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PMTS - Q4 2015 CPI Card Group Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen and welcome to the CPI Card Group Inc. Fourth Quarter 2015 Earnings Conference Call.

At this time all participants are in a listen-only mode. (Operator Instructions)

As a reminder this call is being recorded. I would now like to introduce your host for today's conference, [Will Mania] from [ICR]. You may begin sir.

Will Mania - *ICR*

Thank you, operator. And good afternoon, ladies and gentlemen. Welcome to the CPI Card Group Fourth Quarter and Full Year 2015 Earnings Conference Call. Participating on today's call from CPI Card Group are Steve Montross, President and Chief Executive Officer and Dave Brush, Chief Financial Officer.

Before we begin, I'd like to remind everyone that this call may contain forward-looking statements as they are defined under the Private Securities Litigation Reform Act of 1995. Please refer to disclosures at the end of the Company's Earnings Press Release for information about forward-looking statements that they may be made or discussed on this call.

The earnings press release is posted on CPI's web site. Please review information along with the filings with the SEC and [CEDAR] for a disclosure of the factors that may impact subjects discussed on this call. All forward-looking statements made today reflect our current expectations only and we undertake no obligation to update any statements to reflect the events that occur after this call.

Also during the course of today's call, the Company will be discussing on or more non-GAAP financial measures including EBITDA, adjusted EBITDA, adjust EBITDA on margin, adjusted net income from continuing operations, pro forma diluted earnings per share, adjusted diluted earnings per share from continuing operations, [bank accounts] and currency. Please see the earnings release on CPI's web site, the disclosures by the SEC -- for the required disclosures by the SEC including reconciliations to the most comparable GAAP numbers.

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On this call and we may also be referencing certain industry and market data included in our initial public offering prospectus, which was derived from a report prepared by First Annapolis Consulting. For additional information, please see our prospectus filed with the SEC on October 9, 2015.

And now I'd like to turn the call over to Steve Montross, President and Chief Executive Officer.

Steve Montross - *CPI Card Group Inc - President and CEO*

Thanks, Will. And thank you, everyone, for joining us today for our Fourth Quarter and Full Year 2015 Earnings Conference Call. Our fourth quarter results kept a great year for CPI Card Group and demonstrate the strength of our business model and solid execution by our entire team.

In 2015, we continued to advance our leading position in the U.S. financial payment card market by executing the growth strategies we discussed with you during our initial public offering and on the third quarter 2015 earnings call. Let me share with you some highlights from the year. Net sales for the full year 2015 were $374.1 million, an increase of 43.3% year-over-year. Adjusted EBITDA was $96.2 million, up 77.5% over 2014 and adjusted net income from continuing operations was $47.3 million or $0.083 per share more than doubling our 2014 adjusted net income.

In addition to our strong revenue and earnings growth, we also reached a significant milestone in our Company's history when we completed our initial public offering in October. Our success in 2015 is made possible by all of CPI Card Groups nearly 1,400 employees, and I want to thank each of them personally for their dedication and continued hardwork.

I'm also pleased to announce that today our Board of Directors initiated a quarterly cash dividend of [$0.045] each share which amounts to just over $2.5 million per quarter which is consistent with our discussions during the initial public offering process. The initiation of quarterly dividend reflects CPI's significant cash generation capabilities, our strong balance sheet and our ability to sustain growth with relatively low incremental capital requirements. It also reflects the confidence with our Management and Board have in our long-term growth prospects, as well as our commitment to enhancing total shareholder value.

Before turning to a review of our quarter, I would also like to highlight that we recently strengthen our board of directors with the addition of two new members. Diane Fulton joined our Board in December of 2015 and Doug Pearce joined in January of this year. Diane is the President and Chief Investment Officer of the Vancouver Foundation. Doug was the founding Chief Executive Officer and Chief Investment Officer of the British Columbia Investment Management Corporation, one of the Canada's largest institutional money managers.

We expect CPI to benefit greatly from both Diane and Doug's wealth of experience and insights. Now, on to some highlights for the fourth quarter and a review of our segment performance, for the fourth quarter, our net sales were $93.6 million which was 6.5% increase over the prior year period. Adjusted EBITDA was $21.8 million, a 20.8% increase over the prior year period and adjusted net income from continuing operations was $8.8 million or $0.016 per share on a pro forma basis up 7.6% over the prior year period. Our fourth quarter results were driven primarily by our U.S. Debit and Credit Segment with the U.S. Prepaid Debit also contributing to our growth.

Turning now to our operating segments, U.S. Debit and Credit Segment net sales were $67.5 million for the fourth quarter, an 11.2% increase over the prior year period and segment EBITDA was $19 million, a 23.7% increase. The increases in revenue and EBITDA were predominantly driven by 21.3% growth in EMV card shipments to 38.9 million cards in quarter as the conversion of the U.S. market for magnetic stripe financial payment cards to EMV cards continued. Our EMV card sales in the fourth quarter were down slightly from the third quarter which was in line with our expectations and consistent with our comments in our third quarter earnings call.

After substantial purchases in the first half of 2015, many of the large issuers ease their pace of EMV card purchases through the second half of the year as they began working toward catching up their EMV card issuance activity to their card purchases. I'll discuss this further in a moment in the context of my view of current EMV market activity and expectations for 2016. For the fourth quarter, U.S. Prepaid Debit Segment net sales were $12.4 million, up 1.4 percent year-over-year and segment EBITDA remains flat year-over-year at $3.3 million.

As we discussed with you last quarter, volumes in this segment shift throughout the year reflecting the timing by Prepaid Program managers of product introductions and [refreshes] in management of their distribution channel. This volume shifts were more evident in 2015 as we experience

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the very strong first quarter [doing part] was significant number of replenishment orders from a large customer who depleted its distribution channel in late 2014 followed by a moderate second half of the year.

In the fourth quarter of 2015, our revenues in this segment were up slightly and our earnings reflect [compared] the same through in 2014 as good retail prepaid sales plus the customer base was offset by significant product launches and [refreshes] for two large customers in 2014 but were not replicated in 2015. We are very pleased with our full year 2015 results. The segment was up 11.1% in revenues and up 23.3% in EBITDA over 2014.

Finally, the U.K. Limited Segment Fourth Quarter net sales were $10.8 million, a 2.3% decline from the prior year period and EBITDA was $1.5 million down 2.4% year-over-year. It's important to note though that our U.K. Limited Segment results were impacted by a favorable currency exchange rate fluctuations and on a constant currency basis sales and EBITDA for the fourth quarter were up 1.9% and 1.8% respectively over the prior year period.

Loking ahead in 2016, we expect to continue to benefit from the ongoing conversion in the U.S. for magnetic stripe to EMV financial payment card. Based on recent industry studies, public commentary by the card brands and our own analysis, we estimate less than 50% of debit and credit card issued in the U.S. or EMV at yearend 2015. We estimate that approximately 25% of debit cards and 50% of credit cards have been converted to EMV by the end of 2015. So, debit EMV conversions to date have been low.

We currently anticipate EMV penetration will grow to approximately 90% of debit and credit card issued in the U.S. by the end of 2017. In 2016, we anticipate strong growth in EMV debit implementations and accordingly, accelerating demand for EMV products from our core small to mid-sized issuer market, which is heavily weighted to debit. At the end of 2015, we estimated less than 30% of small and mid-sized issuer market had converted their card portfolios to EMV.

As you know, we are the leader in the U.S. small and mid-sized issuer market and expect the benefit from this shift to strong EMV growth in the small and mid-sized issuer market in 2016. As the EMV conversions in the small, the mid-sized issuer market continue to accelerate, we expect a very strong second half in 2016 for EMV activity in this segment. It's a terrific opportunity for us. We anticipate continued steady demand for the large issuer market for EMV cards. The large issuers are ahead of the small to mid-sized issuers in terms of [post management] cards converted to EMV.

But in light of the overall market conversion levels, we believe that there's still remains significant EMV conversion activity ahead for the large issuer market. As I mentioned a moment ago, there was heavy EMV card [mine] by the large issuers in the middle of 2015 with the [pays] to purchases easing through the remainder of the year as the issuers work to catch up their card issuances with their card purchases.

We see this dynamic continuing into early 2016. We have reasonably good visibility into the overall EMV demand by large issuers in 2016 which gives us confidence in our growth projections for the year. But the current dynamic in the large issuer market leaves us to expect that EM -- that the EMV activity with the large issuers will be weighted to the second half of the year.

We've also discussed previously the growth opportunity associated with the issuance of dual interface EMV cards. Following this initial conversion to EMV cards in the marketplace, we expect a second conversion for a portion of the market to dual interface or what we call tap-and-go cards. We are seeing increase activity with dual interface. We recently [won] a pilot with a major issuer, the manufacturer personalized and fulfilled dual interface cards and we're working with a number of other issuers to get dual interface products into their product roadmaps.

With the continued build out of the point of sale terminal infrastructure to accept and pack this transactions and the consumer use case for dual interface card strengthening whether it's for transit applications, faster payment experience or [into] your substitute for cash. We expect to see increasing dual interface card issuance starting from a low level in 2016 and growing to a more meaningful market penetration over the next few years.

With respect to prepaid, we anticipate continued health demand in the retailed prepaid [sharing] and we're very excited about the [sworn] growth prospect in our significant growth opportunity in the [B to D] and [B to C] channels of the prepaid market. The prepaid market is a strong segment

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for us and we'll continue to be an important growth driver for the business over the next several years. Focusing for a moment on the service side of our business, we continue to see strong demand for our card services solutions into 2016.

We ended 2015 with over 4,000 [installation lists] or what we call card at once installations which was double our installed base at yearend 2014, and that momentum has continued into this year.

We are also seeing strong customer activity in our card personalization and fulfillment services and security packaging. Our service revenue were up approximately 30% in 2015 over 2014. Our overall service revenue in the fourth quarter of 2015 year-over-year but the growth was [meshed] by the closure of our card services operation in Petersfield, U.K. earlier in 2015. Within our services business, we experience strong growth in our personalization and fulfillment services in the fourth quarter of 2015.

As we've discussed previously, our services business is an important focus in growth avenue for us and we expect to continue to realize substantial benefits from our broad and robust service offerings which we further enhanced through the acquisition of the [FT] source.

In conclusion, I'm pleased by our fourth quarter and full year 2015 results. Our story is the same was what we have previously discussed [sound] into industry fundamentals and strong markets in which we are well positioned to continue our strong growth trajectory. In 2016, we will remain intensely focus on the execution of our growth initiatives.

We expect to grow as our customers in markets grow, driven by powerful secular tailwinds, increased our share of our customer's wallets through cross-filling our robust suite of products and services, growth and focused innovation and development of products and services grow by broadening our market reach and to do attractive market verticals and grow through selective strategic acquisitions.

I'm excited about the opportunities available to us and confident, we are well positioned to capitalize on those opportunities in 2016 and beyond. I'll now turn the call over to Dave who will take you through our financial results in more detail and discuss our 2016 guidance.

All right, Dave?

David Brush - *CPI Card Group Inc - CFO*

Thank you, Steve, and good afternoon, everyone. I will begin by summarizing the results of our fourth quarter and full year 2015. I will then provide our current guidance for full year 2016 before opening the call for questions.

Fourth quarter net sales were $93.6 million up 6.5% from $87.9 million in the fourth quarter of 2014. When factor in the Petersfield closure of the Q4 net sales, we're up 9.5% in 2015. Our net sales for this quarter continued the benefit from the ongoing conversion in the U.S. financial card payment space from magnetic stripe cards to EMV chip cards. Fourth quarter products net revenue grew 10.9% year-over-year to 63.3 million.

Service net revenue declined 1.7% year-over-year to 30.3 million in the fourth quarter primarily due to the closing of our Petersfield, U.K. operation in Q3 2015 which made an upset, the growth in other areas.

For the full year 2015, our service revenue increased by 30.2% driven by strong demand for a value-added services including card personalization, fulfillment, packaging and our card at one solution. Looking to 2016, we continue -- we expect demand for these services to remain robust. For the yearend at December 31, 2015, net sales were $374.1 million, an increase of a $113.1 million or 43.3% over the prior year. Gross profit for the fourth quarter grew 7.4% to $31.4 million representing a gross margin of 33.6% compared with gross profit of 29.3 million and a gross margin of 33.3% in Q4 2014.

For full year 2015, gross profit was $135.8 million or 36.3% of net sales compared with 31.3% in 2014 which represented a 66.2% year-over-year growth. Income from operations in the fourth quarter was $10 million compared with $11.2 million in the prior year period. Higher stock-based compensation expenses including a $6.9 million charge related to the full settlement of our Phantom Stock Plan, an incremental cost associated with operating into public company offset revenue and gross profit in the fourth quarter.

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For full year 2015, operating income with $67.7 million, an increase of $33.2 million or 96.4% from $34.5 million in the prior year. We reported a net loss from continuing operations at $1.6 million or $0.03 per share in the fourth quarter of 2015 compared with net income of $5.6 million and a loss of $0.017 per share in the fourth quarter of 2014. Note that our 2015 Q4 net loss from continuing operations reflect the impact of $4.7 million or $0.06 per share of accelerated amortization of debt issuance cost and discounts primarily related to the repayment of $112.5 million of debt using proceeds from our IPO.

A charge of $6.9 million or $0.08 per share related to the settlement of our Phantom Stock Plan and $1.5 million or $0.03 per share of one-time tax expense items including an NOL valuation allowance related to the Petersfield operation that closed in 2015 and prior year returned the provision adjustments.

For full year 2015, net income from continuing operations was $31.3 million, an increase by $15.3 million or 95.7% over the prior year. Earnings per share reflect a deduction for the first stock dividends that [accrued] in the related quarter. Important to note that the first stock is fully redeemed in Q4 2015 and there will be no further impacts in 2016.

Now, turning to our non-GAAP financial measures. Adjusted EBITDA for the fourth quarter of 2015 was 21.8 million representing a 20.8% increase over the 18.1 million reported in the fourth quarter of 2014. Adjusted EBITDA margin was 23.3% in the fourth quarter reflecting an improvement of 280 basis points over the prior year for the quarter. Adjusted EBITDA margin of 20.5%.

For full year 2015, we generated adjusted EBITDA of 96.2 million representing an increase of 77.5% versus the prior year. Full year 2015 adjusted EBITDA margin was 25.7% up approximately 490 basis points with 20.8% in the prior year.

Adjusted net income from continuing operations was 8.8 million for the fourth quarter of 2015 representing a 7.6% increase compared to 8.2 million in the prior year period driven by the factors I previously mentioned.

For full year 2015 adjusted net income was set to 47.3 million, an increase of 107.6% of the prior year. Giving pro forma back to our issuance of 15 million shares of common stock in the IPO. Adjusted, diluted earnings per share from continuing operations in the fourth quarter of 2015 were $0.16 compared to $0.14 in the prior year period.

For full year 2015, pro forma adjusted diluted earnings per share from continuing operations were $0.83 compared with $0.40 in the prior year. Our adjusted EPS from continuing operations using actual weighted-average diluted shares outstanding was $0.16 and $0.20 for the fourth quarter of 2015 and 2014 respectively and $1.05 and $0.55 for the years ended December 31, 2015 and 2014 respectively.

These diluted per share amounts do not reflect the impact of preferred stock dividends, which are recorded as the deductions from net income from continuing operations and computing basic and diluted earnings per share amounts in our financial statements.

With the reduction of the Series A Preferred Stock in the third and fourth quarters of 2015, the Series A Preferred Stock no longer have this effect on the company's financial statements beginning with the Q1 2016.

Our effective tax rate in the fourth quarter is not comparable to the 36.3% rate in the fourth quarter of 2014. The small loss from operations during the period generated in that net tax benefit that was more than offset by the 1.5 million tax dispense items recorded during Q4 that we treated as an add back and rising at adjusted net income from continuing operations.

Moving to key cash flow and balance sheet items. Cash flow from operations for full year 2015 was 43.9 million compared with 26.6 million in the prior year and representing operating cash flow conversion of nearly 100% of adjusted net income.

Capital expenditures in 2015 were 18.7 million yielding free cash flow defined as cash flow from operations less capital expenditures with 25.3 million up from 9.7 million in the prior year. We can add that to one time 13.9 million payment associated with the Phantom stock reduction of free cash flow for 2015 full year with 39.1 million. We ended 2015 with the cash balance of 13.6 million with total debt outstanding was 309 million net of deferred financing cost and discount.

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As a reminder, we use the proceeds from the October 2015 IPO to repay debt of 112.5 million redeeming all of the remaining Series A Preferred Stock Outstanding and repaying the company's liability under its Phantom Stock Plan.

During the fourth quarter, we paid down an additional 10 million of the term loan debt and cash generated during the quarter. At December 31, 2015, our net debt leverage ratio was 3.2 times compared with 4.5 times at the end of the third quarter. As of December 31, 2015, we had approximately 53.5 million of available liquidity comprised of 39.9 million [undrawn revolver] and 13.6 million of cash in the balance sheet.

We will continue to be committed to maintaining the strong liquidity. The initial quarterly dividend that we announced [definitely] today of $0.045 per share is payable on April 7, 2016 to stockholders of record at the close of business on March 17, 2016.

On an annualized basis, the dividend represents a 2.4% yield based on today's stock closing price, but the quarterly amount of $0.045 per share equates to 10.2 million annually and is consistent with the amount that we indicated during the IPO process.

Now, turning to our 2016 guidance. In 2016, we continue to expect the benefit from the ongoing conversion in the U.S. Financial Payment Card Space from magnetic stripe cards to EMV chip cards. In addition to ongoing demand from the large issuer market, we anticipate strong demand from our core, small and midsize customers that they accelerate the conversion of their debit card portfolios over the course of the year. In addition, we continue to see healthy demand for our value-added services including card personalization, fulfillment packaging and card solutions.

For full year 2016, we currently expect net sales between 431 million and 445 million representing growth of 15.2% to 18.9%. As is typical for business, we expect higher net sales in the second half of 2016 versus the first half. The weighting of net sales to the second half in 2016 will be driven by the prepaid business, which has historically been a second-half driven business in the ramp up of the small and midsize issuer market conversions to EMV, which we expect to be more significant in the second half of 2016.

Further and as Steve mentioned, the first half of 2016 will be influenced by the large issuer market as they catch up their issuances to the purchases made in 2015. We would expect the Q1 net sales as a percentage of the full year to be roughly similar to that of Q1 2015.

For full year 2016, we expect currently to generate adjusted EBITDA between 111 million and a 116 million representing growth of 15.4% to 20.6%. Within the range of guidance, the adjusted EBITDA is a percentage of net sales representing improvement to approximately 26%. Further, I'll point out that the guidance reflects -- the guidance range reflects increased expenses associated with our being a public company.

We expect full year 2016 pro forma adjusted diluted earnings per share of $0.92 to $0.97 representing a growth range of 10.8% and 16.9%. We provided Exhibit F in the earnings announcement that breaks out the amount and description of the non-GAAP adjustments we expect for 2016 from both adjusted EBITDA and pro forma adjusted EPS.

Finally, I would like to point out that the 2016 guidance does not reflect any acquisitions so the guidance just reflects organic growth. All the free cash flow after paying the dividend announced today of 10 million under the guidance ranges is assumed to go to our [staff] reduction.

With that operator, please open the call for questions.

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

And our first question comes from the line of S.K. Persadbora from Goldman Sachs. Your line is now open.

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S.K. Persadbora - *Goldman Sachs - Analyst*

Thanks Steve, Dave. Thanks for taking my question. Good [quarter] and guidance.

Probably to start off, how should we think about the growth coming from different segments of U.S. and U.K. [full Q]? It does seem like U.K. was slightly better than expected and probably there were some pricing pressure as this U.S. large issuer market is concerned so how should we think about estimates for 2016 in terms of the split and cross-segments?

David Brush - *CPI Card Group Inc - CFO*

Yes S.K. This is Dave. Thanks for calling in. You know, I think the significant growth in the -- in the year is going to come from, you know, a combination of the -- the product business and the -- and the services business and, you know, we -- well in the guidance we don't break out that individualing or the individual reporting segments, I think I would -- I'll give you some broad ranges on how to think about the product and service split and that, you know, I think within the guidance range we would see, you know, sort of 15.8% to 19.6% growth in the -- in the product business to roughly 14% to 17% growth in the -- in the services business.

You know, obviously the -- the majority of the growth that we expect in 2016 is going to come from U.S. debit and credit. I think prepaid a little bit flatter under the guidance ranges in U.K. and the other segment, you know, sort of low -- low single digits in terms of what our growth percentages would be.

S.K. Persadbora - *Goldman Sachs - Analyst*

Okay. That's great. And with regards to the CapEx, it seems a bit higher than expected, is it something we should be investing in terms of dual interface ramp up or is there something one needs to take note of because it seems like higher than expected and should we expect the trend to continue into next two years.

Steve Montross - *CPI Card Group Inc - President and CEO*

S.K. Persad, no, the -- it's not for dual interface specifically. We've made those investments over the past several years and so we really build out our capacity around for contact EMV as well as dual interface and we thought some of the overall build out and it wasn't specifically for dual interface, again, that was part of the investments overall over the last several years, but continued build out in 2015 as we -- we build out the capacity around EMV in particular, but also build out our personalization fulfillment capacity so those -- it was investments and services and then also investments around EMV [end-stage] study, the larger -- larger amount of CapEx in 2015 and then what we anticipate in 2016 and beyond and I think in previous discussions, we had signaled that we anticipated that CapEx is going to be about $12.5 million a year on a runway basis going forward and we feel good with that estimate.

S.K. Persadbora - *Goldman Sachs - Analyst*

Okay and just last one from my end, the deductions towards new market verticals or opportunities in new market verticals and also strategic acquisitions, given free cash flow is still pretty healthy, can you elaborate on some of those points or some of the areas, which you're looking at in terms of vertical expansion and also the strategic acquisitions. That's pretty much from my end. Thanks.

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Steve Montross - *CPI Card Group Inc - President and CEO*

Sure and again if I -- if I don't get everything then please -- please followup, but in terms of just market verticals you mentioned, we think we're really excited about some of the things we're working on around market verticals particularly in the prepaid space. We think that there is really growth gold opportunity there and so we -- we still I think feel really good prepaid overall.

We've got a great [rescaled] prepaid business, but we are very excited about this out-of-market verticals where we think we're going to see stronger -- stronger growth than what we're seeing in retail prepaid we'll see in these -- these other market verticals and so what we look into -- we will be making investments to address those -- those market segments and then also I think part of your question was just in terms of M&A or acquisitions and where we're going to be looking.

I think we had 74 services business is really, really important focus of ours and we will continue to really focus on building out services business than we are and the thinking is that -- that we already are a manager of secured data and so we have that trusted position with -- with the customers and we want to continue to really leverage that trusted position by having other data services that we can be providing to our customers. We like the nature of the services. They are very -- They are very scalable. Also, the speaking nature of those services and the recurring nature of that business we really like a lot.

So, we'll continue to really focus on personalization, fulfillment services. We'll look to add other services to our capabilities as well and we will also not necessarily around M&A, but we'll also look to continue to make some investments around mobile services and continuing to enhance our capabilities there, but I think our service business is that -- is an area of focus for us around M&A.

Around products, we have some exciting things going on around new product development and those are just investments we're making and not necessarily attached to M&A, but we're -- we're very excited about some of the new products that -- that we're working on that we would look to bring to the market some time this year or on to 2017.

S.K. Persadbora - *Goldman Sachs - Analyst*

Thanks Steve. Thanks Dave. Good quarter.

David Brush - *CPI Card Group Inc - CFO*

Thank you.

Steve Montross - *CPI Card Group Inc - President and CEO*

Thank you.

Operator

And our next question comes from the line of Paulo Ribeiro from BMO. Your line is now open.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

Thank you. Hi Steve. Hi Dave. Good quarter. Thanks for the guidance with 2016.

And, but looking at 2015 and Steve thanks for your comment and Dave on the EMV roll out, does it -- did it come as a surprise to you, you know, when you looked back and where we are today versus what was a -- what was expected is the first question.

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Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, I would say overall, you know, on a -- it's where things turned out was what we expected for the year. I think that the -- the difference was just the -- the order patterns that we saw in 2015. That was a little -- That was a little bit different than what we expected. We expected it was going to be acceleration as we got through the year and what -- what ended up happening was and 2015 was really dominated by the large issuers.

They were the ones that were really dominating the purchase activities around EMV in 2015 and I think the large issuers were really taking the position that they wanted to make sure they had assurance of supply and so there was heavy purchases by the large issuers as we got into the second quarter and then into the early third quarter and then after that heavy buying that those as I mentioned the [caseload] purchaser of those purchases started to ease off as we got through the rest of the year and then the large issuers really focus on catching their issuance activities off with their card purchase activities.

And I think if you -- in some of the comments from some of the other companies that have reported thus far, I think you got a sense of that from their comments as well that they were experiencing that same kind of market dynamic, but so if there was a difference that was it all. It wasn't -- It wasn't really a difference around where we thought the market was going to end up for the year.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

Perfect. In terms of looking at 2016 and then compare it with 2015, how -- how did pricing behave if we talk about volumes now in 2015 and does it, you know, could we not necessarily putting numbers, but given that the roll out in 2016 should weigh a little bit more towards the smaller medium size, which you -- you guys have particularly stronger presence, could the average the price, you know, look better on -- on 2016.

Steve Montross - *CPI Card Group Inc - President and CEO*

We think it will. What we saw in 2015 was that as the purchase business with the large issuers really ramp up and prices related to volumes so when the volume goes up, prices go down and so we saw that dynamic, also the competitive intensity in the market increase around -- around the large issuers, not the small, but around large issuers so we saw definitely pricing pressure in the marketplace and on average, our price went down.

In the third quarter, it was about $0.93 and in the fourth quarter, average price was about $0.87 and there's a -- and there's a difference there because our price that we were seeing from the large issuer was -- was around $0.85 or so that we discussed before in the price with the small and midsized issuer was over a dollar and so average price though was down around that $0.87 range and that's really indicative of the purchases that are being dominated by the large issuers, but we expect that as we get into 2016 and see the increasing activity with the small issuer that we're going to see a real moderation in -- in any kind of pricing pressure in the marketplace overall so average pricing we think is going to be relatively stable as the small issuers really step up and increase their activity in the market.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

Perfect. So a couple of last questions, one of them, speaking -- speaking of one [that we thought as], in terms of CapEx then and you refer them to guidance for 2000 and, you know, the 12.5 million go in for the next couple of years so you guys are at, you know, reach, you know, your [cruising] altitude in terms of EMV production, you invested where we saw along in 2014 and 2015 to ramp up that so you are where -- where you need to be in terms of EMV more specifically [right out] their CapEx might be as you put it out, the mobile, your products, prepaid, but the EMV you are where you want to be.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes. We end up. Yes, we are.

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We are where we want to be and -- and what we see if part of the question was where do we see spending the money going forward, I think we've seen really good growth in our personalization fulfillment business and it's growing. We're -- We're expanding our customer base and it's a -- that's an area of focus for us and so we'll continue to make investments around there. We'll continue to make investments in -- in our -- in our -- well like I said in our personalization fulfillment business.

Also, we will make investments is we are talking about in prepaid, we have we think some exciting growth prospects in some of the market verticals. We're going to be building on our capabilities to serve those particular market verticals because there are some unique requirements to serve those -- those market verticals. And so we will be making investments to make sure that we can really -- we can serve both segments.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

And what just -- just to clarify, so those are new verticals where you don't have a presence or not as strong as they can be, so this could be additional revenue stream for you down the road.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, it definitely will be. We don't have a strong presence. We're doing some business in those verticals but not nearly to the depth that we think we can and that's why we're really excited about it. It's some of the same customers that we're already serving, so we got really good relationships with them and it's a matter of really adding unto our existing capabilities to serve those other segments but it definitely is a revenue driver for us.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

Fantastic, thank you very much.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes.

Operator

And our next question comes from the line of Bob Napoli from William Blair. Your line is now open.

Bob Napoli - *William Blair & Company - Analyst*

Hi good afternoon. Just quickly, most of the questions were answered I guess, but the first quarter you would expect -- you would expect EBITDA margins to be lower than they would be in the second and third and fourth quarters primarily, right? I mean just top-line leverage.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes -- no, that's right Bob.

Bob Napoli - *William Blair & Company - Analyst*

Then just your discussions on the dual interface with the major issuer, is that -- is a one-off or is that unusual, what area of -- is it credit is -- maybe any color around that would be helpful.

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Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, Bob, it's credit. It's credit, it's the major issuer, it would be for a credit card.

Bob Napoli - *William Blair & Company - Analyst*

Okay, something like that could possibly get the market moving I guess and their --

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, there's a lot of discussion about that and people are getting ready because as we mentioned we're working with some of the large issuers to get dual interface products and their product roadmaps, and so they're putting their attention to it, they're looking at it. No firm plans in terms of rolling it out except AMEX has been issuing dual interface card.

We've been doing -- we've been producing dual interface cards for two customers but they -- it's low level, it's a low level of volume right now. But it is -- if people are looking at it and we think that this is a product definitely for the future.

Bob Napoli - *William Blair & Company - Analyst*

Thank you. I appreciate it.

Operator

And again ladies and gentlemen, i you want to ask a question, please press star and the one key on your touch tone telephone and that is star and the one key. And our next question comes from the line of Dave Koning from Baird. Your line is now open.

David Koning - *Robert W. Baird & Company, Inc - Analyst*

Yes, hey guys, thanks for taking my call. First of all good results, secondly, just magstripe card, I know a lot of the talk, the discussion has been around EMV. Do you expect magstripe card production to grow this year?

Steve Montross - *CPI Card Group Inc - President and CEO*

For the market or for us Dave?

David Koning - *Robert W. Baird & Company, Inc - Analyst*

Yes, for you. Do you expect it to be like flat, up, down, I'm just wondering just on magstripe in particular?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, we think that overall it's going to be down. It's the substitution of all by EMV for magstripe cards continues at a strong pace. Overall for the market but particularly with the small issuer market, we think that magstripe volumes are going to down year over year as we had that substitution effect.

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David Koning - *Robert W. Baird & Company, Inc - Analyst*

Okay, secondly, why wouldn't personalization services be up significantly next year because only 25% of debit is on EMV cards right now and that's probably just the bigger banks that even do their own personalization and now we're going to get this huge amount of (inaudible) that's starting?

Steve Montross - *CPI Card Group Inc - President and CEO*

Dave, sorry, you cut out. Could you repeat the question?

David Koning - *Robert W. Baird & Company, Inc - Analyst*

Yes, sure, it seems like all the data points are lining ups at the small banks are in the [infancy] of sending out the debit card. It just seems like you could grow your personalization like 100% next year just as these little banks start sending the cards out.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes and we do believe that we're going to grow personalization. First we're -- as I mentioned we're increasing our customer base and so we're seeing really good goals from there. Also, we -- the revenues from personalization of an EMV card are slightly higher than they are for magstripe card, so we're going to see a lift of revenues from doing the EMV cards to the magstripe card but also what's happening is there's again personalization business is the -- it's substitution where the issuer instead of issuing a magstripe card is now issuing an EMV card.

So there isn't this -- this surge where there's EMV on top of the magstripe volumes. There's a substitution that's going on, so yes, we will see an increase in our personalization fulfillment revenues from growth and customer base but also this -- this uplift that we get by doing EMV but it wouldn't be some exponential growth because EMV is going to be on top of everything else that we're doing.

David Koning - *Robert W. Baird & Company, Inc - Analyst*

Yes, that actually makes a lot of sense. I just kind of forgot about the substitution effect. And Dave, just one question on interest expense, I know this quarter there was a kind of that non-recurring card but what's the normalized like Q1, should we expect just over 5 million of interest expense and that kind of trailed off through the years you pay on debt?

David Brush - *CPI Card Group Inc - CFO*

Yes, a couple of things on that Dave. I think the first thing is I think the cash interest rates for the full year is, you know, call it 5.5% which (inaudible) and then we got this ongoing amortization of original issuance discount. And so I think one, we would -- we would love to see interest expense for the year be in the neighborhood of -- I'm just looking to get you the exact numbers, sorry Dave, at roughly 5 million a quarter which is [blended] to two and then the -- that the pay down of debt is largely in the second half of the year.

So you know, I think, think about it as 20 million throughout the whole year but that's going to include some additional one-time charge as we pay down significant amounts in the -- in the fourth quarter of the year. I think we reflected that on -- yes, on the exhibit F. So a 20 million - there's a million in the latter half of the year related to the write-off when we pay down the debts and then you have roughly the 19 million spread pretty rapidly across each of the quarter.

David Koning - *Robert W. Baird & Company, Inc - Analyst*

Okay, no that's great, thanks a lot.

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David Brush - *CPI Card Group Inc - CFO*

Yes.

Operator

And our next question comes from the line of Wayne Johnson from Raymond James. Your line is now open.

William Johnson - *Raymond James & Associates, Inc - Analyst*

Hi, yes, good afternoon. Is there any type of opportunity for dual interface or the actual EMV type of chip to be embedded on any of the prepaid card or some of these other product categories. And I apologize if you hit on this, I was -- I got dropped off and I just got back on, so if you could address that, I appreciate it and good results by the way [guys], so thank you for that.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, good, thanks Wayne, thanks. Yes, so we actually are providing and this is already rolled out for two customers that we have up in Canada. We're providing dual interface prepaid cards and so there -- that's already been rolled out and we have a pilot with another customer up in Canada.

William Johnson - *Raymond James & Associates, Inc - Analyst*

Is that so, what kind of prepaid is that, is that -- is that private label or is that general purpose?

Steve Montross - *CPI Card Group Inc - President and CEO*

General purpose.

William Johnson - *Raymond James & Associates, Inc - Analyst*

Okay, I'm sorry I interrupted you, okay.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, so we have that in Canada then in the U.S. we have -- we have pilots with two prepaid program managers for -- it would be contact, it wouldn't be dual interface, it would be contact EMV cards for general purpose reloadable cards. So, there's activity, there's -- there's certainly interest but now we've seen it convert besides interest and discussions about it, there's -- we are now seeing some real activity with this.

We also had discussion for a while with their program managers about -- about EMV and has spent a bunch of time with them from a technical standpoint, exactly what it would mean and what they would need to do for their networks in terms of processing EMV transactions. So, there's -- there's a lot of analysis that's been done around that.

William Johnson - *Raymond James & Associates, Inc - Analyst*

Great I appreciate that color, so two quick followups if I could. The first is, have you seen anything in the healthcare market that you think that you guys can take advantage of or that you could provide a service to that's the first question and I'll let you address that one before I follow up.

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Steve Montross - *CPI Card Group Inc - President and CEO*

Well there is -- there's absolutely an opportunity and that would fall into what we call like the enterprise prepaid vertical around healthcare where you have these health spending accounts or the FSAs. And so there's -- that's an opportunity in the healthcare market for us is doing that and we do some of that already.

William Johnson - *Raymond James & Associates, Inc - Analyst*

Great and could you comment on the competitive dynamics in the U.S. for the products and services that you're providing, have you seen any changes in the competitive landscape over the last six months or so from some of the bigger overseas competitors like an [Orbiter] or Gemalto for example?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, we have -- we've seen the competitive intensity with the large issuer. It's really in the large issuer segment that you referred to large European competitors that we have. That's where we've seen the competitive intensity is around the large issuer market.

We haven't seen it in a small to mid-size issuer market, that's a -- as we discussed that's a harder market to service and yes, that's why we got that great position in that market we do but definitely the competitive intensity in the large issuer market has picked quite a bit in 2015. And then also -- so that's the dynamic going on in debit and credit and then in prepaid we've seen competitive -- the competitive pressure if you will step up a bit in the low end gift card market and so we've seen competition coming into that [work] like [simpler] product designs on the low end of that market.

William Johnson - *Raymond James & Associates, Inc - Analyst*

Great, thank you.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes.

Operator

And our next question comes from the line of [Veran Shoya] from CIBC. Your line is now open.

Veran Shoya - *CIBC World Markets - Analyst*

Hi good afternoon, thanks for taking my question. Just touching on the pilots that you're currently working on for dual interface, was that a -- are these pilots like typically are speed or is it born from my discussion with the clients?

Steve Montross - *CPI Card Group Inc - President and CEO*

It's born with discussions with the client.

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Veran Shoya - *CIBC World Markets - Analyst*

And how long do I typically, when you start a discussion, until you end up in a sort of pilot, do you have like a sense of time frame that you see out there?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes -- no, we have been doing -- these are -- these are our customers where we've been doing some business with them already. So, we know that we had discussions for a while and then finally they have matured to the point where they want to instead of just having the discussion, they actually want to start doing a pilot get some familiarity with the product.

Veran Shoya - *CIBC World Markets - Analyst*

Okay, okay and my followup question is on the mobile space. Can you provide some more color on your partnership with Sequent and what sort of opportunities can you tackle on the mobile space?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, so our partnership with Sequent -- Sequent, yes, provide the software platform or the applications and also a mobile wallet that we would then for instance with the mobile wallet, we would white label that for financial card issuer and that's our -- that is our target market is the financial card issuers.

And so we work with Sequent, they provide the backbone, so to speak, around the software platform. They also have that mobile wallet that we inferred would white label for that financial card issuer and then with the software platform that they have, we would be using that platform as the trusted manager, if you will, of the secured data with that financial card issuer.

We would then be using that platform to then initialize or provision the credentials for that customers for those management card issuers whether we do it through the [call] or we do it through a secured element, the capabilities that Sequent has with that software platform enables us to do that provision in [any] of those credential, and so we continue to work with them quite a bit.

We had really good relationship with them. We work with that in terms of specific discussions that we had with customers in the marketplace and so there's -- we believe that they got really good capability.

They also provide the software platform for mobile payments that Rogers uses -- Rogers Communications uses up in Canada. So they are very, very credible player in the mobile space and that's the reason why we have a relationship with them, is that the strength that they're offering that they have. But that's -- that's the nature of our working together and that's also the nature of the discussions that we're having with financial card issuers.

Veran Shoya - *CIBC World Markets - Analyst*

Okay, great thanks for taking my question, [I'll pass] one.

Operator

And our next question comes from the line of Jordan Hymowitz from Philadelphia Financial. Your line is now open.

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Jordan Hymowitz - *Philadelphia Financial - Analyst*

Thanks guys. This pilot program for advanced EMV or dual contact EMV, can we have a sense of size, I know you don't (inaudible) [smudges] like is it millions, isn't it -- could you give a sense of what the magnitude is?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes -- no, Jordan, it's not million, it's a small pilot and they want to move from the discussion phase to let's get some practical experience now and also see how we -- this works within our systems. And that's part of it too -- is that and what they're also doing in conjunction with this is going back and really looking at the market and looking at what this would do for their customers and the customer experience they have with the -- with their -- the experience their customers have at the retail level.

And that's one of the things that a number of these large issuers are evaluating is what's the customer experience because they want to make sure that they continue to provide a leading experience to those customers, their top of wallet. So as a result, they're looking at what does dual interface do to that customer experience. Does it really enhance it for them and therefore provide some really tangible benefits.

But, they want to take it to the next step in terms of actually having a product now that they can be evaluating and getting the people to use and that's -- so that's what this pilot is all about is giving it to people to use and get some practical experience, see what that -- that result is, what the attractiveness is and then they can make better informed decisions as they move forward.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

And it's the top five issuer you said?

Steve Montross - *CPI Card Group Inc - President and CEO*

It is a top 10 issuer.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

Okay and last question, in dual contact or contact with EMV seems to be the norm in Canada and increasingly in Europe but just not here. Do you think one of the reasons that this company is testing it out is they want to make sure the issuers stay ahead of the Apple pace and the like and if that occurs, then it won't happen as much, especially because the chip and [bin] seems to be a slower regulatory driven process versus what happens to be more of a consumer driven phenomenon, does that make sense?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes -- yes and I think the -- what the really -- what the issuers and [just] issuer is that -- but the most interesting is just making sure that they're really top of wallet and it's not so much use the strategy that would be a response to mobile payments because I think everybody use the traction around mobile payment is being very slow. It's another way to pay and so it's not -- so it's not really a reaction to that as much as how do we continue to enhance the consumer experience.

Because you're right, Canada has gone almost completely to tap-and-go and when you talk to -- and we do because we're providing a lot of those dual interface cards in the Canadian market with our facility that we have up in Canada. And as you talk to the people up in Canada, the issuers and the consumers, they could not manage not having that kind of convenience.

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And so the issuers and this issuer in particular is looking at, well how does this really enhance the customer experience and therefore it enhances our business with that customer. So, it wasn't as much a response to mobile as much as how did they continue to drive better customer experience.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

And the price of the dual contact is almost twice what the EMV is, correct?

Steve Montross - *CPI Card Group Inc - President and CEO*

It is, that's right Jordan.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

Okay, so hypothetically if there would be a next generation, your revenues could hypothetically double the what -- the EMV revenues would be?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, they're going to have a significant impact because right now the revenues are about doubled for dual interface card versus the contact EMV card.

Jordan Hymowitz - *Philadelphia Financial - Analyst*

Okay, thank you.

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes, thank you. Okay, I think we have time for one more question.

Operator

And we do have a followup from Paulo Ribeiro from BMO. Your line is now open.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

Thank you. Just a quick reminder on the tax rates because Dave you stressed that the 36.3 for, you know, the fourth quarter was we're going to have a tax loss that [offset]. Is 35 is still the rate we should look for the -- going forward for 2016?

Steve Montross - *CPI Card Group Inc - President and CEO*

Yes as I mentioned last quarter on the call, we think the right range for '16 is a range between 34% and 35%.

Paulo Ribeiro - *BMO Capital Markets - Analyst*

Okay perfect, that's all, thank you.

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David Brush - *CPI Card Group Inc - CFO*

Okay great.

Operator

And that does conclude our Q&A session. I would now like to turn the call back to Mr. Steve Montross for any further remarks.

Steve Montross - *CPI Card Group Inc - President and CEO*

Okay, I want to thank all of you for your questions but also thanks for your participation in our earnings call and we look forward to communicating with all of you next quarter. With that, thank you.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes today's program. You may now all disconnect. Everyone have a great day.

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