**Mace Security International Inc.**

**Moderator: Barrus, Mark**

**April 2, 2019**

**10:00 AM ET**

OPERATOR: This is Conference # 8172817

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| Operator | Good morning my name is Julie, and I will be your conference operator today. At this time, I would like to welcome everyone to the Fourth Quarter 2018 Earnings Release Conference Call.   All lines have been placed on mute to prevent any background noise.  After the speaker's remarks, there will be a question and answer session. If you'd like to ask a question during this time, simply press star then the number one on your telephone keypad. If you'd like to withdraw your question, press the pound key.   Thank you. Mr. Mark Barrus, you may begin your conference. |
| Mark Barrus | Thank you Julian. Good morning, everyone. With me this morning is Gary Medved, President and Chief Executive Officer of mace. Please visit mace.com.investor relations/transcriptionpresentations where we've loaded materials for this call.  Before proceeding, I'd like to point out the certain statements and information during this conference call constitutes forward looking statements and are based on management's expectations and information currently in possession of management. When used during our conference call the words or phrases will likely result, are expected to, will continue, is anticipated, estimate, projected or intended to are some expressions that are intended to identify forward looking statements.  Such statements are subject to certain risks, known and unknown, and uncertainties including but not limited to economic conditions, limit of capital resources and the ability of management to effectively manage the business, and integrated acquired businesses. Such factors can materially adversely affect maces financial performance. It could cause mace's actual results for the future periods to differ materially from any opinions or statements expressed during this call.  I'll turn the call over to Gary to comment on a summary of the fourth quarter. |
| Gary Medved | Thank you Mark, and welcome everyone. This is our first earnings call as a new management team here at mace. I’m thrilled to be part of a company that has such an iconic brand and is the market leader in the consumer, law enforcement, and tactical markets. When the board asked me to step into this role, I looked forward to the challenge of profitably grow in this company by better understanding our customers and their needs. In the short time since January of this year that I have been CEO, we have refocused on understanding our customers, their needs, and how we can create better products to fill those needs.  With that being said, our financial performance of two thousand and eighteen was not acceptable, and our team is committed to understanding and fixing the causes underlying these results.  I will now turn the call over to Mark to discuss details behind the financial performance. |
| Mark Barrus | Thank you Gary.   As to the financial highlights themselves, fourth quarter net sales were two point eight three six million compared to two point nine three five million of last year, a decrease of ninety nine thousand dollars or approximately three percent. This is also a sequential decline and eighteen percent or six hundred ten thousand dollars from third quarter sales of three point four six million.   The modest decrease in quarter over quarter sales was due to a combination of factors, primarily softness in our international sales and some softness in consumer sales, partially offset by strong performance in our custom business.  Gross profit for the fourth quarter of two thousand eighteen totaled six hundred and fifty five thousand dollars with a twenty three percentage point to gross margin compared to one point four two three million, and forty eight percent gross margin in two thousand seventeen, and a gross margin of one point four nine seven million or forty three percent in Q3 of two thousand eighteen. This represents a year over year quarterly decrease of seven hundred sixty nine thousand dollars or twenty five margin points. This is primarily due to inventory write-downs in the Q4 two thousand eighteen just over four hundred thousand dollars, as well as a shift in sales mix from higher margin businesses to lower margin channels.  Selling, general, administrative expenses for the fourth quarter were one point three zero six million compared to one point three four eight million in the fourth quarter of two thousand seventeen, a decrease of forty three thousand dollars or three percent. Most of this decrease was attributable to the lower salary expense in the fourth quarter, partially offset by an increase in advertising expense in our ecommerce related channels.  As a result of the above, the company reported a net loss, after tax, of one million eight hundred fifty nine thousand dollars for the quarter compared with thirty thousand dollar loss in two thousand seventeen, a one million eight hundred twenty nine thousand dollars decline.   EBITDA for the quarter was one point seven four nine million loss compared to an EBITDA positive EBITDA of seventy four thousand dollars in two thousand seventeen, which amounts to a one point eight point two three million decline.  Turning to the full year two thousand eighteen, net sales for the year were eleven million four hundred and ninety thousand compared to nine million nine hundred eighty three thousand dollars last year, an increase of one point five zero seven million or fifteen percent. The increases due to increase sales in our ecommerce channels, particular our Amazon sales, reflective of a full year of sales from the Vigilant acquisition in October of two thousand seventeen and Washington Labs in March of two thousand seventeen, partially offset by softness in international and tactical.  Gross profit for two thousand eighteen totaled four point three five six million with thirty eight percent gross margin compared to four point four zero three million and forty four percent gross margin two thousand seventeen, a decrease of approximately forty seven thousand dollars six margin points.  Gross margin was impacted by the four hundred six thousand dollar inventory write down in fourth quarter, and the sales mix of increased sales in our lower margin custom business partially offset by increased ecommerce sales in two thousand eighteen, which carry a higher gross margin.  Selling, general, and administrative expenses for the year were four point seven five four million for approximately forty one percent of sales compared to four point one two millions or forty one percent of sales in two thousand seventeen, which is an increase of approximately six hundred thirty two thousand dollars. Higher advertising and Amazon fulfillment expenses were the chief contributor to the overall increase, but SG&A as a percentage of sales was flat, part due to increase sales.  Net loss for two thousand eighteen was a loss of one point nine four six million compared to the net loss of sixty five thousand dollars in two thousand seventeen. On a non-gap basis, EBITDA in two thousand eighteen was a loss of one five two three million compared to income of two hundred forty eight thousand dollars in two thousand seventeen.  Adjusted EBITDA was a hundred seventy two thousand in two thousand eighteen compared to three hundred and seventy seven thousand in two thousand seventeen, after considering adjustments primarily for impairments (inaudible) receivable, slow moving and obsolete inventory adjustments, certain other non-cash asset write downs, and adjustments for non-cash compensation expense.  I will now, talk, turn the call back over to Gary, who will discuss outlook and priorities for two thousand nineteen. |
| Gary Medved | Thank you Mark.  As stated previously, we are not satisfied by the financial performance in two thousand and eighteen, but we are encouraged that we have recognize many of the issues on our balance sheet and have a good starting point in two thousand nineteen. Unfortunately in Q1 of two thousand nineteen, we expect to recognize additional expenses due (inaudible) performance due to contractual severance arrangements and related legal fees, relating to our CEO transition of about three hundred thousand dollars. We do not proceed any further financial impact from this transition.  On a more positive note, we believe that we have now closed the book on our successful acquisitions of Washington Labs, and Vigilant, and that those applications have helped grow the top line as previously discussed. The Washington Labs acquisition will service the platform to help us grow our custom business, which allows us to serve customers that we would not otherwise be reaching. Vigilant has also helped us grow our ecommerce channel, which is increasingly important as the traditional retail industry continues to evolve in the face of ecommerce an online shopping.  We intend to focus on better understanding our customers and their product needs, as well as, to invest in promoting and or industry leader leading mace brand in two thousand nineteen. We have engaged outside branding and content marketing experts to help us engaging and understand our customers, as well as, better tell our brand story. We expect these actions will result in immediate pay backs through increased sales, better traffic to our ecommerce sites, and increased traction with customers.  In addition to the management changes announced in January, we have also recently strengthen our internal management team and capabilities by adding a talented Vice President of Sales, Julie Koenig, who will bring strong retail sales leadership to mace. We have also improved our operations team by re dedicating Carl Smith, who previously led both finance and operations into a pure operations role. Carl is rebuilding our- is building our operations team, and we are currently working on shop for and operational improvements using both in house and outside resources. We expect this to result in measurable cost improvements in two thousand and nineteen.  Regarding our two thousand and nineteen outlook, we completed the small previously announced tornado acquisition in Q1, which we have largely integrated and are now working on expanding and growing customer relations, with tornado customers. I expect we will pause any significant new acquisitions while the new management team continues to work our customer focus brand and operational initiatives. We also expect return to a positive EBITDA positioning in two thousand and nineteen, although, we will not be providing any specific guidance at this time.  At this time, I will stop and open the lines to questions. I would ask each caller to limit themselves to one question with one follow on, to allow everyone a chance to participate. If we have additional time, we'll try to get you back into the queue. Julie please open the line for questions. |
| Operator | At this time I would like to remind everyone in order to ask a question press star one on your telephone keypad. We'll pause for a moment to compile the Q&A roster. Your first question comes from a line of Thurman Willis, Private Investor. Your line is now open. |
| Thurman Willis | Mark and Gary thank you for taking my call. My question is, with the past experience that you two gentleman have and your cognizant in the past, why did you choose to come to mace, and what do you see going forward? |
| Gary Medved | Thank you Thurman this is Gary. The number one thing that stood out from me first and foremost was the brand. This is branded we all know what has been around for decades, it was the original. It’s the authentic pepper spray. It has a history of innovation. And, when I was first reached out to about this opportunity, my initial homework told me very quickly that it was under leveraged. I thought the company could be doing a lot more in a lot more channels.  The brand just look like it needed lifted, and my history has been, Thurman (inaudible) is taking on challenges and really digging down to bedrock, and starting to build from that point. And it's been everything as I expected since I come in here, and not a moment goes by that I'm not happy that I took this role. It's an exciting challenge and a powerful brand to be working with.  Mark. |
| Mark Barrus | I would just add to that Thurman that I was attracted by the same things that Gary saw, I was also attracted. I think the business fundamentals here are very strong. This is a conservative balance sheet; there's not a lot of debt on the balance sheet. It has shown the company's shown the ability to increase sales in the core businesses, once it once it's paired back to the core businesses that we now have. Over the last several years, I think there's, both, a tremendous undervaluing of the company, as well as, a tremendous opportunity to increase financial performance. And I think our, for example, our top line growth year over year has shown that this is a business that's very capable of stronger increased financial performance in the coming years. |
| Thurman Willis | Thank you for that, and if I could asked my follow on. I know that both you gentlemen, with your backgrounds, have done this turn around before. Ninety nine percent of the public, in my opinion, view mace as a spray on a keychain, and have no idea about the vast array of products that mace has. What are plans to educate and promote our products to increase those sales? |
| Gary Medved | Thanks Thurman. This is Gary again.  There are basically six parts to the sales cycle. And the first two are awareness and education, followed by get it on the shelf, and hopefully somebody buys it. I think mace over the years, the recent history, has been the step three and four, if you will, with not a large focus on the first two steps of that process. And since we're now working with an external marketing group, that is their primary role is to establish awareness of the brand and educate the public through multiple channels, okay, not just online, but through advertising, podcast, whatever it may be.  But as time goes forward, you're going to see and hear more about the mace brand, and it's going to be primarily focused on the awareness in the education side. We have a huge opportunity out there. When you think of the generation that develop the mace brand versus the generation that's out there today more apt to purchase a product, there's a huge opportunity for us to create that awareness, educate them on the different products we have, and ultimately driving sales either online through one of our ecommerce channels or brick and mortar. And, I think it's all going to start with the awareness and education process. |
| Thurman Willis | Thank you for taking my questions. And following your instructions, I'll back out of the queue and just say that I for one, a long term investor, am happy to see you gentleman on board, and excited about the future. |
| Gary Medved | Thanks Thurman. |
| Mark Barrus | Thanks Thurman. |
| Operator | Again. If you'd like to ask a question press star one on your telephone keypad. Your next question comes from the line of Andrew Shapiro from Lawndale Capital Management. Your line is open. |
| Andrew Shapiro | Hi. Good morning. Can you hear me okay, because I'm calling in from the road. |
| Gary Medved | You sound fine Andrew, good morning. |
| Mark Barrus | Morning. |
| Andrew Shapiro | Great, thank you. Hi.   So, on prior calls since Roll-Kraft became the lead investor and Chuck and Sanjay headed up the board, it was discussed a long term strategic plan was in process of development. It’s been a full year since their purchase from Ancora and the board leadership change, and we have now had a hiring of a new CEO and CFO, and certainly they interviewed you guys extensively, and then you've been inside and formulated your own views, along with the vision they've shared with you.  I had asked this several quarters ago, there is time that has come by now, I'm hopeful there's not a long period, if they're even has to be any period, but can someone provide us some insight into the strategic plan or at least what products in door segments or channels are they get greater resource allocation and lesser resource allocation?   There was a lot of emphasis on the delayed or missed opportunities regarding Mace Tactical. I don't really think in your script that was much mention of it, so I'm going to specifically ask about Mace Tactical.  But, can you guys provide us some insight on the strategic plan or the focus that you're formulating in carrying out the vision, that I'm sure, the board has shared with you, when they interviewed and screened you guys, and decided you were the leadership team to run with going forward? |
| Gary Medved | Thank you Andrew. Gary here.  First and foremost moved from a strategic standpoint, okay, product, as I mentioned earlier, product was getting on the shelf in certain channels. If you want to just look at brick and mortar retail whether its consumer sporting goods, there's a difference between just getting product on the shelf and truly engaging with your customers, okay, and I'm talking about potential customers, customer who never thought they would you need or want your product, and so forth.  And I think first, brick and mortar retail offers us a huge opportunity for placement out there, but we got to step back and actually develop a strategy on why would a consumer need or want this product. And I think once that's developed, and working with our marketing group, and again creating the awareness and the education out there, the two really go hand in hand, I can tell you after the first ten weeks on the job or whatever it's been, I am even more excited about our opportunities out there, and we do have a lot in the chamber so to speak that we're developing.  And there's a there's a full slate of projects, we're not short on projects in terms of your retail. We look at ecommerce, whether it's one of the big market places out there, or our own website mace.com, and the opportunity and the growth that we've experienced there, and as time goes forward, more and more people are shopping online, and we're setting ourselves up to be ready for that. And again, it's going to get back to the awareness and education, and we will be able to do more of that on mace.com than we would on other market place sites out there.  To touch on the tactical side, first and foremost, the law enforcement, the LEM market to us, it remains a valuable part of our portfolio. I’m continually- continuing to evaluate it. We do have some pieces in place, and as time goes on, working with, closely with, tactical folks on the outside of the company, we are developing a strategy that, for the most part right now, it's being implemented, okay, as we speak.  I realize the program itself is had stopping go over the last few years, there were reasons for that. And just when we really got in saddle and started kicking it into gear this year, then we have the government shutdown, which impacted ATF, and paperwork, and so forth, but now we have everything. We have the right people, in the right seats, on the right track, one in the right direction.   I'm not gonna say we're done with the evolution of that program, but we are continuing. We're going forward with it. I'd, like I said, it's important. I see some growth opportunity there, and we're just in the beginning phases of get this thing rolling. |
| Mark Barrus | I'll add to that Andrew.   The board was, in the few meetings that we've been part of early on, has been extremely clear and extremely focused on their expectations to improve financial performance. So one of the first things that I wanted to do was to take a very hard look at our balance sheet to ensure that we're where we need to be, and that we're not going to have a lot of noise impacting performance further on down the road.  And that's why, for the fourth quarter of two thousand eighteen, we did an extremely detailed review, operationally, of our inventory, all the way down to the things on deposit across the world, amounts that we capitalized in prior periods, and really took a hard look and said: what is the benefit for those? Are those still good assets, and is this still good inventory?  So as a result of that review, you saw that we took a fairly significant inventory charge that was not only related inventory but also some of those other deposits that resulted in a non-cash charge. By the same token, we took a hard look at it two of the bigger assets on our balance sheet, which were on notes from two of the businesses that were divested several years ago. And unfortunately both of these particular notes were called into question really in the fourth quarter.   I don't want to go too much into the details about what has transpired, but rest assured, we're going to actively pursue the obligations under these notes. But from an accounting perspective, we felt there was enough significant doubt on their flexibility that we reserved, not quite in the entirety, but the vast majority of those amounts. So, our starting point is we think we have a clean balance sheet going into the second quarter of two thousand nineteen. |
| Andrew Shapiro | Okay. So it sounds like those things now still remain as we will call it a highly contingent assets, but with the write off those note receivables and other earlier license deals, what are your views regarding monetization and licensing of the mace brand? This seems like a huge high margin opportunity that's not been effectively exploited. And also, kind of over the next three years, no one's asking for near term guidance, what do you see as a realistic EBITDA margin target for the reenergize mace that you both envision? |
| Gary Medved | Andrew, I'll tackle a little bit of that. So on the licensing, I think we all fully realizes realize what the performance that, financial performance that can happen in the business, specifically from licensing. You're absolutely right, if we're able to bring in royalties or other arrangements that would result in, call it relatively quick returns on the income statement, that would have the advantage of not only helping financial performance and adding resources, but also absorb some of the tax net operating loss.   Having said that, we have to be very careful with the value of our brand, which is our biggest asset, and be cautious with licensing transactions. We had some experience in the past with licensing transactions, and we want to continue to learn from the past. So I think it's fair to say, we're going to be pretty selective. We certainly see that licensing is attractive, call it additional revenue stream or additional channel if you will, but I think, at this point where we're going to be fairly cautious on that.  In terms of sort of projecting where we go. We're still new here. The vision is certainly that there will be a compounded increase in EBITDA year over year, which will come, not only from top line, but also performance in the expense category, and pretty much all throughout the company.  It's really too early to say. I can say that we do know very early on, it's the end of the first quarter, we are in the process of wrapping up the first quarter, but we are pleased to see that we had a very nice topline performance in the first quarter.   That percentage increase year over year from nineteen eighteen is very much in line with the fifty percent growth that resulted annually between eighteen and seventeen. So we're continuing to see that increase in top line performance here in the first quarter of nineteen. I think beyond that, in terms of EBITDA, it's very hard to say where things will go, year over a year, and we will continue to keep an eye on that. |
| Andrew Shapiro | Okay. I’ll back out and I have some other detailed questions, but you addressed the tax NOL. Can I just quickly ask what the level of the tax level NOL is and how much is expiring in the coming year or two? And then, I have other questions, but I'll back out. |
| Mark Barrus | Okay sure. I'll cover that one real quickly.   So the tax net operating loss coming into two thousand nineteen is just around sixty million gross, which obviously we wrote it off on our balance sheet, so you won't see it there. But if you consider a twenty, twenty five percent tax rate, that gets you into the mid twenty million dollar value of that asset.  Expiration beginning nineteen and they are a couple million bucks a year. The actual, there's actually a schedule back on page twenty seven of our financials, that shows the specific NOL, year by year. So we have to figure out where we are in eighteen tax wise and hopefully we will be adding to that, although we're not a hundred percent sure on that, if we do, it probably won't be significantly.  The real, as you know Andrew, the real key to the tax that are operating loss is to monitor. Can anything happen to it? New NOLs don't have expiration dates, but these old guys do. So we keep a very close eye on ownership changes that potentially limit the use of this, and we do have a little bit in the bag of tricks to play with near term expirations.   Unfortunately, there's not a ton of things you can do with a company the size of ours. So really, we look at it like the most important things are make money as soon as quickly as possible to help absorb that, and then keep an eye on the ownership changes. |
| Andrew Shapiro | Thank you. I'll back out. Please come back to me, I have more questions to drill down on. |
| Gary Medved | Sure. Sure we will. Thank you Andrew. |
| Mark Barrus | Thank you Andrew. |
| Operator | Your next question comes from a line of Thurman Willis, Private Investor. Your line is open. |
| Thurman Willis | Thank you for coming back to me. I had to other questions. You've talked about branding, and the mace brand alone, to me, appears to be worth the market cap of the company, which is around twenty million, so I'm saying that the stock, to me, is highly undervalued. What are your specific plans to get more fans in the stands? In other words, what are your plans to get new investors involved with mace, because of limited investors now have been around for a long time, and we just seemingly don't have any attempts in the past to bring new investors in the fold. So what are your plans for doing that, please? |
| Mark Barrus | Yes Thurman, this is Mark. I'll cover the investor one; then, I'll flip it to Gary to kind of talk about strategy, a little more specifically.   So the investor one is a tough one. Given the size of our company and given the OTC trading market, it's very difficult to attract institutional investors to a company of our size. And so, the traditional bigger company approaches of investor relations don't work too well here. So what is the main thing that we're going to do is to increase our performance, so that over time the company becomes more valuable and that the bumping around in the stock price, that you and others have lived through for quite some time, can be overcome and that with increased performance, that will attract more investors.   But in terms of concrete thing, we're not, at this point, going to go out and have a big heavy duty third party funded investor relations bonanza, in terms of hiring parties or trying to make a big splash. We just we just don't have a great story to tell.  I mean, we have a we have a great company, and a great brand name, and great assets, but they haven't frankly been capitalize on to the degree that the performance is there. So, our plan is to prepare ourselves to be ready for when our performance increases, and we will |