Q2 2020 Earnings Call

Company Participants

- John Murphy, Executive Vice President & Chief Financial Officer
- Jonathan Vass, Vice President of Investor Relations
- Shantanu Narayen, Chairman, President & Chief Executive Officer

Other Participants

- Alex Zukin, Analyst
- Brad Zelnick, Analyst
- Brent Thill, Analyst
- Jay Vleeschhouwer, Analyst
- Jennifer Lowe, UBS
- Kash Rangan, Analyst
- Keith Bachman, Analyst
- Keith Weiss, Analyst
- Kirk Materne, Analyst
- Mark Moerdler, Analyst
- Saket Kalia, Analyst

Presentation

Operator

Good afternoon, and welcome to the Adobe Q2 FY '20 Quarterly Earnings Call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions will be given at that time. Today's conference is being recorded.

I'd like to turn the conference over to our Vice President of Investor Relations, Jonathan Vass. Please go ahead, sir.

Jonathan Vass

Good afternoon, and thank you for joining us. With me on the call today from their home offices are Shantanu Narayen, Adobe's President and CEO, John Murphy, Executive Vice President and CFO, as well as Mike Saviage, who in March announced his retirement as Adobe's Head of Investor Relations and is continuing to assist with the transition.

On this call we will discuss Adobe's second quarter fiscal year 2020 financial results. By now, you should have a copy of the press release, which crossed the wire approximately one hour ago. We've also posted PDFs of our prepared remarks and an updated data sheet on Adobe's Investor Relations website.

Before we get started, we want to emphasize that some of the information discussed in this call, including our financial targets and product plans, is based on information as of today, June 11, 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 and uncertainties, you should review the Forward-Looking Statements Disclosure in our press release we issued today, as well as Adobe's SEC filings.

On this call we will discuss GAAP and non-GAAP financial measures. Reconciliations between the two are available in our earnings release and on Adobe's Investor Relations website. Call participants are advised that the audio of this conference call is being webcast live and is also being recorded for playback purposes. An archive of the webcast will be made available on Adobe's Investor Relations website for approximately 45 days. The call audio and the webcast may not be re-recorded, or otherwise reproduced or distributed without Adobe's prior written permission.

I will now turn the call over to Shantanu.

Shantanu Narayen {BIO 3332391 <GO>}

Thanks, Jonathan and good afternoon. I hope you and your families are safe and healthy. Adobe's second quarter coincided with what we hope was the peak of the COVID-19 pandemic. Around the world people shifted their attention to their health and their families. Businesses focused on protecting their employees, financial stability and continuing to serve their customers. Unfortunately, millions of people have lost their jobs and small and medium sized businesses have been hit particularly hard.

Through this crisis, Adobe's focus remains on employee health and safety, serving our customers and on ensuring business continuity. We took early and decisive action to direct our teams to work from home, suspend travel and cancel in-person events through 2020 to flatten the curve.

To support the communities in which we live and work we have donated over $5 million and 22,000 hours of virtual volunteer time to COVID-19 relief organizations. We are also proud to be part of the coalition that developed the COVID-19 Testing Data Response Platform, providing test screening, appointments and insights for public health officials and government.

We immediately instituted workstreams to control discretionary expenses and evaluate our strategic priorities to double down on those that will drive the greatest growth and profitability for the long term. Through all of this, the resiliency and flexibility of our employees has been awe-inspiring. I am proud of how our employees transitioned to this new reality.

Adobe is the digital experiences company, with millions of global customers relying on our products every day to create the world's content, automate critical document processes and engage with their customers digitally. Adobe's leadership in three large and growing categories: Creative Cloud, Document Cloud and Experience Cloud is driving our performance.

Adobe drove strong Q2 performance across Adobe Creative Cloud, Adobe Document Cloud, and Adobe Experience Cloud. We delivered $3.13 billion in revenue in Q2, representing 14% year-over-year growth. GAAP earnings per share for the quarter was $2.27, and non-GAAP earnings per share was $2.45.

In our Digital Media business, we drove strong revenue growth in both Creative Cloud and Document Cloud in Q2. Net new Digital Media Annualized Recurring Revenue or ARR was $443 million, and total Digital Media ARR exiting Q2 grew to $9.17 billion.

Q2 Creative revenue was $1.87 billion, which represents 17% year-over-year growth. Net new Creative Cloud ARR was $352 million. The past couple of months have shown us that in times of uncertainty people are turning to creative expression to learn, cope and make an impact. Adobe Creative Cloud is the center of this new creative renaissance, unleashing creativity for all and empowering millions of people around the world to tell their stories. As schools faced physical closures and moved online, we focused our attention on enabling them to create from home. We immediately provisioned 30 million students at home with Creative Cloud and provided teachers distance learning support.

In Q2 we saw historic highs in adobe.com traffic across both Creative Cloud and Document Cloud. Demand for our professional video products was particularly high with strong engagement for Adobe Premiere Pro and After Effects. We continue to see steady growth from social content creators using Premiere Rush, which saw a 75% increase in monthly active users quarter over quarter. Mobile traffic, member sign-ups and monetization continues to accelerate. Adobe Fresco has seen a greater than 40% increase in downloads since the start of 2020. Photoshop Express has surpassed 20 million in monthly active users.

Our teams are gearing up for a significant Creative Cloud update later this month featuring exciting new product innovation as well as new capabilities designed to facilitate collaboration between creators, particularly important in this environment. We're excited to make Photoshop Camera generally available on iOS and Android this week, bringing the magic of Photoshop to the point of capture. Photoshop Camera is a fun and easy consumer app targeted at social creators, an increasingly important segment for Adobe.

At Adobe, we believe everyone is a creator and we need to make products suitable for different skill levels. Adobe Spark, available both on the web and as a mobile app, is targeted at the large group of communicators who need to create social graphics, web pages and short videos for their business, school or community. As part of the strategic review of our Creative business, we've decided to increase our investment in two exciting areas: providing new solutions that address the unmet needs of the communicator segment and ensuring that the web browser is a first-class authoring platform.

We're proud of the role we play in inspiring the global creative community. With our Honor Heroes campaign we galvanized our community to create artwork honoring essential workers on the frontlines. We created an Adobe Fresco-compatible Digital Coloring Book and launched a creative campaign with musician Marshmello challenging fans to create a video for his latest single Be Kind.

Document Cloud revenue in Q2 was a record $360 million and we grew Document Cloud ARR to $1.24 billion. With Adobe Document Cloud, we're accelerating document productivity, enabling our customers to engage, transact and collaborate seamlessly in a remote work environment. As we did with Creative Cloud we implemented several programs to support our customers. This included making our web based PDF services on adobe.com free and implementing a Government Rapid Response program to assist local governments by providing extended trials for Adobe Document Cloud.

The shift to remote work has driven a surge in demand for digital documents, with use of web-based PDF services up nearly 40% quarter over quarter and the number of documents shared in Acrobat increasing 50% year-over-year. We continued to drive strong adoption for Adobe Sign, our cloud-based electronic signature solution, with usage increasing 175% since the start of our fiscal year. Mobile usage exploded with Acrobat Reader installations increasing 43% year-over-year and Adobe Scan installations up 66% year-over-year.

We're proud of the role our technology is playing in enabling our government customers to accelerate their transition to digital. The City of Seattle's digital workplace division deployed Adobe Sign across its departments when the city quickly shifted to telework. The State of Utah is using Adobe Acrobat and Sign as part of its telework initiative to facilitate emergency response and streamline communication across the state.

As part of the strategic review of our Document business we are increasing investment in Adobe Sign and our PDF services on the web and availability of PDF functionality through APIs to capitalize on the wholesale shift to remote work and digital-first document processes.

In our Digital Experience business, we achieved Experience Cloud revenue of $826 million for the quarter. As outlined at our last earnings call, we saw anticipated delays in enterprise bookings and consulting services implementations as companies prioritized employee and financial well-being. The extreme economic challenges that enterprise customers in certain verticals experienced as well as weakness in our commercial segment that targets small and medium sized businesses also adversely impacted bookings. In addition, the significant global decline in advertising spending impacted our Advertising Cloud revenue.

Despite the short-term challenges, the mandate to digitally transform has taken on heightened urgency. Enterprises continue to recognize Adobe's leadership in Customer Experience Management. Key customer wins in the quarter included IBM, Walgreens, Safeway, Astellas Pharma, and Allianz.

We are dedicated to our customers' success and proud to see the impact our technology is having. Government organizations such as the US Census Bureau are relying on Adobe Experience Cloud to modernize citizen experiences. 3M and Verizon are reaping the benefits of the Adobe Experience Platform and we now cumulatively have over 10 billion active customer profiles running on Adobe Experience Platform.

Adobe Experience Cloud was named a leader with the highest position among 19 vendors in the Gartner Magic Quadrant for Multichannel Marketing Hubs as well as a leader by Forrester in the B2B and B2C Commerce Suites Wave reports. We successfully transitioned Adobe Summit to an exclusively digital event where we debuted new Adobe Experience Cloud innovation, including Intelligent Services, Customer Journey Analytics and the Customer Experience Management Playbook. The Adobe Summit Live virtual experience enabled us to engage a far larger audience than an in-person event and set the bar for virtual events. Cumulatively we have engaged with more than half a million visitors.

While it was difficult to imagine only conducting business with CMOs and CIOs virtually, a side benefit of everyone working at home is that we are able to schedule and engage with far more customers across multiple continents. In all these discussions with business leaders it is clear that investments in digital and specifically customer experience are more important than ever. As a result of the strategic review of our Digital Experience business it is clear that we have an unparalleled value proposition and market leading solutions across content and commerce, customer journey management, and customer data and insights, all powered by the Adobe Experience Platform.

To further our lead, we are increasing our investment in AI and machine learning, next-generation applications and services on the Adobe Experience Platform, and accelerated integration of our content and commerce offerings. Our current advertising offerings consist of Advertising Cloud software solutions as well as Advertising Cloud transaction-driven solutions. We will continue to offer our Advertising Cloud software solutions to our Digital Experience customers, but this will not be an area of growth moving forward. CMOs want a single source of reporting and attribution for their advertising investment which we can uniquely offer through the combination of Advertising Cloud and the Adobe Experience Cloud. We have decided to accelerate our previously stated strategy of eliminating the low-margin Advertising Cloud transaction-driven offerings. These offerings are no longer core to our overall value proposition of delivering on customer experience management, nor contributing to our subscription-based bookings and revenue, and in fact are extremely resource intensive.

The impact of this strategic shift was evident in our Q2 revenue, cost of goods sold, and gross margin results and will be factored into future Digital Experience targets.

Earlier this year, we hired Anil Chakravarthy to drive the immense enterprise opportunity. Over the past few months, Anil continued to expand his charter with responsibility for strategy, product engineering and marketing, consulting and customer success for the Digital Experience business. Coincident with the long-planned retirement of Matt Thompson, Adobe's Executive Vice President of Worldwide Field Operations, Anil will now be adding responsibility for the entire Worldwide Enterprise Field organization.

Over the past 13 years, Matt has played a pivotal role in the company's transformation to a subscription software model in the Digital Media business as well as the creation of the Digital Marketing category. He has built a world class go-to-market organization and championed customer centricity. I will miss our partnership and wish Matt well in his retirement. Matt has built a deep management bench and I am confident that this combined organization will thrive under Anil's leadership.

Adobe is the market leader in customer experience management, and we have invested in deep product integration, platform innovation and a robust ecosystem. We're well positioned to execute on the growing total addressable market for Customer Experience Management.

At Adobe, we are guided by our belief that it's not only what we do, but how we do it that is core to our success. We believe that everyone deserves respect and equal treatment and we are outraged at the senseless violence against the Black community in the US. This is a painful reminder of the injustice and systematic racism that exists in our country. We can and must do better and we are committed to doing so at Adobe.

Great companies are defined by how they lead through adversity. We have successfully navigated several crises and have always used them as a catalyst to make strategic and structural change to emerge stronger. I am particularly proud of how our employees embraced the current challenges and rallied to ensure that innovation, customer centricity and adherence to our core values remains front and center. Our employees, broad and diverse portfolio of products, strong balance sheet and rigorous operating cadence put us in a rarified atmosphere among companies of our size and scale. We will emerge stronger than ever. John?

John Murphy {BIO 16018871 <GO>}

Thanks, Shantanu. In the second quarter of FY '20, Adobe achieved record revenue of $3.13 billion, which represents 14% year-over-year growth. GAAP diluted earnings per share in Q2 was $2.27 and non-GAAP diluted earnings per share was $2.45. Business and financial highlights in Q2 included: Digital Media revenue of $2.23 billion; Net new Digital Media ARR of $443 million; Digital Experience revenue of $826 million; Expanding profitability with strong earnings per share; Cash flows from operations of $1.18 billion; and Repurchasing approximately 2.6 million shares of our stock during the quarter.

Adobe's strong second quarter performance demonstrates our continued top-line and bottom-line growth despite an ongoing global pandemic. We are well positioned to navigate the continuing crisis given our resilient business model and a healthy balance sheet. In the work-from-home and distance learning environment, our strategy of fueling content creation, digital workflows and digital transformation is more relevant than ever, as digital engagement continues to underpin the global economy.

In our Digital Media segment, we achieved 18% year-over-year revenue growth in Q2. On an FX adjusted basis using rates in effect as of the start of our Q2, Digital Media revenue grew 19% year-over-year. During Q2 we added $443 million of net new Digital Media ARR, our strongest Q2 on record. Total Digital Media ARR exiting the quarter was $9.17 billion.

Within Digital Media, we achieved another strong quarter with our Creative business. Creative revenue grew 17% year-over-year and we increased Creative ARR by $352 million. During the second quarter we saw increased demand for our solutions on adobe.com amid the work from home environment, and usage of our products spiked notably during the quarter.

Q2 Creative growth drivers included: Strong new user growth across all geographies, including single app adoption by individuals; Adoption of our professional video products, including single-app Premiere Pro subscriptions, as engagement from communicators and Youtubers increased significantly; Strength in migrating students and trial users to paid subscriptions; Significant unit growth for paid mobile subscriptions; and continued focus on targeted campaigns using insights from our data-driven operating model, which drove significant growth in web traffic during the quarter.

Adobe Document Cloud delivered another quarter of strong revenue growth. We achieved record Document Cloud revenue of $360 million, which represents 22% year-over-year growth, and we added $91 million of net new Document Cloud ARR during the quarter. As with our Creative business, Document Cloud benefitted from tailwinds associated with knowledge workers and communicators working from home, and we had a particularly strong quarter driving new business for Adobe Sign, with net new ARR more than doubling year-over-year.

Document Cloud performance during Q2 was driven by a strength on adobe.com across the individual and SMB segments. Significant growth in consumer adoption of mobile apps and PDF services. Shortened deal cycles for enterprise Acrobat and Sign customers, as the imperative to translate paper processes to digital accelerates across the globe. Increased pipeline and improved execution in the government segment, particularly for our Sign solution and conversion of free mobile app users and our Reader install base to paid subscriptions.

Across Digital Media consistent with our expectations, we experienced some weakness for the SMB offerings in the reseller channel and adobe.com.

Turning to our Digital Experience segment, our primary focus is to grow software-based subscription revenue across our portfolio of products. Our Adobe Experience Cloud revenue includes: Subscription revenue, which includes revenues from Advertising Cloud, Professional services revenue, and other, which includes perpetual, OEM and support revenue.

In Q2, we achieved quarterly Digital Experience revenue of $826 million, which represents 5% year-over-year growth. Digital Experience subscription revenue was $707 million, representing 8% year-over-year growth. Digital Experience subscription revenue, excluding Advertising Cloud revenue, grew 18% year-over-year. As outlined on our Q1 earnings call, our Advertising Cloud revenue was negatively impacted given the COVID-19 situation. As we saw the extent of the global decline in advertising spend, we made the strategic decision mid-quarter to cease pursuing transaction-driven Advertising Cloud deals. Together this resulted in a shortfall of approximately $50 million relative to our targeted Q2 revenue.

A significant portion of the revenue from the transaction-driven Advertising Cloud offerings is recognized on a gross basis, with the related cost of media purchased recognized as cost of goods sold, resulting in low gross margin percentages for these offerings. While the discontinuation of these offerings will negatively impact revenue, it will enable us to drive improvements to our overall gross margins, DSO and the profitability of our Digital Experience segment, as already evident in this quarter's results.

We now expect approximately $200 million total Advertising Cloud revenue for the full fiscal year, with $70 million for the second half, decelerating from the first half of the year. As comparison, we achieved $360 million in Advertising Cloud revenue in fiscal 2019 and our original 2020 targets assumed that Advertising Cloud would grow at rates consistent with the overall subscription revenue for Digital Experience.

In Q2, our professional services revenue in Digital Experience declined approximately 8% year-over-year. While there were some delays in converting consulting backlog to revenue early in Q2, we saw progress in implementations as the quarter progressed. Through a challenging quarter we continued to build pipeline and saw strength in our Content and Commerce offerings, particularly in the enterprise segment. As with consulting, we saw some momentum late in the quarter in our commercial segment that targets small and medium businesses.

Across Adobe as we navigate the economic downturn we are managing the business carefully to drive growth and profitability. We reduced discretionary spending and delivered a strong operating margin. Our operating expense declined sequentially quarter over quarter as a result of a reduction in the pace of hiring, savings across travel and entertainment and in-person event cancellations. Having completed our strategic review and reprioritization, we will now turn our focus to investing appropriately for continued long-term growth.

From a quarter-over-quarter currency perspective, FX decreased revenue by $18 million. We had $5 million in hedge gains in Q2 FY '20, versus $7 million in hedge gains in Q1 FY '20 thus, the net sequential currency decrease to revenue considering hedging gains was $20 million. From a year-over-year currency perspective, FX decreased revenue by $37 million. The $5 million in hedge gains in Q2 FY '20, versus the $9 million in hedge gains in Q2 FY '19 resulted in a net year-over-year currency decrease to revenue considering hedging gains of $41 million. Adobe's effective tax rate in Q2 was minus 10% on a GAAP basis and 10% on a non-GAAP basis, in line with our Q2 targets.

Our trade DSO was 40 days, which compares to 42 days in the year-ago quarter, and 41 days last quarter. Remaining Performance Obligation or RPO grew by 19% year-over-year to $9.92 billion exiting Q2 and was relatively flat quarter-over-quarter, adobe.com cloud offerings, typically billed monthly, are reported as unbilled backlog, whereas channel offerings billed annually up front are reported as deferred revenue. The strength in acquisition from adobe.com during the quarter drove a mix-shift from deferred revenue to unbilled backlog. We exited Q2 with $3.46 billion in deferred revenue.

Our ending cash and short-term investment position exiting Q2 was $4.35 billion, and cash flows from operations was $1.18 billion in the quarter. Consistent with macroeconomic trends, we saw some increase in customer requests for billing concessions, we continue to be focused on working with our customers to ensure their success while managing our cash flows.

In Q2 we repurchased approximately 2.6 million shares at a cost of $850 million. We currently have $3.4 billion remaining of our $8 billion repurchase authority granted in May 2018 which goes through 2021. In light of the macroeconomic environment and the strategic shifts for Advertising Cloud, we are withdrawing the annual fiscal 2020 targets.

Our targets factor current macroeconomic conditions, continued impacts of the pandemic and typical Q3 seasonality across the summer months of June, July and August. For Q3, we are targeting: Revenue of approximately $3.15 billion; Digital Media segment year-over-year revenue growth of approximately 16%; Net new Digital Media ARR of approximately $340 million; Digital Experience segment revenue flat year-over-year; Digital Experience subscription revenue growing 5% year-over-year, or 14% when excluding Advertising Cloud revenue; Tax rate of approximately 10% on a GAAP and non-GAAP basis; Share count of approximately 485 million shares; GAAP earnings per share of approximately $1.78, and non-GAAP earnings per share of approximately $2.40.

We expect typical seasonal strength in Q4 across our Digital Media and Digital Experience business. We expect our operating expenses to increase in line with growth rates in previous years as we continue to invest for growth.

In summary, our resilient business model, healthy balance sheet and data-driven operating model enabled us to successfully navigate this unprecedented macroeconomic environment. We are extremely proud of how our employees have continued to innovate and remain productive. Our long-term opportunity remains robust given digital technologies will increasingly drive the global economy.

I'll now turn the call back over to Jonathan.

Jonathan Vass

Thanks, John. As we announced last month, we have shifted Adobe MAX, our annual creativity conference to be an online event this October. Information about the event can be found online at max.adobe.com. We plan to host a virtual financial analyst meeting later in the fall. Invitations will be sent to our analyst and investor email list this summer.

If you wish to listen to a playback of today's conference call, a webcast archive of the call will be available on Adobe's IR site later today. If you wish to listen to a playback of today's conference call, a webcast archive of the call will be available on Adobe's IR site later today. You can also listen to a phone replay by calling the numbers shown above. The phone playback service will be available beginning at 5 pm Pacific Time today and ending at 5 pm Pacific Time on June 18.

We would now be happy to take your questions and we ask that you limit your questions to one per person. Operator?

Questions And Answers

Operator

Thank you. (Operator Instructions) And we'll take our first question today from Brent Thill with Jefferies.

Q - Brent Thill {BIO 1556691 <GO>}

Good afternoon. Shantanu for the third quarter Digital Experience you're guiding to flat revenue growth, and I think many are just curious, given the digital tailwinds, why such a steep headwind on this business? And also the follow-up, if you could just talk to the field changes with Matt's departure and Anil picking up just reassurance around the field, and that there won't be any major changes. That'd be great. Thank you.

A - Shantanu Narayen {BIO 3332391 <GO>}

Sure, Brent. Happy to answer both of the questions. I mean first as it relates to Digital Experience I think as we said, while we saw a little bit of slowness in interest at the beginning of the quarter, we certainly, as people dealt with the employee issues as well as financial stability the interest and demand in Digital Experience absolutely continues to grow stronger.

With respect to Matt and Anil's transition we really don't expect any issue. Matt has been planning for this for a long time. Anil has certainly in his role as CEO at Informatica managed a field. There is a deep bench. Matt is available for a transition, and he is certainly going to remain a friend of the company.

And so I would not anticipate any issues whatsoever with respect to the field transition because the next layer is completely in place and has tremendous experience with Adobe.

I think as it relates to the revenue expectations for Q3, Brent I think maybe I can touch a little bit on what we've said with the advertising cloud again just to make sure everybody understands that which is the opportunity, if you take a step back around both digital experience and customer experience management there is no question that it's larger than prior to this pandemic and as you know Brent we have an unbelievably unique portfolio of products.

And so what we did was we said, let's take the opportunity to really prioritize the largest growth vectors as well as look at profitability. Content and commerce had a great quarter. Customer experience orchestration continues to be really important. Analytics and insight is really important, and Advertising Cloud as it relates to the solutions that we have for attribution and insight they add a significant amount of value for our customers.

However, again as we said, given an Advertising Cloud, they are two separate businesses the software-driven and the transaction-driven we did take the opportunity to accelerate our moving away from the lower margin transaction business something as you remember, we actually signaled at our Analyst Meeting last year.

And so when you take out the revenue impact associated with that, you will find that the strength of the business continues as it relates to bookings in Q2, we achieved the book of business per subscription bookings was greater than 15%, that in this current climate, I would say was excellent performance. And so we continue to feel really positive about the business, but hopefully that gives some color.

And the last thing I'd say is even if you think about our Q2 Brent when we guided to $3.175 billion and we said that we had $50 million in advertising revenue that we decisively decided to stop pursuing you know with the numbers that we posted you could see that we had a really good quarter.

Q - Brent Thill {BIO 1556691 <GO>}

Thank you.

Operator

Next question we hear from Keith Weiss with Morgan Stanley.

Q - Keith Weiss {BIO 6993337 <GO>}

Thank you guys for taking the question, and very nice job on the quarter. Shifting focus to the digital media side of the equation. John, in your comments you talked about seeing some weakness in the commercial, and SMB side of the equation. Frankly with to $443 million in net new ARR addition it doesn't really show through in terms of the numbers.

So it's pretty remarkable you saw that kind of strength even with the weakness, but can you walk us through kind of the puts and takes on that like what were the areas that were weaker, and sort of what were the areas that has such strong outperformance that you guys were able to even with that exceed your like 380 target?

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah. May be I'll start as well, Keith and then John can certainly add. I mean overall clearly when you think about the Creative and the Document business working from home, shelter-in-place and the ability to both create and tell their story as well as what's happening with the documents, you're right. I mean we had guided to about $385 million, it's a record for a Q2 for us in our business. So it was strong.

I think what we were trying to also give color was the different routes to market and when you think about the routes to market certainly adobe.com the traffic right through the quarter was very strong, because as you know, we have a data-driven operating model. We use the effective marketing tools to continue to drive visit our acquisition across the globe. I think small and medium businesses we would all say it was probably the most impacted as you think about our customer segment and therefore through the channel what we were trying to indicate was the back revenue was lower than we would have normally seen. We fully expect that business is going to come back as that segment continues to get strong, but Document Cloud, Sign, Video, single apps all did really strong Keith as it relates to what happened on adobe.com.

So it was more a route to market and there's probably some aspect of folks who typically transacted through the channel who are also probably coming to adobe.com as a result.

Q - Keith Weiss {BIO 6993337 <GO>}

Got it. Excellent.

A - John Murphy {BIO 16018871 <GO>}

Yeah. I mean probably I wouldn't add anything. Shantanu covered all the points there.

Q - Keith Weiss {BIO 6993337 <GO>}

Thank you very much.

Operator

Next we'll hear from Jennifer Lowe with UBS.

Q - Jennifer Lowe {BIO 6926228 <GO>}

Great. Thank you. Actually I wanted to follow up on Keith question a little bit, and maybe get a bit more granular because we certainly heard about some of the things that work in your favor this quarter. You put them in contrast of guidance which you to imply things being down sequentially, pretty significantly. How -- I know this is hard to parse out, but maybe just looking at the linearity of net new ARR you move through the quarter, where there sort of upswing and then sort of slowdown in demand as you kind of saw a surge as people move to shelter in place and work from home and that drove a specific level of demand that you don't expect to continue in Q3, because it seems like a lot of these things are durable.

So I'm just curious if you have any way of parsing out what might have been sort of a point in time around shifts in how people work, and maybe consumer demand attached to being at home relative to things which seem like they should be favorable durable shifts for the business?

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah. Jennifer, again I think the sheltering-in-place, work at home began when we lost spoke to you it was I think 10 days into the quarter, and we said that we had actually seen limited impact of COVID. And then we did see an increase as it related to the traffic, which actually continued quite high right through the quarter. So we continue to see the strength in that particular business, on the acquisition side, it's early, but the first few days of the quarter again we continue to see the strength in Q3.

I think as you know and have followed us for a while Q3 tends to be our seasonally weak quarter. We have such a great insight into the business as it relates to the data-driven operating model. So while the overall against the addressable market is certainly a durable trend. I think we're factoring in normal seasonality. We're not assuming that things will get better as it relates to the small and medium business. But overall, whether it's the Document Cloud or the Creative Cloud we continue to feel good.

I think if there was one thing that we probably overestimated, the impact of COVID as it related to the consumer space and now I think the number of you are like wow, that was great outperformance. And we, if you look at our Q3 numbers as well, it will clearly demonstrate continued momentum in that business.

Q - Jennifer Lowe {BIO 6926228 <GO>}

Thank you.

Operator

Saket Kalia with Barclays Capital has our next question.

Q - Saket Kalia {BIO 16417197 <GO>}

Okay, great. Thanks guys here for taking my questions, and hope all is well. Shantanu maybe for you. Can you just talk about the bigger picture, with the decision on Advertising Cloud. It seems like the margin benefit have slightly lower focus from the transactional part of the ad cloud. Kind of has an interesting by-product with the margin. And so perhaps the bigger question is, do you feel the team is perhaps going to balance profitability a little bit more with growth in the DX business than it has in the past?

A - Shantanu Narayen {BIO 3332391 <GO>}

Well. First Saket unlike other companies in the enterprise space, we've never pursued revenue that is not good profitable revenue which I know other companies do. And so I would say what we did really well in the quarter will say how do we take a step back, understand strategically what are the really long-term growth opportunities, and how is the business going to get transformed as a result of what we saw. In that particular context when every company on the planet, whether it's a small and medium, or large business is saying how do I engage digitally with customers? It's clear that the Content and Commerce associated with our offerings what we can do around customer journey orchestration, and the core analytics and insights is really where all of these built on experience platform is where we are unparalleled in terms of the unique differentiation

On the advertising side, they really were two businesses and this is something that we have talked about, which is there's a software driven business that shows how attribution works, that really can benefit from the Adobe analytics insight in terms of making sure you're spending that money well. And so that we will continue to offer. But we doubt that, that's going to be a huge growth opportunity.

It was the transaction business, which is very resource-intensive and that one we had always signal that we were going to be reducing that business. But we certainly use the pandemic as a catalyst to say let's make a change right now, so we can double down our resources on what really represent durable, long-term opportunity.

So hopefully that gives you a little bit of color on strategically why waste the prices in terms of making the changes that know you can make to be a stronger company.

Q - Saket Kalia {BIO 16417197 <GO>}

Very helpful. Thanks.

Operator

Our next question will come from Brad Zelnick with Credit Suisse.

Q - Brad Zelnick {BIO 16211883 <GO>}

Great. Thank you so much, and congrats to you all on a great quarter. My question is for John. John in your prepared remarks you stated there coming away from the strategic review, we will now turn our focus to investing appropriately for continued long-term growth. Can you expand on what exactly you mean by that? And how is that any different than what Adobe has always done?

A - John Murphy {BIO 16018871 <GO>}

Yeah, that's a fair question, Brett. I think when we look at Q2 because of the pandemic, we obviously benefited in earnings and our margin related to expenses, that basically slowed down because we couldn't hire the way we would typically hire, we can't travel we want to travel and certainly the cancellation of the adverse events. But we certainly are growth-oriented company, so the point really was to say, hey, we're going to invest in growth going forward.

We've got this great opportunities in front of as Shantanu laid out, and so the operating margin that we achieved in Q2 is one that I would pencil as a trend line is really what I was trying to get to. We have great opportunities to invest in growth and we've proven as we continue to grow revenue, we'll continue to grow profitability in long term.

A - Shantanu Narayen {BIO 3332391 <GO>}

And Brad, maybe just to add a little bit to what John added. I mean we actually took very decisive action at the beginning of the quarter because we did not know how widespread, how long the pandemic would be to make sure that we controlled our expenses. When you look at the opportunities that we have on the Document Cloud, when you look at the opportunities that we have with Experience Platform, the ability to continue on variable marketing to make sure that we're acquiring the right customers that will deliver the right long-term value.

I think that's really important for us to continue to make sure that we're opening up the company back to the long-term opportunities that we have because we going to be an even more unique place than the smaller companies.

So, to your point earlier, Brad, it is something that we always do. I think John was also referring to the early actions that we took and saying, hey, we understand our business, and so it's time to really focus on the long-term opportunities that will continue to drive both top and bottom line growth.

Q - Brad Zelnick {BIO 16211883 <GO>}

Thanks, again.

Operator

We now hear from Mark Moerdler with Bernstein Research.

Q - Mark Moerdler {BIO 16855032 <GO>}

Thank you very much for taking my question. And again, congrats on the quarter, given all the moving parts, it's a tough thing to work your way through. Document Cloud and Sign were really strong this quarter. As you mentioned, COVID -19 was a tailwind. Can you give us some color about how you think about those tailwinds going forward? Do they abate as people start to move back to their -- continue as they move back. Any color would be much appreciated.

And as a quick follow-up, can you give any color on how much of revenues now came through adobe.com versus traditionally? Thank you.

A - Shantanu Narayen {BIO 3332391 <GO>}

Mark, I think this is similar to the question that Jennifer asked which is nobody is going to go back to business as usual. I mean if you take, Adobe, as a company and how we also think about re-entry, I think the new normal is going to be people working in remote locations, engaging more digitally, making sure that digitization continues to be a really important phenomenon.

So I think as it relates to the Document as you know, Mark we've been excited about it. We always talked about the move from perpetual to subscriptions. We had talked about PDF services on the web and as we said that's all substantial growth making sure PDF, API functionality is available for anybody who wants a document as part of any system that they're trying to accomplish.

And so we don't think that abates. We think that these will just continue to be secular tailwind trends that we will benefit from. And I think that again going back maybe to Brad's question is the reason why we feel optimistic given everything that we've seen to make sure that we continue to capitalize on those particular opportunity. And so the Document business that is always been a growth, it just accelerated and we think, that's a trend that will be durable.

Q - Mark Moerdler {BIO 16855032 <GO>}

Helpful.

Operator

Next we'll hear from Kirk Materne with Evercore ISI.

Q - Kirk Materne {BIO 5771115 <GO>}

Thanks very much. As I want to stay in the same topic, in terms of the Document Cloud, Shantanu given that this might be the new normal, and maybe demand is getting pulled forward, are you apply more resources to that area from our sales capacity perspective either verticalizing even further. Just what you're doing I guess to capture maybe what is the pull forward in terms how people are thinking about the digitization of Documents?

And then John just on a related topic your bookings come back in Document ARR, Document Cloud ARR been up 30%, I think the last two quarters. Either, it seems to be an upward bias perhaps on revenue in that segment. Is that a fair assumption going forward? Thanks.

A - Shantanu Narayen {BIO 3332391 <GO>}

Kirk your first question is a good one. And again, going back to what we were able to do during this we have made it so that, the offerings that we have that combine the strength of what we are doing on Adobe Sign with the strength that we have on content in the Digital Experience business, and what we were delivering with forms, whether that was for the public sector, we have our entire field organization now out there evangelizing what we can do on the Document side.

So that gives you one example of a significant shift as it relates to making sure that we have our entire organization, aligned around the go-to-market. I think in terms of partnerships, and partnerships that we've done on the Document side, and Sign and the API functionality would always talk about the opportunity that we have with Microsoft and the integration.

We also announced a really strategic partnership with ServiceNow. If you think what ServiceNow is able to do, which is really change how workflows happen in an enterprise. Every single one of those workflows they need the statement of record as it relates to a PDF, that then makes that a tangible. So again that one, we've been able to do.

So really great question, and that's one of the ways in which we are able to pivot like a nimble small company rather than, and use our brand rather than wait. And so that's an example of the entire DX field organization also now has an offering associated with Sign that they can take into every one of our customers.

A - John Murphy {BIO 16018871 <GO>}

And, I think on the -- in terms of a bias towards Document Cloud revenue growth versus Creative you know both are just huge opportunities, and we continue to see growth opportunities coming from both. Certainly, obviously the pandemic kind of it -- may be accentuated the move to Digital Document workflows and on signatures. But as we talked about, we see some of these smaller businesses come back. We certainly expect them to come back in the Creative side as well because content creation is not going away as it's imperative going forward for these businesses. So I think we just are excited about the opportunity in both of those files and all the solutions associated with them.

Q - Kirk Materne {BIO 5771115 <GO>}

Thank you.

Operator

Jay Vleeschhouwer with Griffin Securities has our next question.

Q - Jay Vleeschhouwer {BIO 1498201 <GO>}

Thank you. Good evening. Shantanu, John does the strategic mix shift in DX improve the feasibility of you're getting back to a 65% or better gross margin in DX which is where you were before the TubeMogul acquisition? And perhaps as part of your overall strategy, you could also talk about the role of increasing self-serve, which we've talked about on prior calls.

Additionally at Summit, Adobe had some very interesting things to say about some new initiatives and technologies such as scalable content optimized personalization, pervasive commerce, which is really interesting one. And then of course applications and intelligent services. So maybe talk about the latter, in terms of how are you thinking about resources, for those an incremental business opportunity from those?

A - Shantanu Narayen {BIO 3332391 <GO>}

As always the Jay that was three questions, mirrored in one, but I appreciate all of them. I think as it relates to the COGS I think, and the gross margin you've actually seeing that improve even as you look at the data sheet that you have for Q2. So I think it's something like $35 million or something on quarter-over-quarter.

So I think you see the improvement in the COGS, we're constantly looking at our COGS and we want to make sure we improve. I think your question around Summit and the excitement that we have around all the things that we announced, is another reason why when you have that differentiated solution that's really where I think our value add to a customer is so much higher, and there's a lot of interest.

But there, a lot of interest as people look at it and say, all of this data that they are now drowning in how can they used Adobe's intelligent services so that it automatically personalize it whatever is required for a user across multiple channels. So you are right, I mean Summit for us was very interesting in that we were able to transact with a lot more folks.

We've got a lot more awareness out. We were able to, actually advance what we would do with Summit there were globally rolled out. I would say it's probably a little less mature pipeline and that's one thing that you miss the ability to move that forward. But all of that's now, we expect that trend as we move into the second half in 2021, because that is going to be top of mind.

So that's a little bit of how we're looking at it.

Q - Jay Vleeschhouwer {BIO 1498201 <GO>}

Thank you.

Operator

We'll now hear from Kash Rangan with Bank of America.

Q - Kash Rangan {BIO 22095432 <GO>}

Yeah. Thank you very much. First off, I want to just congratulate my friend Brent to on his 25 years of being a software analyst, Shantanu in case, you do not know that's my value add for you today.

But my question for you, Shantanu as far as Adobe, what were the lessons learnt by Adobe in this quarter, operating virtually as the company, what are the windows of or snippets of insight you could offer to us that go-to-market of product development, partnership, marketing the things that you were able to accomplish virtually and as a result how much of this it's here to stay as you look at 2021 and beyond. And the kind of savings, costs, expenses, whatever it as a revenue opportunities, how we should frame Adobe post pandemic?

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah, Kash. I mean, it's something that we are all focused on a lot as a company. I mean first, I will reiterate the fact that overnight as a company 20,000 employees all around the world are productive. I mean in my internal note to the company as part of this earnings I said I was just blown away. We had our first ever of virtual close the IT organization, in terms of how they've made sure that we are all productive through video conferences.

And I would actually say when you look at existing projects most people would say that their productivity is actually greater than 100% because, they are saving on travel, they are saving on the ability to be very productive without too many meetings, and so I think as it relates to the new normal on the product engineering side, it's been phenomenally successful.

I think we need a little bit more focused on what happens with respect to creating new projects. So that's one of the brainstorming that happens as it relates to the virtual whiteboarding. So that's something that we will continue to focus on.

On the dealing with customers, which was the other part. So internally we feel very good. On the dealing with customers I think that went through a little bit of a slow phase as customers were first thinking about their internal, but frankly right now, I mean sometimes you feel like you've conquered time and space because you can have meetings with people across four continents on the same day makes for a long day Kash, but it actually feels really good that we're now engaging with customers.

So we just feel that our ability to attract talent also wherever they might live that's going to improve. And so net-net, I would say, for a company like Adobe internally, our productivity is overall higher, but even more important, I think it does brought a pattern inflection point because every single company is now going to say, hey, I need to go talk to Adobe, whether it's about creative, whether it's about Documents, or whether about Digital Experience.

So I think the macro tailwinds is probably going to be the longer lasting benefit to a company like Adobe. And certainly, Brent congratulations on 25 years. I mean, the two of you have been great sort of followers of the company and very insightful. So congratulations.

Operator

We'll now hear from Keith Bachman with Bank of Montreal.

Q - Keith Bachman {BIO 3018411 <GO>}

Hi, thank you very much. Shantanu, I wanted to ask this to you. In the past you've talked about the growth of Creative being both people are units as well as price mix, and suggested that the growth of users, has been a greater contributor to the net growth rates of Creative. And, I just wanted to see given the pandemic over the next few quarters is that still true? And how are you thinking about potential price increases when you're normally introduced new products with the Creative suite? And then also just wanted to sneak in one to see if you could give us an update on Magento on traction and integration, and any kind of anecdotes on the run rates we've got property? Thanks very much.

A - Shantanu Narayen {BIO 3332391 <GO>}

Yeah, I think on your first question, there is no question that the Creative market and everybody who has a story to tell, it only getting larger. I mean, as we said we were proud of $30 million of provisioned feat for education, which is going to be I think a great base for us to build on. And I wouldn't say it is one segment or the other, I think really Keith, it's all of the different segments. Mobile did very well. We have different price points. We have spar for communicators. And again it is our vision is very clear.

It's the one-stop shop for everything from inspiration to monetization. So expect us to continue to see more offerings more price points and using our DDOM, frankly to both acquire them as well as to make sure that we serve them appropriately.

I'm glad you asked the question on Commerce. Commerce usage has certainly gone up very dramatically in terms of how we've seen it. The enterprise adoption of our Commerce solutions was very strong in the quarter. I think it's important for all of you to also remember that the way we do that is it's typically licensed base with a band of how many transactions.

So it's really not about -- the transaction doesn't immediately result in revenue, but whether it's a true-up or whether it's a increased band than they will have to go to shore. New customer acquisition was good in that. Usage is certainly gone up, it's almost like you're having Black Friday or Cyber Monday as every day. But we will continue to hopefully see that as we talk about renewals, how they get into higher bands.

A - Jonathan Vass

Operator we're coming up on the top of the hour. We'll take one more question, please.

Operator

Our final question will come from Alex Zukin with RBC Capital Markets.

Q - Alex Zukin {BIO 18006605 <GO>}

Shantanu, thank you guys for squeezing me in, and congrats to Brent for 25 years. I guess maybe, Shantanu can you talk a little bit about as you look at the linearity of the quarter, particularly for the Digital Experience business kind of is taking out the Advertising Cloud piece. Where are we in terms of sales cycle normalization in your mind? And then maybe as a, just a quick follow-up on the margins, given the new positive tailwind to gross margin from some of these initiatives, is it fair to say that the new operating margin profile should be somewhere between the 1Q and 2Q levels?

A - Shantanu Narayen {BIO 3332391 <GO>}

John, certainly you can add on the margin. I think, Alex as it relates to the linearity during the quarter, I think the month of March and this is probably true for most of the businesses that was where the real impact was felt, and then April actually became worse. I think as we got into May, people started to engage a lot more we saw signs of improvement. I think John touched on that as well.

And so I think that's the way I would highlighted for a month, month and a half, everybody new Digital was an imperative, but they had other fires that they were fighting. And then as it related to March, I mean, May -- sorry, it all started to open up and we're having far more conversations with customers.

So hopefully that gives you some feeling about linearity, which is why we are optimistic about moving forward as we have that pipeline, how we will deal with. The operating margin will be between the Q1 and Q2 levels. If you think about it, you're not going to see any big change dramatically. But as John said, I think we continue to invest it. And I realize we ran a little bit long with the prepared remarks, and so, you know we may not be able to get all of the questions.

But let me let me again say I'm really proud. I'm proud of what the company was able to accomplish in Q2. And I'm even more excited about what the future growth opportunities offer Adobe, because there is no question that digital is going to be even more of a driver of the economy. It's going to amplify the urgency for individuals to be creative and collaborative. It's going to improve the urgency for enterprises to engage digitally, and when you think about the portfolio of products that we have learning is no longer--learning to be creative will no longer be a luxury.

Dealing with electronic document is going to be the way business is transacted. The PDF platform and ecosystem is thriving. And on the DX side engaging digitally with customers is going to be mission critical irrespective of the size of the business. And so we're proud of our unique business model, growth is a priority for us but we will always focus as we have with great cash flow and high profitability.

I'm proud again as I said that we use this prices to further refine our strategy, and align the organization on what truly matters, which is sustained innovation and delighting our customers. Please stay safe, stay healthy. And thank you very much for joining us today.

A - Jonathan Vass

This concludes our call. Thanks, everyone.