, point-of-sale advertising, essentially any customer action that can be improved with the injection of data, our belief and our strategy is to provide the connections that allow that data to be utilized in that interaction. But again, on average, we're somewhere between 10 and 11, and so that suggest that there's a lot of room for usage increase there.

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Hey, Kip, one other thing that I would add that we're all referring to that we're extremely proud of right now is that we are accelerating growth rate for the year. One thing that we would clarify for everyone's models though is, we would now expect our growth rate year-over-year in Connectivity to be closer to 45% than to 50%. And that's just [ph] our (47:36) looking at our estimates, looking at our revenue estimates for both Q3 and Q4. So, extremely strong growth, lot of positive momentum heading into the back half of the year that would put our overall Connectivity growth rate for the year at about 45%.

Kip Paulson

Analyst, Cantor Fitzgerald Securities

Q

All right, very helpful. Thanks, guys.

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

A

Thank you.

Operator: And at this point, I'd like to turn the call back to Warren Jenson for closing remarks.

Warren C. Jenson

Chief Financial Officer, Executive Vice President & President of International, Acxiom Corp.

Again, thanks to all of you for joining us today. I'd end with three quick summary remarks. First of all, we believe that Q2 was really yet another proof point in demonstrating really a very positive trend of continuous improvement at Acxiom and continuous value creation. [ph] Next, today (48:25), an awesome quarter for Connectivity and LiveRamp. Connectivity is performing beautifully and is an asset that compares very favorably to best-in-class SaaS. And then finally, would note that we continue to walk the talk when it comes to balancing growth and reinvestment with a return on capital to our shareowners. Thanks again for joining us. We look forward to speaking to all of you over the course of the next couple of days.

Operator: This conclude today's conference call. Thank you for your participation. You may now disconnect.