

Q3 2022 Earnings Call

Company Participants

- Anil Chakravarthy, President, Digital Experience Business
- Dan Durn, Executive Vice President and Chief Financial Officer
- David Wadhwani, President, Digital Media
- Jonathan Vaas, Vice President, Investor Relations, Associate General Counsel
- Shantanu Narayen, Chairman and Chief Executive Officer

Other Participants

- Alex Zukin, Analyst
- Brad Sills, Analyst
- Brad Zelnick, Analyst
- Brent Thill, Analyst
- Jay Vleeschhouwer, Analyst
- Kash Rangan, Analyst
- Keith Weiss, Analyst
- Kirk Materne, Analyst
- Philip A. Winslow, Analyst
- Saket Kalia, Analyst

Presentation

Operator

Good day and welcome to the Q3 FY '22 Adobe Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Jonathan Vaas, VP of Investor Relations. Please go ahead, sir.

Jonathan Vaas {BIO 21700508 <GO>}

Good morning and thank you for joining us. With me on the call today are Shantanu Narayen Adobe Chairman and CEO, David Wadhwani, President of Digital Media, Anil Chakravarthy, President of Digital Experience and Dan Durn, Executive Vice President and CFO. On this call, which is being recorded. We will discuss Adobe's third quarter fiscal year 2022 financial results.

You can find our Q3 press release as well as PDF's of our prepared remarks and financial results on Adobe's Investor Relations website. The information discussed on this call, including our financial targets and product plans is as of today, September 15 and

contains forward-looking statements that involve risk, uncertainty and assumptions, actual results may differ materially from those set forth in these statements.

For a discussion of these risks, you should review the factors discussed in today's press release and then Adobe's SEC filings. On this call, we will discuss GAAP and non-GAAP financial measures. Our reported results include GAAP growth rates as well as adjusted growth rates in constant currency. During this presentation Adobe's executives will refer to constant currency growth rates. Unless otherwise stated reconciliations between the two are available in our earnings release and on Adobe's Investor Relations website.

I will now turn the call over to Shantanu.

Shantanu Narayen {BIO 3332391 <GO>}

Thanks, Jonathan, and thank you for joining us. Adobe had another record quarter, achieving \$4.43 billion in revenue, which represents 15% year-over-year growth. GAAP earnings per share for the quarter was \$2.42 and non-GAAP earnings per share was \$3.40. In our Digital Media business, we achieved \$3.23 billion in revenue. Net new Digital Media annualized recurring revenue or ARR was \$449 million. And total Digital Media ARR exiting Q3 grew to \$13.40 billion.

In our Experience Cloud business, we achieved \$1.12 billion in revenue and subscription revenue was \$981 million. In this digital first world, Adobe Creative Cloud, Document Cloud and Experience Cloud, have become even more mission-critical to an increasingly wide range of customers, from students to

Creative professionals to small businesses to the world's largest enterprises. Fueled by our groundbreaking technology, track record of creating and leading categories and consistently strong execution, our opportunity is larger than ever before.

Adobe's greatness has been rooted in defining new categories and platforms and delivering cutting-edge solutions through both, organic innovation and inorganic acquisitions. Throughout our history, Adobe's innovations have touched billions of lives around the globe. From revolutionizing imaging and creative expression with Photoshop, to pioneering electronic documents through PDF, to creating the digital marketing category with Adobe Experience Cloud, Adobe continues to invent and transform categories. We are in the golden age of design, and we believe we have a unique opportunity to usher in a new era of collaborative creative computing.

I am thrilled to share that today we announced our intention to acquire Figma, a leading web-first design platform that will help us accelerate this vision. Figma enables designers, developers and all stakeholders to collaborate in the product design process from ideation to design to delivery. The combination of Adobe and Figma will significantly expand our reach and market opportunity while making the creative process more accessible and productive to more people.

I will now turn it over to David to share more about our vision for Adobe and Figma, and momentum in the Digital Media business. David?

David Wadhwani {BIO 16728396 <GO>}

It's an exciting day for Adobe and Figma. Figma's mission is to help teams collaborate visually and make design accessible to all. Dylan Field, Figma's CEO, and his team launched Figma as the first design tool purpose-built for the web in 2012. Figma and FigJam make it possible for all stakeholders designing interactive mobile and web applications to collaborate through multi-player workflows, sophisticated design systems and a rich extensible developer ecosystem. Figma has built an incredible product and an outstanding business, delivering world-class ARR growth and net dollar retention with a disciplined and efficient operating model.

Figma has attracted a new generation of millions of designers and developers and a loyal student following. To give you a sense of their scale and financial success, Figma is expected to add approximately \$200 million in net new ARR this year, surpassing \$400 million in total ARR, exiting 2022 with greater than 150% net dollar retention rate. With a total addressable market of \$16.5 billion by 2025, Figma is just getting started.

Adobe has always been focused on empowering everyone to create digital experiences, and the combination of Adobe and Figma is the perfect better together opportunity. The combination of Adobe and Figma will create new opportunities and accelerate our strategy in a few ways. First, reimagining the future of creativity and productivity, Adobe and Figma share a passion for helping individuals and teams be more creative and productive. Adobe and Figma now have a new opportunity to make content creation more efficient, collaborative and fun by bringing together Adobe Express, Acrobat and FigJam, an online whiteboarding solution for teams. With the combination of these products, we can offer tremendous value to hundreds of millions of customers.

Second, accelerating creativity on the web. As creativity becomes increasingly collaborative, the web makes it easier for teams to create together. Figma's web-based, multi-player platform can accelerate the delivery of Adobe's Creative Cloud technologies on the web, making the creative process accessible to more people. This will dramatically increase Adobe's reach and addressable market opportunity.

Third, advancing product design. Web and mobile applications are increasingly underpinning how we live and work. This is driving explosive growth in the product design category. The combination of Adobe and Figma will benefit all stakeholders in the product design process, from designers to product managers to developers, by bringing powerful capabilities from Adobe's imaging, photography, illustration, video, 3D and font technologies, into the Figma platform over time.

And, fourth, empowering and expanding the community. Throughout our history, Adobe's community has been a constant source of inspiration and a catalyst for innovation. Figma has a thriving community who develop and share everything from tutorials, templates and plug-ins with their large and growing

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Ecosystem. The combination of our communities will bring designers and developers closer together to unlock the future of collaborative design.

Adobe and Figma could not be a better match. Our people, innovative technology and joint mission to democratize creativity and collaboration will deliver increased value to a growing base of customers. I look forward to welcoming Dylan and the entire Figma team to Adobe, once the transaction closes.

The acquisition of Figma could not come at a more exciting time for Adobe's Digital Media business, which surpassed \$13 billion in ARR this quarter, growing 16% year-over-year exiting the quarter.

Adobe Creative Cloud remains the world's creative engine, empowering everyone to create whenever and wherever inspiration strikes. In Q3, we achieved net new Creative Cloud ARR of \$330 million and revenue of \$2.63 billion, which grew 14% year-over-year. Q3 highlights include strong momentum for Adobe Express, with significant growth in new users. Adobe Express is serving an expansive universe of creative professionals, communicators and knowledge workers, from students to small business owners to social influencers. It's exciting to see the rapid innovation we're delivering to enable millions of customers to create standout multimedia content.

Adobe Express has thousands of templates, millions of stock assets and quick action functionality that make it easy to do any creative task. Millions of new users are coming to Adobe Express, driven by viral adoption and our creative marketing campaigns. Fast Company recently named Adobe Express one of the best new productivity apps of 2022.

Strength in our Photoshop and Lightroom offerings across desktop and mobile, tailwinds in our video segment for Premiere Pro and Frame.io, our integrated video editing and collaboration offering, demand for our Substance products, as brands across every industry embrace 3D and immersive content as a new medium and momentum in the Adobe Stock business, emphasizing the importance of content velocity for businesses of all sizes.

And, finally, we are really excited about Adobe MAX, the world's largest creativity conference. It will be held in Los Angeles and streamed live for our global community. In addition to unveiling amazing new Creative Cloud innovations, we will hear from luminaries, including renowned film directors, artists and musicians.

Now on to our Document Cloud business. Digital documents are enabling individuals and businesses to be productive in a digital-first world. With more than 300 billion PDFs opened and more than 8 billion digital signatures processed each year, Adobe Document Cloud is accelerating document productivity and workflows across web, desktop and mobile.

Document Cloud had its best Q3 ever, achieving net new Document Cloud ARR of \$119 million and record revenue of \$607 million, which grew 25% year-over-year.

Q3 highlights include, continued adoption of PDF across every computing surface, with over 2.6 billion cumulative installs of Acrobat and Reader. Significant enhancements to the Acrobat web experience, making popular verbs like view, edit and collaborate, easier than ever and adding accessibility capabilities such as Read Out Loud and High Contrast support.

Acrobat Web MAU continues to see tremendous growth driven by the high volume of web searches for document actions. Strong growth in Adobe Sign, driven by integrated e-signature functionality in Acrobat, integrated workflows between Acrobat Desktop, Acrobat Web and Adobe Express; and key enterprise customer wins, including Amazon, Boeing, Chubb, Lloyds Bank and ServiceNow.

Demand for our industry leading Digital Media products remained strong across a growing base of customers. We're accelerating momentum across the business with continued product innovation, strong go-to-market capabilities and a proven data-driven operating model.

I'll now pass it to Anil.

Anil Chakravarthy {BIO 16628903 <GO>}

Thanks, David. Hello, everyone. One thing has become abundantly clear in this environment, digital has become the critical channel to engage customers and drive growth. Across the globe, companies in every industry are prioritizing investments in software solutions and services that enable them to anticipate and meet the

Expectations of their consumers.

Customer experience management is an imperative and Adobe is the category leader. Adobe Experience Cloud delivers predictive, personalized, real-time digital experiences from acquisition to monetization to retention across content and commerce, customer journeys, data insights and audiences and marketing workflow. In particular, we are driving strong enterprise adoption of Adobe Experience Platform and Real-Time CDP, which are foundational to this next-generation enterprise architecture.

FC Bayern, one of the world's most successful football clubs, is leveraging Adobe Experience Cloud and Real-Time CDP to transform their fan experience. This gives them a holistic view of every fan's engagement online and offline, enabling them to deliver personalized experiences such as discounts at the stadium or an immersive shopping experience for viewers at home.

In Q3, we continued to drive strong Experience Cloud growth, achieving a record \$1.12 billion in revenue. Subscription revenue was \$981 million for the quarter, representing 15% year-over-year growth.

Q3 highlights include strong momentum for Adobe Experience Platform and AEP-native applications, with the book of business more than doubling year-over-year, significant

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growth for Adobe Commerce, underscoring the demand for digital storefronts and marketplaces. Experience Cloud was named a leader for the sixth consecutive year in the Gartner Magic Quadrant for Digital Commerce and achieved the highest position in the Forrester Wave for Enterprise Marketing Suites, and key customer wins, including Credit Agricole, Morgan Stanley, NASA, Qualcomm, T-Mobile and UnitedHealth Group.

Looking forward, Adobe is leading an explosive growth category that's increasingly important to enterprises of all sizes. Adobe is well-positioned to help enterprises deliver exceptional customer experiences with industry-leading platforms and applications, a strong track record of deploying solutions successfully for thousands of customers and a proven ability to deliver the next generation architecture for customer experience management.

Dan, over to you.

Dan Durn {BIO 17483115 <GO>}

Thanks, Anil. Today, I'll start by summarizing Adobe's performance in Q3 fiscal 2022, highlighting growth drivers across our businesses. Then I'll discuss the announced acquisition of Figma, and I'll finish with financial targets.

Adobe delivered a solid Q3, continuing to demonstrate that our products are mission-critical to our customers' success in any macro environment from the millions of individuals who use our offerings to create digital content, to the small businesses that run their document workflows on Adobe, to the large enterprises that have transformed how they interact with their end users by providing personalization at scale.

Q3 business and financial highlights included record revenue of \$4.43 billion, GAAP diluted earnings per share of \$2.42 and non-GAAP diluted earnings per share of \$3.40. Digital Media revenue of \$3.23 billion, net new Digital Media ARR of \$449 million, Digital Experience revenue of \$1.12 billion, Cash flows from operations of \$1.70 billion, RPO of \$14.11 billion, exiting the quarter and repurchasing approximately 5.1 million shares of our stock during the quarter.

In our Digital Media segment, we achieved 13% year-over-year revenue growth in Q3, or 16% in constant currency. We exited the quarter with \$13.40 billion of Digital Media ARR. We saw expected summer seasonality in the quarter, with the overall acquisition and engagement environment for our offerings remaining strong.

We achieved Creative revenue of \$2.63 billion, which represents 11% year-over-year growth, or 14% in constant currency. We added \$330 million of net new Creative ARR in the quarter.

Third quarter Creative growth drivers included, momentum in small and medium businesses with our teams offering, where we continue to drive strong new customer acquisition and are seeing engagement and retention at all-time highs, strong growth in our Illustrator and InDesign businesses, demand for our flagship photography, imaging

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and video applications, Adobe Stock, where we continue to drive strong book of business growth and momentum in our new growth initiatives, such as Frame.io and Substance, each of which grew ending ARR greater than 50% year-over-year exiting the quarter.

Adobe achieved Document Cloud revenue of \$607 million, which represents 23% year-over-year growth or 25% in constant currency. We added \$119 million of net new Document Cloud ARR in the quarter, our strongest Q3 to-date. Third quarter Document Cloud growth drivers included, accelerated adoption of PDF and Adobe Reader across multiple surfaces, growth of Acrobat Web, fueled by online searches for PDF and document actions, strong performance of Acrobat and Adobe Sign; performance of our reseller channel continuing to drive new Document Cloud subscriptions, particularly with small and medium businesses; and continued seat expansion in the enterprise. In August, we began to roll out the new Acrobat integrated with Sign offering, which included updated pricing.

Turning to our Digital Experience segment. In Q3, we achieved revenue of \$1.12 billion, which represents 14% year-over-year growth or 15% in constant currency. Digital Experience subscription revenue was \$981 million. Third quarter Digital Experience growth drivers included strong retention, up-sell and enterprise bookings in the quarter across our solutions, particularly in the US, success closing numerous million dollar deals, as well as larger transformational deals that span our portfolio of solutions, continued momentum with our foundational Adobe Experience Platform and Real-Time CDP business. With our book of business for Platform and AEP-native applications more than doubling year-over-year exiting the quarter, success integrating our solutions with workflow, including Workfront, which grew revenue greater than 35% year-over-year in the quarter; and Higher customer demand for professional services, as enterprises focus on implementations and value realization.

In Q3, we focused on making disciplined investments to drive growth, including a strong class of university hires and marketing campaigns to raise awareness of new and flagship offerings. We continue to have world-class operating margins and drove strong EPS performance in the quarter. Adobe's effective tax rate in Q3 was 22% on a GAAP basis and 17.5% on a non-GAAP basis. The GAAP tax rate came in lower, primarily due to benefits associated with share-based payments.

The non-GAAP tax rate came in lower, primarily due to additional US income tax credits. RPO exiting the quarter was \$14.11 billion, growing 12% year-over-year, or 15% when factoring in a 3% foreign exchange headwind. Our ending cash and short-term investment position exiting Q3 was \$5.76 billion and cash flows from operations in the quarter were \$1.70 billion, up 20% year-over-year.

In Q3, we repurchased approximately 5.1 million shares at a cost of \$1.80 billion, including shares received for the final settlement of our ASR entered into in December 2021. We currently have \$8.3 billion remaining of our \$15 billion authorization granted in December 2020, which goes through 2024.

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As Shantanu and David mentioned, we are thrilled about the opportunity to acquire Figma, which will accelerate Adobe's strategy. Under the definitive agreement, we've agreed to acquire Figma for approximately \$20 billion, comprised of approximately half cash and half stock, subject to customary adjustments. Approximately 6 million additional restricted stock units will be granted to Figma's CEO and employees that will vest over four years subsequent to closing.

The transaction is expected to close in 2023, subject to regulatory approvals. We plan to finance the cash portion of the consideration with cash on hand. And if necessary, a term loan to be paid down from our operating cash flows following the closing. Figma's products address a \$16.5 billion market opportunity, and the company has an impressive financial profile. This year they are expected to add \$200 million in net new ARR, surpassing \$400 million total ARR by the end of the year, with greater than 150% net dollar retention. We have a disciplined efficient operating model with gross margins of approximately 90% and positive operating cash flows. Figma has strong business momentum, a large and expanding customer base and we are incredibly excited about what we can bring to this combination from a financial perspective.

While this transaction is primarily about creating new markets, expanding adjacent opportunities and accelerating growth, we are committed to maintaining Adobe's strong profitability and maximizing EPS for our investors. In year one and two after closing, the transaction will be dilutive to Adobe's non-GAAP EPS, and we expect it to be breakeven in year three and accretive at the end of year three. While the transaction has not yet closed, I want to provide color on the path to non-GAAP EPS accretion as a combined company exiting year three, assuming Adobe's operating margin for the second half of fiscal 2022 as the baseline.

The combination will accelerate top-line growth for both Adobe and Figma based on three primary drivers. One, we extend Figma's reach to our customers and through our global go-to-market footprint. Two, Figma accelerates the delivery of new Adobe offerings on the web to the next generation of users. And three, we jointly introduce new offerings to market as we unlock the possibilities of collaborative creativity. Clearly, the explosive revenue growth of Figma combined with their efficient operating model would result in an expanding standalone operating margin.

Figma's innovative technology platform will accelerate our R&D roadmap, including the delivery of our Creative Cloud technologies on the web, which will allow Adobe to focus and manage our future R&D investments. We will quickly pay down any term loan, if necessary, after close. And then resume stock repurchases to reduce Adobe's share count. While the transaction is pending, at a minimum, we expect to maintain share repurchases sufficient to offset the dilution of equity issuances to Adobe employees.

We will now provide Q4 targets, which factor in the overall macroeconomic environment. FX headwinds, as the US dollar has continued to strengthen against foreign currencies and typical year-end seasonal strength in demand for our offerings. As a result, for Q4 we are targeting total Adobe revenue of approximately \$4.52 billion, net new Digital Media ARR of approximately \$550 million, Digital Media segment revenue growth of approximately 10% year-over-year, or 14% in constant currency, Digital Experience

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segment revenue growth of approximately 13% year-over-year or 15% in constant currency, Digital Experience subscription revenue growth of approximately 13% year-over-year or 15% in constant currency, tax rate of approximately 23% on a GAAP basis and 17.5% on a non-GAAP basis and GAAP earnings per share of approximately \$2.44, and non-GAAP earnings per share of approximately \$3.50.

In summary, Adobe continues to drive performance across Creative Cloud, Document Cloud and Experience Cloud, while making transformational investments in strategic growth initiatives. I look forward to sharing more about our growth opportunities next month in Los Angeles at Adobe's Financial Analyst Meeting.

Shantanu, back to you.

Shantanu Narayen {BIO 3332391 <GO>}

Thanks, Dan. It was great to be back on the road this quarter, meeting customers and partners as businesses returned to a new hybrid work model. I was inspired and energized welcoming our new hires and meeting Adobe employees across multiple sites who will together drive the next phase of innovation, growth and culture. Adobe's strength has always come from our most important asset, people. I am incredibly proud of the recognition we continue to receive as a great place to work.

This quarter, Adobe was named to Fast Company's Best Workplace for Innovators and Fortune's Best Workplaces in Tech. Next week, we will hold our Adobe For All conference to bring employees together to celebrate our shared values of diversity, equity and inclusion. It's an exciting time at Adobe. Our strategy to unleash creativity for all, accelerate document productivity and power digital businesses is working.

We are delivering on our innovative product roadmap, driving growth across new and established businesses and delighting a growing universe of customers. In addition to achieving all this success, we continue to look around the corner for new transformational opportunities that will drive decades of growth for Adobe.

We believe that every individual, team and business will strive to be more creative and productive in this digital era. Adobe has a unique opportunity to usher in a world of collaborative creativity. In my conversations with Dylan at Figma, it became abundantly clear that together we could accelerate this new vision, delivering great value to our customers and shareholders. I look forward to welcoming Figma into the Adobe family upon close of the transaction. We look forward to seeing you at MAX and closing the year strong.

Now, we'll take questions. Operator?

Questions And Answers

Operator

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Thank you. (Operator Instructions). Our first question comes from a Kash Rangan of Goldman Sachs.

Q - Kash Rangan {BIO 22837283 <GO>}

Hello, thank you very much. Congratulations on really massive step forward to the management team. Shantanu and team. I wonder if you can talk about the persona of Figma, and if there is any overlap at all between what Adobe wanted to be in the future with its a creative family and where Figma was going. And if you net it out, what is the incremental opportunity? It looks like \$16 billion TAM, but your own creative business you've outlined is having a more than a \$40 billion TAM. So, I'm wondering what the TAM could look like for Figma in the future as it integrates into Adobe you had [ph] identified new personas.

And for Dan, three years to breakeven. Sounds like there are some conservative assumptions built in, especially because Figma is generating cash. I'm wondering what the assumptions are for the rather lengthy duration to breakeven. Thank you so much and congrats.

A - Shantanu Narayen {BIO 3332391 <GO>}

Thanks, Kash, and congratulations to you as well for the conference that is happening right now. And given our quiet period as you know we can't attend, but let me take a step back and talk about why we believe this is a fundamentally transformative move for Adobe, when we think about the future of what's happening with creativity, and in a sense what's going to happen as it relates to multiple people engaging in that, with respect to collaboration.

We just believe that this is going to be an incredible value and a way to attract a whole bunch of new customers to the combined platform. When you think about Adobe, certainly we target knowledge workers, we target communicators, we target creative professionals, Figma really focus as a lot also on developers, they focus very much on the other stakeholders, who are involved in the product design process.

So, when we talk about the fact that Figma has a \$16 billion TAM, that's referring to the as it exist today. In terms of what they are doing, both as it relates to product design as well as as it relates to collaborative white boarding and ideation, which as you know FigJam's this incredible product that has, I believe, a much, much larger available addressable opportunity.

But if you take a really, what we think is the massive opportunity and putting this together, I think there are four aspects that are really exciting for us. First, there is going to be a next generation of creative collaboration that happens in the industry. And we believe that the combination of the two companies enables us to really position Adobe and deliver great value for this creative collaboration industry.

Second, we continue to believe that we can accelerate what it means to create on the web. What Figma has done is, they've delivered a really incredible technology platform and

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solved the number of the issues that need to be solved to allow multiple people to collaborate on the web.

Third, we think that we can advance product designs. And if you take the decades of Adobe technology that exists, our imaging technology, our vector technology, the video technology that we have and think about what that means to bring that to the web and dramatically increase the number of customers who can then benefit from it.

And last but not least, I think, to your question, this is now really addresses that sort of holy grail of anybody creating a mobile application, anybody creating a website, anybody creating an application for any device that has a screen, combining what we can do on the designers, developers and the stakeholders to make that happen. So, I think today what we shared with you is what they talk about as their addressable market opportunity, what we talk about as ours. But I think the real benefit of this combination is creating brand new markets, much like we have done with digital experience and other industries that we are part of. So, thank you, and we're really excited about this.

A - David Wadhwani {BIO 16728396 <GO>}

Yeah. Then from an accretion standpoint, first and foremost, this deal is about growth. This was about positioning the company to define new categories and drive growth for decade to come. And as we think about that growth trajectory walked into, walked through a number of those drivers. It's about extending the performance of that platform as part of the combined company, getting it access to our customers and our go-to-market -- global go-to-market footprint. It's about accelerating the delivery of new Adobe offerings on the web. And then jointly introduce new offerings as we unlock those possibilities and collaborative creativity. This gives us an opportunity to focus and manage the R&D investments as we drive that roadmap and striking the balance between accelerating the growth and preserving that growth trajectory, but doing it in a disciplined way, we're going to deliver tremendous amount of value over time to investors. Starting in year two, post close, you'll see our EPS growth rate faster than our overall revenue growth will be accretive exiting year three and we're poised to deliver a lot of value.

Q - Kash Rangan {BIO 22837283 <GO>}

Wonderful. Thank you so much and best wishes.

Operator

Our next question comes from Brad Zelnick of Deutsche Bank.

Q - Brad Zelnick {BIO 16211883 <GO>}

Thank you very much and congratulations. This is obviously a big moment for Adobe, it's pretty clear what Figma brings to the table in terms of innovation, collaboration and communities, and I appreciate the comments about Figma helping to further Webify [ph] core Adobe products, but what do you say to the perspective that this \$20 billion acquisition, seems more reactive versus proactive? And perhaps more importantly, how do we get comfortable that Adobe's organic innovation engine is alive and well for capturing the trends and opportunities that lie ahead and creative?

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A - Shantanu Narayen {BIO 3332391 <GO>}

Brad, it's a good question and I understand that in these markets in particular, acquisitions and maybe large ones are viewed with some skepticism. We certainly believe and I'll talk about it that Figma will be a transformative deal for the customers and industries and it dramatically increases our TAM we can deliver great value to an increasing set of customers, but I also want to reassure all of you. And if you look at our results. this no way changes our focus on our excitement on our current portfolio. We're growing well, we're demonstrating strength across all of our three cloud offerings and we continue to execute against our current initiatives.

And so if you look at the multiple internal businesses that are achieving velocity, whether it's Adobe Experience Platform and the apps that are built natively on top of it, what's happening with 3D and immersive, what's happening with Acrobat forms, what's happening with frame. This is additive. And when opportunities like this present themselves, Brad, I think it's the great companies that look at it and say, are you going to focus on the -- here and now only or are you going to seize on the opportunity that really positions Adobe for the next few decades? And so, it's a great question. We understand that there'll be questions associated with valuation. We certainly believe that it provides valuation to our shareholders as well when you look at what this means for us. But in no way diminishes my excitement around our current portfolio.

Q - Brad Zelnick {BIO 16211883 <GO>}

Very fair. Thank you and look forward to seeing it all on display at MAX next month. Thanks, guys, congrats.

A - Shantanu Narayen {BIO 3332391 <GO>}

Thank you, Brad.

Operator

And we can go to Alex Zukin of Wolfe Research.

Q - Alex Zukin {BIO 18006605 <GO>}

Hey, guys. So I'll start with with a non-Figma question and then layer in Figma. I guess, Shantanu, can you talk or David, can you guys can give us the kind of lay of the land on the demand environment? How it trended throughout the quarter? Obviously a lot of companies are seeing some elongation of deal cycles descoping even our channel checks on the Digital Experience side suggested that their deals are taking longer to close. They're requiring a lot more signatures. So, I guess, first of all, what are you seeing in the demand environment and what are -- because one of the questions we're getting from investors is, why now, given that we may be entering a more recessionary environment, couldn't you have done this type of transaction cheaper later. So that's kind of how I want to read [ph] this.

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah. Let me address the first part, which was your second part of the question, which is why now. Again, and as I said, we just believe that this new vision that we can create for what we can do with collaborative creativity. There's no time like the present to start working on top of it. And when opportunities like this present themselves, you have to act upon it rather than kicking that can down the road, Alex. So from my perspective, we know how to make this deliver great value to our customers. I'll have David also speak to the demand environment in the creative side.

On the enterprise side, as we said, we had strong results. I mean the AEP plus apps business that book of business is doubling, which really reflects the foundational aspects of what we are delivering. But, again, I go back to opportunities like this present themselves rarely and Figma is one of those rare companies that has achieved the kind of escape velocity and technology platform that they have. But we equally believe that it's even rarer for a company like Adobe to be able to take advantage of what they deliver and actually accelerate it and provide greater value. And so, from my perspective, there is no time like the present.

A - David Wadhwani {BIO 16728396 <GO>}

Yes, And on the Digital Media side, we began the year with the guide of \$1.9 billion. And, of course, we hope to beat that. And in the context of everything happening in the macro. If you look at Q1, Q2, Q3 and our guide for Q4, we're at \$1.88 billion. And in the context of everything happening in the world, we're very proud of this performance. And, of course, we're an aggressive company. We hope to beat that number and all the leading indicators remain strong, new user acquisition is strong, engagement and retention continues to be strong, monthly active users, continue to be strong. And so we feel really good about our ability to navigate the macro despite what's happening in the world around us.

And then in the context of, as we start looking for opportunities to grow, we have so much product innovation coming out and we'll see a lot of it at MAX accelerating what's happening in our flagship applications, what's happening around Express and the kinds of capabilities we're putting in there, we're seeing great growth and momentum in terms of use and NPS there Photoshop and Illustrator coming to the web. We have a lot of share for review collaborative capabilities coming as well.

And then, as you look at the conversation around Figma, we've known Dylan years and we've shared very common values and vision and the opportunities to grow that business faster and the synergies we have in mind are -- just allow us to take what is already a strong business and make it even stronger and faster.

Q - Alex Zukin {BIO 18006605 <GO>}

Perfect. Thank you, guys.

Operator

The next question is from Brent Thill of Jefferies.

Q - Brent Thill {BIO 1556691 <GO>}

Shan, you -- everyone's admired your ability stay disciplined on M&A over the last decade, I guess, many are kind of feeling like you're broke the mold on this. And I think everyone just wants to hear on the multiple -- even if revenue doubled again it'd be over 25 times ARR. So, what was it that was so special. And if you think about in the last few years you've always said XD could carry you why -- what happened with XD, what happens with XD now as this scales?

A - Shantanu Narayen {BIO 3332391 <GO>}

So, two things to that Brent. The first is, I understand that, what you're seeing in effect is some people will say, hey, show me how this value is accruing to Adobe shareholders as well. And we certainly believe that otherwise we wouldn't be doing it. And we do believe that it will be value-generating for the Adobe shareholders.

I think as it relates to XD and as it relates to Figma, I mean, we certainly for designers were targeting what needed to happen as it related to screen design with the desktop product. I think the much newer market that emerged which Figma effectively both, addressed and pioneered was the ability to do this in a collaborative way and dramatically increase the scale and they over the last decade have really invested invested in and solved some of the hard technical problems that existed to make this happen on the web friction free. So, from our perspective, the creative products continue to be strong, the ability to really tie the designers and developers is really where there's this unique opportunity as well as to create new markets.

I mean, I'll give you one more sort of what if scenario in terms of how we think about it, which is you combine what they've done with white boarding and ideation and what will be the future of work. And if you think about the presence of Acrobat and what we have with Acrobat or if you think about the notion of brainstorming and what happens with FigJam with what happens with Adobe Express. I think the opportunities are tremendous. I understand that there'll be some sentiment associated with the price and ball's in our court to go demonstrate, how we execute against our current initiatives as well as to demonstrate the value of this new one.

Q - Alex Zukin {BIO 18006605 <GO>}

Thanks, Shantanu [ph].

Operator

You can go to Keith Weiss of Morgan Stanley.

Q - Keith Weiss {BIO 6993337 <GO>}

Thank you guys for taking the question. One just real brief one on Figma, I don't want to beat dead horse too much, and then some questions on the core business. On Figma, we've definitely heard a lot about then in the field, and it's a great asset, you guys are acquiring it does seem like it overlaps pretty directly with InDesign.

So can you talk a little bit about sort of the -- is there a rationalization of those two products or is Figma just kind of the go forward product there. And then on the core

business, last week you gave -- last week. Last quarter, you gave us a little bit of an update on kind of how pricing was impacted -- impacting Digital Media net new ARR. I was hoping to get an update of sort of how the pricing impact flowed through this quarter. And then on the margin front, it looks like you guys pulled back on hiring a little bit, can you talk to us about the pace of investments on a go-forward basis. And whether that's going to be a little bit more measured given the macro impact starting to build up. Thank you very much.

A - David Wadhvani {BIO 16728396 <GO>}

Yeah. I'll start by talking about InDesign and Figma. They are very different products at the core. InDesign is around building print and publishing workflows and doing layout, Figma is really all about enabling product design and the collaborative product design model. In fact, if you look at InDesign, it's our traditional base of users, predominantly designers that are using it. One of the things that's really interesting about Figma is the makeup of their user base. In fact, two, third of their users are not designers, there are developers and other stakeholders in the process and the foundation of that collaborative model is what makes this such as special an accretive acquisition for us.

If you think about going forward, the primary focus is going to be about bringing Figma into the family and then taking all of the capabilities we have across illustration and video and creative imaging and building it on top of the Figma platform to enable a whole new generation of capabilities that are going to resonate with digital native and next generation creative professionals and we're very excited about them. The two products are quite different.

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah. Then from an investment standpoint, one of the great things about Adobe is, we've got tremendous growth opportunities. We've got an opportunity to drive the core franchise to \$30 billion and \$40 billion of revenue, but we're going to do what we've always done, which is invest in a disciplined way and drive that growth with strong profitability and strong cash flow. And so we'll do what we've always done, we're going to orient towards growth, we're back to utilizing our facilities, we're investing to scale our business, we're investing in our products go-to-market marketing, we're driving PLG motions, but we're going to do it in a disciplined way that deliver strong profitability and cash flow while growing this business in a strong and robust way. So, we'll do what we've always done, operating disciplined business.

Q - Keith Weiss {BIO 6993337 <GO>}

Got it. And on the pricing side.

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah. On the pricing side. First of all, pricing for us is all about value. The business that we've been building is all based on new user acquisition up-selling, and of course occasional pricing moves. And the pricing is always associated with added value. So on the Creative side, we've been adding lots of apps. We've been enabling Frame.io integration into Creative into our Creative Cloud applications. We've been building a lot

of share and review workflows, as an example, a lot of stock and content images in there as well.

And then, on the Acrobat Pro side, we've been doing a lot more deep integration with sign around bulk signatures, brandings, web forms, payments. So, the foundation is that pricing is always connected to the real value that we're adding. And in doing that. We continue to see pricing play out the way we expected and all of this was baked into what we had planned for the year.

Operator

The next question comes from Brad Sills of Bank of America Securities.

Q - Brad Sills {BIO 15854296 <GO>}

Oh, great. Thanks so much. Another question here on Figma. It looks like the company is well positioned for designer, developer use cases. Much like Frame.io for video editing bringing you into more of those use cases, really extending the reach for Creative Cloud. I guess the question is, where does Creative Cloud end up, where does that footprint end and the Figma footprint begin? In other words, could you see a scenario where this acquisition and these use cases bring through -- pull through more sales of Creative Cloud subscriptions?

A - Shantanu Narayen {BIO 3332391 <GO>}

I think there are three ways in which we look at that. First, in terms of the customers for Figma, I think, as David mentioned, the number of developers who are part of this products set is actually extremely extensive. But in addition to the product set associated with Figma design for developers as well as stakeholders, I do want to again emphasize the product fit as it relates to FigJam for anybody who is a knowledge worker and anybody who wants to ideate.

So, if you think about the value of ideation and brainstorming, I mean the reality is, they have tens of millions of people who signed up and trialed Figma, we have hundreds of millions of people who have used our products. And so the adjacency in terms of enabling both of those combined sets of customers to use each other's products, we continue to believe that drives great value. So this is really about in our sense. And then if you take Acrobat and the penetration that Acrobat has everybody who is using Acrobat also wants to both share as well as ideate and brainstorm. So I know there's a lot of questions around Figma design, which has clearly achieved escape velocity. I would urge you also to spend a little time looking at FigJam as I know you have.

And then really understand that also dramatically expands the customer base. So, yes, getting Creative Cloud to a more diverse set of customers on the web, allowing collaboration and enabling it much like you said with frame that's very much part of the strategy and that's why even in the press release, we talk about accelerating creativity on the web as one of the key pillars.

Q - Brad Sills {BIO 15854296 <GO>}

Thanks so much, Shantanu. Dan, one for you, please, if I could. You've talked about in the past some healthy pipeline builds for Q4, backing your confidence for Digital Media ARR guidance based on some good pipeline activity there for Q4, any update on that, please? Thank you.

A - Dan Durn {BIO 17483115 <GO>}

Yeah. No it's playing out as we expected, as we take a look at the enterprise business closing \$1 million-plus deals, transformational deals as we look forward off of that momentum into Q4 pipeline's building nicely. Team's doing a good job executing against the opportunity and it's playing out as expected.

Q - Brad Sills {BIO 15854296 <GO>}

Thank you so much.

Operator

The next question is from Jay Vleeschhouwer of Griffin Securities.

Q - Jay Vleeschhouwer {BIO 1498201 <GO>}

Thank you. Good morning, Shantanu, in some of your remarks and Dan, in one of your bullet points regarding the rationale for Figma, you made some interesting references to their platform and accelerating your products on the cloud. Are you suggesting perhaps that there's something in their DevOps, let's call it that may lead ultimately to a material change in Adobe's product release cadence or product packaging, how do you see your portfolio evolving and your underlying R&D, let's call it infrastructure or process, because there's something into in terms of how they develop products that I think you're hoping to splice in that kind of DNA.

And then secondly, it's not unprecedented for Adobe to purchase a dynamic competitor, we can go back many years. You done this before, maybe put this in the context of some of those prior acquisitions, where you bought a competitor that had meaningful either competitive impact or complementary technology and thinking of course about the material impact of the Macromedia acquisition had many years ago.

A - Shantanu Narayen {BIO 3332391 <GO>}

So, Jay, let me first cover the first one, and there's no doubt that what Figma has been able to do on the web by solving a lot of these multiplayer high scalability requirements to allow the 10s of millions of people to use Figma design and even more important FigJam on the web is an engineering marvel. And having access to that technology and being able to take advantage of it to dramatically increase anybody who is participating in our design products, whether they'd be stakeholders and developers, will I think dramatically increase our TAM as well. And so, first and foremost, their DevOps is great. I mean, we certainly have a lot of that expertise on the Digital Experience side of the house as it relates to, you know the trillions of transactions, but for the creative, we really believe that this is one of the key pieces of technology that we're getting that are going to be really amazing.

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I think as it relates to your second question, we really view these as, when you have the right altitude, for us it's all about how do you take things that might seem competitive but are actually more complementary and expand the nature of the market. And for me when I think about what we did with Macromedia, it was really about saying we're going to target more graphics professionals, and not just focus on imaging. We're going to focus on what's happening with video on the web or gaming. And so I think it was an expansive part of how we looked at it, and that's the same situation here.

For us, it's really not about you know what we had on the desktop, it's really about expanding to the web. Multi-surface is something that we have talked about a lot. It's about a community in many ways, Jay, and what they have done as it relates to their communities and plug-ins and how they have been able to use artificial intelligence, all of that also power we bring to bear to the combined. So from my perspective, this is really about adjacency, it's about complementary things that we have done. Certainly, we did have a presence in screen design on the desktop, but big picture, this is all about dramatically expanding it and that's the conversation that David, Dylan, Scott and I have been having.

And David, feel free to add to that.

A - David Wadhwani {BIO 16728396 <GO>}

Yes, from the beginning of the conversations with Dylan, the primary focus has been on things that we couldn't do individually. What are the things that we could do and bring to market that -- that combining the two products and the two product sets and two companies could really enable a better together story. And in particular, what we see is that we have this incredible wealth of technology and expertise around illustration and video and imaging and photography and 3D, all from coming from the lens of our flagship applications and as Shantanu mentioned, they've built such a rich platform for collaboration. Bringing these things together, allow us to re-imagine what the basically creative content creation should look like in the future, by taking our technology, integrating it on top of -- we're building it on top of the Figma platform and then enabling a whole set of new use cases that would never have happened were it not for this combination.

Q - Jay Vleeschhouwer {BIO 1498201 <GO>}

Thank you.

Operator

The next question comes from Saket Kalia of Barclays.

Q - Saket Kalia {BIO 16417197 <GO>}

Okay, great. Hey guys, thanks for taking my question and congrats to all on the announcement. Dan, maybe for you, just to maybe focus on the core business for a minute and then loop in, are there any puts and takes with margins this year that we should keep in mind when thinking about organic margins next year? And of course I understand you are not guiding to it, but just sort of anything that you want us to note. And then on top of

that, how do you think about the EBIT profitability for Figma and where that can go over time?

A - Dan Durn {BIO 17483115 <GO>}

Sure. So let me take them in order. So as we think about our margins this year, I think you can see the trajectory throughout the year. What I would say is, what we're seeing in the back half of 2022 I think is more reflective of a normalized environment. We talked about continuing to invest in the products, how we market those products, how we drive product-led growth, how we're going to market, but also complementing it with repopulating the campuses, being back to in-person interactions, getting on planes and that's a bit more reflective of a normalized operating environment. So, that's what I would say, think about maybe the second half of 2022 as a bit more of a normalized environment.

As we think about margins in the context of Figma and the transaction, we talked a couple of -- about a couple of things, we talked about this is about growth, this is delivering that growth in a disciplined way. So when I think about operating margins in that context, we talked about the second half of 2022 being that baseline more normalized run rate. And if I think about the first couple of years post close, year-one year-two post close, think about margins that are may be one to two points delta versus where we would be on a standalone basis. And then by the time we get to year-three, I would expect it to be more neutral from an influence standpoint.

And again, I also want to register the point that I mentioned earlier in Q&A. As we get past year-one, we're going to start growing EPS faster than our revenue growth profile and so we feel good about that inflection point and driving it in a disciplined way. When we look at GAAP operating margins, obviously you'll see a bigger delta in the near term. To account for the stock-based compensation, we really view that stock-based compensation to incentivize the employees to stay with the Company and unlock those growth potentials, and you'll see that amortize over a four-year period consistent with our equity program, and then we'll be back to a more normalized run rate after that amortization period. So you'll see more impact on the GAAP side and we feel pretty good about the trajectory from a non-GAAP operating margin standpoint.

Q - Saket Kalia {BIO 16417197 <GO>}

Very, very helpful. Thanks, Dan. Congrats again.

A - Dan Durn {BIO 17483115 <GO>}

Thanks.

A - Shantanu Narayen {BIO 3332391 <GO>}

Hey operator, we're coming up on the top of the hour. Let's try to squeeze in two more questions, please.

Operator

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Certainly. We can go straight to Phil Winslow of Credit Suisse.

Q - Philip A. Winslow {BIO 6300579 <GO>}

Hi, yes. Thanks for taking my question. I just wanted to focus on a little bit on more in the near term in terms of your guidance for Q4. If we were going back the last year, you saw sort of a lower uplift around sort of the Black Friday selling period, as compared to prior years. Now obviously, going into this Q4, it always is your seasonally stronger business or enterprise spend period for Adobe, but we're also going into that sort of the Black Friday period again -- again, obviously, when you think about your guidance for Q4, what are you baking in compared to last year for sort of those Black Friday trends, but also that sort of seasonal uplift in the business spending?

A - Shantanu Narayen {BIO 3332391 <GO>}

I think as we said in our prepared remarks, well, we are guiding in typical seasonality, Q4 tends to be a strong season, both in terms of the enterprise business for us and closing the enterprise business and the pipeline that we've built over the year, as well as some consumer commerce days as you mentioned, and all of that is factored into the targets that we are guiding. We're not changing that based on anything different that we've seen. So I think we continue to believe that our business is resilient and if you look at the initial targets that we're providing, we would expect to have another strong seasonal close to the year.

Q - Philip A. Winslow {BIO 6300579 <GO>}

Great. Thanks guys.

Operator

And the final question today comes from Kirk Materne of Evercore ISI.

Q - Kirk Materne {BIO 5771115 <GO>}

Yes. Thanks very much and congrats on the acquisition. Dan, I just wanted to follow up on your comments maybe on the dilution around the deal. I think just based on what Shantanu and all of you have said about sort of the complementary nature of the deal, the ability to expand the market, I think people are asking why isn't there more sort of a synergy from a go-to-market perspective with this deal, meaning bringing Figma onto your platform would theoretically just turbocharge sales immediately given sort of your scale. So I just -- how much of that's baked into the dilution forecast? Are you -- I realize it's early, but are you leaving that more for upside? Because I think the length of the dilution given that this should be complementary from a go-to-market perspective, I think is what's somewhat confusing the folks. Thanks.

A - Shantanu Narayen {BIO 3332391 <GO>}

Well, certainly for us, this is all about the top line growth and you know what, if you look at actually what we would expect in terms of their continued growth and our continued growth, I think the top line of both companies they would accelerate and so I think maybe at the FA meeting as we get more time, we're happy to share more color associated with

it, but from my perspective, we actually think that we have a plan that allows us to really show the benefits of the combination, as well as continue to overachieve against those. And since that is the -- go ahead.

Q - Kirk Materne {BIO 5771115 <GO>}

Just a follow up on that. It's just too difficult for us to, meaning you both can grow faster, are these new developers that require sort of new efforts to go get them from Adobe perspective? I'm just trying to get a sense of the overlap of the opportunity would seemingly think that you guys combined could actually do it more effectively together, which would create greater operating leverage to a certain degree sooner. So I'm just trying to -- I realize there's a lot of moving parts in the near term to this, but I was just kind of curious if that was sort of embedded in your expectations, or are you sort of leaving that for, to see what happens as you get, I guess a little bit closer to the deal closing?

A - Shantanu Narayen {BIO 3332391 <GO>}

I think for us, we're just factoring in everything including the fact that this is a stock purchase and half of it is approximately in stock and what that means in terms of dilution. As we said, we will start to offset that. We have tremendous cash flow generation. But from our perspective, we are going to be aggressive about making sure that we continue to drive the top line and the bottom line. And so that is very much on our mind in terms of delivering great value to the customers and the industry and creating new opportunities.

And from my perspective, what I do want to say, since that was the last question, was first and foremost, we're really excited about our current business. I mean the current business is growing at a great clip in this macroeconomic environment. We have multiple growth initiatives that are all demonstrating how mission critical they are and how relevant they are, in this new digital first world, where whether it's work, life, play, everything is going to be impacted by digital. So, first and foremost, we are very confident about our existing portfolio and the growth trajectory of the current portfolio.

The addition of Figma from my perspective is the ability to turbocharge that, in terms of both the opportunity that the Company has, as well as the ability to serve a ever broadening set of customers. And so, I hope you all view that within that context, which is, a lot of confidence about our existing business and more excitement about making sure that we're setting in place a greater future opportunities. We will look forward to having a lot of you at MAX. I hope you do come there. We are planning a FA part of that section as well. And so, we'd be happy to share more with you when we join that.

And with that, I'll turn it over to Jonathan.

A - Jonathan Vaas {BIO 21700508 <GO>}

Thanks, Shantanu and thanks everyone for joining us this morning. This concludes the call.

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