PubMatic

# PUBMATIC Q4 AND FY 2022 EARNINGS CALL: PREPARED REMARKS

***SAFE HARBOR***

*A copy of our press release and accompanying slides can be found on our website at investors.pubmatic.com.*

*I would like to remind participants that during this call, management will make forward-looking statements, including without limitation, statements regarding our future performance, market opportunity, growth strategy and financial outlook.*

*Forward-looking statements are based on our current expectations and assumptions regarding our business, the economy and other future conditions. These forward-looking statements are subject to inherent risks, uncertainties and changes in circumstances that are difficult to predict. You can find more information about these risks, uncertainties and other factors in our reports filed from time to time with the Securities and Exchange Commission, including our most recent Form 10-K and any subsequent filings on Forms 10-Q or 8-K, which are on file with the Securities and Exchange Commission and are available at investors.pubmatic.com.*

*Our actual results may differ materially from those contemplated by the forward-looking statements. We caution you therefore against relying on any of these forward-looking statements. All information discussed today is as of February 28th, 2023 and we do not intend, and undertake no obligation, to update any forward-looking statement, whether as a result of new information, future developments or otherwise, except as may be required by law.*

*In addition, today's discussion will include references to certain non-GAAP financial measures, including Adjusted EBITDA and Non-GAAP Net Income. These non-GAAP measures are presented for supplemental informational purposes only and should not be considered a substitute for financial information presented in accordance with GAAP. A reconciliation of these measures to the most directly comparable GAAP measures is available in our press release.*

*And with that, I will now turn the call over to Rajeev.*

## CEO REMARKS

Thank you, Stacie and welcome everyone.

Revenue for the year grew 13% over 2021, yet again outpacing the global digital ad market forecasts of 8.6% growth. Omnichannel video grew 42% year over year, and CTV alone tripled over last year as the format continues to evolve toward programmatic. These high growth, highly profitable channels drove adjusted EBITDA margins of 38%. We generated over $87 million in net cash from operating activities and $38 million in free cash flow. Altogether, a compelling financial profile combined with on-going, targeted investments for long term growth.

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The fourth quarter undoubtedly had its challenges. Performance was slightly below expectations as sharp declines in ad spend across the industry, particularly in December, impacted our business. In our case, we saw the largest sequential drop over November in the last ten years. This primarily impacted the display portion of our business, which declined 11% over last year and continues to pressure overall growth. While omnichannel video continues to gain share at a rapid pace, display remains roughly two-thirds of our business.

Revenues for our omnichannel video businesses in the fourth quarter continued to grow 25% year over year and CTV/OTT more than doubled over Q4 last year. These high-growth areas remain intact and we have reorganized resources to move quickly to innovate and execute across these areas. While these long-term growth drivers will diversify our revenue over time, we believe that when ad spend re-accelerates, display will recover as well.

While visibility is limited due to the uncertain economic environment, our business model is unique with respect to our ability to consistently generate cash and maintain 30% plus annual adjusted EBITDA margins while also investing in future growth opportunities. We are efficient as a company and technology platform. We are highly nimble and innovative, leading in our category. And we have a strong balance sheet coupled with a long track record of profitability. As a result, we will use the current challenging economic environment to build even deeper relationships with our customers and make highly focused innovation investments that we believe will position us for outsized gains when digital ad spend growth inevitably turns upward. Moreover, we have taken significant steps to operate within the current environment, protect our cash flow and set ourselves up for higher margins in the future.

## CONTINUED MARKET SHARE GAINS

We ended 2022 with an estimated market share of 4-4.5%, significantly up from when we went public just over two years ago. We are well on our way to our stated goal from the time of our IPO of 20% market share, and we intend to use the downturn to further accelerate our gains.

Stepping back, the opportunity for open internet advertising has never been greater. Advertisers and publishers continue to seek alternatives to the walled gardens. This tailwind, along with structural changes including ongoing antitrust activities, will only expand our total addressable market as an independent technology provider. Moreover, consumers are increasingly seeking ad-supported content experiences to offset other household budgetary priorities. As the ecosystem grows more complex, the need for greater efficiency is driving publishers and buyers toward technologies that help them better compete. The challenges of today’s macro environment will pass, and we believe the investments we make today will have exponential impact as we continue to increase the value proposition and stickiness of our platform and expand our addressable market.

We have a sizeable, global TAM that includes high growth ad formats such as CTV, online video, and mobile. In addition, as we recently entered new markets like France, Spain, South Korea, and non-domestic China, we expand our addressable market even further. We see strong signs of success in these new markets with nearly 90 customers signed in 2022 alone such as French media company, Amaury Media, Spanish mass media company Vocento, the CTV content and ad business of electronics giant TCL, TCL Ffalcon, and Korean addressable TV leader SKBroadband.

We have 1,600+ publishers we already work with and continue to acquire new marquee customers, such as Roku and TiVo in CTV and Kroger in Retail Media.

## GO TO MARKET FOCUS

In this slower economic environment, our priority is to deepen our relationships with existing customers and build the technical pipes or integrations with our customers for inventory and data access so that we are in an advantaged position when ad spend growth picks up. Publishers are actively looking to add the right partners that can help them increase their revenue in these uncertain times. I have spent significant time in the last several months with a number of customers and my view is that today’s economic environment is likely to accelerate programmatic growth as publishers seek greater



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operational efficiencies to the alternatively high-costs of managing a traditional, insertion order-based business. In fact, we closed 50% more new customer additions and upsells in January 2023 as compared to January 2022.

Once we sign a new customer, our focus turns to expanding that relationship through our sticky portfolio of solutions such as our wrapper, mobile app SDK, identity, and data solutions, which further embed us into publisher monetization and workflows. Once integrated, customers continue to grow with PubMatic. In 2022, we had high publisher logo retention of 97% and benefit from a high net dollar-based retention rate of 108%.

We spent the last two years investing in our sales and customer success team. We believe we have strong market coverage in place to continue to execute and drive market share gains. We enter 2023 having significantly reduced the pace of hiring, focusing instead on a very select number of high priority roles.

At the same time, ad buyers are looking for more data driven decision making and measurable results. Major ad buyers are looking to consolidate their budgets with fewer partners in order to drive operational efficiency and effectiveness. The majority of ad spend comes from top agencies and advertisers. These powerhouses typically have multi-layered decision makers across multiple regions and require vast market coverage and expertise. We believe we are well positioned to gain share for two reasons. First, we've made the investments in our go-to-market coverage over the last two years and our teams are already executing. Second, our differentiating technology, including workflow and data solutions, provide buyers with greater control over their ad budgets and ultimately higher return on ad spend.

Activity from SPO grew to over 30% in Q4 2022, up from 21% in 2020. We continue to expand our relationships with major holding companies like GroupM and Havas, and recently with independent agencies like Horizon. We are one of only two independent, global, and omnichannel platforms at scale, and so it's quite possible that this economic environment will accelerate our SPO penetration in 2023.

## PRODUCT INNOVATION

Let me turn now to our focus as it relates to product innovation. In 2022 we increased the number of products and features released by 30% over 2021 to almost 400, including Connect, OpenWrap for CTV and mobile app, Private Marketplaces, CTV monetization, agency-specific solutions, and infrastructure upgrades. Looking to 2023, the key pillars of our focus for this year are Supply Path Optimization and Retail Media. We are accelerating our cadence of product releases in these two areas based on product and engineering investments made over the last couple of years and our acquisition of Martin last Fall.

Our first priority is expanding our SPO offering. We have been hard at work integrating Martin technology and we are receiving great feedback from agencies and advertisers on how we can help them further drive return on ad spend, measurement, and operational efficiency. We will make a series of product releases for buyers on our platform over the course of this year with a particular focus on CTV and online video optimization.

Our second priority is Retail Media, which is one of the fastest growing categories within our addressable market. Over the past several quarters, we have been readying existing capabilities in onsite monetization, data management, and audience targeting specifically for retail media customers. Over the course of this year, we will make a series of product launches that brings automation, scale, and efficiency to this market.

## CONCLUDING REMARKS

There is no doubt that we are in a challenging economic environment with muted digital ad spend growth in the near term. Based on our prior experience in such downturns, however, we expect to come out of this period even better positioned. We believe this environment favors scaled companies like PubMatic that are efficient, highly innovative, nimble, and profitable. Our focus on acquiring new customers and deepening integrations with existing customers, as well as rapidly innovating in SPO and retail media, will be well rewarded when ad spend growth re-accelerates. Importantly, we have



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built a durable business and we enter this period with a very strong financial profile, generating healthy free cash flow and no debt.

This attractive profile provides us with an opportunity to expand our priorities with respect to capital allocation. We operate in a large and growing market, and so we will continue to appropriately invest in the business to drive market share gains both organically and via acquisition from time to time. In addition, we are announcing a share repurchase program that allows us to return more value to shareholders.

And finally, I want to add that we have aligned our investment strategy and continue to optimize for maximum productivity in anticipation of a less robust economic environment in the second half of the year compared to what many are assuming. If the economy rebounds at a faster rate, we will adjust our plans appropriately to capture the opportunity.

And now, let me turn it over to Steve to provide additional detail.

# CFO REMARKS

Thank you Rajeev and welcome everyone.

As noted by other digital ad companies, December spending across the ecosystem was uncharacteristically soft. As a result, our fourth quarter revenue was $74.3 million, down 1.7% year over year, driven by an 11% decline in display, which is about two thirds of our revenues. This result was below our expectations. Importantly, our high growth areas continued to shine. Revenue from omnichannel video grew 25% year over year driven by CTV revenue which more than doubled.

At the outset of the fourth quarter, our outlook assumed continued weakness in display but not the severe industry-wide deceleration that occurred in December. Our display revenues were down 15% vs the prior December. We are taking actions to mitigate the display impact to our business.

Despite these challenges, we continued to outpace the overall market and were up 13% year over year to a record $256.4 million. This growth was on top of 2021’s growth of 53%. Significantly, we are seeing the benefits of our investments in long-term growth drivers like omnichannel video which grew 42% year over year on top of 2021’s growth of 79%. These investments and others have enabled us to more than double our revenues from 2019.

2022 was our 7th straight year of GAAP Net Income and 10th straight year of adjusted EBITDA. And notably, our business generates significant cash flow. 2022 was our 9th straight year of positive cash from operations and since 2016 we have generated approximately $150 million in free cash flow. This consistent performance stands out amongst our peer set.

### CONSISTENT AND DIFFERENTIATED FINANCIAL RESULTS

Q4 Adjusted EBITDA was $32.6 million, a 44% margin. We generated $19.4 million in net cash from operating activities and $7 million in free cash flow. Full year adjusted EBITDA was $98 million, a 38% margin. We generated $87.2 million in net cash from operating activities and $38.3 million in free cash flow or 15% free cash flow margin. In the last two years alone, we have generated $88 million in free cash flow, and that is after investing $60 million in platform infrastructure with an expected average lifetime of over 5 years.



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These financial results are driven by our strong publisher and buyer relationships, our diversified omnichannel platform, and our owned and operated infrastructure.

We have built an effective land and expand go to market organization and our pipeline continues to build in 2023. We focus on expanding publisher relationships and drive healthy multi-year net dollar retention rates. On a trailing twelve-month basis, publisher net dollar retention was 108%, representing a robust balance between new and existing publishers.

Turning to our buyers, our supply path optimization efforts over the last several years have resulted in increased overall ad spend and greater spend retention. Similar to our publisher strategy, once we land new SPO relationships, we successfully ramp them across formats and geographies. Viewed through the same retention lens as publishers, the net spend retention rate for SPO buyers with at least three years of spending has been about 124% each year. Since we pioneered SPO four years ago, we have retained nearly 100% of SPO ad buyers, highlighting the stickiness of our platform and the increased value we bring to them.

The diversity of our platform is a key strength.

Our omnichannel video revenues span across desktop, mobile, and CTV devices, and was 34% of revenues in Q4, up from 22% of revenues in Q1 2021. From a device perspective, mobile advertising revenues, across all formats, increased to 57% of revenues in Q4 2022, up from 53% of revenues in Q1 2021.

We are also well diversified across ad verticals, which contributes to our resiliency. For example, in Q4 we saw Automotive and Food & Drink both grow 25% year over year. This growth helped offset weakness in Shopping, Technology and Personal Finance, which in aggregate declined 13% year over year. Overall, our top 10 ad verticals were flat in the fourth quarter compared to last year.

Another source of strength is our geographic diversity. In Q4, EMEA revenues increased 11.5% year over year partially offsetting a decline in the US. Earlier in the year, Americas growth helped balance softness in EMEA and APAC. For the full year, all regions expanded revenues by double digits.

## OPERATIONAL STRENGTH

Now turning to our operational strength which gives us several significant levers in our business that allow us to maintain 30% plus annual adjusted EBITDA margins, generate healthy cash flows and invest for continued long-term growth in an expanding addressable market.

First by owning and operating our infrastructure, we have significant leverage and operational control, a key competitive differentiator for us. Since 2019, we have invested approximately $90 million to expand our impression capacity and platform capabilities. This has allowed us to grow our market share. For example, over the last three years, we increased the number of impressions we processed by over 400% to capitalize on our expanded publisher relationships.

In 2023, our focus is on leveraging prior investments and driving increased optimization through the software and hardware layers. These efforts will further increase capacity while reducing our capex by more than 50%. We anticipate seeing the margin benefits in the second half. We also expect our optimization efforts will lead to further margin expansion next year.

Second, we operate a highly efficient and productive development organization in India. We estimate that we are saving over $30 million per year building software using our India team vs. deploying those resources onshore. Over 80% of our tech hiring in 2022 was in India which rolled out 30% more product releases last year.

And third, with our long-term focus on profitability we take a nimble approach to managing our business. In the second half of 2022, we moved quickly to adjust our expense structure and investment plans once it became clear that overall ad



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spending growth was trending down. These actions contributed about $10 million to our bottom-line by the end of 2022. Our operating plans for 2023 call for significant reduction in the pace of hiring as compared to 2022.

## OPERATING EXPENSES

Q4 GAAP opex was $34.8 million or 13% increase year over year. Excluding stock based compensation costs and acquisition related costs, operating expense growth was 4%.

Full year GAAP opex was $134.3 million or 22% increase year over year. Excluding stock based compensation costs and acquisition related costs, operating expense growth was 16%.

## NET INCOME

Q4 marked our 15th straight quarter of GAAP net income and was $12.8 million or 17% net margin. Full year net income was $28.7 million or 11% net margin.

Q4 Non-GAAP net income, which adjusts for unrealized (gain) or loss on equity investments, stock-based compensation expense, acquisition-related and other expenses, and related adjustments for income taxes, was $18.7 million or 25% of revenue. Full year Non-GAAP net income was $52.2 million or 20% margin.

Q4 diluted EPS was $0.22 and Non-GAAP diluted EPS was $0.33.

2022 diluted EPS was $0.50 and Non-GAAP diluted EPS was $0.92.

## BALANCE SHEET AND CASH

Turning to cash, since our IPO 26 months ago, we have generated more than $180 million in cash from operations. We have used this cash for working capital, investments in long-term organic growth and the acquisition of Martin.

At the end of 2022, we had $174 million in cash and marketable securities and no debt. Our priority is to drive shareholder value. There is no shortage of opportunities in our huge industry with years of growth ahead and you will see us continue to drive growth and gain market share, both organically and from time to time via M&A. In addition, our board of directors has approved the repurchase of up to $75 million of our Class A common stock, through the end of 2024.

## FINANCIAL OUTLOOK

Now turning to our 2023 outlook. There is considerable uncertainty about the trajectory for digital ad spend this year due to the pronounced December weakness and persistent overhang of macro headwinds across the globe. Display, in particular, continues to see pressure. These trends and challenging conditions have led to a wide range of industry forecasts for 2023.

Given these circumstances, we have built our investment plan assuming a low to mid single digit rate of growth for digital advertising in 2023. We anticipate continued softness in the first half followed by tempered improvement in the second half. Overall, the plan we have in place is expected to deliver three important outcomes:

1. Generate similar free cash flow as we did in 2022;
2. Position us for revenue acceleration when ad spend stabilizes; and
3. Establish a new level of efficiency in our cost structure that will lead to margin expansion by the end of 2023 and beyond.

For Q1 2023, we anticipate revenue to be in the range of $50 to $52 million. December weakness continued into January, with display revenue down 13% over January 2022. Online video also started the year off slowly and was down in January year over year. CTV continued its strong trajectory and grew double digits. Overall, omnichannel video grew year over year.



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From a regional perspective, EMEA thus far has grown double digits year over year, while both the Americas and APAC were down. Over the last several weeks we have seen trends improve sequentially over January. If these trends continue, we anticipate that Q2 revenues will sequentially increase by approximately 10%, in line with our historical 10-year average.

In light of this, we have taken actions to drive incremental productivity across every aspect of our business. We expect to reduce capex by over 50% compared to 2022 and reduce our discretionary spend plans. In addition, we have reorganized our go to market and technology teams to apply incremental resources towards the fastest growing areas in video, including CTV, supply path optimization, and retail media.

GAAP cost of revenue in Q1 will grow sequentially from Q4 by approximately $1.4 million due to the full quarter impact of year end 2022 capex and inflation cost increases passed through by our colo providers that took effect in January. Over the coming quarters, as a function of proactive steps on productivity and cost saving measures, we anticipate keeping sequential cost increases in the low single digits.

We expect Q1 GAAP opex to increase approximately $7 million vs Q4. This increase absorbs the Q4 run rate of expense, incremental Martin expense plus an additional cost related to our January global sales conference. We anticipate Q2 opex will be lower than Q1 by about $1 million with sequential increases in the low single digits thereafter. Excluding stock based compensation and Martin acquisition related costs, Q1 non GAAP opex will be $4 million higher vs Q4.

Given our revenue guidance and our cost structure which is largely fixed in the near term by design, we expect our Q1 adjusted EBITDA to be between $4 and $6 million or approximately 10% margin at the midpoint. As a reminder, historically our first quarter is impacted by prior year investments carried forward during a period of low seasonal ad spend.

We expect profitability to improve as the year progresses driven by the full effect of our cost reductions, optimizations and typical seasonal increases in ad spend. We anticipate Q3 and Q4 adjusted EBITDA margin levels to be above 30%.

For the full year, we expect adjusted EBITDA margin to be over 30%.

We expect capex to be $13 to $16 million for the full year, more than 50% lower than 2022.

## IN CLOSING

As I mentioned earlier, we have built our plan assuming low to mid single digit growth in digital ad spend this year. As a leading technology platform, we expect to continue to outpace the market rate of growth and gain share as a result. Accordingly, to the extent that industry growth rates are higher than our current assumption, we would expect to grow faster. In addition, the recently announced closure of several Sell-Side Platforms gives us even greater opportunity for incremental share gains over time, which are not included in our current 2023 expectations.

We have strong publisher and buyer relationships, a diversified omnichannel platform, and a durable business model.

We anticipate that the work we are doing now to increase productivity and leverage prior investments will result in margin expansion and increased cash flows later this year and well into 2024.

With that, I will turn the call over to Stacie.



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