

**INTELLIGENT SYSTEMS CORPORATION**

**Moderator: Strange, Leland**

**June 5, 2019**

**11:00 AM ET**

**OPERATOR:** This is Conference # 9882445

**Operator** Good morning, my name is April, and I will be your conference operator today. At this time, I would like to welcome everyone to the Investor Update 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 would like to ask a question during that time, simply press star then the number one on your telephone keypad. If you would like to withdraw your question press the pound key.

Thank you, I will now turn the call over to Leland Strange.

**Leland Strange** Thank you for joining our call. For those that picked this call up through a transcript, thanks for taking the time to read. We will have the edited transcript of the call up on our website in a few hours. I suggest you check it on our corporate website [intelsys.com](http://intelsys.com) rather than Seeking Alpha or other sites because the speech to text automatic transcription often fails to convert some industry terms correctly.

Of course, maybe my southern drawl is the problem, but the transcript on our website cleans it up along with my grammar I might add. As often on my calls, I have both script and bullet points, but I won't hesitate to go extemporaneous when I think, as I talk, I may have not fully covered the point. I'll take questions at the end but plan to cut off after thirty minutes total call time.

I can tell you I've received a ton of advice on what to say and not say from shareholders, employees, investment bankers, and lawyers. I'm taking it all into consideration, but I certainly won't please everyone. I can summarize the response from the few customers who have messaged as "who cares?". I'm, of course, taking this part of the advice I get from counsel that I need to preface the remarks by noting the protection provided to the company and company executives with forward-looking statements within the meaning of the federal securities laws.

Everything I say, that's not a historical fact, should be treated and read as speculation. It's what I think or believe as of this moment and believe I have a good basis for it, but it may be proven incorrect in the future. I may expect, project, believe, plan, intend, or use any number of other similar words in this call and these are all forward-looking statements.

Note also the New York Stock Exchange has decided to halt trading in the stock until after the call or after the transcript is posted to our website. I'm actually not sure when it'll open. I personally don't think there will be information here that should cause volatility, but that wasn't my call. It was theirs. The call is precipitated by two recent commentaries that we believe to be "short and distort" hit pieces.

Regardless of the quality of the reports, they achieved their objective of driving the stock price down. If they closed their short positions earlier, they've been handsomely rewarded. When the reports came out, I received many calls and emails from folks who were angry at the flimsy and even laughable attempts to discredit the company.

They expected me to immediately jump up and down and scream and maybe were not happy with me as I was pretty sanguine about it knowing that ultimately the truth and company performance would trump distortions and false inuendo.

You see, I believe there is a place for shorting in our market system. It is as fair to bet on a stock price going down as it is to bet on a stock price going up. I've certainly done that in my personal portfolio. Sometimes the short players actually discover and root out dodgy or dishonest accounting or managements.

I feel differently, however, when they take easily googled public facts and stream them together in a misleading narrative. I think that pushes over the boundary of legitimate and ethical market activity, but that's for others to decide. My purpose

here is to provide enough information about some of the claims so you can get on with determining the value of the company based on its merits. The market then decides the appropriate stock price. Achieving or maintain a certain price is NOT my objective. My personal opinion of where the stock should trade is unimportant and irrelevant.

A quick note that should give current and potential investors pause about the Grizzly report specifically, INS is the only thing on their recently setup website. A few days ago, the Grizzly website disclaimer that is identical to one for Gotham City Research still had an accidental reference to Gotham City.

Gotham City is another anonymous short website that appears to have published one report last year and none this year. Also, the Grizzly INS report shows the logo for INS to be the one used by a Japanese gaming company called Intelligent Systems. Neither is important on their own, but as I tell my grandkids, consider the source.

In trying to decide how to approach this call, my first thought was, let's go to the most damaging facts. In musing about that approach, I found it difficult because there was absolutely no damaging factual information disseminated in either report. The facts all came from our filings or information openly available with any Google search.

I then considered opening with a discussion of how they got to Intelligent Systems in the first place. The answer to that question is pretty obvious. One of our directors with an 18-year tenure on the board, has been accused of various revenue manipulation practices as CEO of his former company.

The company was the object of a highly publicized short attack. He denies the accusation. The company's investigation claims it true along with other charges. The short players following that company found he is a director of Intelligent Systems and determined to target our company based on his association.

They have come up with some innocuous claims about us to make it appear we were up to some worrying practices. His being on or off the board does not change the accusations and innuendo. If he stays on the board for now, they will say we have a problem by association.

Leaving the board at this point in time, they will say that we are trying to sweep the problem under the table and make it go away by him leaving. This is NOT the subject of today's call, but I will address more on the board later in the call.

Usually, a predicate for the ability to successfully originate a short attack is an over-valued stock that has been pumped by the CEO or proxies. Even the commentaries from the shorts admit I have not in any way tried to hype the stock. A careful reading would even conclude I have, as some say, talked the stock down.

It is kind of original where they blame the investors and speculators for pushing the price up and not management. So, let's go to the root of the problem and talk about the opinions that affect valuation. The stock has declined substantially since the reports last week. We have to assume the narrative around the facts along with the opinions that they expressed HAVE affected the market valuation as they put a \$5 to \$12 tag on the stock price,

Probably the best argument they have is, and I am going to quote and read an edited paragraph from the commentary:

“We view INS as largely a niche Indian outsourcing business. In our opinion, shares have been propelled to highs by speculators chasing recent headlines in pursuit of quick profits. We believe it's only of matter of time until the stock reverts to valuation more reflective of the underlying economics.

INS trades at premium valuation of 15 times trailing revenues and 40 times trailing EBITDA. If INS were to revert to a valuation of around 2-5 times trailing sales, a multiple typical of Indian outsourcing business, such as Wipro as well as larger processing companies, such as First Data, the stock would be worth roughly \$5 to \$12 per share.”

This is their statement and their opinion. They view comps for INS as Wipro and First Data. They and everyone else are entitled to their opinion. We respectfully disagree on the outsourcing characterization and don't operate, manage, or think of ourselves as an Indian outsourcing company. We have spent, over the years, over \$50 million developing what we believe to be unique transaction processing software.

We own it, license it, and use it ourselves. Some very high-quality large enterprises with deep technical resources have chosen to use CoreCard software

for their transaction processing requirements. We will not confirm or deny that the enterprises in the short commentaries are accurate, but the companies mentioned do represent the kind and quality of customers who have chosen to use our software.

If you completely disregard that we are a software company, just an outsourcing company – (and we are not) – and look at the Wipro argument, their valuation conclusions still fail. My numbers may not be exact, but I believe Wipro expects to grow revenues 5% in 2019 compared to INS target of 25%. If you believe our company growing revenue is 5 times as fast as Wipro should be trading at the same earnings multiple, then you can buy their argument, and we are worth maybe \$12.

We do agree with their opinion that we are in the same business as First Data. We are similar to First Data's Global Financial Solutions segment, GFS. That is their issuing business. First Data reported 4<sup>th</sup> quarter segment revenue was down 9% from the prior year but up 7% on an organic constant currency basis.

So, just stick with the mid-point and say they were flat. INS 4<sup>th</sup> quarter revenue was up 138% compared to First Data's no growth. Our operating income went from a loss of \$700,000 to earnings of \$2.3 million from prior year compare that to First Data's 2% EBITDA growth.

So, even if you accept ALL of the short commentaries' key valuation comparable arguments, they fall apart when looking at the great disparity in growth rates. This is the key quantitative argument they've made for saying the stock was worth \$5 to \$12, and it fails miserably when you shed light on all of the numbers.

Moving on from the valuation observations, I think the most serious allegation that was made with the goal of impugning the company's accounting is that the company is recycling, round tripping, or siphoning off revenue. You read on the press release announcing this call a little about our response to this topic

We referenced an example of a very successful first round, maybe even their first outside dollars, investment of \$100,000 that required them to use CoreCard as their processor. We could have negotiated the arrangement with a loan, a convertible note, a preferred or common equity instrument, or we could have just said we will handle the setup of your program for free and waive the first six months of potential revenue or minimum, which could equate to maybe \$100,000 in services.

The larger processors have many ways to offer customers incentives, or in some cases, they compensate sales persons big bucks – and we are not paying any of those – or spend a lot of marketing dollars - which we don't spend – to attain a customer and its attendant revenue.

As I have said before, we don't buy customers. We don't give away much of anything, but we will do what we believe will get us the optimum total return from customer engagement. And we will take some risks like we have over our 35-year history looking at opportunities from a venture capital perspective.

I would hope shareholders would expect nothing less. We don't design a program to maximize how we present and look on a quarterly basis or where things end up on the income statement or balance sheet. We make decisions as if we were a private company with a long-term horizon as we craft terms.

We will win on some and lose on some. I certainly don't expect many, if any, to turn out as successful as this successful instance where we get a 15 times return on the investment and again 50 times the investment in profitable processing revenue over 5 or so years.

The investment of \$235,000 that was referenced in the report yielded approximately \$41,000 revenue in 2018 representing .2% of our revenue. That is not 2% but 2 tenths of a percent, and so far in 2019 it represents .03%, 3 100ths percent of our revenue. If I were trying to round-tip revenue, I certainly think I could do it in a lot more competent fashion. I am tempted to say this is just noise, but actually, it is so small, you would need a hearing aid or amplifier to even hear a squeak.

Imagine what they could have said and what I would have to be saying differently right now if the company that we had invested in had paid CoreCard last year \$200,000 in processing fees. I could not have said it is just at noise level like I just said. I would then be talking here about much we expect to get in the future rather than how little we got, and I would be much happier. Simple conclusion, we are going to do what makes business sense and then leave it to the accountants to handle the accounting.

The rest of the claims in the Grizzly piece are just as baseless. CoreCard does use some independent contractors for specialty work in India, and sometimes they represent on their resumes or LinkedIn pages that they work for CoreCard, when

in fact they did work for CoreCard as a contractor or employee of another company.

We don't go around the world and police what people say on their resumes. And most people who have done work for CoreCard in India like to brag about it because we are a very well-respected organization. Actually, our subsidiary in India is named ISC Pvt not CoreCard. Employees just say CoreCard.

Now, that may be the next scandal some short reports when they report they have searched the corporate records in India and find CoreCard does not exist and has no employees. Technically, that is correct, but there are 400 plus employees in India of a wholly owned subsidiary of Intelligent Systems as reported in all of our filings that work for CoreCard.

We also have licensed software from an India testing company in which one of our India managers has an interest. By the way, I tried to make an investment on behalf of our company in that testing company. But instead of this being a case of siphoning off revenue as accused, CoreCard got a very special and favorable deal because of the relationship.

It was fully vetted by me and our CFO at the time of contract execution. Some point to relationships as bad. Keep in mind, that can go just as easily the other way. We have good policies in place to monitor and manage potential conflicts. Now I am not going to claim there will never be one, but I can tell you the company will never knowingly allow one to happen that is disadvantageous to shareholders. Remember, I am a pretty large shareholder myself.

What else, the first report pointed out there is a relationship among the directors. That is true. Three of us are alumni of Georgia Tech and are financial supporters of the school. Russ Chandler is a director of Intelligent Systems. I watch Georgia Tech baseball play at Russ Chandler stadium on the Tech campus.

Russ may go to a conference or symposium in the Jane & Leland Strange Entrepreneurial wing located in the college of management building, or I might go to a Georgia Tech Research Institute meeting held in the Petit Bioengineering building. We have that in common. We did not graduate the same year nor know each other while at Tech.

We were not fraternity brothers and don't hang out socially together. I don't think we have all been in the same room or area together in the last 20 years except for

Intelligent Systems Board meetings, Georgia Tech Foundation Trustee meetings, and in the same stadium for Georgia Tech football games.

The fourth director, Phil Moise, is retired general counsel for a public company that was taken private. Prior to that position as general counsel of that company, he served as Intelligent Systems outside counsel. He has a long history that brings valuable insight to board meetings.

However, having said that, criticism about the board is somewhat valid, and we take note of that. With the Intelligent Systems now much higher valuation and our decision to concentrate on Fintech with the CoreCard business, we are highly likely to both increase the board size and restructure board personnel to focus on directors who can bring that type of expertise and relationships to the company.

Moving on, the first short report discussed licensing and quoted some experts about how it works. They also named customers, which I cannot comment on as a result of contract terms. I will not confirm or deny the accuracy, but it is fair to assume the logic around their premise about how many cards any new program is going to issue.

None of us have a good feel for the number of cards. You don't know. I don't know, but you do know they were writing the reports in an effort to lower our stock price. So, it would be logical that they would use worse case. I will also state that their consultant was wrong in trying to project likely terms of our license agreements.

Our terms are typically much better than he opined as to what is normal, but I am not going to breakdown the economics of a specific license agreement for competitive reasons. It is generally true that the license price for an active account goes down as the quantity as active cards goes up.

It is also true that sometimes there is a negotiated maximum price for a very large number of cards, but we are talking about really big numbers to get that point and maintenance and support is triggered indefinitely for that big number. Another question was about scale. We think we have scaled about as well as any company the last year or two and will continue.

If we were growing as slowly as First Data, we would not have to add more employees to take on more business, but our growth is substantially higher, so it requires a commensurate number of additional trained employees. Let me be

crystal clear on this point. We are going to support the large license customer to the nth degree and throttle growth as necessary in order to do that.

If as a shareholder, you value quarterly growth at any cost, you are investing in the wrong management. This has nothing to do with scale but everything to do with priorities. And choosing this priority, in the opinion of management and this large shareholder, is best for the company over the long haul.

I am going to wrap up by talking a little about future performance because this is what should be the driver of enterprise valuation. I have consistently said as of the middle of 2018 – and was quoted accurately throughout one of the reports – that I expected the company to grow revenue at an average 25% per year for the next few years. That is still the case.

We don't normally and don't plan on giving more guidance. However, I will add a little finer tuning to what we think about this year and next:

We believe that 2019 revenues will exceed those of 2018 by at least 25%. If 2019 is up by 25%, we believe 2020 revenues will be up another approximately 25%. Listen carefully to the wording as I don't want any misunderstanding. I am saying our average increase the next two years is anticipated to be 25% per year. If 2019 increases by 40%, I can tell you right now, it is highly unlikely that the next year will be 25%

Likewise, if the increase in 2019 should only be 20%, it is highly likely that the increase in 2020 will be more than 25%. I have explained in previous earnings calls the effect of license revenue pops. Why do I not have a clearer picture in June of 2019 of what our revenues will be for the second half of the year? It is because I don't not know with a certainty when the large licensed program will go live, which means more revenue for us, and have no idea how many cards will be issued this year.

But I am comfortable with guessing a middle ground estimate of revenue over two years combined. I just don't know the distribution by year. That is why I continue to say that the 2019 and 2020 years should have an approximate 25% average revenue growth rate. Operating income growth is likely to be slightly higher over the two years unless we make a strategic decision to substantially increase expenses to prepare for a bigger 2021 and thereafter.

I don't really have a lot more to add. You can make your own decisions, and we will just keep doing what we have been doing. We have just a few more minutes

left for questioning, but we'll do what I said in the beginning and close the call at about 30 minutes. You can save the other questions for our next earnings call. So, operator, you can see if there are any questions.

Operator At this time, I would like to remind everyone if you would like to ask a question, please press star then the number one on your telephone keypad, and your first question is from Kelvin Seetoh.

Leland  
Strange Hey Kelvin.

Kelvin  
Seetoh Hey, all right, Kelvin here, just a little bit of advice coming from you. So, you obviously talk about what we see in the shorts report, but I just wanted to [inaudible], how do you see the landscape of payment for [data] because we saw the majority of [software] companies [unintelligible]. So, what does it mean for a new [product] or maybe a smaller size payment [unintelligible]. Will it be harder or [tougher] for us to update new customers? So, I'd just like to find out your opinion on that.

Leland  
Strange I appreciate the question, but I'd rather hold this to things about what we talked about in the short report. We can talk about the other later.

Kelvin  
Seetoh I'll [get you next time] thank you.

Leland  
Strange Any other questions?

Operator Your next question is from Nuclear Vest.

Nuclear  
Vest What are the steps you will take if the accusations continue?

Leland  
Strange I don't think we're going to do anything else. They're entitled to do whatever they do, and shareholders decide what they want to do. We're going to focus on running the company. We're not going to engage with them and try to pick a fight. There's no reason to, and I know a lot of shareholders want us to, but our view is we're not. We're just going to keep doing what we do.

Nuclear Vest Okay, also can you share regards of -- talk about why is it that the [CNB] did not exercise the option back then when they have the opportunity because this is also mentioned in the short report, so probably you could share this about this more clearly on this part.

Leland Strange Sure, I'll be happy to. First, they got the institution wrong, and I'm not going to name the institution, but they got the institution wrong. It was not Central Bank of Kansas is what I think they said. Second is, put yourself in the position of our company. Seven years ago, we gave an option to buy a portion of CoreCard.

CoreCard was not wholly owned at that point in time by Intelligent Systems, but we did have control. Seven years later, I'm not going to send out a notice and bring to the attention of someone who has an option to buy a position in the company at a very low price. It's their obligation to keep up with that. So, we had no discussions.

We did not notify them their option was expiring. We think they just totally forgot about it, and we're just happy as we can be that they forgot about it. And we didn't notify them. Now, that's one explanation. Another explanation could be that they did know about it, but I suspect if they did, they would have said something to us, even if they had not exercised.

So, the other explanation is a bank is not in position -- is not typically an investor in companies in which they do business with. So, I don't know what their answer is. I'm not going to ask them. I've never brought this up with them. We have a continuing relationship in other ways, and it's just not something that matters to us, but it's not the institution that they mentioned.

Nuclear Vest Okay, and also can you also share regards of what was your conviction in CoreCard that make you continue to invest with ChemFree profits, previously? This would also give us an idea of what you thought about CoreCard's business.

Leland Strange I not sure what you meant. I mean, we, in the past, have invested and built many businesses, and we are opportunistic in terms of when we get in and when we get out. We try to make the best decision based on what we see, and at the time ChemFree we had -- it was not up for sale. We did not have a broker or anybody trying to sell it.

We had an inquiry from a very legitimate good potential buyer that we thought it would probably fit better with them than it would be if we kept running it. So, we made the decision to sell it to them. Kind of same thing we do here. We're not out trying to sell anything. We listen to anybody comes in the door and make a decision at that point.

It was fortunate. It was good that they bought it at that point. It gave us more cash, although we truly didn't need any more cash. We've been fine with our cash. ChemFree was very profitable. So, I hope that answers your question. We didn't make a strategic decision to get out of it. We had already begun to focus on CoreCard, but it was just an opportune time based on someone coming in the door and offering a good price.

Okay, let's see if we have a question for someone else at this point because we'll only take one or two more.

Operator Your next question is from Daryl Luw.

Leland Okay.  
Strange

Daryl Luw Hey, Mr. Strange, this question is for Matt.

Leland Well go ahead. I'm going to have to answer the questions today. Go ahead with  
Strange the question please.

Daryl Luw I really like how both of you [unintelligible] number. Can you share how INS set to meet our prior auditor?

Leland We're having some problems with the phone and not able to understand the  
Strange question. Was it about something I said or something about the short report because that's what we're going to talk about here.

Daryl Luw Do you have any comments on the audit fees?

Leland I'm sorry, I'm still having some confusion on the question. Was it a question  
Strange about the auditors?

Daryl Luw Yes, correct. How did you get to meet the current auditors?

Leland Okay, I'll be glad to do that. Matt wasn't here at the time they were chosen. Our  
Strange previous auditor had one public company client and that was Intelligent  
Systems. And they notified us that they were going to get out of the public  
accounting -- public companies stock auditing business and told us we had to  
find another auditor.

No issues or disagreements about anything. In fact, I know the partner there  
very well, and it was just they made a company decision to get out of auditing  
public companies. It's very expensive to audit a public company as an auditor.  
So, our CFO Bonnie Herron obviously decided she needed to start interviewing  
people for auditors.

And I had met this gentleman at church. Frankly, I didn't even know what he  
did the time I served with him on a committee. Later, I understand he was in the  
accounting business, and I suggested to her that she might want to see what they  
do and if they do it. So, Bonnie handled the whole process. She interviewed  
Nichols Cauley.

She interviewed two others, and then the audit committee got involved. And  
they chose to do Nichols Cauley, so that's how it happened pure and simple.  
Again, no close relationships, we go to the same church that's for sure, and we  
see each other at church, but it has no other bearing on the choice.

Daryl Luw Understand okay thank you, Mr. Leland. Are there any comments on the audit  
fee?

Leland On the audit fee, well we think it's good. We always negotiate for low prices in  
Strange every darn thing we do. I would hope people wouldn't think we totally pay a  
high fee that's a good thing. We don't pay any more than we have to for  
anything, okay.

Daryl Luw Yeah, okay [unintelligible]

Leland Strange I can't name the companies that we've done. We report as we're required in our filings. Can we give someone else a chance to ask one question, and then we're going to cut it off? You've had two or three. Let's see if there's one more out there operator.

Operator And your last question is from Sam Rebotsky.

Sam Rebotsky Yes, good morning Leland, I have a couple of positive comments to say about you. My first investment about sixty years ago was American Research and Development. I was introduced to Intelligent Systems in nineteen ninety-three by John Gaffenreid. I've been on the call. There was a -- for the longest time as anybody. In April third two thousand, there was a Baron's write-up on speaking of dividends on Intelligent Systems. It was trading at nine bucks.

And you have performed admirably as a venture capital as an investment company, and anybody that's been long-term and not short, not a short seller has been very happy with what you've done. Unfortunately, the short sellers don't file that they have five percent. They don't do other things. They're not scrutinized by the SEC in the same way as an investor is.

And I'm very proud to be an owner, even though I've taken profits because the stock has run up significantly, and I think everybody has to make judgment on value of a stock. But you have performed admirably and anybody who is invested should be happy. That's my comment Leland.

Leland Strange That's a great way for us to end with the last question. We appreciate your comments, and we understand fully that shareholders are in this to make money, and they should make their own decisions of when to take profits as we will do. So, with that, I will say thank you everyone for joining.

I hope we've given you the information you need to make an informed decision about what you do with your stock, whether you own or anticipating owning, happy to talk with you, but those are the -- I think, those are the highlights. And again, we appreciate your interest thank you everyone.

Operator Thank you for joining today's conference call. You may now disconnect.