Business Update and FY2022 Outlook Conference Call Transcript

Melbourne, Australia; 18 January 2022: Redbubble Limited (ASX: RBL)

The transcript of the Business Update and FY2022 Outlook conference call on 18 January 2022 is attached.

For further information, please contact:
Louise Lambeth
Head of Investor Relations
louise.lambeth@redbubble.com

This announcement was authorised for release to the ASX by the Redbubble Limited Board Chair.

Operator: Thank you for standing by and welcome to the Redbubble Limited business and FY2022 Outlook Update. All participants are in a listen only mode. There will be a presentation followed by a question-and-answer session. If you wish to ask a question, you will need to press the star key followed by the number one on your telephone keypad. I would now like to hand the conference over to Ms Louise Lambeth, Head of Investor Relations. Please go ahead.

Louise Lambeth: Thank you. Good morning everyone here in Australia and good afternoon and evening for our US investors. This is Louise Lambeth, Head of Investor Relations for Redbubble Group. Welcome to this investor call following the release of a business update provided earlier today. With me on the line, I have Redbubble's CEO, Michael Ilczynski and CFO, Emma Clark. The key information for today's update is contained in the ASX announcement provided earlier today. Please note that the preliminary financial results and strategic and operational metrics are from internal management reports and have not been subject to audit reviews.

Mike and Emma will speak shortly and we will then open up the lines for questions. This session is also being recorded. Before we start, I would like to call your attention to the safe harbour statement regarding forward-looking information in our ASX release. That safe harbour statement also applies to this investor call. I will now pass onto Mike.

Michael Ilczynski: Thank you Louise, good morning or good afternoon to everyone. Thank you all for taking the time to attend this session. Redbubble Group released the trading updates to the market earlier today in accordance with the Company's ASX continuous disclosure obligations. We would like to take this opportunity to provide some additional context and answer any questions you may have.

I'll be providing a summary of what we experienced over the peak holiday period and in the second quarter, walk through how we responded to the trading environment, the impact on the business and why we are updating our FY22 outlook. I will then pass to Emma who will discuss the preliminary financial and revised outlook in more detail. Finally, I will outline the strategic and investment decisions that we are making in the business before opening the lines up for Q&A.

First half underlying marketplace revenue, which excludes masks and is on a paid basis of $283 million, down 5% year on year on both a floating and constant currency basis. The underlying revenue performance in the second quarter was just below our expectations which overall we were pleased with, given we experienced strong competition for customers during the second quarter and this was particularly felt through the peak holiday period.

The increased competition impacted both organic unpaid demand, mainly the acquisition of new customers through unpaid channels, as well as our paid marketing acquisition costs. The increased caps continued what we saw in Q1 as the impact of IOS 14 and the IDFA changes resulted in increased, broad based, less targeted spend across the marketing landscape. This spend came from both online and more traditional offline retailers and was predominantly

large names with strong established brands. Many of these companies invested heavily in both brand and acquisition spend both on and offline during the period.

We responded to these changes in the landscape by increasing our promotional activities in total paid acquisition spend. These actions across both businesses, Redbubble and TeePublic, positively impacted our revenue result but at a lower contribution margin. This, in combination with our decision to absorb increased shipping costs over the holiday period, impacted gross profit and GPAPA, which is gross profit after paid acquisition, margin and this flowed through to the bottom line, resulting in lower EBITDA in the quarter and the half.

Despite our performance at the GPAPA level not being where we'd hoped, I was really pleased with how the teams reacted to a pretty challenging period. From a revenue perspective, the half for the group is still up 60% on two years ago, the last pre-COVID half the business had. There are a number of real positives in the half that I will speak to later that reinforce the potential for the business and the work we need to do to capitalise on this potential.

Given this opportunity and our significant cash balance, in the second half we will be continuing to invest in our technology platforms in particular to enable future growth. Due to the combination of the first half result, our revised revenue outlook at our decision to continue investing in second half, we are updating our FY22 outlook across both marketplace revenue and EBITDA.

I'll now pass on to Redbubble Group CFO, Emma Clark. Emma.

Emma Clark: Thanks Mike and hello to everyone. Please be aware that unless otherwise stated, the financial results discussed are on a delivered basis, however are preliminary and have not yet been subject to audit review. I will quote growth rates on both a floating and constant currency basis as I normally do, however this may sound a little repetitive as FX ultimately has had minimal impact on the half year numbers and so therefore the rates are almost the same.

In the first half of financial year 2022, Redbubble will report gross transaction value of $381 million. Year on year this was down 14% and also 14% on a constant currency basis. However, compared to two years ago, GTV has grown 64%. First half reported marketplace revenue is expected to be $288 million, down 18% year on year and also 18% on a constant currency basis. Excluding masks and on a paid basis, which is how we disclose underlying numbers, marketplace revenue will be $283 million, down 5% versus prior year.

As we have flagged in previous outlook statements, we had expected that first half revenue growth would likely be negative due to the cycling of strong prior-year numbers which were driven by COVID-related lockdowns and mask sales. We did see strengths in the largest geographic and product category, being North American apparel sales, which represents over 40% of total sales on the platform and this geographic and product category grew 10% in the second quarter and 7% in the first half. However, this was offset by weaker year on year performance in categories such as European homewares, which were down 25% in the first half. Compared to two years ago, marketplace revenue has grown 60%.

The second quarter's revenue profile did differ from previous years, with some holiday spend being pulled forward into October as customers responded to media reports of potential supply chain constraints and shipping delays. The

Thanksgiving period was weaker than expected, with a portion of this weakness offset by longer last-order-by dates which effectively extended the peak sales season. However, the reported revenue numbers came at a higher than anticipated cost on both the gross margin and paid acquisition lines.

In the first half, Redbubble is expecting gross profit of $108 million, down 25% year on year and 25% on a constant currency basis. Gross margin came in at 37.5% for the half and 36.1% for the second quarter. Whilst product mix, manifesting as a combination of lower mask, higher apparel and lower homewares and artwork sales, acted as a slight headwind to margin, the main drivers were increased shipping costs that were not passed on to customers and the extension of promotional activities over the quarter.

Whilst we are not anticipating running increased promotional activity through the second half, we do anticipate that shipping costs will continue to be a headwind to margin and together with uncertainty over the overall inflationary environment in the near term, we anticipate overall margin to be closer to 38% than 40%. On a two-year basis, gross profit has still grown substantially and was up 63% for the half. Further down the income statement, we have continued to see higher paid acquisition costs and this will be 15.5% for the half after remaining elevated at 16.1% in the second quarter.

Entering into the holidays, we had expected the challenging digital marketing environment to continue as the entire industry continued to adapt to the IDFA privacy changes. Even so, this is higher than what we were expecting and as Mike mentioned earlier, was driven by stronger competition from both online and offline brands. That being said, even at these levels of paid acquisition spend, the business still maintains positive unit economics and each dollar of revenue is on average a positive contribution towards GPAPA.

Unfortunately at the Group’s current revenue scale and with an expected EBITDA margin in the mid-single digits, a 2% reduction on margin and a 3% increase in paid acquisition costs will result in EBITDA generation falling by the same amount. On a preliminary basis, the first half EBITDA is expected to be $8 million, compared to $48.8 million in the first half of last financial year and $4.3 million in the first half two years ago. EBITDA margin for the first half will therefore be 2.8%.

Finally, we recorded a total of $143 million in cash at the end of December, providing the business with a strong balance sheet. This represents an all-time high and whilst some of this will be paid out to artists and to sellers over the current quarter, the business will still be holding a significant amount of cash providing continuing strategic flexibility, including the funding of near-term growth investments.

Looking ahead, Redbubble expects financial year 2022 marketplace revenue to be slightly below financial year 2021 underlying marketplace revenue of $497 million. This will still represent solid growth on the $350 million achieved in financial year 2020. We remain committed to our mid-term aspirations and the investments that will be required to deliver on our growth objectives. As such, in the second half we will be continuing to invest into the business which will increase our operation expense runway. We will be funding these investments out of our existing cash reserves.

The combination of the decreased first-half EBITDA, continuing headwinds on shipping costs and customer acquisition costs and increased operating expense investments, the EBITDA margin as a percentage of marketplace revenue is now expected to be negative low single digits for the current financial year, with the margin expected to expand over the medium term in line with top line growth.

I will now pass back to Mike.

Michael Ilczynski: Thanks Emma. It's important to emphasise that we remain committed to our mission to create the world's largest marketplace for independent artists. The Redbubble Group is uniquely positioned to capitalise on its medium to longer-term growth potential and emerge as a significant company in what are very large and growing addressable markets. When we spoke in October last year, we had flagged that while there are definitely many uncertainties ahead, as our various markets moved towards a post-COVID normal, the early data points we saw gave us confidence for our business over the medium to longer term.

My confidence of the tremendous upside potential remains unchanged and I'm confident in the strategy that the business has embarked on. Viewed across the longer term, as I said, first half marketplace revenue has grown 60% since first half FY20 or 68% on a constant currency basis. The business is now substantially larger and we are working towards furthering our scale to build resilience and improve profitability.

While the first half had some challenges, as Emma mentioned, the fact that we saw year-on-year growth in North American apparel, our largest product geo segment, gives us confidence that we are going to stabilise and trend back to ongoing growth. We were encouraged to see an increase in our repeat base, with 45% of first-half marketplace revenue coming from repeat customers, up from 40% in the first half last year. We've talked before about the importance of increasing loyalty and repeat rates and of driving customers to become members. We saw in the second quarter a good uplift in both membership sign-up rates and the per cent of marketplace revenue generated from members versus a year ago.

We also saw mobile apps, again an area we've flagged that we would focus on growing, increase to 14.3% of Redbubble's marketplace revenue in the second quarter versus 12.6% in the second quarter last year. From an operations perspective, our supply chain logistics and customer service teams saw significant improvements in last-order-by dates, on-time delivery percentages and customer satisfaction relative to last year. We will expand on these highlights at our full half-year update in February. These highlights reinforce the strategy that we have is right; we need to continue with it, with a focus on customer engagement, retention and loyalty.

Looking to the medium to longer term, we remain confident of the business's unit economics. Every dollar of revenue, whether from organic or paid channels, is contribution margin positive, emphasising that by investing to grow to drive scale, we will drive improving levels of profitability from this scale and the operating leverage inherent in the business model. The Company is well capitalised with a strong cash balance of $143 million at the half, an all-time high and we will be continuing to fund near-term investments from these cash reserves to expand capabilities and capacity across the Group. These resources will focus on improving our technology platform, the artist and customer experience and our brand in order to enable this future growth.

So there's a clear and well-defined strategy with multiple growth levers and given our strong cash balance, our decision to continue investment reflects the upside potential that can be unlocked by pursuing this opportunity. Across the Group, teams will continue targeting initiatives that will expand the scale of the business towards our medium-term aspirations, which remain unchanged, to grow GTV to more than $1.5 billion, to grow artist revenue to over $250 million and to produce marketplace revenue of $1.25 billion per annum. With that, EBITDA margins will expand over the medium term with this top line growth.

With that, we'll now open up the lines for questions.

Operator: Thank you. If you wish to ask a question, please press star one on your telephone and wait for your name to be announced. If you wish to cancel your request, please press star two. If you are on a speakerphone, please pick up the handset to ask your question. Your first question comes from Aryan Norozi from Barrenjoey. Please go ahead.

Aryan Norozi: (Barrenjoey, Analyst) Hi guys, hope you're well. Just the first one from me, just around your medium to long-term aspirations, you've obviously reiterated the top line piece, but just around your margins EBITDA, you've previously quantified it at 13% to 18%, this time it's qualitative. Can I just confirm that there's no change around that 13% to 18% way you're thinking in that or is it a new change in thinking in your business please?

Emma Clark: We confirm no change to those EBITDA margins at that level of top line scale.

Aryan Norozi: (Barrenjoey, Analyst) Perfect and just in terms of the marketing costs, so it's about 10.5% in the second quarter. If I was to break it down in terms of one-off or recurring versus non-recurring, how do I think about that and where should I put that generally delivered over the next 12-18 months as the market digests these IDFA changes please?

Emma Clark: Yes, look I think it's probably fair, Aryan, it's not necessarily one off. I mean obviously as we came out in October and we talked about the experimentation we had been doing as part of our response to those IDFA changes, they were one off in nature. What we really saw in the second quarter was just a massive increase in competition which drove CACs up. Now in looking at and obviously coming out today, we've also looked at what's happened in January and month-to-date as well, can say that those CACs come back down after the peak holiday season.

But it just highlights to us that it is a continuing volatile environment, it's very hard to predict and so prudently we would say that there will continue to be volatility in that over the remainder of the half and so therefore there will be periods potentially of stronger competition and periods of weaker competition. So we've effectively thought that there will probably be – previously we'd said it was 12.5%, around 12%, it's clearly going to most likely be higher than that for the half and hence some of the reason behind the change to our guidance.

Aryan Norozi: (Barrenjoey, Analyst) Perfect. The gross margins, the 38% you flagged, are you talking in that second half?

Emma Clark: Yes, pretty much for the second half and the year. As you can see, the first half was 37.5% anyway, so what we're effectively flagging is that what we've seen in the last half is likely to see something in the second half, but depends on shipping margin.

Aryan Norozi: (Barrenjoey, Analyst) Okay and within that gross margin, were there any pressure points around rising input costs, like costs and prices which are more flagged in the industry, has there been any change embedded in the results from that?

Emma Clark: Yes, it's a really good question and I know it's obviously an area of focus for everybody because there's so much media on it at the moment. As we discussed in the October update, we had a couple of the sellers come to us, only three or four out of obviously quite a large number and request some price increases, but nothing further than that. That remains the case. We would expect that there will be continuing pressure on prices as we go through the second half, both from, as you say, an input perspective but also a labour perspective. We will monitor those as they come in and decide at the time how much of that can be passed through to customers versus how much of that is absorbed by the business.

Aryan Norozi: (Barrenjoey, Analyst) So is the guidance that you've made for the full year, is that factoring in input costs pressure or is that just factoring in a continuation of freight costs being elevated and promotion intensities being high but easing off, off Christmas?

Emma Clark: Yes, largely the latter two, but what I would say is based on where we sit with our supply chain at the moment, it also does incorporate our views on overall inflationary pressures within the margin line, so the 38% is total margin, not just the shipping component of it, if that makes sense.

Aryan Norozi: (Barrenjoey, Analyst) So it incorporates the rising import costs as well as the…

Emma Clark: Yes, what we would expect to see in terms of rising import costs at the moment and what we would expect to do with rising import costs.

Aryan Norozi: (Barrenjoey, Analyst) Yes, perfect. If I can squeeze one more in, please, so just around the hiring. Can you give us an update around how many heads you've hired so far, how many more you need to do for the rest of the year and just a headcount circa please?

Michael Ilczynski: We'll talk about the exact, the more specific numbers at the full half-year results. What we had when we spoke in October, I think like a lot of organisations, hiring hadn't come along as fast as we hoped, particularly in the first quarter and that has impacted, while it had a positive impact on OpEx, it impacted our ability to make changes. As we move into the second half, we're revamping a little bit our employee mix, so we'll add an additional – we'll add some contractors, our hiring is coming along better, so that's why we're, in some ways, we're probably more confident in our employee position, but also in the OpEx ramp in the second half.

Aryan Norozi: (Barrenjoey, Analyst) That's perfect, thanks guys.

Operator: Thank you. The next question comes from Anna Guan from Goldman Sachs. Please go ahead.

Anna Guan: (Goldman Sachs, Analyst) Morning guys, thanks for taking my questions. Just a couple of follow-ups from the earlier comments and previous questions, just firstly, Emma, in your opening commentary you mentioned something around extended peak selling season, particularly off the back of Thanksgiving. I think I only caught part of it. Can you just help me understand that a little bit more please?

Emma Clark: Of course, not a problem, Anna. So what I said was that the actual Thanksgiving peak season, which is normally that four or five days across the Thanksgiving weekend, was weaker than we had expected and some of that weakness was offset by the fact that this year we had extended last-order-by dates. So if you'll recall, going back 12 months to holiday season the year prior, there was a lot of challenges with the ability to ship products at that time. Some of the shipping carriers had put in caps, we had to run really early last-order-by dates, which compressed that particular holiday season.

We knew coming into this particular holiday season that those conditions didn't exist. Whilst there's still uncertainty around COVID and there's some COVID impacts, the shipping carriers had not put on caps and we had made some improvements in our systems that meant we could also run longer last-order-by dates. So instead of closing off, say, the first week of December, we were able to close off a lot in the second week of December. So what that did was that gave the customer shopping on the platform those extra days to be able to continue doing their Christmas shopping and know that they would get their thing before Christmas.

Anna Guan: (Goldman Sachs, Analyst) Yes, okay, understood. So net-net really is more of a mutual impact from a top line point of view.

Emma Clark: Slightly down, I would actually say, Anna, to be honest. The weakness across those sort of four or five days is only partially offset by the extension to last-order-by dates, not fully. I mean obviously we're talking primarily about changes due to gross profit margin and paid acquisition costs, but want to be very clear that revenue is slightly below what we would have ideally like to have seen for the quarter as well.

Anna Guan: (Goldman Sachs, Analyst) Yes, got you. Then my second question is just around shipping. Obviously you guys called out that as one of the two factors driving the slightly lower margins. Are you guys able to quantify that?

Emma Clark: Not as specifically, sorry Anna. We don't disclose shipping margins separate to product margin, that's considered to be commercially sensitive, which is why I reiterated that the overall margin is going to be closer to 38% than 40% so that you guys can encapsulate that impact without me having to disclose detail that we shouldn't disclose.

Anna Guan: (Goldman Sachs, Analyst) Yes, no that makes sense. Just lastly…

Michael Ilczynski: Sorry Anna, it's probably worth just adding because it goes to import decision, is with the shipping margin, when we saw those increased shipping costs, it was a deliberate decision by us not to pass those through to customers. We had flagged, we had talked about it both in our August results and in our October results, that our medium-term objective is to decrease shipping margin. We know that lower shipping costs to customers helps with conversion and particularly helps with repeat rate. That was a decision that we made as we were flowing through.

Anna Guan: (Goldman Sachs, Analyst) Yes, that makes sense. Just lastly and I think you kind of answered part of the question, but I just want to get a summary comment from you guys, I'm just trying to understand what changed in the implied second half 2022 guidance versus, I suppose the previous guidance. Because obviously you mentioned earlier, you are pretty much assuming the lower cap to partly continue throughout the rest of the year, and also would just need to continue into the second half. Is there anything else that's changed in that in the prior second half, or is this a previous update you guys see that?

Emma Clark: Yes, so the last, so you've captured correctly, other than CAC, we're assuming continues at a somewhat inflated rate, albeit not as aggressive as what we saw through the second quarter for the rest of the next half. The one missing piece is that revenue is slightly down. So the prior guidance said that revenue would be slightly above the prior year's underlying revenue. We've obviously changed that guidance to be slightly below prior year's underlying revenue. So there is a decrease to revenue, a small decrease to revenue.

Anna Guan: (Goldman Sachs, Analyst) Yes, and just the operating leverage that comes with it?

Emma Clark: Absolutely.

Anna Guan: (Goldman Sachs, Analyst) Okay, excellent, thanks very much guys.

Operator: Thank you. The next question comes is from Tim Piper from UBS. Please go ahead.

Tim Piper: (UBS, Analyst): Oh, morning team, thanks. I'll just ask a couple of questions and then jump back in the queue. Just firstly around the fulfiller network. We're obviously hearing some commentary from US companies around labour shortages disrupting distribution centres, et cetera. Is it fair to assume that the print-on-demand industry largely dodged that bullet in that seasonal demands sort of peak through November/December? Or are you starting to hear some of the fulfillers come up against capacity constraints now due to labour?

Michael Ilczynski: Yes, thanks Tim, your summary is correct that most of the fulfillers in the network were able to navigate through the holiday period quite well. Which is why we talked about being able to extend those last order-by dates. The model works better. Obviously now is a relatively lower period traditionally as we come off the seasonal high. So those who are having some labour challenges, there's obviously less demand at least coming from the likes of us. So yes, your summary is right that in general the network has avoided some of those pressures.

Tim Piper: (UBS, Analyst): So you're not seeing anything that could be a head wind right now?

Michael Ilczynski: Look, not at the moment. I mean it's pretty uncertain. We've got to be clear, it's pretty uncertain. But no, right now the network's in reasonable shape.

Tim Piper: (UBS, Analyst): Okay, great. Just a second one on I guess the quarterly run rate of revenue through the second quarter. You called out organic demand. Then maybe a slightly lower than anticipated sort of Christmas and November/December. Are you confident that that has been a bit of a one-off in terms of pull forward? The exit run rate in this quarter going into the second half, I mean is that captured in your lower guidance on the revenue line?

Have you seen enough trading now to be confident that it was just a pull forward, and not so much a drop-off in demand?

Emma Clark: Yes, Tim, and as we said before, in coming out today we obviously have not just looked at the half and that quarter, we have also looked at the first two weeks of January. So in terms of all of our guidance updates, they actually incorporate what we're seeing so far for half a month in January as well. So in terms of the changed profile within the quarter, which I obviously called out previously, that is quite different to prior years. As I said, we believe it's driven by obviously all of the media attention and the supply chain concerns.

So I would categorise that more as a one-off. But what it does highlight to us as a business is just the predictability of prior patterns at any point in time is not necessarily there at the moment. I know we came out in October and said we were seeing a return to more normalised patterns. The holiday quarter actually had quite a different profile because of all these macro events. So therefore it just underscored to us that there is just that continuing unpredictability in the, in sort of the shape of sales over a year at the moment.

Tim Piper: (UBS, Analyst): Okay, got it. Just one last one on your product mix. You called out a couple of categories there, like apparel, strong apparel growth in the US, and a decline in I think it was homewares in Europe. I mean are you typically seeing this as economies reopen, is it, is that what's driving it? The product mix changes that you're seeing, how much impact has that had on your gross margins set down quarter-on-quarter?

Michael Ilczynski: Yes, thanks, Emma can probably comment on the gross margin. It’s had a little bit of an impact. Masks were really high margin, clothing is a little bit lower. So it's had a little bit of an impact, but not much. But I think your broader point that what we saw, if we go back a year ago, we had some really COVID winners. So we saw that homewares, wall art, they really took off. They grew way over 100% year-on-year. Then obviously now, but - and apparel was okay, but not as strong as those were a year ago.

We get to now and, as we said, we see our more traditional areas, which is, apparel has been one of the core areas for Redbubble and TeePublic through its history, actually growing quite strongly. But those areas that really took off during COVID, like homewares and wall art and masks, have come right back down. They're still quite a bit up on where they were two years' ago, but definitely they’ve come back down. Which to be honest, that’s the pattern that we expected would occur through this time. The positives of having that diversified product portfolio has really, has helped us overall, and continues to be something that we'll add to.

When we come out in February we'll have the full breakdowns like we normally do for each product set. So that will come out in February as normal.

Emma Clark: Yes, I think what we're simply flagging here is, in terms of changing our guidance we already had expected that product mix to swing in our prior guidance. So it's not necessarily a divergent factor in terms of updating guidance today. So therefore the impact of it in terms of what we're actually saying that’s different is minimal.

Tim Piper: (UBS, Analyst): Okay, understood. Thanks for taking the questions.

Operator: Thank you. The next question is from Owen Humphries from Canaccord. Please go ahead.

Owen Humphries: (Canaccord, Analyst) G'day guys. A couple of quick ones from me just around the artist margin. I just noticed in that second quarter picking up to almost 31%, which is record highs. Can you just talk me through the dynamics behind that?

Emma Clark: We'd have to look at how you've calculated that, Owen, because we don't, the numbers I've got in front of me don't show such a big swing in the artist margin. You've got to keep in mind the bridge between gross transactional value and marketplace revenue also incorporates taxes. So there's be movement in tax as well. So obviously when we go through the full half at February we'll provide all of that breakdown so that you can calculate all of those percentages. But I would say that your - that's not what's happened. There's not been a big increase in artist margin in the quarter.

Owen Humphries: (Canaccord, Analyst) Okay, I'll go back and have a look. Then just around the GPAPA margins. Obviously your historical range has been around that 25% to 27%, that's kind of the target. Obviously a low point at the moment, and you explained that. Just understanding what your views are over the medium-term around that target range?

Michael Ilczynski: Yes, thanks Owen. Look, we definitely expect those GPAPA margins to come back up for two things. (1) We scale, we know that scale helps out traditionally. (2) With the work that we can do to improve gross margins, working with the fulfilment network as we scale to reduce input cost, working to reduce, to improve our shipping costs. We talk a lot about shipping margin, but the other way to attack that area is to actually reduce our shipping cost through better routing, through different arrangements with the logistics providers, et cetera.

So we have a really - you've talked about investing in our technology platform. One of the areas that we will and are investing in is our supply chain and logistics network so that we can more proactively drive that gross margin. Gross margin is such a huge driver of the business, every percentage point that we can proactively improve there goes straight through to the bottom line. So that's a big focus for us.

Then thirdly, on our marketing spend, as you know, all of our marketing spend at the moment is paid acquisition. We've talked about moving forward we do want to start investing in our brand. That will add to that in the short-term, but at the same time we really believe that in the medium-term that's going to actually reduce our reliance on paid acquisition. We think it's really important that over the medium-term we build our brand so that we can increase our organic customers. Increase the percent of customers coming through organic channels, because they know our brand. Because they love the proposition of Redbubble and TeePublic. That will reduce our reliance on our paid channels.

So we still remain when we look at our models and our plans, we still remain really confident and committed in those medium-term EBITDA margins which require our GPAPA margin to be, and frankly to be better, a lot better than where it was this half.

Emma Clark: Yes, I would just add a couple of points to this. So one is that year of where we had the sudden growth because of COVID actually demonstrated that. So we have actually, we've demonstrated that step-up the top line, hold everything stable for a period of time and this thing throws off EBITDA very quickly.

We have been very clear that we’re going into an investment phase at the moment, and we're in one. So therefore the challenge is that at our current scale is, it only takes small movements, as I highlighted, on gross margin and paid acquisition and they flow straight through to a relatively low EBITDA margin. But none of that actually, if we were to hypothetically have another $200 million on the top line, and being at more like $700 million, those unit economics come back really quickly. So we're very confident in our ability to deliver that over that medium-term.

Owen Humphries: (Canaccord, Analyst) Good one, thanks. Just on the OpEx base of $32 million for the quarter, I know the second quarter is normally a bit higher than the other quarters. But it sounds like you're still hiring. Is that the new base now between that $32 million to $35 million per quarter?

Emma Clark: Obviously not giving precise forecast at that level of detail, Owen. But I would think historically, as you yourself point out, that second quarter does tend to be slightly higher than all of the other quarters. I would expect even in an investment environment for that to be the case, there still to be a little bit of seasonality in it. So I expect it to step back slightly off that.

Owen Humphries: (Canaccord, Analyst) Good one. Just a last quick question from me. $143 million of cash on hand, so very well capitalised. You’ve put the business now into kind of just slightly negative EBITDA for this year. What's the Board and your views I guess around EBITDA profitability over the next couple of years?

Michael Ilczynski: Sorry, I was mute again, I hit on the wrong button. Apologies Owen. I think in terms of our EBITDA margin and our cash balance, the Board, myself, the Management Team of both businesses, we're really aligned on the potential for the business. That cash balance gives us tremendous strategic flexibility primarily to invest in ourself. To primarily to invest in our platforms, in our capability, and in our brand. To go after that scale that Emma talked about.

It's really clear the operating leverage in this business, we saw it on the upswing last year, and unfortunately you see it, you see if we miss slightly on revenue with a couple of other hits, you see the reverse. So we know the operating leverage in the business. Our job is to drive that scale. So our number one focus is to invest in the business. We've got that big, we've got a really good cash reserve that enables us to invest in the business to go after that scale.

Then obviously beyond that the cash balance does give us more strategic flexibility beyond just investing in ourselves. Whether that’s potential M&A or other activities. But our number one focus is to drive, is to invest and drive scale over the medium-term.

Owen Humphries: (Canaccord, Analyst) Good one, thanks guys.

Operator: Thank you. The next question comes from Paul Mason from E&P. Please go ahead.

Paul Mason: (E&P, Analyst) Hey guys. A bunch of mine have been asked. So I've just got one which is, in terms of the cash balance and the growth versus the EBITDA, it sort of sounds like basically the main source of that is probably a build-up in payables to your artists or to other suppliers. Was there anything else that's sort of helped that along besides the $8 million of EBITDA and then sort of maybe delayed payouts to suppliers? Or is that basically an explanation for the build-up?

Emma Clark: Yes, so, hey, Paul, we always see a seasonal build-up in cash at 31 December. In terms of any 12 month period it's usually our highest point of cash. Because as you can imagine, we have obviously received the increased flow of customer sales on the platform for November and December, but haven't yet paid out all of the suppliers. That generally happens in January. So it comes down, so we always have a cash out-flow obviously in Q3 as a result of that.

I think the point that we made when we were talking earlier on the call was that, we know obviously about these seasonal trends. They're actually quite predictable. You can look back at our prior year cash balances to see how it normally moves. But we're obviously going to have still a substantial amount of cash post all of those payouts. It probably settles back down somewhere between the range of $100 million and $110 million. So that’s obviously still quite a decent cash balance, and gives us that continued strategic flexibility to invest as we need to.

Paul Mason: (E&P, Analyst) Yes, great, thank you.

Operator: Thank you. The next question is from Joseph Michael from Morgan Stanley. Please go ahead.

Joseph Michael: (Morgan Stanley, Analyst) Good morning guys, thanks for your time this morning. Just a couple from me. So firstly just on the medium-term targets, so just to clarify. Previously you had the comment in there that you can grow marketplace revenue at a CAGR of 20% to 30%. Is that still part of the guidance?

Michael Ilczynski: Oh, hi Joe. Look, absolutely, that’s our goal over the medium-term for this business to be growing at 20% / 30%. We generally believe that that’s possible between the markets that we're playing in and the growth that we think that our sector is going to achieve, and the growth that we believe we can drive ourselves. I think it's really important, that’s not going to be linear. That’s, you know that that’s not the way that these things work.

What we're really clear on is where we need to invest over these next couple of years in order to go after and get to that growth. As we said, we can see the green shoots of our strategy in terms of the need to focus on investing in our brands. We need to focus on driving members, we need to focus on our apps, we need to focus on repeat rates, loyalty, customer retention, et cetera.

So yes, so we absolutely believe that that sort of growth over a medium-term is possible. That’s the growth that we saw in the business pre-COVID. Obviously off a smaller scale. That’s the growth that we believe we can achieve once we get back to some, to restabilising our product lines, put in investment we need to, and start seeing the investment we're making actually show up for artists and customers.

Joseph Michael: (Morgan Stanley, Analyst) Okay, great. Then the next question I had was just around CACs, and I know we've sort of talked about this quite a bit. But just trying to understand, is this a sort of structural issue with

performance marketing? Is it, is the cost of acquiring customers just going to be, continue going up? Is that sort of lack of visibility going to remain? Or do you sort of see this as more of a one-off issue, and at some point everything recalibrates and kind of rebases?

Michael Ilczynski: Yes, look, to be honest, it's a really critical question. I think for us to say that we know exactly when this plays out would be wrong. So we think that this uncertainty that’s in the digital marketing landscape, this sort of chaos, it does feel chaotic at the moment, will continue for a little bit. But it has to normalise out over time. There are a lot of players similar to us who are working hard to get back to being able to target audiences much more effectively.

What we saw in that second quarter was because of some of the IDFA changes, the inability to target as accurately, particularly from some of the big brands, is that a lot of the response was just to put more spend into much more broad-based audiences. So that just drove up the CAC for everybody across the market. I'm sure as it did for us that has to, to be honest by definition, impact everybody's profitability.

So whether that’s a strategy that other players, the largest customers who effectively drive the market, whether that’s something that they'll repeat in the future I think is a reasonable question. Because it must have impacted everybody's profitability. So we would see, we would expect that that ability to target audiences more effectively than we can, than all players can at the moment, and the impact that’s having on behaviour, will normalise out over time.

But I would, we don’t expect it to return to normal in the next three months, that’s for sure. I think that that’s why we've tried to be really explicit with our outlook for this half moving forward, that we expect that some of this behaviour to continue. Hence one of the reasons why we're saying that our marketing costs are likely to remain elevated versus what we would, we had experienced last year.

Joseph Michael: (Morgan Stanley, Analyst) Okay, got it. Then just one last question just around sort of customer retention. I think at the last update you said something like, seven out of 13 loyalty experiments you were running were showing positive retention signals. Just wondering if you can give us an update on those loyalty experiments? Are you still seeing higher retention from some of those initiatives?

Michael Ilczynski: Oh, look, thanks for the question. Again, that’s probably an area we'll talk in more detail in February. That as we spoke in August, in October, that was really our first crack under this kind of test and experiment concept that we ran through the middle of last year. Those experiments that did sort of show a real clear positive uplift we have continued within the businesses where that occurred.

The other ones, some of them that showed a positive uplift but were at a small scale, as part of our planning for calendar year '22, that we're in at the moment, we hope those will repeat but at a much larger scale, which some of those we'll embed as ongoing business. I think overall what we want to emphasise is that concept of driving loyalty, driving retention, driving repeat rate, is one of the areas of importance for the business.

Again we're seeing some very small green shoots. We've got a lot of work to do here. We've spoken a lot around the fact that there's no silver bullet. There's no one thing we can do. There's lots of different things we need to do to drive that. Part of it is investing in our brand, part of it is investing in the experience, part of it is lowering the shipping costs

over time to customers - that customers experience. Part of it is increasing our quality and the end customer experience. So we've got a lot of work to do in a lot of areas. But I think what continues to be the positive for us is we can see all of the improvement opportunities. Our job is to get out there and go after them.

Joseph Michael: (Morgan Stanley, Analyst) Great, that's all I had. Thanks Michael.

Operator: Thank you. The next question comes from Chami Ratnapala from RBC. Please go ahead.

Chami Ratnapala: (RBC, Analyst) Hi Mike and Emma, thanks for taking my question. I just had a quick question in terms of the low CACs that you talked about. Specifically looking at the first two weeks of January. Are you able to provide any commentary on the competitive environment, particularly looking more at the third quarter? Thank you.

Emma Clark: Yes, thanks for the question, Chami. So yes, what we've really seen is the competitive intensity has come off in the first two weeks of January. So as Mike said earlier in the call, a lot of the response to these privacy changes has been lots of big brands just throwing lots of money in over holidays, extending promotions. Spending a higher amount to acquire those customers with a high intensive spend.

That has all - we would seasonally expect the CACs to come down sort of November/December to January anyway. But obviously they were higher than we expected during that period. They've come back down at the moment to within what we would consider to be a normal range for January. I think the thing I just want to continually highlight is we don't know how long it persists at that exact level for. Because it is chaotic it can move around quite a bit even within a month.

But so far the first two weeks of January would say, actually much more sort of in terms of what we had said previously for guidance, as opposed to the elevated levels. But we've not assumed that that remains for the prior six months.

Chami Ratnapala: (RBC, Analyst) All right, thanks for that Emma. With that 12% to 15% guidance, I mean are we sort of still talking to that? Or how would you sort of look at that guidance? Or would the next probably four months to five months be a more indicator to sort of come back to that?

Emma Clark: Yes, a few things to answer that question. So one is, it comes back into the prior answer about those mid-term aspirations. So at that level of scale we obviously had that range within marketing, and we've been I think pretty clear that we're not moving away from any of those mid-term aspiration targets in terms of margin and percentages. So we definitely still believe longer-term that that's the range. I think what we're also trying to be very clear about is in the short-term it's going to be higher than that.

Chami Ratnapala: (RBC, Analyst) Thanks for that.

Operator: Thank you. There are no further questions at this time. I will now hand back to Michael for closing remarks.

Michael Ilczynski: Thanks very much. I just want to say thanks again for everyone joining us for this update today on short notice. I will remind you that we will be speaking again at our scheduled half year results release in early

February, providing a complete and audited set of financial statements. As well as a much expanded strategic and operational discussion at that time.

So thanks again for your attendance and we will now close the call.

Operator: Thank you. That does conclude our conference for today. Thank you for participating, you may now disconnect.

End of Transcript