PUBMATIC Q1 2022 EARNINGS CALL: PREPARED REMARKS

SAFE HARBOR

Thank you, operator, and good afternoon, everyone.

Thank you for joining us on PubMatic's earnings call for the first quarter ended March 31, 2022. Joining me on the call are Rajeev Goel, co-founder and CEO; and Steve Pantelick, CFO.

Today's prepared remarks have been recorded after which Rajeev and Steve will host live Q&A.

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

Before we start, 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 May 9th, 2022 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. 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 now, I will turn the call over to Rajeev.

CEO REMARKS

Thank you Stacie, and welcome everyone. We delivered our seventh consecutive quarter of durable growth, with a compelling combination of high-growth revenue, significant profitability and meaningful cash generation.

Organic revenue in the quarter grew 25% year over year, reflecting the strength of our usage-based software platform. Adjusted EBITDA margin was 31%, demonstrating the tremendous leverage in our business. Cash flow from operations, an important indicator of the health of the overall business, was $19 million. Our long track record of profitability allows us to continually invest in innovation to capture the long-term growth opportunities in the face of a dynamic macro-economic environment.

PUBMATIC FLYWHEEL DRIVES CONSISTENT PERFORMANCE

Our consistent performance is driven by our unique infrastructure driven approach to digital advertising. We own our own infrastructure, which gives us the ability to control and optimize the entire technology stack as well as benefit from significant leverage from increased usage of our platform. The resulting flywheel of high margin revenue, re-investment in innovation, and expanded customer usage is a key competitive differentiator underpinning our results.

We are hard at work building the digital advertising supply chain of the future. This is a supply chain that connects publishers, agencies, advertisers, data owners, and e-retailers with each other and with consumers on a global basis across ad formats and devices. It is a supply chain that is efficient, transparent, free of fraud, and both rich in data and respectful of consumers' desires for privacy. And ultimately, it's a supply chain that maximizes value for our customers in terms of publisher revenue and advertiser return on investment.

LONG RUNWAY OF GROWTH

This vision creates a long runway for growth. Global digital ad spend is expected to be almost $630 billion in 2024, and it continues to grow at a rapid rate.[1] A programmatic approach is the only way to efficiently manage the growing variety of channels and ad formats alongside the expanding volume of inventory and advertisers.

As a pioneer in programmatic advertising, we believe we are in the early days of a long runway for growth. We entered the year with an estimated market share of 3-4%. Over the long term, our objective is to grow our market share to 20%.

To accomplish this, we are continuing to invest in multiple growth drivers that fuel the supply chain of the future, including supply path optimization, omnichannel technology and audience addressability, all with a dual focus on short-term results and long-term opportunity.

SUPPLY PATH OPTIMIZATION (SPO)

Buyers are actively consolidating their ad spend on fewer supply paths as they look to optimize their spend through robust targeting, direct technology integrations and workflows, and premium ad inventory across channels. Additionally, buyers are seeking more transparent and efficient media buying across the open internet. We are partnering with buyers to build for this future.

For Q1, SPO represented over 27% of total activity on our platform, up from 10% two years ago.

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[1] Source: MAGNA Global, 2021

Our partnership with GroupM is a great example of the SPO journey we are on with many of our buyers. After working together for multiple years in different parts of the world, we first announced a PubMatic and GroupM partnership in March of 2021. In February of this year, we announced the expansion of our global partnership which is rolling out in multiple stages over the course of the year. As part of this expansion, PubMatic will enable the GroupM Premium Marketplace, a programmatic marketplace focused on Connected TV and online video that will increase media buying transparency and efficiency. With our technology, GroupM is able to make the media buying process simpler and more transparent, enabling publishers to gain better inventory monetization and exposure to new clients within the GroupM portfolio as advertisers will be able to shift more of their ad spend to programmatic buying.

OMNICHANNEL GROWTH

As more spending moves towards programmatic channels, we see opportunity in our omnichannel capabilities as buyers and publishers seek to simplify their workflows and tech stacks by leveraging a single technology platform that works across formats and channels.

For instance, we continue to drive expansion across the fastest growing ad formats – CTV, online video and mobile app and web. With our single platform, we match buyer needs to publisher inventory at scale, regardless of device or content type in-use by the consumer. This omnichannel approach has positioned us as being particularly resilient over the last two years, as we've seen rapid changes in consumer behavior.

CTV is in the early stages of market adoption, however it's growing quickly. GroupM estimates global CTV ad spend to be $20 billion this year, growing to $32 billion by 2026. We believe this market can be substantially greater with the onslaught of premium inventory as large broadcasters and publishers broaden their offerings with ad-supported models. We are building for this future whether it's data enriched deals, Private Marketplace deals, or Programmatic Guaranteed transactions.

Our vision continues to rapidly gain market traction and we delivered another great quarter of outsized growth. Revenue from CTV grew more than 5 times over Q1 2021. We continue to add more premium CTV inventory to our platform and are now monetizing inventory from 176 CTV publishers. We're also working with device manufacturers, rising stakeholders within the CTV ecosystem. We recently signed three of the top five largest connected TV manufacturers who are utilizing our platform to gain access to the rapidly growing programmatic CTV advertising demand that we bring to them.

In addition, we are seeing growth and significant opportunity in the mobile app channel. We recently partnered with ironSource to bring incremental brand advertising demand to their in-app publishing inventory. These ads kept users engaged and inside the app, promoting a better user experience that benefits both advertisers and publishers and proving the value buyers and publishers gain with in-app video.

AUDIENCE ADDRESSABILITY

A critical aspect of the digital advertising supply chain of the future is audience addressability. As third- party data becomes less sustainable and relevant, the value of data is shifting to the sell side at the nexus of the publisher and the consumer. We see a significant role to play as a result of our being a leading technology provider to publishers. We offer a portfolio of solutions using known identity, first-party data, contextual advertising, and cohorts. With this approach, we can create a stronger, more sustainable, and privacy-safe advertising ecosystem that delivers superior monetization for publishers and increased ROI for buyers.

Our investments and advancements in addressability solutions help us unlock the massive retail media opportunity and expand our addressable market. Retail media is expected to be a more than $140 billion market by 2024. We are building technology and solutions to help retailers monetize their own media, extend their data offsite to monetize impressions from non-retail publishers, and to optimize ROI for buyers. At the same time, our addressability solutions are gaining traction with retailers and ecommerce companies today.

A major grocery chain and other retail giants are already choosing PubMatic to monetize their valuable first-party data off-site to unlock incremental revenue streams. In addition, digital savvy e-commerce platforms are leveraging PubMatic technology to power on-site audience-based private marketplaces.

CONCLUDING REMARKS

In summary, I'm extremely proud of the team and all that we've accomplished. We operate in a large and growing market with significant long-term opportunity. Regardless of the near term macro-economic conditions, we are incredibly excited about and focused on the long-term growth runway ahead of us. We've demonstrated resilience through peaks and valleys of the economic cycle, leveraging the strength of our infrastructure-driven approach, usage-based business model, and deep focus on innovation. Our profitability allows us to focus on and invest in long-term innovation and serve our customers while delivering consistent, durable growth quarter after quarter.

Let me now turn it over to our Chief Financial Officer, Steve Pantelick, to provide additional detail.

CFO REMARKS

Thank you, Rajeev, and welcome everyone.

In Q1, PubMatic continued its outstanding track record of durable growth, market share gains, and profitability with revenue of $54.6 million representing year over year growth of 25%, the 7th straight quarter above our long-term target of 20+%. It was also our 12th straight quarter of positive GAAP Net Income and our 24th consecutive quarter of positive Adjusted EBITDA. As a reminder, 2021 was our 9th straight year of Adjusted EBITDA profitability.

These results are particularly noteworthy and demonstrate the strength and resiliency of our business in view of the various macro headwinds that have emerged over the last several months, notably in EMEA. Robust growth in the Americas and APAC regions have helped offset these challenges.

Our investments in innovation, go-to-market resources and infrastructure have been instrumental to our financial results and produce a powerful network effect with increased visibility and scale, driving higher revenues from existing customers and delivering significant benefits to our customers and us.

We continued to outperform on the bottom line with first quarter GAAP Net income of $4.8 million and Adjusted EBITDA of $17.0 million, representing margins of 9% and 31% respectively. Our cash flow from operations was $19.3 million and free cash flow was $14.9 million, or 27% of revenue.

Before turning to the details of the quarter, I want to highlight the drivers that have underpinned our financial success to date and give us confidence in our long-term growth and profit trajectory.

First, we have built a scaled business in a highly fragmented industry that offers an omnichannel and global solution for publishers and buyers. Our purpose-built, globally distributed private cloud infrastructure and local go to market presence enable us to do business in every major ad market apart from China. This foundation allows us to expand across the world effectively and efficiently.

Second, our usage-based model combined with our proven ability to retain and grow revenues from existing customers provides a high degree of revenue stickiness and corresponding visibility.

Third, we have built a business with structural advantages emanating from our owned and operated infrastructure and offshore R&D that enables us to expand our competitive moat and consistently invest in innovation on behalf of our publishers and buyers.

Fourth, our operating model and global team have consistently achieved strong profit margins by staying focused on operational excellence while delivering value to our customers.

And lastly, we generate consistent cash flow, through rigorous working capital management and efficient capital expenditure.

REVENUE

Now turning to the highlights for Q1.

Despite the various macro headwinds in the quarter, we successfully navigated our business to deliver strong revenue growth across formats and channels. We benefited from having a broad set of over 60,000 advertisers, who leveraged our omnichannel, global platform. Our 25% growth in the quarter combined with last year's increase, translates to a two-year stack growth of 79%.

In aggregate, spending from our top 10 ad verticals increased over 40% year over year. Shopping grew well above the average, supported by a strong rebound in Travel at 150% and Arts & Entertainment at nearly 100%. All top 10 verticals grew double digits or more. The benefit of having diverse business activity on our platform was borne out in the quarter with faster growth verticals offsetting slower growth in the Automotive and Health & Fitness verticals. In April, we saw some softening in several verticals that was partially offset by continued strength in Shopping and Travel.

Revenues for our mobile and omnichannel video businesses, the combination of online video and Connected TV, grew 41% year-over-year, and accounted for 67% of our total revenues in Q1. This growth was on top of the prior year's growth of more than 63%. Revenue from CTV, inclusive of OTT, grew over 5X over Q1 2021. Our total desktop business comprised of display and online video also performed well with revenue up 15% year over year on top of the prior year's 23% growth.

We also continued to diversify our customer base as Yahoo! revenues represented less than 15% of our total revenues in the first quarter.

Supply Path Optimization relationships play a key role in terms of our growth and revenue stickiness as advertisers and agencies expand usage of our platform. In Q1 we continued to sign new SPO deals, renew existing agreements and grow ad spending via these deals. Our multi-year success with SPO supports further investment behind this opportunity, and we are building more tools to allow buyers to find the right audiences and media on our platform.The proportion of SPO spend to total ad spend increased from Q4 and represented over 27% of spending in the quarter.

An important indicator of publisher satisfaction and usage of our platform is net dollar-based retention. We again performed very well against this metric. For the last twelve months through Q1 2022, net dollar-based retention was 140%. As a reminder, it will naturally normalize and come down from this level once Q2 2020 results are no longer in the comparison set.

GROSS MARGIN

Our long-term success in achieving high gross margins is the result of our strategy and execution. We aim to put in service our maximum capacity every calendar year by the beginning of Q4. Once capacity is put in place it becomes a fixed cost in the near term that we then leverage over the succeeding periods. In seasonally lower spend periods such as Q1 and Q2, our gross margins are typically lower than second half levels.

As the year progresses, the combination of ongoing infrastructure optimization, the expansion of activity with our new and existing customers and higher seasonal ad spending results in significant structural leverage.

By owning and operating our infrastructure we have been able to drive down our unit costs. Over the last two years, we have reduced our cost of revenue per million impressions processed by 50%. Our experience has shown us that the return on investment for incremental capacity is high and typically pays for itself on a cash basis in months. With this cost advantage, we plan to continue expanding our processing capacity to capitalize on growth opportunities and to increase our competitive moat.

OPERATING EXPENSES

In Q1, the combination of increased headcount for growth and stock-based compensation resulted in operating expenses of $32 million, up 30% year over year. Excluding stock-based compensation, Q1 operating expenses increased 25%. Over the last 12 months we increased our technology team by 39% and our go to market team by 14%.

NET INCOME AND ADJUSTED EBITDA

Q1 GAAP net income was $4.8 million. Non-GAAP net income, which adjusts for stock-based compensation, the unrealized gain on equity investments, and related income tax effects, was $8.1 million or 15% of revenue.

Diluted EPS was $0.08 and Non-GAAP diluted EPS for Q1 was $0.14.

BALANCE SHEET AND CASH

Turning to our cash flow, we generated net cash from operating activities of $19.3 million in Q1 2022. Our free cash flow was $14.9 million, equal to a free cash flow margin of 27%.We ended Q1 2022 with cash, cash equivalents and marketable securities of $175 million and no debt.

FINANCIAL OUTLOOK

Now, onto our Q2 and full year 2022 guidance.

First and foremost, the factors that are driving our durable revenue, profit and cash generation remain solidly intact. We are confident in our long-term growth trajectory. We have built a business with strong innovation capabilities which allows us to capture digital advertising’s biggest opportunities in mobile and omnichannel video today while positioning us to take advantage of new opportunities that are emerging.

Looking to Q2, while we see several headwinds, our revenue is trending within the range of our expectations. To be clear, there is potential for further softening of European consumer demand amidst the Ukraine/Russia war, and challenging economic conditions ranging from high inflation to rising interest rates that may dampen consumer activity and advertisers' spending levels. In addition, there is of course, the reality that some parts of the world remain in Covid-induced lockdowns that affect both the supply chain and consumer activity. If any of these trends significantly worsen, our Q2 revenues may be affected.

For Q2, we expect revenue growth of 20% to 25%, or $60 to $62 million. As a reminder, we had a very strong Q2 last year with 88% growth. On a two-year stacked basis, our guidance translates to over 100% for the two-year period. We expect Adjusted EBITDA between $18 and $20 million, or approximately a 31% margin at the midpoint.

In terms of our investments to achieve our long-term growth potential, we plan to maintain our previously disclosed strategy of stepped-up investment in our technology organization. Over the next several quarters we aim to double this team with the majority of new hires to be added in our India technology center. Our hiring was slower than anticipated in the quarter but we have seen solid progress thus far in Q2. We also plan to continue adding key go-to-market team members across the globe to drive new product adoption and new market expansion.

We believe we are still in the early days of our growth and realizing the considerable business opportunity ahead of us. Accordingly, we are making investments now for long-term market share gains. Of course, we will revisit these plans if there are any major changes in macro conditions.

We are maintaining our full year revenue guidance of $282 to $286 million or 25% growth at the midpoint, supported by the anticipated robust second half growth from our SPO relationships, continued ramp up of our CTV business and political ad spending. Our full year guidance today assumes that macro conditions do not deteriorate significantly from where they are currently. In terms of FX exposure, we believe the risk is limited because most of the transactions flowing through our platform are denominated in US dollars.

On a full-year basis, we anticipate that GAAP operating expenses will increase in absolute dollars at roughly a similar percentage rate as 2021 with some quarter-to-quarter variability as the year progresses based on timing of hiring and investments.

Our operating expense assumptions include incremental operating costs of $5 to $6 million, related to the new offices we are adding, office reopening's and significantly higher travel and entertainment expenses as our team re-engages in-person with customers around the globe.

We are also maintaining our full year Adjusted EBITDA range between $101 and $106 million, or approximately 36% to 37% margin.

We expect capex for the year to be $33 to $36 million, up from our original expectations at the beginning of the year. We continue to see supply chain delays and therefore will be accelerating some 2023 investments into 2022. Based on timing of equipment availability and shipments, the bulk of our capex will occur in Q3 and will disproportionately affect free cash flow in that period.

As noted earlier, our proven track record of return on investment for incremental capacity is high and we believe this positions us well for future growth. Overall, we expect to increase the total number of impressions processed in 2022 by over 50% compared to 2021.

IN CLOSING

In closing, our first quarter results underscore the strength of our platform and the basis for our confidence in our future prospects. We believe we have the right platform and the right approach to be at the forefront of our industry. PubMatic delivers a compelling combination of durable growth and profitability, including cash generation, due to our unique infrastructure-driven approach to digital advertising.

We see a long runway of growth ahead of us as our TAM continues to grow. We are consolidating the sell side as one of the few scaled, global omnichannel platforms. And our profitability gives us a high degree of agility and the ability to invest in long-term market share gains, which is our plan.

With that, I will turn the call over to Stacie to open it up for questions.