May 17, 2022

Zacks Small-Cap Research

Sponsored – Impartial - Comprehensive

M. Marin
312-265-9211
mmarin@zacks.com

scr.zacks.com
10 S. Riverside Plaza, Chicago, IL 60606

VIQ Solutions (VQS-NASDAQ)

VQS: On Track for Strong Revenue Growth, Margin Expansion

VIQ's 1Q22 revenue of $11.5M advanced 40% y/y primarily reflecting the integration of Auscript and TTA. The company is on track to reach targeted revenue of about $50M or more in 2022. VIQ signed two new technology services contracts in 1Q22 to support court recording and transcription services. These are valued at a combined roughly $1.9M per annum and advance the company's goal of shifting to high margin revenue and SaaS bundled solutions.

OUTLOOK

On an adjusted basis excluding COVID-19 subsidies, VIQ registered 1Q22 gross margin of 47.6% compared to 47.3% in 1Q21, implying an improvement of about 30 bps, with further margin expansion anticipated. VIQ expects to leverage recently acquired Auscript to expand globally, including via cross-promoting its growing suite of products and service offerings. Moreover, as the product mix continues to shift towards Auscript services, FirstDraft and other AI-powered offerings, this trend is expected to have a positive impact on margins.

Current Price (5/16/22)	$1.02
Valuation	**$10.00**

SUMMARY DATA

52-Week High	**$7.60**
52-Week Low	**$0.93**
One-Year Return (%)	**-85.85**
Beta	**-0.49**
Average Daily Volume (sh)	**51,158**
Shares Outstanding (mil)	**30**
Market Capitalization ($mil)	**$30**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**10%**
Insider Ownership (%)	**24%**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2022 Estimate	**N/A**
P/E using 2023 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**High**
Type of Stock	**N/A**
Industry	**Technology Services**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2019	6.4	6.2	6.5	6.1	25.1
2020	7.5A	8.3A	8.2A	7.8A	31.7 A
2021	8.3A	8.2A	7.1A	7.5A	31.0 A
2022	11.5A	12.3E	13.3E	13.4E	50.5 E

Per Share Data

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2019	-0.12	-0.17	0.04	-0.25	-0.49
2020	-0.37A	-0.05A	-0.02A	- 0.18A	-0.62A
2021	-0.07A	-0.42A	-0.15A	-0.12A	-0.74A
2022	-0.07A	-0.09E	-0.06E	0.04E	-0.17E

Quarters might not sum due to rounding & share counts

Disclosures on page 11

© Copyright 2022, Zacks Investment Research. All Rights Reserved.

KEY POINTS

- ***Reiterated 2022 guidance …*** VIQ reported 1Q22 results last week, with revenue of $11.5 million advancing 40% year-over-year primarily reflecting the integration of Auscript and TTA. The company expects to reach about $50 million or more in annual revenue in 2022, reflecting existing business of roughly $31 million to $32 million, the integration of Auscript and TTA and the commencement of the Queensland courts contract.

- VIQ signed two new technology services contracts in 1Q22 to support court recording and transcription services. These contracts are valued at a combined roughly $1.9 million per annum. Importantly, in our view, the company is also advancing its goal of shifting to high margin revenue and SaaS bundled solutions.

- VIQ intends to continue shifting its revenue base toward recurring, higher margin technology revenue. The company believes the strong reception to the FirstDraft product will facilitate the goal to cross-promote and cross-sell its growing suite of digital products and SaaS model. VIQ also is working with several customers in the U.K. Court vertical to use FirstDraft.

- ***Adjusted margin improvements, with further margin expansion expected*** On an adjusted basis excluding COVID-19 subsidies, the company registered a 1Q22 gross margin of 47.6% compared to 47.3% in 1Q21. This implies gross margin improvement on an adjusted basis (of about 30 bps), with further margin expansion anticipated, reflecting the integration of the company's technology platforms across all verticals, including courts, as courts emerge from pandemic-related closures.

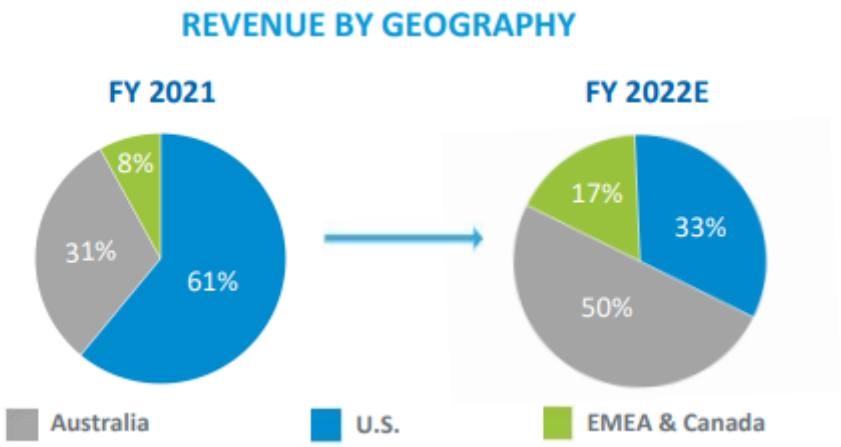
1Q22 HIGHLIGHTS

Shift to high margin products, SaaS bundled solutions

VIQ Solutions (VQS-NASDAQ and VQS-TSX) reported 1Q22 results last week, with revenue of $11.5 million advancing 40% year-over-year compared to $8.3 million in 1Q21. The improvement primarily reflects the integration of Auscript and TTA, which VIQ acquired in 2021. This increase was partially offset by lower technology sales. The company signed two new technology services contracts in 1Q22 to support court recording and transcription services. These contracts are valued at a combined roughly $1.9 million per annum. Importantly, in our view, the company is also advancing its goal of shifting to SaaS bundled solutions.

VIQ intends to continue shifting its revenue base toward recurring, higher margin technology revenue. The company believes the enthusiastic reception to the FirstDraft product will facilitate this goal, as FirstDraft and other high margin products gain traction. The company indicated that its technology and technology services pipeline has grown, which supports this goal, as well. Moreover, VIQ recently introduced NetScribe in the U.K. and Canada. As demand for digital transcription and documentation services continues to rise, VIQ expects to transition existing and prospective customers to the digital platform, which further facilitates the goal to cross-promote and cross-sell its growing suite of digital products and SaaS model.

The strong 1Q22 topline puts VIQ on track to reach (or exceed) the targeted at least $50 million in revenue in 2022. The improvement in 1Q22 revenue notwithstanding, court closures continue to impact results. COVID-19 cases continue to fluctuate in many markets, which led to an estimated $0.5 million negative impact on revenue in 1Q22. Courts represent the company's largest vertical (contributing 58% of 1Q22 total revenue). Australia went into lockdown for about two weeks, which meant court closures in VIQ's largest geographic market (Australia represented 54% of 1Q22 total revenue). Australia is expected to contribute an estimated 50% of total revenue in 2022, up from about 31% in 2021. The shift primarily reflects the above noted integration of Auscript.



Source: Company reports

In 1Q22, VIQ's revenue mix shirted towards the Legal (Courts) vertical, which contributed 58% of total revenue, as noted. The Criminal Justice (including Law Enforcement) vertical represented 13%, Insurance was 15% and the Media, Corporate and Government vertical added another 14%.

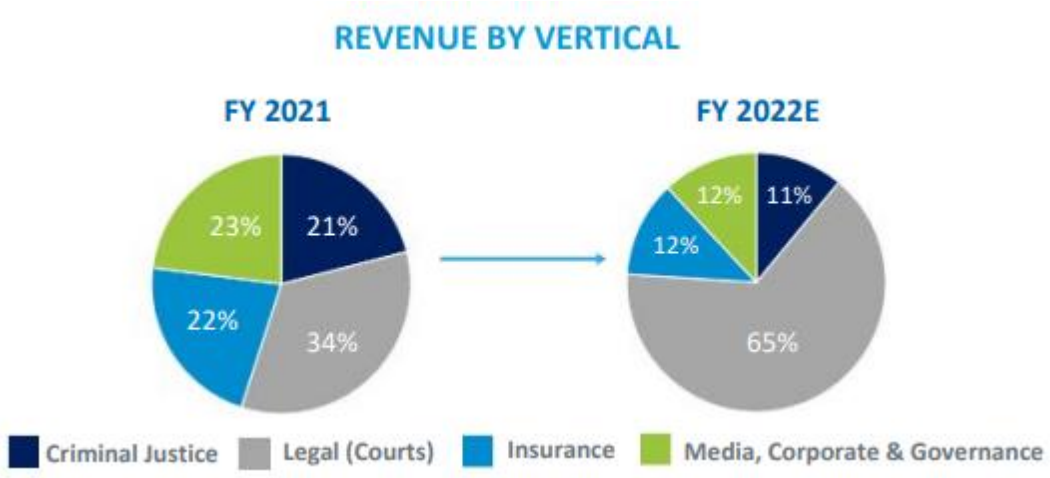
Adjusted margin improvements, with further margin expansion expected

The company registered 1Q22 gross profit of $5.5 million and a gross margin of 47.6%. This compares to $4.0 million and a 48.7% gross margin in 1Q21. Gross margins were lower because VIQ recorded lower volumes of high-margin technology revenue in 1Q22. Moreover, last year's 1Q included $0.1 million in COVID-19-related wage subsidies, while there were no such subsidies in 1Q22. On an adjusted basis excluding COVID-19 subsidies, gross margins would have been the above noted 47.6% compared to 47.3% in 1Q21. This implies gross margin improvement on an adjusted basis (of about 30 bps), with further margin expansion anticipated.

VIQ expects further gross margin expansion over 2022, reflecting the integration of the company's technology platforms across all verticals, including courts, as courts emerge from pandemic-related closures. For example, VIQ is working with several customers in the U.K. Court vertical to use FirstDraft, which enables users to get a written document quickly to improve the accessibility of information in almost real-time. VIQ expects that margins will benefit as the company integrates new acquisitions and migrates its new customers to the AI-enabled platform. VIQ expects the ongoing roll-out of *FirstDraft* and other high margin products to accelerate revenue growth and shift the product mix towards higher margins. VQS reported a 1Q22 net loss of ($1.6) million, or ($0.07) per share, compared to a net loss of ($1.7) million, or ($0.07) per share, recognized in 1Q21.

Supporting growth targets in 2022

VQS remains committed to further advancing its growth strategy in 2022, including through integrating recently acquired operations and expanding its suite of product and service offerings. Towards this goal, VIQ's recent strategic partnership with software development company LegalCraft is expected to help the company consolidate and grow its strategic market position in the legal sector. LegalCraft focuses on technology innovations for the legal sector particularly via its flagship product Lexel, makes VIQ the first LegalCraft strategic partner to offer Lexel in the U.S. Lexel enables law professionals to collaborate securely to prepare cases for trial.



Source: VQS presentation

The company expects to reach about $50 million or more in annual revenue in 2022. In addition to the revenue base of roughly $31 million to $32 million from existing business, the company expects the integration of Auscript and TTA to result in a combined incremental roughly $14 million of revenue. Moreover, the commencement of the Queensland courts contract is also expected to add about another $6 million above that.

Shift towards Legal / Courts as Auscript is integrated …

The company expects its revenue mix to shift toward the legal / court sector in 2022. In part, this reflects Auscript and the Queensland courts contract, but this anticipated increase also reflects the resumption of courts activity generally, as the pandemic abates. The sector accounted for about 34% of total revenue in 2021 and is expected to represent about 65% in 2022.

Auscript Australasia Pty Ltd is an Australian court recording and transcription services company with a 100-year operating history VIQ acquired in 2021. Auscript Australasia is expected to enable VIQ to provide exception service and enhance the quality of delivery for all Australian clients, with a significant opportunity to leverage technology to improve overall margins and offer innovation to customers and transcriptionists across Australia. The company expects Auscript to accelerate its expansion in Australia and across the Asia Pacific region and enable cross-promotion of its growing product portfolio, as noted.

The company believes it can also leverage Auscript to expand globally. Moreover, with the addition of more than 2.3 million pages of specialized transcripts and more than 200,000 hours of evidentiary recordings per year, VIQ believes that with Auscript, it is now one of the largest providers of recording and transcription services in the Asia Pacific region. The company also expects to benefit from cross promotional opportunities, including driving FirstDraft and NetScribe™, powered by aiAssist™ adoption in the region.

Revenue from the insurance sector is also expected to grow in 2022, although this growth is somewhat obscured by the expected jump from the legal / court sector reflecting factors noted above. The media vertical contribution might be lower (despite two recent new contracts with leading global news agencies), given the advertising cycle coincident with the U.S. election cycle.

Plus increasing focus on the U.K. expands growth opportunities

VIQ recently acquired The Transcription Agency (TTA). According to management, TTA is a leading supplier of secure outsourced transcription services to clients in private and public sectors in the U.K. The TTA transaction closed on October 1, 2021, giving the company a solid foundation in the U.K. market, where VQS expects to grow. TTA and VQS share a large U.K. customer and service offerings are complementary. VQS anticipates the opportunity to cross-sell its growing suite of products and solutions (see below) to government and non-government entities in the U.K. and recently appointed an experienced executive to drive growth in the U.K.

Following the TTA deal, VIQ introduced NetScribe in the U.K. and Canada. As demand for digital transcription and documentation services continues to rise, VIQ expects to transition existing TTA and prospective customers to the digital platform. In turn, this is also expected to facilitate the company's ability to cross-promote and cross-sell its growing suite of digital products and SaaS model. TTA has qualified for inclusion on the NHS Shared Business Services Group purchasing grid, which is also likely to facilitate VIQ's marketing to prospective customers. Many U.K. law enforcement agencies and insurance providers use this grid.

VIQ also appointed Jayne Perry, an industry veteran with more than 20 years of experience in the court and legal industry, including a prior executive role at Auscript, as Managing Director, United Kingdom and EMEA. She will focus on supporting the integration of TTA and accelerating growth in the U.K. and expanding VIQ's global technology footprint.

No major M&A transactions expected in 2022, as focus is on consolidating operations

VIQ has historically leveraged strategic M&A to complement and enhance organic growth. Following the two key acquisitions noted above, the company expects to consolidate its new units and overall organization in 2022 and therefore expects its operational focus in 2022 to be on execution of its organic growth initiatives and integration of recent acquisitions and new clients into the AI-enabled system. Although the company does not intend to proactively seek prospective M&A candidates, if VQS finds an attractive tuck-in opportunity, we would not be surprised to see a smaller transaction.
At the end of 1Q22, VIQ had about $3.7 million in cash on its balance sheet.

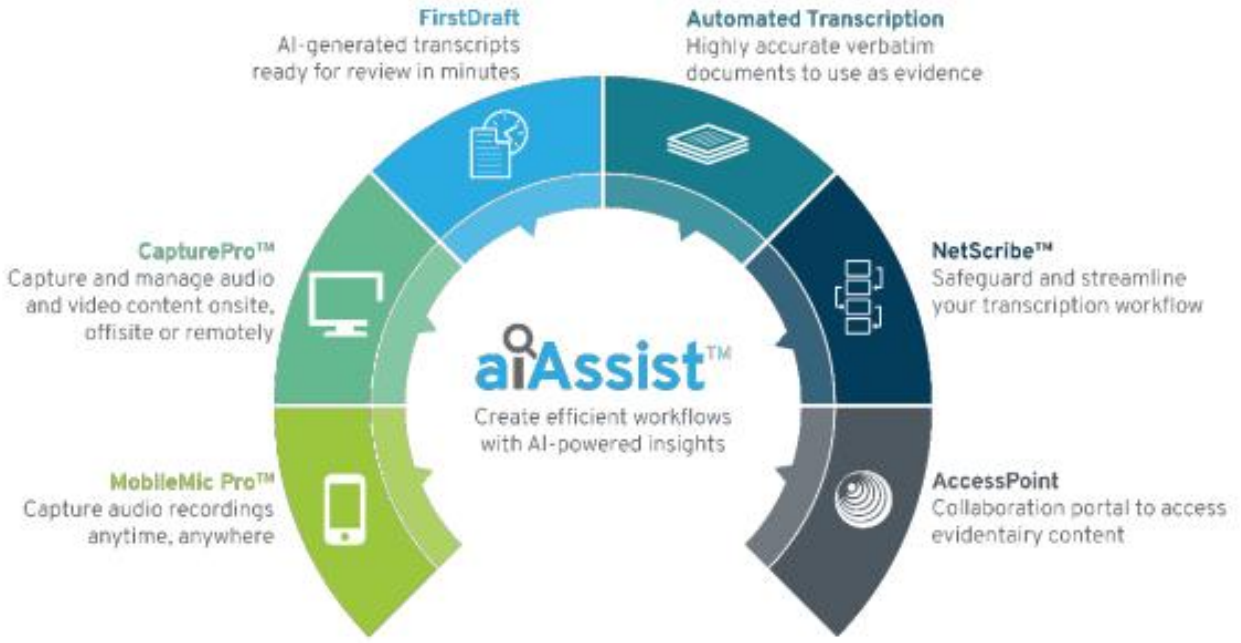
Notably, the first quarter generally represents a slow period in terms of working capital, specifically collection of receivables. Moreover, in 1Q22, working capital was also negatively impacted by the closures in Australia. VIQ has indicated that trends have improved in 2Q22 and the cash balance is expected to improve at the end of the current quarter. Moreover, with EBITDA and cash flow expected to improve over 2022, on higher expected revenue and rising gross margins, the company expects its use of cash to be lower and to reach cash flow breakeven / positive as the year progresses.

CROSS-PROMOTIONAL OPPORTUNITIES & ACTIVITIES

Digitalization, cross-promotion & new product launches, among other strategic initiatives

With its expanding offerings portfolio – including *FirstDraft* – the company believes it can address a greater portion of its targeted addressable market. Concurrently, VIQ believes that recent acquisitions also facilitate the potential to introduce and cross-promote new products and services. Moreover, growing awareness of the need for digitalized content could also be a catalyst to accelerate the company's expected market share gains.

AI-Powered Product Offerings



Source: VIQ Investor presentation

VIQ expects the ongoing roll-out of *FirstDraft* to accelerate revenue growth and shift the product mix towards higher margins. *First Draft* enables faster turnaround of transcripts in advance of editing the transcript. *FirstDraft* converts audio files to text quickly, leveraging the VIQ speech recognition engine, enabling faster turnaround than under prior methods. Although the transcript still needs to be put through editing, the *FirstDraft* transcript allows users to get a written document that they can use quickly. It enables a cost-effective way to digitize large volumes of data. As noted, VIQ and several U.K. Court customers are working to use FirstDraft to improve content delivery and improve the accessibility of information in almost real-time and enable content users to access digital capabilities of the FirstDraft product, which was selected as an honoree in *Fast Company's 2022 World Changing Ideas* awards.

VALUATION

Based on our 2022 revenue forecast, VIQ shares trade at a significant discount to peers in the cloud-based technology space. Peers trade at an average multiple of about 6x to 8x. We also point to Nuance Communications, a large player in the technology/ communications solutions space that helped consolidate the medical transcription market through a series of M&A transactions and organic measures much as VIQ is now doing in its core silos.

As a publically traded company, Nuance shares commanded an even higher than industry average multiple of forward revenue basis, according to consensus data. Moreover, Microsoft acquired Nuance at a valuation that implied a roughly 23% premium to where they had been trading prior to the announced offer. We believe this underscores the importance of the sector and also implies a higher valuation for VIQ shares over time.

We expect the multiple gap on VQS shares to narrow further compared to peers, as the company continues to make strides in its organic and acquisition-driven growth strategy. We anticipate multiple expansion and believe the recent uplisting is a positive in this regard. The uplisting of VIQ shares to the Nasdaq (under the ticker VQS) is expected to boost awareness of the company and the company's prospects, as well as expand the pool of potential investors. Our valuation of $10 equates to only just over about 5x our 2022E estimated revenue. This multiple is below the group average and our revenue forecast does not take into consideration additional possible M&A tuck-in transactions, as noted.

RECENT NEWS

- VIQ announced 1Q22 results on May 11, 2022.
- FirstDraft was selected as an honoree in the Fast Company's 2022 World Changing Ideas Awards on May 4, 2022.
- The company announced 4Q21 results on March 30, 2022.
- VIQ appointed two new board members on March 24, 2022 and another board appointment on April 5, 2022.
- VIQ announced that it was awarded a new U.S. patent on February 08, 2022.
- VIQ announced a strategic partnership with LegalCraft on February 01, 2022.
- On January 04, 2022, VIQ appointed a new managing director to strengthen its U.K. market presence.
- VIQ closed on the Auscript transaction on December 13, 2021.
- VIQ launched NetScribe™ across the U.K. and Canada on October 26, 2021.
- VQS shares began trading on the Nasdaq on August 12, 2021.

RISKS

We believe risks include those outlined below, among others.

- The impact of COVID-19 on VIQ's business could increase if the number of cases escalate and last longer than originally anticipated.
- VIQ might not gain market share or wallet share as quickly as it expects.
- The company might not continue migrating customers to the SaaS model as quickly as management anticipates.
- The company could incur unanticipated costs associated with its growth strategy and for marketing to promote its platform.
- Additional M&A transactions that the company anticipates might take longer than expected to close or might not close at all.
- Competition could increase.
- The company's cash burn rate could be higher than management expects and / or it might not reach positive cash generation as quickly.
- VIQ might need to raise capital to support growth initiatives.

PROJECTED INCOME STATEMENT

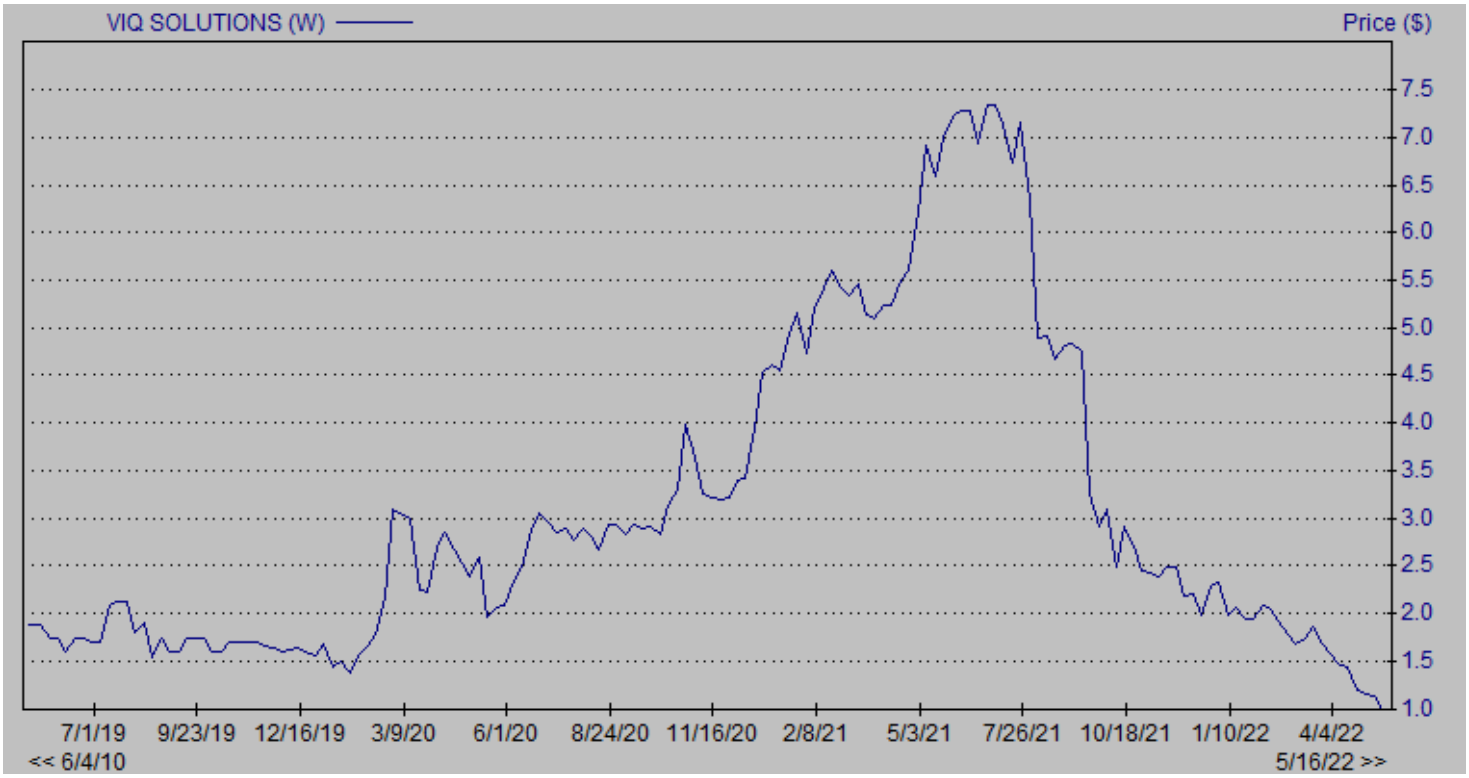
VIQ Solutions Inc. Income Statement & Projections ($)

	2018	2019	2020	Mar-21A	Jun-21A	Sep-21A	Dec-21A	2021A	Mar-22A	Jun-22E	Sep-22E	Dec-22E	2022E
Revenue	$11,462,804	$25,096,308	$31,749,693	$8,254,222	$8,191,812	$7,086,357	$7,514,421	$31,046,812	$11,524,981	$12,287,718	$13,264,078	$13,396,719	$50,473,496
Cost of sales	7,874,219	14,276,321	15,599,437	4,236,387	4,210,733	3,444,259	4,232,474	16,123,853	6,035,932	6,291,312	6,711,624	6,711,756	25,750,623
Gross profit	3,588,585	10,819,987	16,150,256	4,017,835	3,981,079	3,642,098	3,281,947	14,922,959	5,489,049	5,996,406	6,552,455	6,684,963	24,722,873
Gross margin	31.3%	43.1%	50.9%	48.7%	48.6%	51.4%	43.7%	48.1%	47.6%	48.8%	49.4%	49.9%	49.0%
Selling & administrative expenses	5,533,724	8,954,512	11,034,902	3,539,110	3,953,046	6,516,449	5,111,108	19,119,713	6,136,309	6,135,695	6,135,082	6,073,731	24,480,817
Research & development expenses	458,675	994,640	1,074,178	239,663	260,010	317,546	274,889	1,092,108	199,085	197,094	195,123	193,172	784,474
Stock-based compensation	(31,461)	195,113	725,316	85,995	6,687,792	859,119	862,283	8,495,189	952,196	800,000	800,000	800,000	3,352,196
FX & other	198,180	217,040	(132,306)	(95,994)	153,400	(445,978)	(859,948)	(1,248,520)	(623,940)	(630,179)	(636,481)	(642,846)	(2,533,447)
Depreciation & amortization	648,873	3,502,429	5,259,243	1,248,363	1,188,115	1,034,951	1,170,172	4,641,601	1,159,344	1,124,564	1,090,827	1,058,102	4,432,836
Total operating expenses	6,994,435	12,295,345	17,961,333	5,017,137	12,242,363	8,282,087	6,558,504	32,100,091	7,822,994	7,627,174	7,584,551	7,482,159	30,516,877
Operating income	(3,405,850)	(1,475,358)	(1,811,077)	(999,302)	(8,261,284)	(4,639,989)	(3,276,557)	(17,177,132)	(2,333,945)	(1,630,767)	(1,032,096)	(797,196)	(5,794,004)
Interest expense	(96,484)	(1,549,904)	(4,934,517)	(331,419)	(335,594)	(329,598)	(334,489)	(1,331,100)	(339,713)	(339,883)	(340,053)	(340,223)	(1,359,871)
Other	(2,552,729)	(1,399,781)	(5,343,744)	(599,037)	(597,177)	(353,062)	1,322,486	(226,790)	615,045	(895,766)	(670,818)	2,199,131	1,247,592
Total operating inc / (expenses)	(2,649,213)	(2,949,685)	(10,278,261)	(930,456)	(932,771)	(682,660)	987,997	(1,557,890)	275,332	(1,235,648)	(1,010,871)	1,858,908	(112,279)
Pretax income	(6,055,063)	(4,425,043)	(12,089,338)	(1,929,758)	(9,194,055)	(3,957,329)	(3,653,880)	(18,735,022)	(2,058,613)	(2,866,416)	(2,042,967)	1,061,712	(5,906,283)
Tax	(11,571)	(99,155)	944,032	262,969	(1,304,607)	97,824	87	(943,727)	(48,696)	(200,000)	(200,000)	(200,000)	(648,696)
Net inc/ (loss)	(6,066,634)	(4,524,198)	(11,145,306)	(1,666,789)	(10,498,662)	(3,859,505)	(3,653,793)	(19,678,749)	(2,009,917)	(2,666,416)	(1,842,967)	1,261,712	(5,257,587)
FX	(95,899)	(262,811)	56,152		101,642	(432,533)	484,323	153,432	412,798	100,000	100,000	100,000	712,798
Per share data:													
Comprehensive loss	(6,162,533)	(4,787,009)	(11,089,154)	(1,666,789)	(10,397,020)	(4,292,038)	(3,169,470)	(19,525,317)	(1,597,119)	(2,566,416)	(1,742,967)	1,361,712	(4,544,789)
LPS	($0.04)	($0.49)	($0.62)	($0.07)	($0.42)	($0.15)	($0.12)	($0.74)	($0.07)	($0.09)	($0.06)	$0.04	($0.17)
Avg shares out	161,816,064	9,251,546	18,080,533	24,467,151	25,029,019	26,359,517	29,938,689	26,448,594	29,881,717	29,939,689	29,940,689	29,990,689	29,938,196

Source: Company reports, Zacks estimates Quarterly LPS/EPS might not sum to annual reflecting differences in share count.

© Copyright 2022, Zacks Investment Research. All Rights Reserved.

HISTORICAL STOCK PRICE



© Copyright 2022, Zacks Investment Research. All Rights Reserved.

DISCLOSURES

The following disclosures relate to relationships between Zacks Small-Cap Research ("Zacks SCR"), a division of Zacks Investment Research ("ZIR"), and the issuers covered by the Zacks SCR Analysts in the Small-Cap Universe.

ANALYST DISCLOSURES

I, M. Marin, hereby certify that the view expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report. I believe the information used for the creation of this report has been obtained from sources I considered to be reliable, but I can neither guarantee nor represent the completeness or accuracy of the information herewith. Such information and the opinions expressed are subject to change without notice.

INVESTMENT BANKING AND FEES FOR SERVICES

Zacks SCR does not provide investment banking services nor has it received compensation for investment banking services from the issuers of the securities covered in this report or article.
Zacks SCR has received compensation from the issuer directly or from an investor relations consulting firm engaged by the issuer for providing non-investment banking services to this issuer and expects to receive additional compensation for such non-investment banking services provided to this issuer. The non-investment banking services provided to the issuer includes the preparation of this report, investor relations services, investment software, financial database analysis, organization of non-deal road shows, and attendance fees for conferences sponsored or co-sponsored by Zacks SCR. The fees for these services vary on a per-client basis and are subject to the number and types of services contracted. Fees typically range between ten thousand and fifty thousand dollars per annum. Details of fees paid by this issuer are available upon request.

POLICY DISCLOSURES

This report provides an objective valuation of the issuer today and expected valuations of the issuer at various future dates based on applying standard investment valuation methodologies to the revenue and EPS forecasts made by the SCR Analyst of the issuer's business.
SCR Analysts are restricted from holding or trading securities in the issuers that they cover. ZIR and Zacks SCR do not make a market in any security followed by SCR nor do they act as dealers in these securities. Each Zacks SCR Analyst has full discretion over the valuation of the issuer included in this report based on his or her own due diligence. SCR Analysts are paid based on the number of companies they cover. SCR Analyst compensation is not, was not, nor will be, directly or indirectly, related to the specific valuations or views expressed in any report or article.

ADDITIONAL INFORMATION

Additional information is available upon request. Zacks SCR reports and articles are based on data obtained from sources that it believes to be reliable, but are not guaranteed to be accurate nor do they purport to be complete. Because of individual financial or investment objectives and/or financial circumstances, this report or article should not be construed as advice designed to meet the particular investment needs of any investor. Investing involves risk. Any opinions expressed by Zacks SCR Analysts are subject to change without notice. Reports or articles or tweets are not to be construed as an offer or solicitation of an offer to buy or sell the securities herein mentioned.