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Zacks Small-Cap Research

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VIQ Solutions (VQS-NASDAQ)

VQS: Strengthening Key Verticals; Debt Refinancing Alleviates Near-Term Balance Sheet Pressure

VIQ continues to strengthen its four key verticals. For instance, VIQ recently completed the integration of the VIQ Carbon media platform with Sony Ci Media Cloud. The integration enables users to remain within Sony Ci and leverage VIQ's AI-enabled technology and is expected to strengthen VIQ's media offering. VIQ also continues to expand its customer base and solutions in other key verticals, including a recently announced new partnership with a top-10 U.S. insurance company.

Current Price (3/14/23)	$0.30
Valuation	**$3.20**

OUTLOOK

VIQ's focus in 2023 will likely remain on consolidating operations and strengthening its offerings in key verticals, in our view. We expect economic challenges could remain a headwind, but believe the company's ongoing execution of its growth strategy, in success, likely leads to continued new customer wins and operating improvements over time.

SUMMARY DATA

52-Week High	**$1.99**
52-Week Low	**$0.22**
One-Year Return (%)	**-83.1**
Beta	**N/A**
Average Daily Volume (sh)	**174,537**
Shares Outstanding (mil)	**34**
Market Capitalization ($mil)	**$10**
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)
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	12.4A	11.8A	10.7E	46.4 E
2023					49.4 E

Per Share Data

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
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	-0.11A	-0.04A	-0.02E	-0.25E
2023					-0.31E

Quarters might not sum due to rounding & share counts

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KEY POINTS

Positioning platform to benefit from growing need for digitalization, potential market share gains

- VIQ Solutions continues to grow its customer base in its four key verticals organically and via strategic acquisitions, despite near-term economic headwinds. For instance, VIQ recently completed the integration of the VIQ Carbon media platform with Sony Ci Media Cloud. The integration is expected to streamline the media production process and facilitate content creation for the company's media clients within a cyber-secure framework. The integration enables users to remain within Sony Ci and leverage VIQ's AI-enabled technology. It is expected to strengthen VIQ's media offering.

- The company also continues to expand its customer base and solutions in other key verticals. For example, VIQ recently announced a new partnership with a top ten U.S. insurance company to provide recorded claims transcription services. VIQ now works with seven of the top ten U.S. insurance companies, according to management. The company attributes its growth in this vertical to increasing demand among Fortune 500 Insurers, as large insurance companies seek to leverage AI and other automation tools to reduce inefficiencies, improve compliance and expand their bandwidth.

- To strengthen its position and offerings in another key vertical, the Legal / Court space, VIQ entered into a strategic partnership in 2022 with software development company LegalCraft. LegalCraft's flagship product Lexel enables law professionals to collaborate securely to prepare cases for trial. VIQ became the first LegalCraft strategic partner to offer Lexel in the U.S.

- Earlier in 1Q23, VIQ fully refinanced debt that was scheduled to mature in 4Q23. The company obtained a loan for up to US$15 million to refinance all of its existing senior debt and fund near-term working capital and growth initiatives. VIQ has US$3 million available to be drawn under this facility. We view it as a positive that the company has eliminated this balance sheet pressure but note that we believe the possible dilution related to this refinancing (through the potential exercise of warrants) and other recent financings could continue to weigh upon VQS shares until the company announces further milestones in its organic and acquisition-driven growth strategy.

MEDIA OFFERING STRENGTHENED WITH RECENT INTEGRATION

Management expects Media, Corporate & Government vertical to grow …

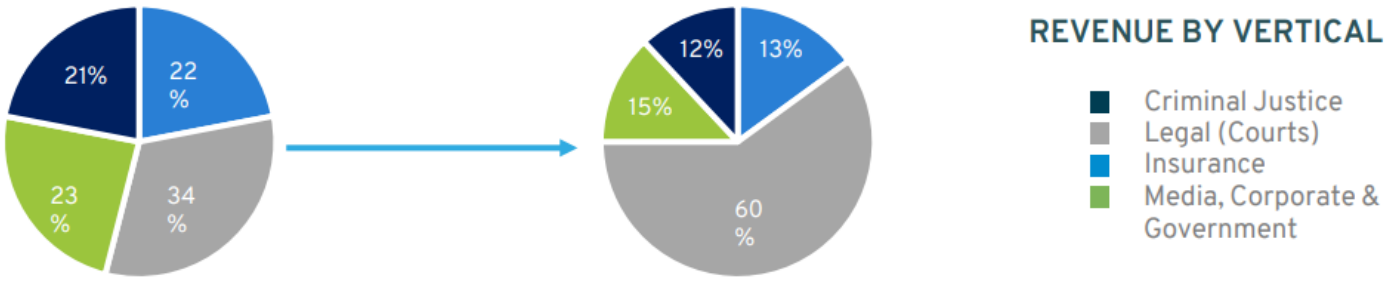
VIQ Solutions (VQS-NASDAQ and VQS-TSX) has more than 4,155 clients across the globe and continues to grow its customer base in its four key verticals organically and via strategic acquisitions. Despite near-term headwinds, including FX challenges and the slowing conversion of new bookings to revenue and executing new contracts, in part reflecting ongoing labor shortages in some markets, VIQ nevertheless continues to expand its client base and expects to accelerate growth and increase its global market penetration over time. For instance, VIQ recently announced a new partnership with a top ten U.S. insurance company (see below) and a multi-year deal with e24 Technologies in India.

We believe the Media, Corporate & Government vertical illustrates the growth potential facing VIQ, as various industries move towards digital data delivery and archiving. The media vertical is a relatively new business for VIQ. The company entered the Media vertical with the 2020 acquisition of ASC Services LLC. The vertical has subsequently become a key focus vertical for VIQ and the company has grown this sector organically and through M&A. For instance, in 3Q22 VIQ entered into an agreement to expand its technology solutions through the purchase of Carbon™, an AI-powered media technology platform. Carbon is a cloud-based media content and text workflow platform. The transaction is expected to accelerate the company's ability to produce captioned video/audio elements using AI-generated text. The

acquisition is consistent with VIQ's goal of advancing its growth strategy and expanding its suite of product and service offerings.

The acquisition of Carbon is expected to strengthen VIQ's Media offering and improve the company's ability to provide real-time solutions to journalists, global media players and other clients. The Carbon technology platform is expected to facilitate revenue growth within the company's media vertical. Overall, VIQ's technical solutions are designed to help customers reduce their costs and turnaround times and improve the accuracy of their transcriptions and content creation.

VIQ Revenue by Vertical, 3Q22 (on right) vs. 3Q21



Source: Company presentation

Positive takeaways of VIQ Carbon & Sony Ci Media Integration …

VIQ recently completed the integration of the VIQ Carbon media platform with Sony Ci Media Cloud. The integration is expected to streamline the media production process and facilitate content creation for the company's media clients within a cyber-secure framework. The integration enables users to remain within Sony Ci and also eliminates redundant steps. VIQ Media customers can leverage VIQ's AI-powered solutions that enable speech-to-text processes, among other capabilities, while remaining inside the Sony Ci platform in a secure cyber-structure. The integration is expected to strengthen VIQ's media offering by managing synched audio and video recordings securely for expedited content creation, while sharing data between Carbon and Sony Ci seamlessly to boost efficiencies and shorten turnaround times of processing projects.

… With integration expected to facilitate market share gains…

The utilization of VIQ's Carbon continues to exceed the company's expectations, according to management, which cites that user growth and production volume have doubled since October 2022. The demand for digitalization of recorded events is expected to continue to grow and the company is optimistic that the integration will enable VIQ Carbon to gain market share as demand continues to grow, particularly given VIQ's focus on providing cyber secure technology solutions.

Continuing to grow Insurance vertical …

The company also continues to expand its customer base and solutions in other key verticals. For example, VIQ recently announced a new partnership with an unnamed top ten U.S. insurance company to provide recorded claims transcription. With this new partnership, VIQ now works with seven of the top ten U.S. insurance companies, according to management. The company attributes its growth in this vertical to increasing demand among Fortune 500 Insurers for strategic solutions to speed and enhance the accuracy of the documentation process, as large insurance companies seek to leverage AI and other automation tools to reduce inefficiencies, improve compliance and expand their bandwidth.
Just as in the media vertical, the company's insurance customers can leverage its speech-to-text tools. The company cites the cyber-secure compliance of its solutions portfolio and ability to scale its offerings

for its growth among the top insurers, as the demand for digitalization of recorded events and evidentiary content creation continues to rise.

… and bolster the Legal vertical through a recent transaction

The above-noted Carbon tuck-in purchase and Sony CI integration follow the company's 2022 strategic partnership with software development company LegalCraft, as VIQ seeks to strengthen its position and offerings in another key vertical, the Legal / Court space. 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. Lexel enables law professionals to collaborate securely to prepare cases for trial. VIQ became the first LegalCraft strategic partner to offer Lexel in the U.S.

The Legal (Courts) vertical continues to represent the company's largest one through the first three quarters of 2022 (contributing 60% of total revenue, as illustrated above). The Criminal Justice (including Law Enforcement) vertical represented 12%, Insurance was 13% and the Media, Corporate and Government vertical added another 15%. The key verticals' respective relative contributions to total revenue can be lumpy on an interim basis reflecting factors such as the timing of court hearings and claims actions and the political advertising cycle, among others.

VALUATION

VIQ has been impacted by extraneous events and general economic uncertainty. For example, court closures – including in its largest market, Australia – constrained revenue in this key vertical during the pandemic. Overall, lockdowns in key markets such as Australia, the U.S. and the UK generally delayed some revenue. Moreover, economic uncertainty has caused some of its customers to shift from large upfront spending on technology to monthly billing arrangements instead. This shift has the benefit of accelerating the company's planned transition toward subscription-based annual recurring revenue (ARR) model but, in the short-term, has led to a shortfall from revenue expectations. In addition, a large contract with the Queensland court system in Australia has proved more difficult to ramp than the company initially expected for several factors, including the general labor shortage that resulted in a shortage of trained and experienced personnel.

Thus, after recording cumulative 4% revenue growth year-to-date through 1H21, the company registered a 1% year-over-year revenue decline in 3Q21. VQS shares fell 39% in the 2+ weeks leading up to VIQ reporting 3Q21 results (compared to relatively flat performance of the NASDAQ) and have remained under pressure subsequently. We believe dilution from capital issuances to finance growth measures and potential balance sheet pressure – VIQ had about $7.8 million of long-term debt at the end of 3Q22 that was scheduled to mature in 4Q23 – have also contributed to share price pressure.

The timing of refinancing the above-noted debt was extremely difficult – with Federal Reserve actions and a rising interest rate environment , but VIQ was able to complete a refinancing. In 1Q23, the company obtained a senior secured loan from Beedie Investments for up to US$15 million. Beedie Investments advanced US$12 million to VIQ as an initial advance, of which about US$9 million was earmarked to refinance all of the company's existing senior debt. The company has also earmarked roughly US$2 million and US$1 million, respectively, for working capital and growth initiatives. An additional US$3 million remains available to be drawn in subsequent minimum US$1 million tranches. If Beedie exercised all roughly 8 million warrants associated with the loan (the warrants expire on January 16, 2030), Beedie would hold a greater than 18% stake in VIQ.

Reflecting the above pressures, VIQ shares trade at a significant discount to peers in the cloud-based technology space based on our 2022-2023 revenue forecasts. We expect the multiple gap to narrow as the company continues to make strides in its organic and acquisition-driven growth strategy. The

company expects its growing customer relationships and ongoing transition to a monthly recurring revenue model to lead to improved revenue and margins over time and to help smooth out lumpiness in monthly and annual revenue flows.

We also note that sector multiples have declined amid market volatility and economic uncertainty. On average, multiples of other cloud-based tech companies have declined to under 4x forward revenue, down from well over 6x pre-pandemic. We are revising our valuation to reflect this and the potential impact of recent funding measures. Our valuation of $3.20 equates to under 3x our newly introduced 2023E revenue estimate, even if Beedie fully exercises its warrants (we have not factored the full exercise of these warrants into our 2023 model). This multiple is well below the group average.

It would not surprise us if management issues guidance above our 2023 revenue forecast, which incorporates the potential headwinds of VIQ's customers slowing and delaying projects, given economic uncertainty and the rising interest rate environment. Our forecast also does not take into consideration additional possible M&A tuck-in transactions. Although we expect VIQ to focus on consolidating and strengthening its existing operations near-term, if an attractive tuck-in opportunity came along, we would expect the company to consider it. Our 2023 forecast also mirrors continued potential upward pressure on labor costs.

RECENT NEWS

- On February 28, 2023, VIQ announced a new partnership with a top-ten U.S. insurance company.
- VIQ implemented the integration of Carbon with Sony Ci on February 22, 2023.
- VIQ announced a new multi-year deal with e24 Technologies in India on February 8, 2023.
- On January 17, 2023, VIQ announced the new US$15 million Beedie credit facility.
- VIQ announced 3Q22 results on November 10, 2022.
- VQS shares began trading on the Nasdaq on August 12, 2021.

RISKS

We believe risks include those outlined below, among others.

- The impact of the economy on VIQ's business could linger longer or be greater 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 additional capital to support growth initiatives.

PROJECTED INCOME STATEMENT

VIQ Solutions Inc. Income Statement & Projections ($)

	2018	2019	2020	2021A	Mar-22A	Jun-22A	Sep-22A	Dec-22E	2022E	2023E
Revenue	$11,462,804	$25,096,308	$31,749,693	$31,046,812	$11,524,981	$12,351,655	$11,785,713	$10,724,999	$46,387,348	$49,402,525
Cost of sales	7,874,219	14,276,321	15,599,437	16,123,853	6,035,932	6,257,453	6,208,528	5,630,624	24,132,537	25,936,326
Gross profit	3,588,585	10,819,987	16,150,256	14,922,959	5,489,049	6,094,202	5,577,185	5,094,374	22,254,810	23,466,200
Gross margin	31.3%	43.1%	50.9%	48.1%	47.6%	49.3%	47.3%	47.5%	48.0%	47.5%
Selling & administrative expenses	5,533,724	8,954,512	11,034,902	19,119,713	6,136,309	6,532,440	5,960,010	6,073,731	24,702,490	25,567,077
Research & development expenses	458,675	994,640	1,074,178	1,092,108	199,085	278,357	164,849	193,172	835,463	864,704
Stock-based compensation	(31,461)	195,113	725,316	8,495,189	952,196	540,580	681,193	800,000	2,973,969	3,003,709
FX & other	198,180	217,040	(132,306)	(1,248,520)	(623,940)	(7,489)	(288,578)	(642,846)	(1,562,853)	(1,594,110)
Depreciation & amortization	648,873	3,502,429	5,259,243	4,641,601	1,159,344	1,219,637	1,272,637	1,279,000	4,930,618	5,103,190
Total operating expenses	6,994,435	12,295,345	17,961,333	32,100,091	7,822,994	8,563,525	7,790,111	7,703,057	31,879,687	32,944,570
Operating income	(3,405,850)	(1,475,358)	(1,811,077)	(17,177,132)	(2,333,945)	(2,469,323)	(2,212,926)	(2,608,683)	(9,624,877)	(9,478,370)
Interest expense	(96,484)	(1,549,904)	(4,934,517)	(1,331,100)	(339,713)	(241,128)	(234,892)	(340,223)	(1,155,956)	(1,204,506)
Other	(2,552,729)	(1,399,781)	(5,343,744)	(226,790)	615,045	(35,583)	1,094,007	1,098,383	2,771,852	277,185
Total operating inc / (expenses)	(2,649,213)	(2,949,685)	(10,278,261)	(1,557,890)	275,332	(276,711)	859,115	758,160	1,615,896	(927,321)
Pretax income	(6,055,063)	(4,425,043)	(12,089,338)	(18,735,022)	(2,058,613)	(2,746,034)	(1,353,811)	(1,850,522)	(8,008,980)	(10,405,691)
Tax	(11,571)	(99,155)	944,032	(943,727)	(48,696)	37,699	(23,871)	(200,000)	(234,868)	(312,171)
Net inc/ (loss)	(6,066,634)	(4,524,198)	(11,145,306)	(19,678,749)	(2,009,917)	(2,783,733)	(1,329,940)	(1,650,522)	(7,774,112)	(10,093,520)
FX	(95,899)	(262,811)	56,152	153,432	412,798	(489,803)	(823,213)	100,000	(800,218)	(184,050)
Per share data:										
Comprehensive loss	(6,162,533)	(4,787,009)	(11,089,154)	(19,525,317)	(1,597,119)	(3,273,536)	(2,153,153)	(1,550,522)	(8,574,330)	(10,277,570)
LPS	($0.04)	($0.49)	($0.62)	($0.74)	($0.07)	($0.11)	($0.04)	($0.02)	($0.25)	($0.31)
Avg shares out	161,816,064	9,251,546	18,080,533	26,448,594	29,881,717	28,653,056	32,749,800	32,754,800	31,009,843	33,054,800

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

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