Transcription

Verisure Group Q1 report 2022

25 May 2022

PRESENTATION

Operator

Hello and welcome to Verisure Group Q1 Report 2022. For the first part of this call, all participants will be in a listen-only mode, and afterwards, there will be a question-and-answer session. I'll now hand it over to the company. Please go ahead.

Vincent Litrico

Thank you, Operator. Good afternoon or good morning everyone, and welcome to our Q1 2022 Results presentation. Participants on this call are our CEO, Austin Lally, and myself, Vincent Litrico, the Group's CFO. As always, our Q1 2022 Earnings Report and presentation can be found in the Investor section of our corporate website.

Before we start, let's have a quick look at the agenda on page four.

As in previous calls, Austin will share an overview of the key highlights of the quarter. Then I will walk you through our financial performance, which will be followed by the usual Q&A session. And with that, I will hand it over to our CEO, Austin.

Austin Lally

Thank you, Vincent, and good morning and good afternoon to all of you joining us today. Thanks for taking the time again to engage with our business.

Today, we will present the First Quarter 2022 Results for the Verisure Group, and I'm very happy to share that we had another really good quarter, both operationally and financially. So, let's start with our Q1 top-line results on slide five.

We had more than 203,000 new installations in the quarter. We are now proud to protect more than 4.4 million customers. We've added over 500,000 customers to our portfolio in the last 12 months. Our total revenues are up 14% in the quarter, as reported. However, portfolio EBITDA was up 16% in the quarter, reaching 490 million euros. Quarter-after-quarter, we reach new all-time high records. Annualised, our portfolio EBITDA is now over 1.63 billion euros. Total adjusted EBITDA was up 6.4% in the quarter. We view this overall as very strong financial performance.

Let's now move to slide six. Our customer portfolio has 518,000 more customers than a year ago. We now have a portfolio of slightly above 4.4 million customers, and that's a net portfolio annualised growth rate of 13.3%, and coincidentally, that's exactly in line with our past five years CAGR also of 13.3%. Let's now move to slide seven.

As I mentioned earlier, it was another very strong quarter on new sales. We added 203,000 new customers to our portfolio. This was our strongest Q1 ever on new sales. It represents a growth of 9% versus the same quarter last year. And as you may remember, new installations in Q3 and Q4 in the second semester of 2020 were exceptionally high because we had a COVID catch-up effect on new sales at that time.

Let me also comment briefly on CPA. In Q1, our CPA was 1,375 euros. This is 14% up versus last year. The key drivers of that remain the same as those we have been talking about in previous calls. We're seeing inflationary pressures on material costs, some of it related to broader supply chain shortages for consumer electronics, as well as on marketing costs.

There's also some phasing on overheads, as we started recruiting again in 2021, coming out of the first period of COVID. But despite that increase in CPA in the quarter, we are still creating very valuable, very attractive lifetime customers. And we continue to innovate, of course, to find more effective and efficient approaches, especially on marketing cost.

We don't give formal forward-looking guidance, but I can say that we continue to be optimistic about the future, even in a more difficult external economic environment. We still see strong continued demand as we operate in relatively low-penetration markets with a long runway ahead.

Let's move to attrition performance on slide eight. Our portfolio, once again, proved its resilience. We maintained our strong attrition performance in Q1. Attrition continued at a low level, 6.5%. We've been below 7% in annualised attrition in every quarter for the last seven years. We believe this performance leads not only our industry, but subscriber-based consumer services overall. This is also encouraging, given the inflationary pressure that many households are feeling today, particularly on utilities.

Now, we obviously monitor the attrition performance extremely carefully. We always act to protect our customer base. We will continue working hard to maintain the trust and loyalty of our customers, who are so valuable and so important to us.

Value creation is not just about the total portfolio, all aggregated and blended. We also pay strict attention to the profitability of individual customers. Unit economics are the foundations of value creation.

We are now going to look at earnings per customer, EPC, on slide nine. In Q1, we continued to enjoy excellent EPC. We reached 31.5 euros per customer per month. That's 1.9% versus last year, and it's an all-time high. Average revenue per user increased to 43.6 euros per customer per month in Q1. That's up 2.9% versus the same period last year. This, together with the portfolio growth discussed before, translated into incremental total portfolio revenue of 81 million in the quarter, compared to the same period last year. Taking a longer-term view, over the past five years, we have grown our EPC by more than five euros per month, and this was broad-based. Unit customer profitability improved in all of our main geographies.

With this, I would now like to hand over to Vincent, our CFO, who will take you through the financial performance in more detail, and I will come back later for the Q&A and for some final closing remarks. Vincent, over to you.

Vincent Litrico

Thank you, Austin. Turning now to slide 10, you will find our key financial metrics for the quarter. Verisure Group delivered another strong quarter of financial results.

Revenues increased to 682 million euros in the quarter, representing an increase of 14% versus last year. Our key cash generation measure, portfolio services EBITDA, continued to increase at very healthy rates and reached a new record high of 409 million euros in the quarter, an improvement of 16% versus last year. Our annualised portfolio EBITDA is now over 1.6 billion euros.

We continue to enjoy sustained high profitability levels in our portfolio. Portfolio EBITDA margin was 72.2% in the quarter. This is slightly lower than last year when we enjoyed all-time Q1 record levels. To put this in context, Q1 2022 portfolio EBITDA margin is 2.1 percentage points higher than two years ago in Q1 2020 and 3.6 percentage points higher than three years ago in Q1 2019. We've improved our portfolio EBITDA margins by 1.4 percentage points per year on average during the last five years. The slight decrease in Q1 2022 is driven by the normalisation of workload activity versus last year, 2021, when we enjoyed abnormally low levels of activity, as well as some inflationary pressures, which we discussed in previous calls.

Total adjusted EBITDA was 276 million euros in the quarter, representing an increase of 5% versus the same period last year.

Cash flow from operating activities generated 249 million euros in the quarter, compared to 190 million euros in the same period last year. This represents a 31% increase. This is a combination of higher cash flow generation before changes in working capital as well as better performance of working capital items.

Total capital expenditures increased 6% versus last year, reaching 186 million euros in the quarter.

As of the end of the quarter, net debt reached 7,216 million euros, an increase of 4% versus last year.

In terms of financial headroom, we count on 439 million euros from a combination of cash on balance and available funds under our 700 million Euro revolver credit facility.

In summary, we've had continued strong financial performance in the quarter.

Now turning to page 11, we show a more detailed income statement for the quarter. Starting with reported financials, excluding separately disclosed items, revenues stood at 682 million euros and total EBITDA at 276 million euros, what translates into a total EBITDA margin of 41%.

Depreciation and amortisation amounted to 124 million euros. This relates primarily to the depreciation of the alarm equipment installed at our customers' premises, as well as the depreciation of capitalised variable sales costs.

Retirements of assets decreased to 18 million euros, down from 32 million euros last year. This represents the remaining balance of capitalised material and direct costs at the time customers leave the portfolio or upgrade to our new platform.

Operating profit closed at 135 million euros, what translates into an operating profit margin of 20%, and net interest expense amounted to 75 million euros in the quarter. The increase versus last year´s result of 59 million euros is driven by the increase in gross debt.

In total, this gets us to a result before taxes of 58 million euros in the quarter.

Let me quickly cover the separately disclosed items. Starting at the top, we incurred 3 million euros of operating SDI expenses during the first quarter. These are mainly related to ongoing transformational projects.

Furthermore, we have recorded 80 million euros of amortisation of acquisition-related intangibles. Most of it relates to the amortisation of the contract portfolio acquired back in 2011 from the Securitas Direct Group. The amount is lower than what we had in previous quarters, as part of the contract portfolios were fully amortised in Q3 2021. This amount is obviously non-cash.

Separately disclosed other financial items amounted to a positive 23 million euros. This is driven by a non-cash FX revaluation of debt items as well as unrealised derivatives of 30 million euros, partly offset by the amortisation of prepaid financing fees of negative 3 million euros, realised derivatives of minus 3 million euros and a negative IFRS 9 adjustment related to the modification of loan agreements of minus 1 million euros.

Finally, if we look to the reported numbers on the right-hand side of the table, we see that income tax for the quarter was 27 million euros.

All in all, this results in a reported net profit for the quarter of 32 million euros, compared to plus 16 million euros in the same period last year.

Let's now turn to slide number 12, where we show an overview of our operating cash flow in the quarter. We've had a strong operating cash flow generation of 249 million euros in Q1, representing an increase of 31% versus the same period last year. Excluding changes in working capital, operating cash flow generation was 269 million euros, up 6% versus Q1 2021.

Our main source of cash flow generation is the recurring cash flows from our customer portfolio, which grows month after month, and which currently stands at 4.4 million customers, as discussed. We generated 409 million euros of portfolio EBITDA during the quarter.

As you know, we do not fully capitalise on the balance sheet all our upfront investments to acquire new customers. Part of the upfront investment is expensed immediately and accounted for in EBITDA. Such effect was 133 million euros this quarter.

Change in working capital negatively impacted operating cash flow by 20 million euros in the quarter. This was mainly driven by additional inventory build-ups and increases in trade receivables, partly offset by increases in other payables.

Finally, paid taxes accounted for 4 million euros and SDIs and other items further contributed to a 3 million euros outflow in the quarter.

Turning now to slide number 13, we illustrate the net debt bridge for the quarter.

Starting from our net debt position as of December 2021 on the left-hand side, you see the 249 million euros of operating cash flow generation we just talked about. Of that, we deliberately reinvested 186 million euros in additional growth for the company. This mainly includes capital expenditures to acquire new customers as well as investments in product development upgrades and IT infrastructure.

Net interest payments amounted to 86 million euros in the quarter, and bank, advisory and other financial items amounted to 4 million euros.

Finally, we also had an increase of lease liability debt of 5 million euros, and other cash flow effects totalling 11 million euros.

All in all, net debt increased to 7.216 billion euros as of March close.

Now turning to the next page, number 14, we show a summary of our quarterly leverage evolution since 2018. As you know, we have delevered and levered up on several occasions in the past years.

We talked in past earning calls about how COVID-19 impacted our operations in terms of volume phasing, cost to acquire, cost to serve customers and working capital. We estimated these impacts to illustrate what our total net leverage would have looked like in 2020 and Q1 ’21, normalised for these COVID-19 effects.

As a reminder, on the back of the Q1 2021 big refinancing and subsequent paid distribution, our total net leverage increased to 6.6x, with a corresponding senior secured net leverage of 5.2x. If we normalise leverage for COVID-19 effects, we estimate total net leverage would have been 6.9x at the end of Q1 2021. We estimate we delevered the business by half a turn during the first three quarters of 2021. The 0.2x increase in Q4 2021 was driven by the 766 million NOK payment to the NCA in December last year, as well as intentional increases in inventory levels to face the continuous supply challenges and manage the equipment phase in and phase out associated with our Moonshot programme.

This working capital trend has continued to some degree in Q1 2022. This, combined with the inflationary pressures we have discussed on material costs and marketing costs, result in a 6.6x total net leverage and 5.2x senior secured net leverage for the period, in line with the previous quarter.

Now, I would like to quickly review the development of our key metrics over the past years, which reflect our ability to continue to grow sales, recurring profit, and cash for the business at a sustained rate.

In slide 15 we illustrate an overview of our resilient track record of successfully delivering strong, high-quality growth, both top and bottom line, every year, irrespective of the external environment.

Starting with the sales engine at the top left-hand side graph, we have had very strong growth in new customer intake over the years. During the last 5 full years, new installations have grown at a CAGR of 16%. As we have explained, customer intake has grown 9% in Q1 2022 versus last year. Now this is, of course, growth on growth.

In parallel, we have a continued to focus on improving customer experience and bringing attrition down to below 7% from an already low industry-leading level.

Strong customer intake and low attrition leads to strong portfolio growth. We've enjoyed double-digit growth in our customer portfolio for several years and now have over 4.4 million customers. It's remarkable that during the last 12 months we have increased our portfolio by over half a million customers.

At the same time, this volume growth is complemented by a continuous improvement in unit economics and profitability by customer, or EPC.

Improved EPC, which you can see in the bottom graph in the middle of the page, is the result of both our ability to earn higher pricing, historically above local inflation, and driven by strong product and service innovation, as well as improved efficiency and cost to serve, supported by operating leverage.

EPC has grown at a CAGR of 4.5% between 2016 and 2021. As talked, Q1 2022 EPC year-on-year growth stood at 1.9%. This growth deceleration is mainly due to the cost inflationary pressures we have been discussing in the last couple of earnings calls.

Overall, as you can see on the right-hand side of the page, strong portfolio growth and continued improvement in unit economics has led to consistent high double-digit growth in our key profit and cash flow measure, portfolio EBITDA. Portfolio EBITDA is now over 1.6 billion euros on an annualised basis.

Now, before handing it over to the operator for the Q&A session, I wanted to illustrate Verisure's solid track record of pricing ahead of inflation, which I'm sure will be of interest given the current market context. I'm now on page 16.

On average, since 2006, we've been able to price significantly over local inflation. This delta of course compounds year after year, as you can see on the left-hand side of the slide.

Our pricing window typically occurs in Q1 every year. We decide price increases during Q3 the prior year, considering latest available inflation estimates, among other things. Of course, we can be surprised by actual realised inflation in a particular year. If this happens, we are able to catch up in the following years.

Our continued strong investment in innovation allows us to offer our customers world-class products with consistent external recognition, as you can see on the right-hand side of the page. We believe that continuous innovation in products and services improves customer experience and increases our ability not only to generate ongoing and sustainable ARPU growth, but also to conduct upselling, while driving loyalty.

With this, we conclude this part of the presentation. I would now like to hand it over to the operator for the Q&A session.

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Q&A

Operator

Thank you, and if you do wish to ask a question, please press 01 on your telephone keypad now.

Our first question comes from the line of Markus Schmitt from Prisma Investment. Please go ahead.

Markus Schmitt

Thanks for taking the question. I have two, actually. The first one is on your cash flow profile. We see the bond markets we have right now, and the rising yields. How do you think about managing your growth in connection with cash needs going forward? In other words, do you need to lower your growth ambition in order to become clearly cash flow positive going forward? Because the old high growth financed by an incremental debt model will probably not work anymore, at least in the short term. So how do you think about it and if you need to change your focus or strategy a bit here?

Vincent Litrico

As you know, we generate very substantial amounts of recurring, solid, predictable cash flows from our existing portfolio. Our focus is actually to continue to delight customers, which we've done. And you've seen in 2022 all the awards we got from innovation, that helps us support this. We deliberately choose to invest a great part of this cash flow generation into new customer acquisition. It boils down to the fact that more customers than those we currently serve today actually aspire to get the service we offer and enjoy the peace-of-mind service we propose. That comes at a very high marginal internal rate of return on the new customer intake that we generate.

That customer intake quality is critical, and so we make sure that we really put capital towards it. When you look at the cash uses, out of the over 1.6-billion-euro portfolio EBITDA cash flow, which is our best proxy for the cash flow generated by our portfolio of customers, we invest a good chunk of it. But not all, of course. There's obviously now an increased amount of debt services that we pay. In 2020 we were cashflow positive. In 2021 though, we have some light cash consumption given the short-term challenges discussed in addition to some headwinds in terms of inflationary pressure and a tight supply environment context.

There's also an element of working capital that I mentioned before. But we are very close to cash flow net breakeven, even after taking into consideration all the cash we redeploy to new customer acquisition. We understand the cost of debt is increasing lately. But it is not getting in the way of continuing to flex our customer acquisition muscles and basically continue to offer our service to more and more households and small businesses.

Markus Schmitt

Okay. But to put us a little bit into context, you have a 2023 maturity, and you have probably to pay 200 basis points more on the bond if the market remains like it is right now. So how do you want to address it? Assuming liquidity flooding by the Central Bank is over, you have some inflationary pressure. Your asset is great. It's my view, one of the best high-yield assets in Europe. But you have to address somehow the cap structure in connection with rising yields, which was later.

Austin Lally

There's obviously a question there, but I don't think it's appropriate for us to comment on future financing reaction that we might take. But obviously we're fully aware of this. The key point Vincent is making is that, when we invest in customer acquisition, we're creating customers with a lifetime of more than 15 years. It's super, super attractive, and even with customer acquisition costs a bit higher this quarter because of some of the pressures we face on material costs, for example, we're still creating incredibly valuable customers. When we decide to invest in customer acquisition, it's always choiceful. It's basically because of the very high IRR that we get on those customers that we create.

Markus Schmitt

No, that's all clear, but the main question is, do you have to change your growth ambition from, let's say, 15% to 20%, as in the past, to maybe 10%, because you need to generate more free cash flow? Do you feel pressured in that sense?

Austin Lally

No, we don't. Consciously slowing down the acquisition of these incredibly valuable customer assets, I think would be actually a poor choice from a value-creation perspective.

Markus Schmitt

Okay. Yeah. That's it for me. Thank you very much.

Austin Lally

Thank you.

Operator

And the next question comes from the line of Sneha Sarawagi from Invesco. Please go ahead.

Sneha Sarawagi

Hi. thank you for taking my question. I understand your comment around EPC. I just wanted to hear a bit on your observations right now. We are in May for this year. How do you plan to have some price increases further? And what do you think how it's going to impact the customers? Do you think there would be some minute losses at that point of time? And I have a subsequent question that I'll ask that later.

Austin Lally

No, generally speaking, we take our annual pricing on the portfolio at the beginning of the year, usually around Q1. We're not really in the game of multiple price increases. Now, there are obviously ongoing positive effects from things like upselling, offering new services to existing customers. There's also the arrival of new customers in the portfolio. That happens all the way through the year. But when it comes to the big driver of ARPU, that's really the Q1 price increase, and that's behind us, which is why the very solid attrition performance is so encouraging.

Sneha Sarawagi

Okay. That's clear. So that means there's no price increases we are going to see for this year. And just a subsequent question to understand this a little more, and how are you finding your cost stack at this point of time? We talk about inflation and the impact of that on wages and input costs, but what are you experiencing so far? Is it too much, or are you having to go for a salary increase?

Austin Lally

Generally speaking, the wage inflation that we've seen in key markets has actually been lower than the pricing we took. So far as you head into 2022, we're actually building margin, so basically more pricing than the cost to serve increase. Now we obviously keep a very, very close eye on this question because, as you well know, wages are the biggest cost that we have. And that is because we're a people-intensive service business. We're obviously going to have to keep wages in the marketplace under review.

That's why Vincent made such a point on slide 16 of showing the company's historical track record of pricing ahead of inflation. This is a business that's very sticky. The value for money perception of the customers is very high. You see that, for example, in the very good net promoter score that we generally deliver. So, if we do face in 2023, for example, more pressure on wages, we're actually quite confident that we've got the pricing power to be able to defend our margins.

Sneha Sarawagi

Okay. That's clear. Thank you. Just to follow up on the previous question, I know we discussed this at length about the gap structure, but I was just trying to understand a little more now that we know that there is a refinancing in the near-term, and there is a high-yield raise environment, and we will be seeing a bit of increase in your interest costs in the cash profile. So, how is Verisure looking at it? I understand the business description side of it, that you're having a robust customer base and it's growing quite fast, but I'm just slightly concerned about the cash profile, so I wanted to hear on your comments on that and the outlook for 2022.

Vincent Litrico

As Austin mentioned before, the capital deployment decisions are deliberate and fully discretionary. So today the plan is not to alter the gross operating revenue we have. In terms of capital markets, though, you talked about cost of debt, etc. Of course, this is something that we look at closely. I'd like to thank the debt capital markets for the confidence they've placed in us over the past years. As always, we are very happy to pay fair price for our debt papers, as you've seen both on the way down as well as on the way up. If you recall back in 2020, we were, I think, the first company in the high-yield space to reopen the market on the back of COVID. I think it was April, and we were perfectly fine to pay probably what was clearly higher cost of debt than what we had been used to in the previous years.

So, same thing here. We do not manage treasury as a profit centre. There's normal, I would say, capital structure hygiene that we take into consideration. We are of course aware that we have a piece of debt, half a billion, coming due a year from now. We are obviously watching closely market conditions. But ultimately, we pay fair price. And we are confident we will continue to get the support from the capital markets given the track record of the company in not only delivering, but actually beating our promises consistently in terms of financial results. But also delivering against the leverage trajectory that we've we feel comfortable with.

Austin Lally

And I would just add to Vincent's comment. I think for credit investors, the most important messages are that the investment choices that we make are deliberate, thoughtful, and unlike many other companies, our growth is completely discretionary. We choose how many salespeople to have. We choose how much marketing investment to make month on month. I think you actually saw, for example, in 2020, as we went through the first waves of the COVID pandemic, how we were able actually to flex majorly our growth choices and our cost structure. I think that for lenders, that should give really great reassurance about the robustness of the model.

Sneha Sarawagi

Thank you, and all the best for that.

Operator

And the next question comes from the line of Paul Brennan from GoldenTree. Please go ahead.

Paul Brennan

Hi, good morning. A couple of questions, the first one was just on the price increase in Q1. I guess you had the slide in the back that shows how historically you've increased ahead of inflation, but this year you're a little bit below inflation. Just trying to understand that better, did you just maybe make a decision in Q3 that you decided to increase by 3% and maybe that just in hindsight, wasn't enough versus inflation, or were there some kind of competitive pressures that led to keeping the price increase at 3% when inflation is actually a bit higher?

Austin Lally

No, I think this is a great topic actually to dig into because the question is really, what inflation are we discussing? Are we talking headline consumer price index inflation, which as we know, has been driven up dramatically by energy, by utilities, by gas, and so on, which are fundamentally not really part of my cost structure? Obviously, our cost structure is predominantly, as I mentioned earlier, people cost. We're a technology company, but we're a technology-enabled human service company. The biggest cost bucket that we address is people cost. We actually priced our portfolio ahead of the wage inflation that we were actually seeing. We were quite thoughtful about this topic, and obviously we're going to continue to keep that under review, as we start thinking about our pricing plans for 2023. We'll take a look at what's the inflation customers are seeing. We'll also take a look at what's the cost pressure that we are seeing, and we'll make what we think is the right decision across that matrix.

Paul Brennan

Okay. Got it. That’s helpful. Thanks. Other question was just in relation to subscriber acquisition costs. It looks to me like the part of that that's charged to customers has been falling for the last few quarters. Could you maybe comment on what's driving that?

Vincent Litrico

If you look at where we are versus same quarter last year, the upfront is 20 euros down. That´s a 4% down. But most of this is tracing to FX. It's about 15 euros of FX impact.

And then there's also 9 euros of almost - call it 10 euros - of IFRS 15 impacts. Like for like, true north, we’ve actually not reduced upfront. But it's fair also to say that we have not increased it as much as we used in the past, to take into consideration the fact that some of our households or new customer prospects faced in some places tougher tension on disposable income due to the energy bill increases they've seen, especially towards the later part of the quarter. Does this answer question?

Paul Brennan

Yes. And just one quick follow-up. Could you just remind me how you determine what part of the subscriber acquisition cost is capitalised and what's expensed and whether there has been any change in how you think about that recently?

Vincent Litrico

Sure. The method doesn't change. We would like to capitalise, frankly, 100%, because this investment creates on average a 15-year relationship and should be, in our view, capitalised and amortised over that timeframe. That's not what IFRS allows us to do. We follow strictly IFRS rules here. What we end up doing net-net is capitalising about 50% of the total net CPA.

If you look at the cost piece now, as a percent of costs, 40% of the cost gets capitalised, and that's all we are allowed to do. And namely, what this includes is two things - the equipment or the material costs that are linked to the alarm equipment - central unit, peripherals, etc. - that we install at the customer premise, as well as the valuable sales cost, basically the sales´ or security installer´s commissions.

These are the two elements we can capitalise. All the rest is expensed, and that's basically 60% of the cost structure that we expense right away that, as you know, kind of counterintuitively depresses EBITDA. The faster we grow, the more we invest, the faster we put capital to work. But unfortunately, we get to capitalise only 40% of these costs, and that's basically leading to slight volatility on the EBITDA front. This is why we tend to guide and lead and talk about portfolio services, which is a lot more stable, predictable measure of the cash flow we generate from the portfolio.

Now, maybe one last point to call out is what are the expenses that we expense? Marketing is for example one of them, and that's one that has suffered strong inflationary pressures. Clearly, we talked it over the last at least two or three quarters.

Then, we have a number of fixed costs associated with the creation of our sales structure, associated with cars leased, for the cars that we equip our sales teams and installers to go to the premise and do the installation. It includes also overheads because our approach to CPAs is actually a fully loaded approach. It's not marginal costs. We closely look at overheads at the branch, at the country headquarter, at the group level, and look at how they split between our customer acquisition segment and our portfolio service business segment. Those rules don't really change, but all the expenses, all these overheads, cannot get capitalised.

Hopefully, that covers the questions you had. Net, the reason of the percent of capitalisation has not changed, the rules have not changed. The reason why for instance, if you look at the CPA cost that got capitalised, we are at 39% this quarter versus 43% in Q1 2021, just has to do with the change in mix of the different spend pool between those that can be capitalised versus those that cannot. Is that making sense?

Paul Brennan

Yeah, that's all very helpful. Thanks very much.

Vincent Litrico

You're welcome.

Operator

Our next question comes from the line of Michael Hemmings from CVC. Please go ahead.

Michael Hemmings

Hi, there. Thanks for taking my questions. I had a quick one on the CPA, given the increased supply chain difficulties that have come to the back of the Ukraine crisis and trying to look down, to particularly, in Q2, I was just wondering if you could directionally give us some colour in how you're viewing that in Q2, and beyond to the rest of the year.

My second question is, regarding the other payables inflow that we saw in the Q1 results, can you just provide a little bit of colour on what that was and if we're expecting that to reverse in the coming quarters? Thank you.

Austin Ally

On the CPA topic. The first thing I'll say, most definitely in the quarter, when it comes to overheads, for example, in overhead allocation, there's definitely a hit there because some of the hiring that we restarted through 2021, it's obviously not in the year-on-year comparison to Q1 last year. Obviously, as we move through the year, that overhead is going to start to anniversary, and so that will help us.

I think the big topic in the quarter isn't overheads, actually. In fact, the volume of sales is up, so in fact, that's clearly a help there on spreading cost. The topics are really material costs increases, and marketing costs increases, which Vincent mentioned in his presentation. Without getting super specific on the absolute change, both of them basically are increasing year on year. If I split them, I don't expect the material cost to really mitigate much through the course of the year, just given that we continue to see tight markets. For us, I think you'd make the same decision in our shoes, we've prioritised supply and making the sales versus, for example, trying to somehow pass on opportunities to sell because we don't like the cost of components.

We've been prepared to take higher material costs, because we're still creating very high value customers. I think we will see the supply situation improving in the second semester, but it will still come at a higher cost than last year. That's inevitable. I think our marketing costs, which was also up in the teens, I think that's a more fluid situation. There's clearly some changes in the marketing environment versus last year, which are affecting everybody. You think of some of the Apple privacy changes, changes to cookies, some changes in algorithms on platforms. We've got a range of initiatives underway in the company to try and address that. Basically, to try and optimise our digital costs.

If you think about the cookie regulations for example, we're working now on first party consent, we're working on server-to-server connections to try to get the targeting accuracy up compared to what we lost. We're working on joint business plans with Google and Facebook. We're also making our creatives work harder. We've launched new creative campaigns in our biggest markets which we think are actually going to get us more bookings, more demand from the same investment.

We're also looking at new marketing channels, which are actually outside TV, and outside of the GAFA. I think the UK is an example. We're working very well with Nextdoor as an app, we're testing TikTok, we're looking at Snap in France, we're exploring new partnerships across the company to get leads.

We're also diversifying, in a way, our go-to-market approaches, month on month. We have a very strong partnership, for example, in Spain with Caixa. What we see in this current pressured market is the importance of the push efforts that you can execute with partners like that. We've got quite successful tests taking place, and right across the company, actually, different companies on retail. You'd be surprised, actually, that that's something where we've historically never really put emphasis, and we're now demonstrating that we can actually get some volume.

So net, on the cost of marketing per sale through the year, I'm working to try and make it as efficient as possible, whether I can bring it down from what we saw in Q1 remains to be seen, but what I will just reinforce, as we said earlier, these investments decisions are deliberate. Even the CPA entries that we saw in Q1 are still associated with very, very high value customers coming in. If I have to invest at that level for the rest of the year, I am prepared to do so. But we obviously work very, very hard the whole time to get more efficient.

Vincent Litrico

Now, let me take the second part of the question on payables. You should look at it in two different buckets. You've got trade payables, which were a negative 60 million on the quarter, which is the same as a year ago.

Trade payables tend to evolve within a tight range of 5-7% of revenue, quite consistently, and so we don't expect this to be different in the future. That equates to roughly 30 days of trade payables. I think your question is probably on the second bucket, which is other payables, which contributed positively by 62 million in the quarter. What we have here is a combination of four things. If I peel the onion further here, you've got customer prepayments, employee accruals, some supplier advances and other costs.

If I start with customer prepayments, our customer join us on different pay plans. Most of them pay on a month-by-month basis, but we also have customers that pay three months in advance, some one year in advance. We actually even have customers that pay all the way to three years in advance. It's a mix that can fluctuate from month to month, quarter to quarter, depending on the module customer intake. Basically, depending on the type of payment plans that they choose at the point of entry in the portfolio.

Likewise, employee accruals can fluctuate a little bit month to month, as well as other accrued costs. This has been a positive contributor historically, we've had favourable working capital evolution from what we call other working capital. If you put aside the usual inventory, trade receivables and trade payables, you're left with the big other bucket, which is mainly made up of the other payables I listed before, as well as some other receivables, mainly prepaid costs, accrued income and prepayments to suppliers.

This one has actually been a positive contribution to cash flow, that more than offsets the cash flow investments needed to support the business when it comes to trade working capital. The other working capital has been consistently favourable, and yes, 62 million positive this quarter in other payables, this may fluctuate up or down.

As you know, I cannot give you specific guidance on what to expect going forward.

I think the key point I want to call out on overall working capital, though, as we did in the last two-three earnings calls, is that we are deliberately dialling up inventory in the context of tight supply challenges, which we worked through. As we said, we expect the situation to ease a bit in the second half of he year. We also have this major phase-in phase-out plan towards our new technology stack, which we call Moonshot. Obviously, we don't want to take any chance here on that front. I think you should expect, as we said before, inventory not to show substantial improvements in 2022. 2023 might be a different story, but right now, we want to protect the business and make sure we don't run out of stock.

Michael Hemmings

Okay, all understood. Appreciate the colour. Thank you.

Operator

The next question comes from the line of David Alty, from Arcano. Please, go ahead.

David Alty

On the average upfront cost to the customer, it's come down quite a lot, not just year on year, but versus 2019 and earlier as well. Is it a mix? Is it a type of customer demographic or is it the level of product that these people are getting? Is it purely you guys are happy to take a bit more of the cost yourself to grow the business?

Secondly, if I look at your deleveraging profile for the past few quarters versus historically, it's also quite a bit slower. I appreciate there's some kind of one-off type stuff in this, but how are you guys thinking about this? Does it call into question how much you'd be willing to, say, dividend out in the future given it's deleveraging more slowly or are you relatively comfortable at this level, it should come down in the next few quarters?

Vincent Litrico

The first question around the upfront, so it's evolving within a range. The first objective of the upfront is to qualify the customer. The upfront price that the customer has to put on the table is one element, but that's, actually, not the only one. We have experience in countries where through various techniques we've refined over the years, customer profiling, scoring, making sure that we are deliberate in terms of which pond we go to fish, and all customers or prospects are not all born equal. We are very attentive to ensure we don't take on board onto our portfolio customers that may not have the ability to actually afford us.

We have countries where we have great experience of slightly lower upfront, but higher cycle fees. There's also an element of balancing depending on customer preferences. It varies quite substantially by country. In some countries, the reference point for customers are the old days of electrician installing, putting wires and drilling holes to install alarms that would come at a cost of sometimes €5,000+, so way more than the democratised model we've implemented. In some countries, the reference point is quite high, and actually we extract easily €1,000 upfront from our customers.

In other countries, the reverse. Customers are willing to actually pay a higher cycle fee every month, but are more cautious about the upfront investment they need to make. For us, the barometer here is ensuring that we have good quality customer intake, that we don't compromise on that, and that can take different shapes and forms.

Austin Lally

I think maybe just to add here. I think the big picture on this one is that Verisure obtains a relatively high upfront from the customer. Now, you're looking on average through last year, it was kind of in the 450-480 type range per installation. Yes, it will fluctuate up and down based on some of the factors that Vincent talked about, but the big picture is actually, we get a higher upfront from the customer, and that's actually quite differentiating in the industry.

There are other players, for example, who are giving away, for example, the equipment for free in many situations, and trying to compensate, therefore with an onerous contract, trying to lock the customer in. We think that that approach, overtime, is associated with significantly higher attrition, because the customer isn't personally invested in the system. Maybe another way to put this point is that we actually don't view the upfront so much through the lens of CPA. Yes, it helps, of course, to defray some of the acquisition costs, but we're not looking at the upfront commodity as a CPA lever, we're actually viewing it as a customer quality indicator lever.

Vincent Litrico

We also have the obvious mix impacts, geographic mix that can lead to fluctuations of plus or minus up to €50, €100 actually. And FX changes, as well as channel mix, that can get in the way, or introduce a bit of noise on that metric.

David Alty

Okay. Fair enough.

Vincent Litrico

Yes. So on leverage, indeed, we acknowledge that the leverage has been flat for a few quarters now for various reasons.

There are two elements that explain the results we've posted. It's actually not so much on the net debt front. Net debt has increased a bit, due to the working capital dynamics we have discussed. In particular, inventory, that I mentioned before, which we're doing very deliberately and for good reasons. The lion's share of the explanation as to why leverage hasn't improved as much as what you've been used to, and we've been used to, is related to the denominator, to EBITDA. Here, specifically, you've seen that portfolio EBITDA continues to be very strong, very healthy, strong margin despite the high inflationary backdrop we operate in.

But the impact has been in the customer acquisition EBITDA side. Again, going back to the point I made on this big chunk of customer acquisition cost that we cannot capitalise. This one has been the most affected by the inflationary pressures, and yet, not being helped by the upfront due to the point we just discussed, as we didn't push up upfront as much. That has been dragging a bit total adjusted EBITDA margin, and as a result, has also put some more pressure on the natural deleveraging we normally deliver.

Now, looking forward, again, we tend to not want to give forward looking guidance, we expect to get back to our more usual deleveraging trajectory over the rest of the year.

David Alty

Okay, great. Thanks very much.

Operator

The next question comes from the line of Guillaume Bertin from Investcorp. Please, go ahead.

Guillaume Bertin

Hi, thanks for taking my questions. Actually, most of them have already been answered, but I was just wondering, maybe in terms of the second last one, consumer behaviour. What are you seeing maybe at the moment, maybe in terms of volume of customer acquisition, or churn in the light of the increase in cost of living? Are you seeing a change in the behaviour of customers?

Austin Lally

No. I would say no material change. We've clearly had to invest a bit more to deliver the booking volumes and sales, but we're still growing really well. When it comes to customer behaviour in the portfolio, again, what you see here is no material change in attrition.

I mentioned we take pricing in Q1. We usually get an increase in cancellation requests when we take a price increase. We have a very high save rate when we have those conversations with customers. I think what we noted in Q1 is that the elevation of cancellation requests certainly lasted a bit longer than we would've seen in a lower inflation environment, but the save rate has been very, very high. Therefore, you don't see a material change in attrition.

I think that that speaks to the robustness of the portfolio and the business model. Maybe it's also just worth commenting on the acquisition point. Penetration remains very low in Europe. This is far from being a mature industry, and, therefore, even in a more difficult economic context externally, there's still an awful lot of headroom and runway for Verisure to grow. I think our results from Q1 confirm that.

Guillaume Bertin

Then just on the last comment about the deleveraging trajectory. As you said, leverage has been quite flat now for a few quarters, and it seems that you expect at some point the deleveraging to resume. What would be the key lever that could enable this to happen, you think? Is it more of the cash generation side of things, or is it more maybe accelerated EBITDA growth?

Vincent Litrico

It's a combination of both things. Portfolio EBITDA has been stepping forward like clockwork. On the customer acquisition EBITDA, so still focusing on the denominator of the leverage metric, we've are seeing the cost of marketing starting to level off a bit. We'll see where that goes.

Now, I think the one piece to call out is working capital, and Inventory in particular. We' not trying to be pennywise and on this one. I'm not going to give you specific guidance. But clearly our trajectory, our plan, our forecast today is that we're going to start posting again, deleveraging. This has been an integral part of our model so far.

Guillaume Bertin

That's great, thank you. One last question, if I may, but from a reputation standpoint. There's been some negative press coverage in Sweden, and I understand, maybe an investigation has been launched on this case. How have you been managing the situation there and what are the actions you intend to take to protect privacy further within the organisation?

Austin Lally

We were very disappointed with this coverage because we certainly don't recognise ourselves in this coverage. We obviously respect the right of journalists and it's a free press to receive reports and allegations and to report them. But we don't recognise ourselves or our processes or systems in there. We've made that super clear in all our responses in Sweden.

First, in terms of our own internal investigation, we've completed that. We're now finalising the report. Our conclusion following the completion of this investigation is that we do not find the substance to support those allegations that were made.

As far as the follow-up investigation by the regulator, our firm aim is to have this investigation closed without material findings against the company or any fine. I think based on the facts available to us today, we think there's a fair chance that a fine can be avoided altogether. That's also been confirmed by our external privacy counsel. As a specific example, our systems, if you take images on our systems, they're actually kept on a secure system. All the activity on that system is logged. The images are actually removed from that system after a period of time. They're not there indefinitely.

As we've gone through, for example, log records on access to images, we've found nothing in our internal investigation that would support privacy breaches. That's why we say we just don't recognise ourselves in this. We have to get back to communicating what we do best, which is that we protect families and small businesses, but that we're the leader in Europe at doing this. Not only are we the biggest and the fastest growing, but we think we do it the best. We're people that protect people.

Probably the saddest thing about the Swedish media coverage is the effect it has on our people. Because the men and women that provide our service, the people that work in our monitoring centres, they're very proud of what they do. They are dealing often with serious incidents. Remember, every single day what we're trying to do in those monitoring centres is we're trying to balance privacy, and doing what we have to do to protect people. That's the very essence of a monitoring centre.

Guillaume Bertin

I get it. If I get you right, at the moment, you don't expect to make a provision in relation to this story.

Austin Lally

Correct.

Guillaume Bertin

Okay. Thank you very much.

Operator

The next question comes from the line of Preeti Agarwal from Black Diamond. Please go ahead.

Preeti Agarwal

My question is around cancellation rates. I appreciate that it's still below 6.5%, but last couple of quarters, it has been low, around 6.4 and overall, if I compare it to 2019 levels, it is still quite high at 6.5. My question was, do we see this rate to be high in quarters ahead, or was this a one off? If so, why?

Austin Lally

I think what you need to remember is it's a rolling 12-month metric. For example, Q1 historically is the quarter when price increases get executed. That last 12-month rolling average will obviously fluctuate depending on the particular quarter that you're in.

Preeti Agarwal

So, you're saying this is a one-off impact because of the price increases?

Austin Lally

No, I'm not saying it's a one-off impact. I'm saying that when you look at the attrition performance, it rolls through the year because the price increases are not constant through the year. They're concentrated in the first quarter. Actually, I think 6.5% as an absolute level is rock solid. As I pointed out in my remarks, we've been for many years below 7%. We have seen, for example, the attrition fluctuate. We've been at 6.3, we've been at 6.5, but I think that range is something I'm very comfortable with.

As a company, probably the important point is it shows how differentiated we are, because I think, without commenting on global competitors, if you look at the attrition profile of some of the publicly traded security companies, for example, around the world, like North America, this Verisure attrition level is much, much lower.

Preeti Agarwal

Understood. Actually, my only concern was because if I see the cancellations in absolute terms, the absolute number of cancellations is quite high in the quarter. If I see 75.7 versus, I compare even in 2021 or 2020 when we saw some part of COVID impact. Is there a reason that it's this high, was my concern? Also, if in quarters ahead, do we see it going down?

Austin Lally

I think when you look at the absolute number, you need to recognise that the portfolio is getting much bigger. That's why we look at it in percentage terms, because obviously if you have 4 million customers, it's a very different thing to having 2 million customers.

Preeti Agarwal

Understood. Got it.

Austin Lally

Yeah. Thank you.

Operator

The next question comes from the line of Miquel Lluesma from Bain Capital. Please go ahead.

Miquel Lluesma

Hi, thank you for the presentation. Following up on the reports from Sweden and the problems there. Are you seeing any changes in attrition levels there?

Austin Lally

No. I would say as of today, nothing material. We've certainly had telephone calls from customers looking for reassurance. I think our team in Sweden have done a magnificent job. This was kind of like weekend work. This was a lot of overtime. This was a lot of people from different departments in the company managing the phone lines to be able to give the right perspective to customers. I think one of the things that's obviously important here is that historically Sweden was one of the portfolios that actually had the lowest levels of attrition in the company. Very sticky, very loyal, very long-established customers.

Miquel Lluesma

Okay. Thank you very much.

Operator

And we just have a follow up from Paul Brennan from GoldenTree. Please go ahead.

Paul Brennan

Hi. Just a quick one on that investigation in Sweden. I know you said that you didn't expect to have to pay any fine, but I'm just wondering, has there been any range of potential fine outlined by the regulator or anything like that?

Austin Lally

No. I would say that the investigation is at a very preliminary stage. Certainly, that would never be the process. What has happened here is that a series of quite serious allegations made in a high circulation newspaper. This is obviously going to prompt the regulator to ask us for the facts. That's what we're doing. We're sharing them what we think the actual facts are. We welcome the investigation because it's an opportunity actually for us to formally clear our name.

Paul Brennan

Understood. Thanks

Operator

As there are no further questions, I'll hand it back to the speakers.

Austin Lally

Well, thanks everyone for the questions. Actually, that was a good session. Hopefully you got the information from us that you needed. I do want to thank you all for participating on the call, but more importantly for the continued interest that you show in the company and the support that you've given us historically in the credit markets.

We remain, as we've said in previous calls, fully aware that these are serious times. We've now got war in Europe, we've got COVID continuing to be a factor in different parts of the world and as we've discussed this afternoon, we've got inflation higher than in our recent past. But we remain a serious company in serious times. We acknowledge that we have a responsibility to our employees, our customers, our investors, and other stakeholders like police and fire services.

Our service levels remain high. The portfolio is robust. Our new sales performance is strong. Our financial delivery is strong, and we've just delivered another strong quarter, both operating and financially. We've set new records again for portfolio and performance metrics.

We continue to believe the future is bright for us, and the opportunities are there more than ever. Penetration in our geographies remains low. We believe that the fundamental customer need that we serve, which is peace of mind, will only increase in the future. That's our aspiration. We want to build Europe and Latin America's number one peace-of-mind platform.

Our intention as a company remains the same, which is to serve more customers, to serve them better, to continue to innovate, to continue to grow, to develop our talent, to reinforce our culture, to be an effective contributor to a more sustainable future, to become stronger, leaner and more effective. In a world that is more volatile and feels less safe, we want to leverage our unique strengths and assets to deliver differentiated value creation for our investors.

Again, in closing, I want to thank you for your interest and support and for the questions today. We look forward to talking to you again in a few months when we can bring our second quarter results to you.

Operator

This concludes our conference call. Thank you all for attending. You may now disconnect your lines.