

SNAP INC. Q3 2023 TRANSCRIPT

OPERATOR

Good afternoon, everyone, and welcome to Snap Inc.'s Third Quarter 2023 Earnings Conference Call. At this time, all participants are in a listen-only mode. I would now like to turn the call over to David Ometer, Head of Investor Relations.

DAVID OMETER, HEAD OF INVESTOR RELATIONS

Thank you, and good afternoon, everyone. Welcome to Snap's Third Quarter 2023 Earnings Conference Call. With us today are Evan Spiegel, Chief Executive Officer and Co-Founder, and Derek Andersen, Chief Financial Officer. Please refer to our Investor Relations website at investor.snap.com to find today's press release, slides, investor letter, and investor presentation.

This conference call includes forward-looking statements which are based on our assumptions as of today. Actual results may differ materially from those expressed in these forward-looking statements and we make no obligation to update our disclosures. For more information about factors that may cause actual results to differ materially from these forward-looking statements, please refer to the press release we issued today, as well as risks described in our most recent Form 10-Q, particularly in the section titled Risk Factors.

Today's call will include both GAAP and non-GAAP measures. Reconciliations between the two can be found in today's press release. Please note that when we discuss all of our expense figures, they will exclude stock-based compensation and related payroll taxes, as well as depreciation and amortization and non-recurring charges. Please refer to our filings with the SEC to understand how we calculate any of the metrics discussed on today's call.

With that, I'd like to turn the call over to Evan.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Hi everyone and thank you all for joining us.

Our revenue returned to positive growth in Q3, increasing 5% year-over-year and flowing through to positive adjusted EBITDA as our reprioritized cost structure demonstrated the leverage in our business model. We are focused on improving our advertising platform to drive higher return on investment for our advertising partners, and we have evolved our go-to-market efforts to better serve our partners and drive customer success. We also made progress toward diversifying our revenue, with Snapchat+

reaching more than 5 million subscribers in the quarter, resulting in Snapchat+ revenue growing more than 250% year-over-year.

Our focus on visual communication between friends and family is a strategic advantage that has enabled us to build engaging and retentive products and services across our platform. Our community grew to 406 million daily active users in Q3, and we are working to further deepen content engagement by focusing on three key areas: investing in our ML models to improve content ranking and personalization across all of our content surfaces, growing our creator community and diversity of content by supporting and rewarding creators, and using content to start conversations and build relationships across our service.

We continue to leverage AI technology to deliver new products and features to our community. Since launching My AI, more than 200 million people have sent more than 20 billion messages, which we believe makes My AI one of the most used AI chatbots available today.

More than 250 million Snapchatters engage with AR experiences on our platform every day on average. On November 9th, we will be livestreaming our sixth annual Lens Fest. We're thrilled to have the opportunity to bring together the vibrant Snap AR community of developers and creators that are collaborating with us to push boundaries, redefine what's possible with augmented reality, and build businesses along the way.

Given the progress we have made with our ad platform, the leadership team we have built, the work we have done to reprioritize our cost structure, and the strength of our balance sheet, we believe we are well positioned to continue making progress on our top strategic priorities. As we move forward into Q4 and 2024, we remain focused on investing in our platform to sustain community growth, investing heavily in our direct-response business to deliver measurable return on ad spend, and cultivating new sources of revenue to diversify our topline growth to build a more resilient business.

I want to thank Jerry Hunter, our Chief Operating Officer, for 7 years of service at Snap. Jerry has notified us of his intent to retire and will be transitioning his responsibilities by the end of the month. I am deeply grateful to Jerry for the meaningful contributions he has made over his many years at Snap. His work to improve our advertising platform, serve our community, and build a strong team has helped to lay the foundation for our future growth.

Thank you, and with that we will begin our Q&A session.

OPERATOR

Thank you. We will now begin the question-and-answer session. Our first question comes from Doug Anmuth with JP Morgan.

DOUG ANMUTH, JP MORGAN

Thanks for taking the questions. Your 4Q revenue guide mostly implies a deceleration versus 3Q, and I think that's coming on much easier comps. I was just hoping you could provide some color on October performance, especially given the war in the Middle East. And we know that 4Q is backend-weighted and I think the brand comps in particular get easier through the quarter. Just hoping you could talk about what's embedded there. Thank you.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Hi there, Doug, it's Derek speaking. I'll take that one for you. First and foremost, you're right, we had a quarter in Q3 that we're pretty pleased with on the progress we made on top line. There's a lot that went into that. We had a number of drivers to that outcome, including the progress we've made on our direct response ad platform.

We continue to make really significant investments in the ad ranking and optimization in quarter creating a much broader range of signals into the ad platform and driving much larger models. And we've also instituted a much faster pace of experimentation. All of that's leading to more precise conversion predictions, improved ROI for advertisers. And as we noted in the letter, in particular, 7/0 has been a bright spot in the quarter in terms of driving Pixel Purchase behavior and the year-over-year and quarter-over-quarter growth that we saw in lower funnel. And I also note that part of the strength in Q3 was around brand advertising, where we saw really good uptake on our total takeover products, including First Story that launched in the period. So, really pleased with the momentum that we saw there.

And I think as you look into Q4, I think we talked about a little bit in the letter, but to share some high level color, we believe we're on the right path to the DR platform. So we're pleased with the continuous progress we're making there, working with our partners on making their privacy safe integrations with the platform higher quality and more performant for them and driving out performance. We're also pleased with what we're seeing on our scaled solutions for small- and medium-sized businesses and what that drove out in terms of quarter-over-quarter growth in Q3 of 11% in aggregate, and the DR business returning to year-over-year growth. So, we're really pleased with fundamentally what we're seeing there and what we're executing against into the new quarter.

I think on the brand side, in particular, coming off of the progress that we saw in Q3 with those new brand products seeing really good uptake, you're right. As we move into Q4, Q4 is a little bit different as a quarter. Historically, we've seen a little bit larger share of the revenue coming from brand products in Q4, and then two, the Q4 business being a little bit more backend-weighted than other quarters historically as well. So both of those things sort of impacting visibility, and brand having grown at a

slower rate in Q3 and being a larger share of the business in Q4 sort of brings a little bit of a mix shift headwind.

And then last, the point that you raised very specifically, which is what we've seen since the onset of the war in the Middle East is we have had a number of primarily brand-oriented campaigns pause spending in the early period after the onset of the war there in the Middle East. I will say that we have seen a lot of those campaigns resume spending, and the impact to our daily run rate has reduced significantly as a result of that. But we also have seen a very small amount of incremental campaign pauses trickle in more recently.

And so, one of the things that we've tried to do here when we're thinking about giving forward-looking information for Q4 is number one, be transparent about what we've seen quarter-to-date on that side. And then, I think when we look back historically, for example, to what we all experienced at the onset of the war in Ukraine and the impact that that had on folks' businesses and the operating environment, I think we've realized that war is fundamentally unpredictable. And as a result, it would be imprudent to provide a formal guide in that kind of an environment.

However, what we did do for the sake of transparency for the investment community is share internal forecast, and that internal forecast assumes an acceleration at the top end, but we've attempted to incorporate everything that we know as of today about the impact of those pauses into the fullness of the range of revenue. So, you can see that. And then, of course, that obviously flows right through to the adjusted EBITDA range as well because we have a very high rate of flow through on those.

So I think just stepping back fundamentally, we're pleased with the progress we're making on the DR business. And we're pleased – we think we're on the right path with that platform, and we're also pleased with the uptake that we saw from those new brand products in Q3 as well. So, I think the progress there is good. We just want to make sure that people are aware of that one headwind we've seen to begin the quarter. And hopefully, that gives you a little bit of color on how we framed that. Thank you.

OPERATOR

Thank you. Our next question is from Ross Sandler with Barclays.

ROSS SANDLER, BARCLAYS

Great. Hey, guys. So Evan, you recently changed the leadership team in North America ad sales and that seems like the area that's not yet caught up with the rest of the business, which is performing quite well. So I guess how do you feel about that change? How confident are we that North America larger accounts are going to step up and commit to more budget with Snap in 2024? And when do you expect

that growth rate to kind of converge with the international business? If you can help us there. Thanks a lot.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Hey, Ross. Thanks so much for the question. We are making some progress in North America, the fastest-growing region quarter-over-quarter, but obviously, a long way from where we'd like it to be. In general, North America has a number of large customers that are simply just more complex to work with. So while we've made a lot of progress with some of the simpler integrations, our 7/0 optimization and whatnot for smaller advertisers, it's just taken more of a focus and more in the details work to drive customer success with larger advertisers.

So, I'm pleased with the progress that we're making. We're fixing stuff every day and getting advertisers closer to hitting their KPIs, or in many cases, above their KPIs, which should translate into improved spend. So making progress there, but definitely more complex customers and we're excited about Patrick's leadership of the team. He's got a wealth of experience to bring.

OPERATOR

Our next question is from Rich Greenfield with LightShed.

RICHARD GREENFIELD, LIGHTSHED

Hi. Thanks for taking the question. One question and then a housekeeping. In the employee memo that leaked a couple weeks ago, it stated a goal of 80% of your daily active users interacting with content. Trying to get a handle on how ambitious of a goal that is for 2024, is content engagement would seem to be a pretty critical driver of your advertising revenue potential, thinking about where ads are embedded. I don't have any idea really where you are in terms of how many DAUs touch content today. And what would be driving the growth to 80% of overall DAU. So, any color you can give us on that goal and where you are today and changes would be great.

And then two, just on the – also in that memo, you mentioned a 20% revenue growth goal for 2024. Evan, is that really hard to do? Like what's your confidence goal on getting 20% growth next year? Thanks.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Thanks, Rich. Yeah. That's an internal memo really designed to motivate and inspire the team around what's possible. When it comes to the content penetration, that's really going to be driven by emerging countries where, in some cases, our growth there is earlier in its cycle. And so, folks are just ramping up with our communications products and have yet to really transition to the content-focused products.

So when we talk about 80% of DAU, in aggregate, what we're really trying to accomplish is drive depth of – sorry, breadth of content engagement in some of the emerging countries, and then really depth of engagement in the more developed countries where we do have a very high rate of DAUs engaging with content already. So, that's really how that strategy – how we're thinking about the content strategy.

The 20% revenue, that's really about making more progress in terms of customer success, especially with the lower funnel. We are excited about the progress that we're seeing. So, we're hoping we can just keep our heads down and keep making more progress there.

OPERATOR

Thank you. Our next question is from Mark Shmulik with Bernstein. You may proceed.

MARK SHMULIK, BERNSTEIN

Yes. Thanks for taking the question. Evan, would love to hear just a little bit more color on My AI, like around usage. Are folks using this daily? What are they really asking their AI companion? And then, is there any like real commercial intent that you're seeing there? And kind of like a sub follow-up, any color you could share on how that Microsoft partnership is going there would be fantastic. Thanks.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Yes. We're excited about the progress we're seeing with My AI. I don't think it's really a daily use case yet. I think we hope that it's really a weekly use case for now, because there are some gaps, it doesn't yet have access to real-time information and those sorts of things. So, our primary focus right now is just improving response quality. As you can imagine, it's a little hard to measure because the responses can be unpredictable. So we think we've built a pretty good way of understanding if the responses people are getting are satisfactory, and we're seeing some of the work we're doing to improve those responses lead to higher retention with the product overall.

But I would say it's just very, very early with this product, and we're going to keep the vast majority of our focus on response quality, which we think can drive more engagement and long-term retention. There's certainly plenty of commercial intent. We are taking steps to integrate that, for example, into our models to help folks see more relevant content and advertising. So, making some progress there as well.

OPERATOR

Thank you. Our next question is from Justin Post with Bank of America.

JUSTIN POST, BANK OF AMERICA

Yes. Maybe I'll ask two. Lots of third-party data out here on engagement and time spent. Just wondering how you'd characterize engagement on the platform and the drivers from here. And then, I think you gave some DAU guidance, some modest slowdown. What are you seeing as far as DAUs in North America and Rest of World in Q4? Thank you.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

I'll let Derek speak to the guidance question, but overall, healthy engagement trends. We certainly see an opportunity in more developed regions like North America, where we do reach a very large percentage of the smartphone population to drive more daily usage with monthly active users. There are plenty of folks who are monthly active but maybe not daily active, who have messages that are unread from friends or Stories available. And so, we do see an opportunity to drive more frequency of use with monthly active users in regions like North America. Of course, plenty more headroom in the Rest of World region in terms of incremental new users.

We are also excited about what we're seeing on the content side. So, we saw year-over-year acceleration in time spent growth globally and some positive trends in the US as well, with US content time spend growing quarter-over-quarter. So I'd say in terms of overall engagement, we're pleased we see opportunity to continue growing it.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

And just to pick up the second part of that on the DAU forecast that we shared for Q4, which is 410 million to 412 million, first, just for context, year-over-year growth right there is about 35 million to 37 million DAU year-over-year. So, still seeing really significant year-over-year growth.

I think you got to look at this a little bit market-by-market. In North America, in particular, as an example, and some of our other more mature markets, we're reaching really high percentages of 13- to 34-year-olds in over 25 countries, and that would include, of course, North America and many Western European countries.

So, we're already at a very, very high penetration there. North America, for example, over 100 million DAU. And I think the latest number we shared on MAU was 150 million. So, the reach there is really, really deep and our focus and much of the growth in the DAU number in total recently has been coming from the Rest of World region. That's been the biggest driver of growth.

We had a very good quarter in the prior year as the comp there. And so, you're seeing that a little bit impacted in the year-over-year rate there. But otherwise, continuing to see substantial year-over-year growth of that internal forecast range, again, implying 35 million to 37 million additional DAU on a

year-over-year basis. So hopefully, that provides a little color.

OPERATOR

Thank you. The next question is from Brian Nowak with Morgan Stanley.

BRIAN NOWAK, MORGAN STANLEY

Thanks for taking my questions. I have two. The first one, little housekeeping, Derek, can you help us out a little bit with sort of the amount of subscription revenue in 3Q? And then, what are you assuming on subscription revenue contribution in your fourth quarter guide at the midpoint of one of the areas?

Then the second one, it sounds like you're starting to make some progress on the performance strategy. Can you give us a few more tangible examples of categories or verticals where you've made the most progress and how you think about the next categories to really sort of improve the performance for advertisers? Thanks.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Sure. Hey. I'll take the first part of that there. In terms of the breakdown on how we're doing on Snapchat+, I think first, we're really excited about what we're seeing there. That's a product that is not very old since we launched it. We reached more than 5 million subscribers in the period. So, we've had really nice momentum there.

I think if you go back to the Investor Day at the beginning of the year, we were – I think we shared then that we were running about close to \$100 million annualized run rate then. You've seen the subscription number grow about 60% then. So, to give you some sort of a ballpark of where we're trending to in the most recent quarter on progress of that product. So, certainly becoming a much more meaningful contributor. And we shared in the letter that it grew at a rate of more than 250% in the most recent quarter. So, really pleased with what we're seeing there in terms of uptake and what that's contributing to the business, both from a top line and margin perspective.

We don't have – obviously, going to break down our forward look for Q4 between different types of revenue, but we would expect to continue some momentum on the subscription business into Q4, just as we would on the advertising business as well. So hopefully, that gives you a little bit of an idea.

I'll talk about – a little bit about where we're seeing some strength with advertisers, and then if Evan wants to chime in with more detail on what – where we expect to go from here. Really, what we're seeing is we've been focusing very heavily on getting our go-to-market efforts and where we're seeing success in the progress of the ad platform really well-aligned. And so, making sure that we're selling

through the products and the optimizations that are going to work for our advertisers and help them grow their business. That's led us to see success with a pretty large variety of sectors. But some of the ones that we've talked about recently that I can share with you is we're seeing good traction with CPG, restaurants, and travel are categories that have been doing well on the platform and combination of retail and e-comm business is also doing well. And that's going to align well to both what I talked about earlier, which is the really good progress we've seen on 7/0 Pixel Purchase optimizations and what that's meant for lower funnel revenue growth year-over-year and quarter-over-quarter, and then also a little bit of the success that we've seen with those new brand takeover products and the traction that we got with those in Q3 that was helpful to the sequential improvement in revenue there. So hopefully, that gives you a little bit of a sense of what we're seeing both on the subscription side and the traction with different verticals of advertisers.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

I could speak just briefly to the progress we've been making on the tech side of things. We're making a lot of headway with our ML platform, being able to run bigger models that have more features. So I think that I feel good about our progress there, obviously more to do. I think kind of the atomic unit of our performance business right now is 7/0 purchase optimization. That's working well for a lot of advertisers. And so really, what we've been trying to do is then build on top of that to solve slightly more sophisticated advertiser needs.

So for example, with our app business, we've been beta testing event optimization for app advertisers. So rather than just optimizing around an install, optimizing around something like completing a level or something like that in a game. And that – those sorts of optimizations are really important for certain performance advertisers. So, I think taking that sort of fundamental building block that's working with 7/0 and then iterating on top of that to meet more advertiser needs is really important right now.

I also think there's more we can do in terms of advertiser cold start for the long tail of advertisers. It takes maybe a little too long and maybe a bit too much spend for these smaller advertisers to get ramped up and to find conversions quickly. So, we've also been iterating a lot there and making progress there. But overall, I feel good about where the various tech pieces are right now.

And one of the things we've just been learning as we go deep with these bigger customers is that it's become a lot more about the way that they're using these different pieces of our platform together, so really auditing signal quality, for example, going deep to make sure advertisers are bidding against the right goals for what they're measuring for. And I think just taking that customer success lens across all of our teams, from product to measurement, PMM, engineering, of course, to debug these more complex setups has yielded a lot of positive momentum as well.

OPERATOR

Thank you. Our next question is from Lloyd Walmsley with UBS.

LLOYD WALMSLEY, UBS

Thanks. A couple of parts to my question here. On the ads within My AI search, can you talk about how those are performing for you all, for advertisers? Are those all powered by Bing or some of them your own ads? And have you integrated that signal in the targeting across the platform? And I guess just broadly, while we're on the topic, how do you think about turning to partners like Microsoft Bing or others, just in general, to enhance monetization across the platform more broadly, similar to what we've seen at Pinterest? Is that something you guys think about doing beyond this Bing integration?

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

It's still early with the partnership. I think the click through rates are very healthy when the ads are relevant. So the big focus has really been on improving relevance, continuing to drive relevance for Sponsored Links in My AI. So far, in terms of signal integration, right now, we're using it to inform interest categories. I think there's a lot more we can do there. But we've sort of taken that initial step again sort of with the test and learn perspective.

So we think about this more as a longer-term investment, especially because the immediate work we're doing on the ad platform is yielding really meaningful results. So we'll keep focusing on the product experience, and of course, experimenting with the partnership, but there are more important priorities, I think, in terms of the ad platform right now.

OPERATOR

Thank you. Our last question comes from Mark Mahaney with Evercore.

MARK MAHANEY, EVERCORE

Okay. Hey. I just want to get into a nuts-and-bolts issue on ARPU or a question on ARPU. You had two kind of interesting trends here. European ARPU kind of jumped a lot. And I know this is an output indicator, but could you just maybe explain why that is, just like a 15% year-over-year growth? And then sequentially, North American ARPU jumped a lot. It's kind of the biggest sequential growth we've seen in a while. So, just any color behind those two metrics. And again, I understand that they're output metrics, but any color would be appreciated.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Hey, Mark, its Derek. Thanks for the question. Look, I think part of what you're seeing there is the fundamental improvements that we're making to the ad platform and the ad products and our go-to-market. So for example, when you're looking at the year-over-year growth in the European region, what we're seeing there is that the fundamental improvements that we've made to the DR ad platform. So some of the things I talked about earlier in terms of the big investments we've made in infrastructure to drive ad ranking and optimization, the work that we've done to incorporate a broader range of signals and features into those models and then those models themselves becoming much larger, the faster pace of experimentation that we're seeing on the DR platform, all of that's driving out much more precise conversion predictions and that's driving improved ROI for advertisers. And you can see that, as I mentioned earlier, in the improvement in lower funnel year-over-year and quarter-over-quarter.

And then the other thing is what I also mentioned earlier, which is these new brand products that we launched earlier this year, they got very nice traction in Q3, including First Story and the total takeover products, and then, of course, the go-to-market improvements that we've been making. And I think one thing in particular, in Europe and to a certain – and to an extent, in the APAC region, is that the new region Presidents for those regions came on prior to us making the significant changes to our ad platform in Q1 and prior to launching these products.

And so, those fundamental improvements to the ad product, the ad platform and the go-to-market, those are not just unique to the European region. For the most part, they're going to be globally applicable, including some of the really good improvements for making a scalable solution for small and medium-sized businesses. But you can see some of that is impacting North America a little later. And that's why North America, for example, was the fastest region quarter-over-quarter at 14% sequentially in growth, and that's a combination of those fundamental improvements coming to bear on the North America market, as well as the improved go-to-market exercise there.

So, I think what you're seeing is the work starting to show up in the output and the fundamental progress we're making with the ad platform, and that's showing up in ARPU, which is great news for the business all around. So, thanks for the question.

OPERATOR

Thank you. This does conclude our question-and-answer session, as well as Snap Inc.'s Third Quarter 2023 Earnings Conference Call. Thank you for attending today's session. You may now disconnect.