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Earnings Call

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Presentation

Operator

Ladies and gentlemen, thank you for standing by. My name is Desiree and I will be your conference operator today. At this time, I would like to welcome everyone to the Talkspace Fourth Quarter and Full Year 2024 Earnings Call. [Operator Instructions]

I would now like to turn the conference over to Jeannine Feyen, Director of Communications. You may begin.

Jeannine Feyen

Director of Communications

Good morning and welcome to Talkspace's Earnings Conference Call for the Fourth Quarter and Full Year of 2024. I hope you've had the opportunity to access the press release we posted on Talkspace's IR website and the presentation of our earnings results. We'll use the presentation to walk you through today's remarks. Leading today's call are our CEO, Dr. Jon Cohen; and our CFO, Ian Harris. Management will offer their prepared remarks and we'll then take your questions. Certain measures we'll discuss on this call are expressed on a non-GAAP basis and have been adjusted to exclude the impact of one-off items. Reconciliations of these non-GAAP measures are included in our earnings release and on our website, investors.talkspace.com.

I also want to remind you that we will be discussing forward-looking information today, which may include forecasts, targets and other statements regarding our plans, goals, strategic priorities and anticipated financial results. While these statements represent our best current judgment about future results and performance as of today, our actual results are subject to many risks and uncertainties that could cause actual results to differ materially from what we expect. Important factors that may affect our future results are described in our most recent SEC reports and today's earnings press release. For more information, please review our safe harbor disclaimer on Slide 2.

Now I will turn it over to Dr. Jon Cohen.

Jon R. Cohen

CEO & Director

Good morning. I'm proud to share that 2024 was another great year for Talkspace. We achieved strong growth with revenue growing 25%, session volume up 45% and EBITDA making a strong improvement of \$20.5 million from a \$13.5 million loss in 2023 to a \$7 million gain in 2024, all while reducing operating expenses by \$7 million. These results align with our vision as we continue to expand our reach, drive awareness and adoption and deliver the best-in-class care. In 13 years since our inception and 3 years as a public company, Talkspace has built a sustainable, profitable business model offering a comprehensive solution that gives us a powerful competitive edge in the marketplace. And with the mental health needs only growing, the future is bright for Talkspace. Over the past 3 years, we have meaningfully advanced our strategic shift from a consumer subscription-only model to a Payor-focused approach.

As a result, we have expanded our total covered lives to 179 million people and have shifted our member acquisition strategy to support unlocking this audience. Our reach now extends beyond commercially insured adults to include teens, seniors through Medicare and active military members and their dependents. Throughout this journey, we have remained committed to the 4 pillars that define success as a high quality health care provider; availability, affordability, accessibility and sustainability. Starting with Pillar 1, availability. We have built a curated network of 6,000 experienced and available licensed providers, an increase of about 10% in 2024 across all 50 states, focusing on over 150 different areas of expertise. Our focus is on maintaining a best-in-class provider-centric experience with a commitment to measuring and monitoring quality across 5 areas: service quality, clinical quality, client experience, documentation and productivity.

We've shifted our marketing model to one of awareness and performance marketing to potential members who are in the market for therapy and likely covered in some way. We are asking that people simply check their coverage to unlock the benefits they probably did not know they had. In fact every January 21 is now known as National Check Your Coverage Day, which was a new day founded by Talkspace to encourage people to check their coverage early in the year when there is typically a desire to set up change for the year. We want people to know that we are available to them and they are likely covered. Moving to Pillar 2, affordability. Affordability is one of the most significant barriers to seeking and getting

care. Our shift to a Payor covered model addressed this issue as over 60% of people with commercial insurance have a \$0 co-pay or just \$15 on average at Talkspace.

As of last week, we are now live in the contiguous 48 states across the U.S. with traditional Medicare and are adding significant numbers of Medicare Advantage lives monthly. The largest Medicare Advantage plan in the U.S. is now live. With this now near national coverage, we are starting to see significant traction. With our military expansion, after successfully launching TRICARE East in August, we extended our reach to TRICARE West in January making Talkspace available to approximately 9.5 million active duty and retired military personnel and their dependents as an in-network benefit with minimal out-of-pocket cost. As with Medicare, adoption is gaining momentum and we're excited about the impact ahead. Our recently announced partnership with USRowing strengthens our commitment to mental health in high performance sports complementing our existing collaboration with the Professional Tennis Players Association.

Like Michael Phelps, these initiatives reinforce our dedication to supporting athletes in their mental demands of their sport. In the teen population, over 500,000 teens in the U.S. now have free access to Talkspace through their city, county or school. That includes New York City, Baltimore County, multiple private schools and as announced in December, the City of Seattle with more than 55,000 teens and young adults between the ages of 13 and 24 now having access to care. We continue to partner with city governments, including the City of Memphis with whom we recently entered our fifth consecutive year providing mental health support to their 8,000 employees and for the first time this year to their dependents, including teens. Our asynchronous platform is a significant differentiator for us as 95% of teens on the platform utilize texting to access therapy.

In addition, we are engaging teens in traditionally hard-to-reach communities as 57% of teens accessing therapy live in areas of high economic disparities. The availability of the therapist network and affordability only work if people can easily and effectively access a provider. To improve the third pillar of accessibility, one of the most important initiatives we are carrying over from 2024 into this new year is our focus on using technology to optimize and improve the member journey from checking eligibility to registration and scheduling to session experience and finally to billing. Every phase of the member journey is being evaluated for improvement. As a result of some new technology efforts among certain test populations, we've seen an 18.5% decrease in no-show rate, a 30% increase in patients completing 3 sessions within 1 month and an increase of 15% in sessions per member.

Improvements such as these are clinically backed to demonstrate better outcomes for members. Our AI innovation team continues to develop tools across 4 areas within the company namely to assist providers as well as improve clinical and network quality, operational excellence and the member experience. I'm very excited about our recent development of Talkcast, a new personalized podcast feature for adults over the age of 18 that will help drive member engagement between sessions, keeping them focused on their own progress and ultimately assist in their clinical improvement. Essentially providers will be able to generate a 3- to 5-minute audio episode tailored to their clients reinforcing key takeaways and themes from their therapy sessions.

This is yet another tool in our expanding provider AI toolkit, which leverages one of the largest mental health data banks in the world with over 10 billion proprietary clinical data points helping to power our AI engine. This clinical data bank is designed to analyze redactive session transcripts to build detailed anonymized client vignettes and map care paths. By categorizing interventions and identifying significant patterns across therapy journeys, the data bank provides the insights to personalized care. Our longstanding relationship in virtual care delivery and innovation is reflected in our financial performance, which gets us to the fourth pillar of sustainability. As you can see in our financials, we have built a model that

is scalable and profitable, all of which Ian will comment on along with his review of the Q4 and full year results.

In conclusion, we believe we have a competitive advantage in the marketplace because of the comprehensive nature of our solution, a highly qualified clinical network of 6,000 therapists, in-network coverage approaching 200 million lives, all virtual modalities to deliver care, a robust infrastructure to deliver high quality clinical care and an advanced technology platform, including AI and a data set to support and grow a profitable business.

And now I turn it over to Ian.

Ian Harris

Chief Financial Officer

Thank you, Jon, and welcome, everyone. As Jon mentioned, Talkspace has transformed into a uniquely scaled business over the past 2 years. In 2024, we achieved our second consecutive year of 25% revenue growth culminating in \$187.6 million in revenue for the full year. Further, a significant milestone for the company was achieving profitability in Q1 of last year, which we've maintained throughout all of 2024 resulting in full year adjusted EBITDA of \$7 million. GAAP net income was \$1.2 million for the year, a \$20.3 million improvement versus 2023. In addition to the business' growth and profitability, our robust financial position is further bolstered by the strength of our balance sheet with \$118 million in cash and cash equivalents, including available-for-sale securities, and 0 debt at the close of 2024. This solid foundation puts us in control of our own destiny and affords us great flexibility in pursuing strategic growth initiatives.

Now let me review our financial performance for the fourth quarter of 2024. We're pleased to report continued strong results building on the momentum we discussed on our third quarter earnings call. Our total revenue for Q4 was \$48.7 million representing a 15% increase compared to the fourth quarter of 2023. This growth was primarily driven by the continued strength in our Payor business, which grew 33% year-on-year and demonstrated solid performance across key metrics such as Payor sessions, which totaled nearly 330,000 in the quarter, an increase of 32% year-over-year. We also saw a 21% growth in unique Payor members completing a session in the quarter reaching nearly 96,000 in the quarter. And we achieved a 9% year-on-year improvement in utilization of sessions per active member.

DTE revenue for the quarter grew 7% versus a year ago with notable new launches in the quarter, including the City of Seattle and the U.S. Navy. Consumer revenue declined by approximately \$3 million versus the same quarter in 2023. Gross profit for the quarter was \$21.5 million, up 3% from the previous year. Our gross margins came in at 44.2% in Q4 compared to 45.6% in Q3 and 49.4% a year ago. As a reminder, as we shift overall revenue mix more towards our Payor business, we expect our gross margins to decline slightly, which we view as an attractive trade-off given the superior long-term unit economics and lifetime value for the new members under the payer-focused strategy. During the quarter, we also maintained our focus on operational efficiency.

Operating expenses decreased by 11% year-over-year to \$21 million representing 43% of revenue in the quarter versus 56% a year ago. We achieved a GAAP net income of \$1.2 million in the quarter, a significant improvement from a loss of \$1.3 million a year ago. And adjusted EBITDA for Q4 was \$2.7 million, up from a loss of approximately \$300,000 in the same period last year. I'm pleased with our cost optimization efforts in 2024 and looking ahead to '25, we will selectively invest some of these G&A savings into revenue-generating areas such as increased marketing efforts and additional technology and product enhancements that we anticipate will help to drive member retention and engagement. Turning to the balance sheet. As I referenced in my opening remarks, our balance sheet remains robust.

We ended the fourth quarter with \$118 million in cash and cash equivalents, a slight decrease from \$119 million in the third quarter and compares to \$124 million a year ago. The \$6 million year-on-year delta was driven by \$11 million of open market share repurchases we completed throughout 2024 including \$3 million in the fourth quarter, which kept our shares outstanding effectively flat versus a year ago. As we look ahead to 2025, we introduce this morning our full year financial outlook consisting

of revenue between \$220 million and \$235 million representing 21% growth at the midpoint and adjusted EBITDA

of \$14 million to \$20 million, an increase of 144% at the midpoint. In 2025, our activation strategy will remain consistent with our previous approach balancing increased marketing spend with sustainable, profitable growth.

As we look to leverage our expanded reach, we will maintain a keen focus on maximizing ROI through strategic partnerships to optimize efficiency. With our coverage now extending to approximately 2/3 of the American public, an increase of more than 85 million lives from 2 years ago, every marketing initiative we invest in has the potential for significantly greater impact. As is typical for us, our marketing investments are anticipated to be more heavily weighted in the first quarter of the year allowing us to reap the benefits of those investments throughout the full year and this will again be the case in part driven by the broadening of our payer outreach aligned with the launch of military and Medicare. As such, we would expect a similar EBITDA trajectory throughout 2025 as we experienced in 2024.

As we assess our capital allocation priorities for the year ahead, our primary focus will continue to be on organic growth opportunities such as further investments in our technology platform to enhance the experience for both providers and members. Second, we remain committed to keeping our share count neutral just as we did in 2024 through our share repurchase programs under which we have approximately \$29 million of remaining capacity, allowing us to be more opportunistic with our buybacks if we so choose. As demonstrated this past year, our cash flow profile can support these first 2 areas and affords us the flexibility to consider a third, utilizing our well-capitalized balance sheet to explore potential inorganic opportunities that may further strengthen our market position. As always, we will continuously evaluate the highest and best use of our capital.

Thank you all for your continued interest in the Talkspace story. We are very excited about the year ahead and about continuing to build towards a Rule of 40 company. We'll now open the call to questions. Operator?

Question and Answer

Operator

[Operator Instructions] And our first question comes from the line of Steven Dechert with KeyBanc.

Steven Craig Dechert

KeyBanc Capital Markets Inc., Research Division

Operating expenses as a percentage of revenue continued to come down. Can you talk about what is driving these efficiencies and where you think you could see further reductions? And then as a follow-up, what factors would determine if you reach the high end of your guide versus the low end of your guide for 2025?

Ian Harris

Chief Financial Officer

Hi Steve, I mean it's sort of generally across the board. As you know, I joined in May and took the first couple of quarters to really review all across the board; I mean head count, G&A, org structures, can we be doing things more efficiently, vendor spend. So there's no specific area I'd highlight on the G&A. And then of course to cut in nominal terms with revenue growing 25% in the year, you get that decline as a percent of revenue pretty naturally. The high end versus low end, I'll let Jon speak to a little bit. The military and Medicare as we've sort of previewed the last couple of quarters, we're really now finally in our first position where we're at what we would describe as critical mass to really launch. So while we spent the last couple of quarters adding these lives, we've just this quarter in earnest, Q1 that is, started seeking to activate those lives. So these early indications are very positive. We feel quite bullish about both categories as well as our general commercial line of business for Payor. We just need some degree of flexibility just because they are new populations overall.

Jon R. Cohen

CEO & Director

So your question is the top line about the -- it's exactly what Ian just said. We remain very encouraged by what we're seeing in both military and Medicare and of course the commercial business plus what you're seeing is our leaning in on the technology side of the member journey, which I've talked about is a significant initiative this year to improve the quality of what we're doing. We're really leaning in on keeping people on the platform and messaging them through some of the mechanisms we've talked about. But we remain really bullish on the growth on the top line.

Operator

And our next question comes from the line of Ryan MacDonald with Needham & Company.

Ryan Michael MacDonald

Needham & Company, LLC, Research Division

Maybe as we think about 2025 and the marketing strategy as you're going after sort of these obviously new and very large populations particularly with Medicare, can you talk about the role and sort of the mix of channels that you're focused on particularly given social media has historically been a pretty big channel and Meta has been getting a bit more restrictive on health and wellness ads and how you target there? Just are you seeing any impacts from that right now? And then given those changes, how are you maybe broadening out or diversifying the marketing strategy?

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Jon R. Cohen*CEO & Director*

Sure. So first off, we held back a little bit on the marketing -- more than a little bit on the marketing spend to really begin this quarter because we really wanted to be in essentially all 50 states. As you saw, we're in 48 of the 50. Plus we wanted to see not just on standard Medicare, but where we were heading on Medicare Advantage because the more people who are in MA in addition to the standard Medicare, the more people who will actually come on to the platform when they look to see if they're actually covered. So having said that, we know and we've done a fair amount of research up to this point about how do we think how to get to seniors. It is very different than some of the other social media channels that we use.

We know for instance that they are bigger users of Facebook than any of the other social platforms and then we also know that they read newspapers, they read direct mail, they're very attuned to onsite visits. So all of that information is going into the marketing plan, which includes putting people which we already have on the ground, to begin to expand and explore actually what's going to work and what's not going to work. But it is early days is what I'm telling you. We really, really have not even begun to scratch the surface on what the Medicare population will respond to and what the strategy will be. Although we've built it, we can't tell you what the results are yet. We are seeing though some early positivity to say the least in terms of people who are coming to the site and registering.

Ian Harris*Chief Financial Officer*

Ryan, specifically to your question on Meta, I've been monitoring that very closely with the team. We've not seen any negative impact since any of the recent changes. It's a fairly small channel for us overall so we don't anticipate that being much of a headwind at all.

Ryan Michael MacDonald*Needham & Company, LLC, Research Division*

Okay. And maybe just given the early stage of the Medicare and military rollout this year, obviously nice to hear some optimism about sort of the early stages of that. But when we think about the sort of range of outcomes in your guidance, can you maybe just provide a bit more color directionally on how you're thinking about growth across Payor versus DTE versus consumer in sort of the implied guidance range?

Ian Harris*Chief Financial Officer*

So the first component of your question, military and Medicare as a percentage of Payor, we're really approaching it opportunistically, right? So we're optimizing to the best returns. Obviously we view and early indications and what we're trying to convey is that it's very positive interest from military and Medicare members. So while we're optimistic on it, if for whatever reason it's not as attractive or not as good of returns that we see over time, we're not going to keep pushing on a string. We'll pivot the budget and drive it to commercial. So we're solving for the best outcome economically overall. In terms of Payor, consumer, DTE mix; I think you should expect continued sort of outsized growth from Payor sort of pulling up the consolidated numbers.

DTE while we don't break out sort of line of business level insights into revenue guidance, what I would say is obviously '24 benefited from a very material new contract in New York City, which we now have base effects to sort of deal with in 2025, right, kind of lapping the initial year of New York. So you saw in Q4 7% year-on-year growth in DTE and just as a reminder, Q4 '23 was the first quarter where we had New York. So I'd point you to that sort of annual growth rate as a sort of base case for DTE. Consumer, I would just echo what I said on the last call in Q3, it will decline slightly obviously as a result of the Payor

strategy and as we grow covered lives, that becomes more and more the case as a better alternative for members to go through the Payor route. Obviously the numbers will be much smaller. So the sort of headwind on the consumer continues to dissipate.

Operator

Next question comes from the line of Ryan Daniels with William Blair.

Jack A. Senft

William Blair & Company L.L.C., Research Division

This is Jack Senft on for Ryan. So gross margin decreased sequentially this quarter, you're at 44.2% versus above 45% last quarter and just really the majority of the year and I know you're calling out a shift towards Payor mix. But is there anything else that really attributed to the contraction? Like I'm assuming some of it could be onboarding of the new partnerships. But if you could elaborate on that, that would be appreciated. And then just kind of how we should think about that going forward in 2025.

Ian Harris

Chief Financial Officer

Sure. I mean it really is almost a coefficient of 1 in [terms of] revenue mix shift. That is really the sole driver of it. I would say just echoing my comments in the prepared remarks, slight decline in '25 as a result of continued mix shift. But the step down you saw in consolidated gross margin from '23 to '24 was much more pronounced than what we would expect going forward. We've identified a bunch of sort of mitigating factors, which we're actioning throughout the year, which will help sort of offset that. But again, we view that trade-off, so to speak, as a no-brainer. The long-term unit economics and also the contribution margins we're getting by pursuing that slightly lower gross margin member session is just far, far more attractive. So we'll continue to do that.

Jack A. Senft

William Blair & Company L.L.C., Research Division

Okay. Understood. And then maybe another modeling question here too. G&A also decreased this quarter and I think you alluded to it in the total OpEx question before, but it's really kind of been the lowest it's been all year. And I'm just kind of wondering is this improvement mainly from the investments you've made back into the business? And then just as a follow-up too, like is this kind of a run rate we should think of going into 2025 in terms of G&A or maybe how should we think about that cadence going forward?

Ian Harris

Chief Financial Officer

Some of it's, yes, the fruits of the investments we made throughout '24. Some of it's just getting sort of full quarter impact of just general cost optimization actions that we took earlier in the year. And again I kind of took the summer to review things and then really started actioning them Q3, Q4. So it's really just that getting pulled through the P&L. As I said in my prepared remarks, while we're obviously pleased with the nominal decline in OpEx dollars, the efficiencies we've gotten in our marketing effort overall, which is, one, just from the new team who came in 2 years ago and really revamped our whole marketing approach, number one. Number 2, it's actually a lot of the partnerships we've announced whether it's Amazon, ZocDoc integration or some of our other sort of referral partners that we've talked about in the past couple of quarters as well as just working more closely with the payors to try to more effectively get to their members, which they're very aligned with.

And so through all those things, the actual sort of marketing efforts have become such a higher ROI for us that what I said in my prepared remarks is we're going to take some of these G&A savings that we've garnered out of other sort of non-revenue-generating OpEx lines so think G&A and reinvest that in 2025 into marketing. So one, because it's more efficient so we're adding more members for every dollar we spend. That's also a function of the fact that we've grown covered lives as much as we have. But then also just echoing Jon's comments, we're really focused on technology and product improvements, which drive engagement which in turn extends sort of retention and utilization for the member, i.e., for every member we're adding; they're doing more sessions, they're staying on the platform longer and are more attractive to us. So for all those reasons, what I'm trying to signal is we're going to lean in a little bit in '25, which will show up in the OpEx line for marketing obviously.

Operator

Our next question comes from the line of Steven Valiquette with Mizuho.

Steven James Valiquette

Mizuho Securities USA LLC, Research Division

Just in regard to the Payor book of business, just curious if you have any commentary on the pricing environment within this customer segment. Last time we spoke, you mentioned it was trending I think actually a little bit better than expected. You were getting pretty good rate increases. So I'm just wondering if that's still the case today as you negotiate and renew more contracts.

Jon R. Cohen

CEO & Director

Yes, I would say a lot of the major contracts have been already negotiated and renewed recently. New ones coming on, we're not seeing any degradation. We're seeing similar rates that we've had in the past. So I would say there's really no change and no indication of any significant decrease in any sense or any way.

Operator

And our last question comes from the line of Bobby Brooks with Northland Capital Markets.

Robert Brooks

Northland Capital Markets, Research Division

In your slides I think it's on Slide 3 under unlocking the membership base, it mentions acquisition strategy optimized towards people checking coverage. Could you just expand on that? Like what are acquisitions in this case?

Ian Harris

Chief Financial Officer

Sorry for the confusion, Bobby, and thanks for the question. That's just talking about customer acquisitions. Our entire marketing message we revamped, call it, 1.5 years ago to lead with the check your eligibility, you may be in network. And obviously that message will continue to resonate better and better as we've grown covered lives.

Robert Brooks

Northland Capital Markets, Research Division

Fair enough. And then a couple of weeks back I kind of put out a note diving into some third-party data that ultimately highlighted your significantly more efficient marketing spend than your largest peer. And I

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just wanted to ask could you maybe just discuss why your marketing team has generated such strong returns? I mean you mentioned it in the last question too since they came in, it's been kind of a sea change. And so I just really kind of wanted to dive a little bit deeper into what you guys think is giving you an edge on marketing.

Ian Harris

Chief Financial Officer

I mean not to puff up their chest too much, but they do an amazing job, number one. Secondly, though and I've said this before, the value prop of our message of hey, you may have this service for free, no surprise is going to resonate much better with folks than hey, pay me x dollars on your -- type in your credit card, [let] me to charge you for this. So I think we're just selling a much better value proposition to the underlying consumer, which leads to better conversion. And then I don't want to discount the impact of these large partners we have who have come to us because we're in network. We have at this point now 170 million-plus covered lives. We're in all 50 states. We're virtual and convenient. They come to us as a convenient solution for their underlying customers and those partnerships really do drive very cost effective awareness for us.

Jon R. Cohen

CEO & Director

Just to give you an example. When we go up on our -- someone goes on to the website, it doesn't cost us anything to add though we're in network with Medicare and we're now in network with TRICARE and military. Think about it that way. So you have these very large populations that have now entered into the fray, right, and are looking for mental health with the same basically spend that we're doing looking at customers holistically. Do you follow me? I mean we certainly upped the dollars towards military and Medicare and look how to improve our outreach of those populations. But in a general sense, right, it doesn't cost us much to add new populations up to the web. And then you get those additional sign-ups as a result of that. That's the difference, right?

Robert Brooks

Northland Capital Markets, Research Division

Yes. That makes perfect sense. Yes, it's just kind of fish in the pond that's becoming ever bigger to fish in. And then just maybe the last one for me. Number of Payor sessions completed has kind of pretty much tracked in line to Payor revenue growth year-over-year. Is that how we should kind of expect things to trend going forward, ultimately Payor revenue growth being kind of a result of the number of sessions completed? Because looking back the past couple of quarters, there's kind of a larger delta. I mean 1Q of '24 was 92% Payor revenue growth year-over-year versus 65% session growth. Just kind of curious on like how to think about that trend going forward.

Ian Harris

Chief Financial Officer

Yes. I mean that's the largest driver. Think of it as like price times volume, that's our volume. On a contribution basis, which takes into account sort of time, right, and I guess like longitudinal performance, then that's where the technology and product and new engagement efforts we have come into play. But in terms of actual session growth and how it ties to revenue, think of it as just like the volume of sales. And then obviously pricing, going back to Steve's question, would play a part in that as well.

Operator

That ends the question-and-answer session. Ladies and gentlemen, this concludes today's conference call. Thank you all for joining and you may now disconnect.

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