IAS Q2 2021 Earnings Script- FINAL

Jonathan Schaffer: Thank you. Good afternoon and welcome to the IAS 2021 second quarter financial results conference call. I am joined on today's call by Lisa Utzschneider, CEO, and Joe Pergola, CFO.

Before we begin, please note that today's call contains forward-looking statements. We refer you to the company's IPO prospectus filed on July 1st and any subsequent reports filed with the SEC for more detail about important risks that could cause actual results to differ materially from our expectations.

On today's call, we will also refer to non-GAAP measures. A reconciliation of non-GAAP measures to the most directly comparable GAAP measures is contained in today's earnings release available on the company's IR site: investors.integrads.com.

With these formalities out of the way, I'd now like to turn the call over to Lisa Utzschneider. Lisa, you may begin.

Lisa Utzschneider: Thank you Jonathan, and thank you to everyone for joining us. I am delighted to speak with you today on IAS's first earnings call as a public company.

I'll start my comments with a few highlights of our Q2 financial performance. I'll then provide a brief overview of IAS and how we believe we are uniquely positioned as the global benchmark for trust and transparency in digital media quality. I'll talk about our 4 growth drivers and our Q2 progress in each of these areas, including a discussion of our acquisition of Publica, a leading Connected TV, or CTV, Advertising platform; Finally, Joe will review our financials and outlook in detail before opening it up for questions.

IAS delivered an outstanding second quarter. We generated revenue growth of 55% year-over-year to $75.1 million, compared to last year's COVID impacted quarter. Our revenue was fueled by the continued strength of our advertiser direct channel and acceleration of our programmatic business, highlighted by the strong contribution from our contextual targeting offering. We also achieved strong profitability with gross margins of 83% and adjusted EBITDA of $25.7 million at a 34% margin.

Our second quarter results reflect IAS's continued dedication to our customers and commitment to making every impression count. The world's leading advertisers, publishers, and platforms trust us to create accountability within the increasingly complex digital advertising ecosystem. Our global customer base is loyal and diverse; composed of over 2,000 marketers and publishers, with an average tenure of over 6.7 years among our top 100 marketers.

IAS offers cookie-free solutions that address ad fraud, viewability, brand safety and suitability. We are deeply embedded in the advertising ecosystem providing solutions for both the buy side and sell side across open web, social platforms, and in every major demand-side platform, or DSP. Our solutions are always on, measuring all impressions on behalf of our advertisers.

Prior to IAS, I spent 20 years in leadership roles at global tech platforms like Microsoft and Amazon and was always field based in order to be close to customers. When I joined IAS in January 2019, my first priority was to listen to the customer and learn how IAS could deliver better outcomes for marketers. I met with dozens of marketing and publisher customers. This customer-first obsession is reflected in how we go to market with new products to meet our customers' needs. Our product pipeline is based on offerings that are global, scalable, and repeatable in multiple markets. Our deep partner integrations are one way in which we lead the market with innovative solutions. Google Automated Tag is a great example of a first-to-market technology we created in partnership with Google.

Let's now discuss our growth strategy and our recent progress. An acceleration of 'digital first' consumer lifestyles, due to COVID-19, means marketers are permanently shifting ad dollars out of linear TV budgets and following consumers onto digital platforms for better engagement and increased ROI.

This fundamental shift in the digital ecosystem is driving increased demand for our solutions in four key segments: international, programmatic, CTV, and social platforms. Let's take a look at each of these growth areas starting with our global footprint.

International revenue grew 58% in the second quarter. Currently, approximately 40% of our revenue comes from markets outside of the Americas,which we believe is considerably higher than any other competitor. We began implementing our global strategy over 8 years ago and today we have a well established global infrastructure that is generating revenue in 111 countries and in over 40 languages. We have successfully signed international brands such as Disney, GSK, Nestle and Adidas to multi-year contracts and serve as their trusted partner in every region across the globe.

EMEA and APAC revenue grew 61% and 51% respectively in the second quarter. Growth was driven by both new contracts with local brands as well as continued upsell and renewals of large existing customers. IAS's position as the premier verification partner in these regions allows us to develop long term relationships with marketers such as Volkswagen, Bayer, Sanofi and Shiseido, who then trust IAS to be their partner as they activate in new territories. For example, we signed an advertiser direct deal out of India this quarter with Samsung who also partners with IAS in the US, Germany, and the UK among other locations.

We see this trend in other emerging markets like Latam as well. We partner with Coca-Cola in many regions across the globe and because of the success of our partnership, Coca-Cola has activated in new markets across Latam. We believe that Latin America and APAC regions represent substantial growth opportunities, and we are investing in developing our business in these markets by way of expanded in-market customer service investment and by leveraging our global relationships.

Turning to programmatic, as programmatic buying becomes a larger part of the advertising ecosystem, marketers are increasingly focused on maximizing the impact of their digital ad spend and verifying the quality of digital media. Privacy legislation, third-party cookie deprecation, and other audience ID changes including Apple's Identifier for Advertisers, are increasing demand for targeting tools that do not rely on gathering audience based data. To address this, IAS launched our market leading contextual targeting solution, Context Control, with The Trade Desk in March of 2020. Context Control classifies content on a page level and analyzes it using our proprietary semantic technology. By the end of 2020, we had integrated with all major DSPs, including Google DV360, and we've seen strong market adoption with Context Control representing over 30% of programmatic revenue in Q2.

Context Control has been a major driver of our programmatic growth overall. This quarter programmatic revenue reached 42% of total revenue, up from 34% last year and we believe on track to reach 50% in 2023.

In Q1, we also acquired Amino Payments which is branded as our Total Visibility offering within programmatic. Total Visibility provides transparency into supply-path optimization of DV360. For example, a brand such as State Farm is able to gain transparency into both supply path costs for ad inventory as well as clearer understanding of the corresponding ad inventory quality. They can then dial up and down their allocated spend accordingly.

Next, I'd like to highlight the opportunity in CTV for IAS. According to eMarketer, the average amount of time spent with Smart TVs and other OTT Devices among U.S. consumers rose 34% year-over-year in 2020 to reach an average of 77 minutes daily; and our own IAS research suggests more than 9 out of 10 CTV users in the U.S. say they watch some form of ad-supported streaming video content. For marketers this represents a tremendous opportunity based on consumer adoption and engagement with streaming content. But as ad dollars shift; fraudsters follow. IAS was the first to bring ad verification to CTV with the world's first fraud and view-completion solution in June 2019.

This week, we are enhancing our leadership position in the space with our acquisition of Publica. As I mentioned earlier, Publica is a leading CTV advertising platform. Publica delivers true TV like experiences to streaming audiences by connecting supply-side platforms, or SSPs, to unique CTV inventory. Its ad server and unified auction for CTV inventory help publishers to obtain the highest yield. Publica can also measure the frequency and placement of ads in CTV environments, helping to solve a significant challenge for publishers. Publica reports that it delivers over 3 billion ads on CTV every month with publisher partners such as Samsung, ViacomCBS, and Fox. Publica reports that publishers using its platform have seen on average a 30% lift in yield for their CTV inventory.

We see both sell- side and buy side synergies that will advance IAS' position in the CTV market. Through this acquisition we are gaining valuable access to content and first party data that enables us to accelerate our CTV product roadmap. We believe that combined, IAS capabilities will enhance Publica's publisher solutions and IAS' reach, international presence, and current market position will enable us to further address large CTV publishers' needs at scale. In the future, we expect that IAS will be able to help advertisers with a trusted way to invest more budgets in CTV and measure the results by providing protection against ad fraud along with brand safety and suitability controls when buying CTV inventory.

IAS has a long standing relationship with Publica, dating back to 2019 and we could not be more excited to welcome the Publica team to IAS .

It's early innings in CTV for all verification providers but Publica really enhances our standing in the market. According to eMarketer, CTV in the US is approximately $13 billion out of $455 billion overall market ad verification opportunity today, but we're very bullish on the product roadmap. Our CTV revenue has grown 404% vs second quarter 2020 off of a small base. We are expecting a more meaningful contribution starting in late '22 into '23.

Finally, we're focused on bringing our ad verification and brand safety solutions to social platforms which are trying to keep pace with increased consumer engagement and the proliferation of user generated content. Social engagement is translating into an incredible share of the global digital advertising spend shifting to social platforms. As ad budgets move to social, marketers are calling for third-party solutions like ours that bring speed, transparency and precision to their social campaigns.

We believe innovation in social live feeds will create durable and sustainable revenue growth in this segment. In Q2 Social already makes up 37% of our advertiser direct revenue and we expect this number to reach 45% by 2023.

We are currently developing our own in-house solutions to detect and protect marketers from undesirable content in live news feeds. By relying on our own proprietary technology, we create the opportunity to scale our solutions to multiple platforms once opportunities become available.

IAS has recently partnered with TikTok to provide a brand safe experience in the live feed. I am excited to share that IAS and TikTok have launched an international brand safety beta, providing advertisers with industry-leading controls aligned with Global Alliance for Responsible Media standards for in-feed video. Our new global solution utilizes proprietary frame by frame video/audio/text classification technology specifically designed for social environments allowing advertisers to confidently promote their brand on TikTok. We look forward to sharing more news on our exciting partnership as we progress throughout the year.

Other notable social updates this quarter include IAS's differentiated platform-wide integration with the LinkedIn Audience Network. IAS is the first and only platform-wide provider for LinkedIn Audience Network.

Thank you again for your interest in IAS. As you know, our common stock began trading on Nasdaq on June 30th. We're excited to be speaking with you today as a newly public company with a tremendous opportunity ahead of us. We believe we have the right team, talent, technology, and partners to extend our leadership in the market. We'll look forward to reporting to you on our progress. And with that, I'll turn it over to Joe to review the financials.

Joe Pergola: Thank you, Lisa. I would also like to welcome all of you and look forward to working with you now that IAS is a public company. Before I review our second quarter results, I would like to remind everyone that my comments today include certain financial measures that will be presented on a non-GAAP basis. A reconciliation to GAAP measures is available in today's release. Let me start with our efficient and highly scalable business model and KPIs, before turning to a review of Q2'21 results and our outlook moving forward.

IAS has an agile and scalable business model, focused on high revenue growth and margins. We have significant re-occurring revenue that provides us with predictability in our forecasting. We partner closely with our advertisers and publishers to build multi-year, minimum impression commitments, as well as fixed fee agreements. Our revenue model is primarily based on impression volume with a blended CPM rate.

The success of this quarter is not only seen through our revenue growth, but the result of our strong and long-term customer relationships. As we continuously review our business effectiveness, efficiency, and execution, I would like to first highlight a few key business metrics that we believe will frame the performance of IAS going forward and then I'll speak about their drivers:

- Our second quarter net revenue retention was 142%, a significant improvement compared to 110% the previous quarter
- Our Total Customers grew 17% to 2,155 which includes 2,018 advertisers and 137 publishers.
- Additionally, our total number of large advertising customers with annual revenue over $200k grew by 21% vs the prior year period, ending the period at 187.

Turning to our financial results, we reported a strong quarter driven by double-digit gains in our Programmatic and Advertiser Direct channels.

Second quarter revenue was $75.1 million, which was a 55% increase from the prior-year period. It is important to note that last year several macro events affected our business in different ways including, but not limited to the global pandemic, social & civil unrest, and as Lisa previously discussed, the acceleration of a 'digital first' lifestyle.

Almost 90% of our total revenue comes through our advertiser direct and programmatic channels. The balance comes from our partnerships with our publishers, who we believe benefit from higher yield and optimization from accessing our data as well as contributions of our CM pixel business.

Our Advertiser direct grew 40% to $35.3 million vs the prior-year period. This $10.1 million increase was the result of higher impression volume, particularly across Facebook and YouTube, as clients such as Coca-Cola, Nestle, LVMH, Sanofi, L'Oreal, and Estee Lauder invest more in Social. We saw strong second quarter growth in Video revenue, which now accounts for 39% of our total Advertiser Direct revenue.

Total Programmatic Revenue grew 94% to $31.8 million vs the prior-year period, as a result of impression volume growth, and an increase in our average CPMs. Our Context Control solutions continue to scale and gain adoption since their launch in early 2020, and made up 30% of total second quarter programmatic revenue. We are seeing some of our larger clients such as American Express, Deutsche Telekom, Disney, Johnson and Johnson, and Volkswagen embrace our Context Control offering, driving up their programmatic spend year over year.

Our International investments and footprint continued to pay off. Our Americas to Rest of World revenue mix finished the second quarter at approximately 60/40. I am immensely proud of our dedicated global teams, and looking forward, I am confident in their ability to further grow and generate revenue in established and emerging markets. Our Geographic revenue splits were as follows:

- For the Americas, total revenue for the quarter came in at $45.4 million, up 54% vs the prior year period.
- EMEA finished at $22 million, up 61% vs the prior year period.
- And APAC finished at $7.6 million, up 51% vs the prior-year period.

Total gross profit was $62.2 million, resulting in a gross margin of 83% for the period, compared to 82% in the prior-year period. The high margins are reflective of our efficient cost-structure.

For Operating expenses, we incurred $41.5 million in stock-compensation expenses during the quarter as a result of our IPO. I will walk you through our operating expenses now, excluding the impact of stock based compensation to assist with comparability:

- Sales and marketing expense, for the second quarter of 2021 was $16.5 million, down 2% from the prior year period. Our cost-structure reflects an efficient go to market strategy and is a testament to our investments in building a scalable platform, both domestically and internationally.
- Product & Tech expenses were $13.2 million, up 3% from the prior year period as we continued to invest in order to maintain our leadership in technology and innovation.
- G&A expense increased to $10 million, or 17%, primarily due to professional fees and costs incurred to support our Initial Public Offering.

For the second quarter, our adjusted EBITDA increased to $25.7 million, from $3.8 million in the prior-year period, reflecting an adjusted EBITDA margin of 34%, driven by our top-line growth, and ability to leverage fixed costs as we scale. Cash generated from operations was $31.7 million for the second quarter.

Our net loss for Q2 was $35.1 million, or ($0.26 cents) per share, compared to a loss of $16.5 million or ($0.12 cents) per share in the prior-year period. However, excluding one time IPO related stock-compensation expenses net income was $6.4 million.

We ended the second quarter with cash and equivalents of $73.2 million compared to $51.7 million at year end 2020. Our financial position has strengthened following our IPO which closed in the third quarter; We raised approximately $275 million in net proceeds from our IPO, as well as the exercise of the underwriters' option, which will be reflected on the Q3'21 balance sheet. Proceeds will be used to reduce long term debt and we are also prioritizing investing in the business through organic and, as you saw from this week's acquisition announcement, M&A initiatives. Publica is a fast growing profitable business operating at similar margins as our core business.

Turning to our guidance,

For the third quarter of 2021, we expect revenue in the range of $74 to $76 million and adjusted EBITDA in the range of $16 to $18 million

For fiscal year 2021, we expect revenue in the range of $308 to $312 million and adjusted EBITDA in the range of $87 to $91 million.

Our guidance includes an anticipated contribution from the Publica acquisition of $3 million in revenue for Q3 and $7 million in revenue for Q4 2021.

Let me share with you a few notes for modeling purposes; We experience fluctuations in revenue that coincide with seasonal fluctuations in the digital ad spending of our customers. The global advertising industry experiences seasonal trends that affect the vast majority of participants in the ecosystem. Most notably, advertisers spend least in -the first quarter increasing spend throughout the year with the fourth quarter being our most important quarter, which includes the holiday shopping season.

Additionally, we expect an annual effective tax rate of 10%. For calculating third quarter 2021 EPS, we expect basic weighted average shares outstanding to be approximately 153.5 million to 155.0 million.

Lisa and I are now ready to take your questions. Operator?