CRITEO

Criteo Q3 2021 Earnings Call | Prepared Remarks

Edouard Lassalle – SVP, Market Relations & Capital Markets 220 words / 1+ min

Good morning, everyone and welcome to Criteo's third quarter 2021 earnings call. We hope you're all doing well today.

Joining us from our global Headquarters in Paris today are CEO Megan Clarken and CFO Sarah Glickman. Todd Parsons, our Chief Product Officer also in Paris, will join as well for Q&A. As usual, you'll find our investor deck on our website now, as well as our script and transcript after the call.

Before we get started, I'd like to remind you that our remarks today will include forward-looking statements, which reflect Criteo's judgment, assumptions and analysis only as of today. Our actual results may differ materially from current expectations based on a number of factors affecting Criteo's business. We do not undertake any obligation to update any forward-looking statements discussed today, except as required by law. For more information, please refer to the risk factors discussed in our earnings release, as well as our most recent Forms 10-K and 10-Q filed with the SEC.

We'll also discuss non-GAAP measures of our performance. Definitions and reconciliations to the most directly comparable GAAP metrics are included in our earnings release published today.

Finally, unless otherwise stated, all growth comparisons made during this call are against the same period in the prior year.

With that, let me now hand it over to Megan.

Megan Clarken – CEO

Thanks Ed and good morning everyone. Thank you all for joining us today.

I'm particularly pleased to announce our Q3 results so close to my second anniversary with Criteo. We delivered yet another strong quarter of double-digit growth and high profitability, above the high-end of our guidance. The sustained momentum in our business and company transformation reflects our steady progress and delivery on the strategy that we've laid out and on each of our strategic priorities. We continue to develop our Commerce Media Platform and strengthen our first-party data capabilities, positioning us to drive sustainable growth and long-term shareholder value.

On our call today, I'll discuss our Commerce Media Platform progress, provide additional color on our expected business resilience with regards to Apple's App Tracking Transparency, or ATT, and talk about our key highlights in the third quarter as we continue to deliver against our key priorities. Sarah will then cover our third quarter performance in more detail and discuss our financial outlook.

Let me start with an overview of our commerce media vision and progress. As you know, Criteo focuses on commerce media – the future of digital advertising that leverages commerce data and machine learning to target consumers throughout their shopping journey. We differentiate ourselves by delivering the best performing commerce audiences at scale – for the marketers and media owners that we serve on the open Internet.

Our Commerce Media Platform offers a holistic suite of solutions that activate the world's largest set of commerce data – for first-party data-based marketing and monetization. Similar to the proven playbook exemplified by the walled gardens, we're able to identify, reach and monetize highly relevant consumers to drive $40 billion of commerce outcomes for 22,000 marketers, a number that continues to grow, and thousands of media owners we have direct access to – including product consideration and sales for marketers like New Balance and Macy's, and rich ad revenue for media owners like Yahoo! Japan or Carrefour in retail media.

Driving the best commerce audiences requires rare assets and capabilities in data, media and AI. It's the combination of our unique data, media access, AI expertise and measurement capabilities that enables us to transform large crowds of generic consumers into highly-relevant, highly-performing commerce audiences. With a global consumer reach of 650 million Daily Active Users, huge scale in commerce data with 1st-party data from 22,000 customers and unique access to over $900B of ecommerce sales, a differentiated Retail Media offering working with various top-25 retailers in the U.S. and in Europe, and 15 years of expertise in commerce-focused AI, we're already a global powerhouse in commerce media with a strong first-mover advantage.

Our Total Addressable Market is expected to reach $100 billion by 2024, growing 22% per annum compared to our serviceable market last year. We're laser-focused on executing on this huge opportunity while continuing to gain share across all our existing markets.

While our team has done great work already, we still have lots to do. We continue to focus on growing our customer base, broadening our direct supply and first-party media network, and strengthening our first-party dataset.

I now want to take a moment to provide additional color on our expected business resilience with regards to Apple's ATT given the recent focus on this. It's important to note that our business is much more oriented towards web-based advertising than apps. While we do target in apps, this is a small part of our business. As a result, we believe we're much more insulated from the overall impact of Apple's ATT than large mobile app-first players. Our Retail Media onsite business does not rely on any third-party identifier and is therefore not impacted by Apple's ATT. Importantly as well, our total exposure to Apple users in our Marketing Solutions business, across both web and app, is limited to less than 10% of Revenue ex-TAC as of October 2021, including about 4% on app.

As part of our commitment to transparency with our shareholders, the expected impact from ATT and iOS15 changes is already reflected in the $55 million privacy and identity impact for 2021 that we had previously communicated to the market, and that Sarah will comment on shortly.

While Apple's changes make it harder for marketers to gain access to the data that enables tracking and affects media owners' ability to best understand and serve a consumer, this serves as an opportunity for us as we serve the market to offer alternatives. We've been working on alternative solutions to iOS and Chrome for over two years and are confident in our position today. To say this another way, we started our transformation journey years ago, and believe we're ahead in the race to drive superior performance in environments deprived of third-party identifiers. Our Commerce Media Platform, built on our First-Party Media Network, allows us to collect alternative, addressable identifiers, to build privacy-by-design audiences and drive commerce outcomes on inventory consumed by Apple users.

In addition, with broad reach of 650 million daily active users globally, we engage consumers not just on their Apple device but in the multiple environments in which they interact. In the U.S. alone, our largest single market and the biggest advertising market in the world, we reach over 50% of the U.S. population, on par with Facebook's app. This means that we have plenty of opportunities to reach and engage consumers along their shopping journey.

Shifting to our third quarter highlights. We continued to deliver against our 3 strategic priorities of growth, execution, and first-party data.

First, Growth. We achieved double-digit growth for the second consecutive quarter, driving Revenue ex-TAC up +14% at constant currency. We delivered the highest growth in our New Solutions in four quarters at +66%. And we're pleased that our new solutions now represent 28% of our total business, up 3 points compared to Q2. This fast growth in our new solutions is accelerating our revenue diversification, a key pillar of our transformation.

Second, Execution. Our team continues to execute steadily, with grit, focus and conviction, across our entire solutions portfolio for marketers and media owners. As I've said every quarter, we're committed to maintaining a high do/say ratio in everything that we do.

Marketing Solutions performed strongly, largely driven by solid growth with Retail Strategic customers like Macy's and BonPrix. We also experienced strength in our Core clients spend and a solid retargeting business. Retargeting remained healthy, growing 1% despite the expected impact from identity restrictions. Excluding incremental identity headwinds, retargeting actually grew 10%.

Within Marketing Solutions, growth in our New Solutions accelerated to 68%, up 16 points vs. Q2, with growing contribution from our Agency partners. Audience-first Targeting is a growing area of focus for us, enjoying steady momentum with both our retailer and brand customers, and the agencies they partner with. Growth in our Audience-first Targeting solutions accelerated 18 points compared to Q2, to close to 50%, as marketers increasingly spend across the entire marketing funnel with us. Omnichannel, our product that helps marketers optimize their marketing investments across online and offline, now represents 20% of our New Solutions business within our Marketing Solutions Portfolio, growing about +140%. We see increased traction from customers willing to target consumers everywhere and bridge the online and offline worlds as ecommerce remains strong and economies increasingly reopen. Lastly, we're launching very exciting tests of our new Shoppable video ads offering that Todd mentioned at our Investor Day. This opportunity is very compelling for our marketer clients and for us, and we are encouraged by the early results.

In Retail Media, we see accelerating momentum as well. We delivered 65% growth in Revenue ex-TAC, accelerating by 16 points vs. Q2. Year-to-date, Retail Media has grown an impressive 70%, accelerating both on a 1-year and 2-year basis. We see continued momentum in our Onsite business, largely driven by the growing network effects of our Retail Media Platform, which provides our unified Retail Media offering for brands and retailers on a single platform. Close to 80% of our Retail Media business in the U.S. already goes through RMP. We had strong growth with our top

U.S. retailer customers, added 10 new retailers globally and launched 10 retailers on the Retail Media Platform, including Walmart Canada, BestBuy and Douglas. We're also thrilled to have our Retail Media Platform power the recently announced retail media programs of large U.S. players including Ulta Beauty and Lowe's. In addition, our marketplace business delivered solid performance during the quarter, accelerated by our successful acquisition of Mabaya performing in line with our expectations. And we continue to make good progress on our offsite business, which allows brands to extend their commerce audiences beyond retailer properties to the open Internet, with a strong retailer pipeline expected to drive acceleration in Q4.

Our third strategic priority is First-Party Data. As we've said before, connecting first-party supply will become the ONLY way for both marketers and media owners to effectively advertise and monetize commerce audiences on the open Internet – once the industry finally moves beyond third party cookies.

We continue to make progress in securing first-party data via Retail Media. Our Commerce Media Platform strategy is anchored in our Retail Media onsite business, which is entirely built on first-party data and does not rely on any type of third-party identifiers – whether cookies or IDFAs –, further strengthening our moat and our lead around first-party data.

We also continue to make progress in securing first-party data via our first-party media network, working directly with media owners to power first-party data media buying on the open internet. Today, approximately 60% of our daily active users on the web are addressable through media owners we have direct access to. Building upon our legacy Direct Bidder product, we're actively increasing our direct integrations with publishers, including as part of our evolution to a full Supply-Side Platform. Our key focus remains the quality of our direct integrations with media owners, ensuring deep relationships with the most strategic players. That's why, in every market, we typically ensure direct paths to the Top 100 publishers giving marketers advantaged and transparent buying on the properties that matter most to their business success.

And, with our Commerce Media Platform, we also deepen our relationships with direct publishers by expanding their inventory reach to key consumers through new sources of marketer demand and greater publisher monetization and addressability. Last quarter, we discussed our initiative to bring Third-Party Demand through the Criteo SSP and broaden our buying scale with our direct media partners. With over 550 global publishers already signed up, our SSP allows us to leverage our commerce data on a larger scale, bring our direct publishers larger buys of supply executed through Criteo or other third-party DSP, and secure our long-term direct access to quality media.

In short, with Retail Media's unique first-party data assets and our larger media purchasing scale, including through more direct media integrations, we're uniquely positioned alongside the Walled Gardens to drive the best commerce audiences on the open Internet based on first-party data.

In closing, we're very pleased with the sustained momentum in our business and company transformation. We're making steady progress and delivering with focus on each of our key priorities of growth, execution and first-party data. We continue to expand our Commerce Media Platform to drive the best commerce audiences on the open Internet, further positioning us for sustainable growth and long-term shareholder value.

With that, I'll turn over to Sarah to discuss our financial performance and guidance. Sarah?

Sarah Glickman – Chief Financial Officer

Thank you Megan, and good morning everyone. I'm delighted to be presenting such a strong quarterly performance today. I will walk you through our financial highlights for Q3 as well as our guidance for the rest of 2021.

Starting with our financial highlights. Revenue was $509 million, growing 8%, with 72% of year-over-year growth driven by existing customers and 28% driven by new clients. Our revenue growth was primarily driven by favorable pricing. The total media spend activated by our Commerce Media Platform was over $2.5 billion over the last 12 months and close to $615 million in Q3, growing 23% at constant currency. Revenue ex-TAC grew 14% to $211 million. As expected and previously communicated in our guidance, this included $17 million of incremental identity and privacy impacts compared to last year. On a two-year basis, Revenue ex-TAC grew an estimated 9% excluding incremental privacy impact, showing solid momentum. Our Revenue ex-TAC margin represented 41.5% of revenue, up 200 basis points year-over-year, largely driven by Retail Media and the acceleration of our client transition to the Retail Media Platform.

Notably, we grew our customer base to close to 22,000 marketers and brands, adding 1,200 net new clients year-over-year, including more than 400 clients in Q3. Large customer wins include landmark names such as Lowe's, Wayfair and New Balance. We grew our same-client Revenue ex-TAC 9%, demonstrating the depth and breadth of our platform as 40% of live customers now use our new solutions. Client retention remains close to 90%.

Looking at verticals, our Retail business, up 16% on a 2-year basis at constant currency across our solutions reflects sustained strong demand, as consumers continue to shop online while enjoying heading back to physical stores. Retailers, large and small, adopt more of our performance-focused products and are driving the solid momentum in our business. Our Q3 spend with Travel clients is slightly increasing and we are signing new business, particularly in the US.

Our performance remained solid and balanced across all regions. We continue to see solid momentum in the Americas, with Revenue ex-TAC up 18% at constant currency, driven by acceleration in our Retail Media business with both large brands and top U.S. retailers, strong performance with Strategic and Core Retail customers, and new business in Travel. We are proud to serve a roster of top retail and ecommerce customers, and continue to strengthen our leading position in the fast-growing Retail Media market in the U.S.

AsiaPac also experienced solid momentum, growing Revenue ex-TAC 15% at constant currency, driven by higher Classifieds, the strong recovery of our Retail business in Japan and sustained performance with enterprise clients in South-East Asia and Korea.

Our EMEA performance, with Revenue ex-TAC growing 8% at constant currency, reflects mixed performance by country and verticals. We continue to see strong traction from Retail customers, notably in Germany, and in Retail Media especially in France, partially offset by lower spend from one large Europe-wide travel customer.

Now a quick note on Retail Media revenue dynamics. As we progressively transition all our Retail Media customers to our Retail Media Platform, an increasing share of our Retail Media revenue, or about 62% in Q3, is now accounted for on a net basis compared to less than 5% in Q3, 2020. As a result of this transition, Retail Media revenue is lower in Q3 2021 compared to the prior year. This is a transitory impact linked to our ongoing client migrations to the platform. Year-over-year, the media spend activated by Retail Media grew 74%, from $90 million to close to $160 million, accelerating from Q2, and Retail Media's underlying performance – reflected by Revenue ex-TAC – remains extremely strong, growing 65%. Once the RMP transition is complete, which we expect by the second part of 2022, revenue and Revenue ex-TAC for our Retail Media onsite business will be recognized on a consistent basis. As a result, this will drive a higher Revenue ex-TAC margin for Retail Media compared to prior periods.

Moving down our P&L, we continued to deliver strong profitability while investing in growth. Our adjusted EBITDA of $68 million was up 37% at constant currency, resulting in an adjusted EBITDA margin of 32%, up 6 points year-over-year and over 3 points on a 2-year basis. We closed the quarter with a global headcount of 2,660 Criteos, the highest level since Q2 2020, reflecting our strong employer value proposition in a tight talent market. Our growth investments are largely funded through productivity, enabling top line leverage as we ramp up commercialization of new solutions. Key investment areas remain new hires in solution selling, go-to-market, R&D and product, in particular for Retail Media, Commerce Insights and Contextual advertising, as well as upgraded tools and processes to support our new solutions growth.

Non-GAAP expenses were $143 million in Q3, up 5% at constant currency. Non-GAAP opex increased $7 million or 6%, including 13% for R&D, and grew 5% before the impact of our higher stock price on social charges. On that same basis, we increased employee costs by $3 million or 3% at constant currency.

We incurred a $2 million gain of pre-tax restructuring and transformation costs in Q3, almost entirely related to lease accounting impact from lease exits and amendments executed as part of our global office right-sizing. As a result, we now anticipate pre-tax restructuring and transformation expenses of about $21 million in 2021.

Depreciation and Amortization increased 3% and the appreciation in our stock price year on year drove share-based compensation expense up 95%. Our solid business performance and disciplined cost management drove a quadrupling of our income from operations with close to 360% growth in net income. Our Q3 effective tax rate was 24%. Our weighted average diluted share count grew 5% to above 64 million as a result of our growing stock price. Diluted EPS was 37 cents, up 310% and adjusted diluted EPS was 64 cents, up 60%. We cancelled just short of 900,000 shares in Q3 and plan to cancel over 630,000 additional shares before the end of 2021, putting our total share count at about 65.7 million by year end, including 5.2 million treasury shares.

Our strong cash generation and cash position continue to provide ample financial flexibility to execute on our commerce media strategy. Free Cash Flow was $35 million in Q3, or 51% of Adjusted EBITDA, reaching $112 million for the first nine months. We closed the quarter with a strong balance sheet and $554 million in cash and marketable securities. With financial liquidity in excess of $1 billion, we maintain a robust capital allocation process with the primary goal of investing in continued organic growth and leveraging M&A to accelerate our Commerce Media Platform.

We repurchased a million shares in Q3 at an average cost of $38.6 per share. Since starting our $100 million share buyback program in March, we have re-purchased $73 million worth of Criteo shares as of end-September, including $38 million in Q3. In October, we extended our current share buy-back program from $100 million to $175 million.

I'll now provide our guidance and business outlook for the remainder of 2021 which reflect our expectations as of today, November 3rd. As we head into Q4, we continue to see strong business momentum, as evidenced by our Revenue ex-TAC growing over 15% in October. While shops reopen, ecommerce remains strong, trending significantly above pre-Covid levels, as consumers increasingly value online shopping convenience and ecommerce continues to benefit from store closures. And as shops continue to reopen, retailers accelerate their investments in multi-channel fulfillment capabilities, making Omnichannel increasingly prevalent in their marketing mix. Overall, we continue to be well-positioned to capitalize on these long-lasting positive trends.

We're experiencing an earlier start to the Holiday season this year, carrying momentum into our fourth quarter to date. In parallel, current inflationary pressures have amplified many marketers' need to advertise for more expensive products. We anticipate the holiday season to span over an extended Cyber-30 curve similar to last year for our U.S. and European ecommerce customers, and expect the tail off in December to be earlier this year. While global supply chain challenges have had pockets of impacts in parts of the Consumer Electronic vertical and Auto, which represent small parts of our business, we have not seen any material impact on our business to date. Our robust growth is supported by our diversified customer base of 22,000 marketers who, in the current environment, remain focused on reaching the right audience at the right time. Our guidance therefore anticipates a strong Holiday Season and continued strength in Retail, with growth in Travel and Consumer Electronics.

As you know, we also have tough comps from last year in Q4. Lastly, our $55 million assumption for incremental identity and privacy impacts in 2021, including ATT and iOS15, remains unchanged and includes a $25 million impact in Q4 specifically, including approximately $15 million for ATT and about $5 million for the new iOS15 changes.

We will not be providing formal 2022 guidance on this call. That being said, looking ahead, we are optimistic about our growth trajectory, and are confident that the robust growth that we expect in New Solutions and Retargeting in 2022 will continue to more than offset the incremental identity and privacy impacts that we anticipate for next year. As of today, we assume that these identity and privacy impacts, incremental to 2021, will amount to less than $60 million in 2022.

Taking all of these factors into consideration, we are **raising our full-year 2021 Revenue ex-TAC growth guidance to approximately +10%** at constant currency. We expect our fast-growing new solutions to grow above 50% in 2021, including 60% for Retail Media, as we continue to strengthen our Commerce Media Platform. We are also increasing our **Adjusted EBITDA margin guidance to about 35% of Revenue ex-TAC**, demonstrating top line strength and operating leverage. In 2021, we expect our Adjusted EBITDA conversion to Free Cash Flow to be about 45%. Due to stronger revenue performance and regional mix, our projected tax rate is expected to be 26% for 2021.

For Q4, we expect **Revenue ex-TAC between $271 and $274 million**, **driving constant currency growth of +8% to +9%**. We expect our New Solutions to grow about 45% in Q4 as we lap strong growth and tougher comps from last year. And we expect **Q4 Adjusted EBITDA between $107 and $110 million**, or a margin of 39% to 40%, as we continue to invest in our growth areas and plan for higher bonus payout and sales commissions for the year.

In closing, we are excited about the momentum in our transformation. Criteo continues to be uniquely positioned to win in commerce media.

With that, I will now open up the floor to your questions.

[…Q&A…]

Edouard Lassalle – SVP, Market Relations & Capital Markets

Thank you Megan, Sarah and Todd. This now concludes our call for today. Thanks everyone for joining. The IR team is available for any additional request. We wish you all a good day.