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Criteo Q1 2021 Earnings Call | Prepared Remarks

<u>Edouard Lassalle</u> – SVP, Market Relations & Capital Markets

Good morning everyone and welcome to Criteo's first quarter 2021 earnings call. We hope you're all doing well and keeping safe.

Joining me on the call today, CEO Megan Clarken and CFO Sarah Glickman are going to share some prepared remarks. After these remarks, Todd Parsons, our Chief Product Officer and Geoffroy Martin, General Manager of our Growth Portfolio, will join us for the Q&A session. As usual, for everyone's convenience, you'll find our investor deck on our website.

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

We'll also discuss non-GAAP measures of our performance on the call. 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, it's my pleasure to hand it over to Megan.

Megan Clarken – CEO

Thanks Ed and good morning everyone. Thank you all for joining us today. I hope everybody is doing well and staying safe.

On our end, I have to say, we feel good today! **We've had a strong start to 2021** and have already achieved a number of solid things in a year of return to growth for Criteo. In particular, we're seeing good momentum across our three priorities of growth, execution and first-party data. In Q1, we've already returned to growth, and good trends in Commerce and online shopping continue to sustain the growth of our clients' business and our own. Our leadership is firmly in place and our teams are aligned and focused on steady, thoughtful execution. To add, recent market developments highlight the need for the industry to grow its focus on first-party data, validating the strategic importance of our own First-Party Media Network. In short, our market opportunity is big, our strategic priorities are clear and our execution is strong. All of this supports our Commerce Media Platform vision that I've talked you through on our past two earnings calls. Today, and looking at 2021 so far, I'm feeling very good about the momentum around our vision coming to life.

Together with Sarah, we'll discuss **three topics** on our call today:

- First, the value that our **Commerce Media Platform** brings to the market,
- Second, how our **steady and thoughtful delivery across our three priorities** of growth, execution and 1P data, **is driving momentum in our business**,
- And third, what drove our **over-performance** against guidance in Q1 and what this means for Q2 and our 2021 growth momentum.

First, our Commerce Media Platform. Our strategy of building the world's leading Commerce Media Platform brings together the best of Criteo to deliver smarter consumer experiences.

Commerce Media is a category of digital advertising that drives commerce outcomes for brands, retailers and publishers by delivering smart experiences to in-market audiences as they browse and purchase online. As a marketing category, Commerce Media is real and growing fast. It's out there and it's big. As I've said before, we view the Commerce Media opportunity as a $60B+ TAM for us.

Our place in Commerce Media is based on our front row position at the intersection of ecommerce, marketing and media monetization. Our unique platform makes Commerce Media work for everyone, driving powerful outcomes for all those that we serve:

- **Brands** like adidas or P&G generate commerce results through powerful, commerce-focused targeting, measurement and optimization capabilities, deployed via both our unique retail media inventory and our huge network of media properties, providing brands with a combination of commerce capabilities and unmatched scale even by the walled garden standards.

- **Retailers** like Target drive commerce outcomes and create new high-margin ad revenue streams for themselves through targeted promotions,
- **Publishers** access existing and new brand marketing dollars previously spent below-the-line,
- And **all of us as consumers** get to enjoy better shopping experiences through better content and personalized ad experiences, while enjoying continued access to ad-supported content online.

Our Commerce Media Platform's unique combination of commerce-focused marketing and media monetization capabilities makes us ideally suited to address the complex needs of our customers. For example, we recently helped one of the world's largest retailers execute their marketing and monetization strategy in Canada. This big client has been laser-focused on growing the ROI of its digital marketing investments at scale during the holiday season and early 2021, while at the same time monetizing its in-market audiences and media with multiple CPG brands. Our marketing services for them, focused on converting the visitors to their site and app, leveraging our strong creative and product recommendation suite, trusted brand safety capabilities and flexible budget allocation tools, to turn their site and app visitors into buyers. On the media monetization side, we helped them launch native and sponsored product ads across their site and apps, and added new ad placements on their grocery-specific inventory. Over Q4 and Q1, the value we delivered to this large retailer helped drive a +195% year-over-year increase in product sales for them, translating into a +100% growth in revenue for us. In 2021 and beyond, we see great opportunities for this retailer to further leverage our full suite of marketing and media monetization solutions with available audiences to drive commerce outcomes on and off its properties for the brand manufacturers it works with.

As you can tell from this example, we focus on being the leader in marketing and media monetization for commerce outside of the Walled Gardens. With our unified offering, we shepherd the buying and selling of advertising and promotions for goods and services -with a strong focus on Commerce- across our massive network of brands, retailers and media partners. We continue to work on making the seamless flow of our 1st-party data across our Commerce Media network a big part of our differentiation.

Moving to my second point: our steady delivery, driving growth. We're making good progress on each of our priorities: growth, execution and first-party data. The **positive momentum** we're seeing across our business is supported by our teams' solid planning and focus, thoughtful decisionmaking and high standard of execution. As I hope you can see, we're executing on a well thought-out transformation plan and overcoming unprecedented circumstances.

Let's start with our first priority: Growth. Our growth turned positive in Q1, earlier than planned, leveraging continued health in online commerce. I'm pleased that our better than anticipated performance was driven by solid momentum across **all** solutions.

Since I joined Criteo, our focus on growth has required us to better utilize our assets. We're growing the business by expanding our product suite and growing the uptake of our new solutions across existing and new clients. Benefiting from our larger Commerce Media product portfolio, our retargeting product continues to show solid resilience and to perform better than expected. In fact, a large part of our overperformance against our guidance in Q1 came from retargeting, highlighting our clients' continued need for superior performance in converting their customers. Whether that conversion is aided by retargeting, brand building, audience targeting, direct retailer promotion, superior access to buying and selling of ad real estate – this is the power of the Commerce Media Platform at work.

Our new solutions, which represent about $176 million Revenue ex-TAC on a last 12-month basis and now 21% of our business, grew 60% in Q1, accelerating from both Q3 and Q4 2020, with strong growth across the board. Retail Media's growth dramatically accelerated to over +120%, as we further expanded our business with new retailers, brands and agencies, and grew our share of wallet with existing ones. We already work with over 50% of the top-25 American and top-20 European ecommerce retailers with monetization programs, and we continue to expand our business with them. While Retail Media is a central piece of our Commerce Media Platform strategy, all of our new solutions continue to grow fast. We're investing in Contextual advertising and Audience Targeting for brands on video and CTV, and continue to expect all our new solutions combined to grow by close to 50% in 2021. And, -last point on growth- we're driving profitable growth too, as we significantly increased our Adjusted EBITDA margin in Q1 while continuing to invest in our growth initiatives.

Execution is our second priority. The team continues to deliver steady, thoughtful execution on all fronts. This spans our execution playbook across organic Build and Partner.

On the **organic** side, we saw continued solid momentum across the business:

- In our **Marketing Solutions** business, we continue to focus our sales efforts across our new solutions. In Q1 we had growth of over 160% in our Omnichannel solutions and mid-teens in our Audience Targeting products. This solid growth is enabled by our teams' to focus on best addressing and servicing the Commerce Media needs of our customers, big or small.

- On the **Product** side, and as discussed on our last call, we launched our next-level Contextual advertising solution. Our solution is a first-of-its-kind product that connects first-party commerce data, like a consumer's recent purchase of Adidas sneakers, with real-time contextual signals, like a particular new site or app, or the key topic of an article. This capability paves the way for marketers to continue to drive and measure incremental revenue in a post-cookie world, we're already seeing good customer adoption and good performance for marketers.
- In **Supply**, we launched our Direct SDK product with a top U.S. news app, adding to the scale of our direct access on the largest news apps. We also started testing in two Asian markets with one of the largest messaging platforms in APAC with huge scale, a significant strategic win for us in the region. As a reminder of our importance to supply partners, premium publishers like NBC, Globo, The Wall Street Journal and Forbes give us direct access to their inventory because they know we deliver high yields per ad unit, combined with advertiser demand at scale in brand-safe and consumer-friendly ways.
- And, speaking of locking in highly-differentiated supply, in **Retail Media**, we executed strongly with new business wins and growth in our existing customer base. On new business, we have signed a 3-year global preferred partnership with Carrefour. The agreement calls for the deployment of the Criteo Retail Media platform in nine Carrefour Group countries, starting with France where Criteo will be the exclusive partner for the marketing of retail media inventories to advertisers and agencies. The Criteo Retail Media Platform will power advertisers' promotion of their products on all of Carrefour's digital assets, i.e. on its web and app shops, through innovative solutions 100%-integrated into the shopper's journey. Carrefour joins retailers like Costco, Target, Macy's and Best Buy in granting us privileged access to their media inventory because our Retail Media solutions generate high-margin ad revenue while protecting the shopper experience through relevant, commerce-native ads. Also in Retail Media, we signed a multi-year agreement with a very large U.S. Home Improvement retailer, along with agreements with six other new retailers in Q1. We expect these contracts, together with potential similar agreements in the future, to continue to sustain and strengthen Retail Media's growth over the next multiple years. In Q1, we also fully integrated our Preferred Deals offering -previously called Commerce Display- into our Retail Media Platform, providing retailers, brands, and agencies with a single unified platform for managing all ad formats across retailer sites and mobile apps.

On the **partnership** front, we continued to expand our strategic API partner program, making it easier for brands and agencies to buy with Criteo. Today, our APIs and partners drive greater stickiness and long term growth for Criteo, including acceleration of our offsite Retail Media offering for brands across the open Internet.

Moving to our third priority, 1st-Party Data. As everyone knows, this is a critical area for the industry and for us. An area where we're actively and methodically securing our moat and differentiation.

First of all, all of our Retail Media onsite solutions **leverage 1st-party data and do not rely on third party cookies**. This means that our growth in Retail Media onsite is not only tremendous in size, but also sheltered from changes in 3rd-party identification and therefore brings steady, durable and predictable growth. This is important in light of our fast growth in this business and the central role that Retail Media plays in the traction of our Commerce Media Platform.

Secondly, in their early March blogpost, Google interestingly reminded everyone of the strategic importance of first-party data to the entire online ecosystem. We found Google's rap to be music to our ears, as the foundation of our Commerce Media Platform is first-party data that we operate on behalf of our partners. Our 1st Party Media Network enables this data to power marketing and monetization across the open Internet, at scale. In partnership with our clients, the constant, safe and protected flow of 1st party data within our broad network is the cornerstone of our data and identity strategy. As changes come in iOS14 and 3rd-party cookies go away, we'll further lean into this asset and continue to offer our clients the ability to achieve their marketing and monetization goals via first-party data. As I mentioned earlier, a strong focus for us is to make our clients' first-party identity data fully interoperable across our 1st-party Media network to ultimately power the Commerce Media Platform in the most seamless way. This means creating durable connections between 1st-party identity data operated on the demand side of our business with 1st-party data operated on the supply side of our business. Our effort requires investment in infrastructure for seamless data rights management, privacy protection and integration with the programmatic ecosystem to differentiate.

Third, in collaboration with industry partners, we further advanced the integration of the universal identifier UID2 solution into our Commerce Media Platform. We worked with The Trade Desk on our new Single Sign-On software called OpenPass, built to support UID2 and to provide publishers and retailers the tools to use 1st-party data as an alternative to 3rd-party cookies. The OpenPass software will be open-sourced and available for all publishers and retailers to easily install on their site and technology stack. We started testing OpenPass with consumers, publishers and retailers in Q1 and Q2, and anticipate it will take up to 12 months to build scale. As we've said before, OpenPass and UID2 are built for interoperability with other consent and identity solutions and OpenPass will operate with identifiers other than UID2, which means both will also enhance other solutions publishers and retailers chose to use.

And finally, we are excited about our customers' interest we're already seeing in our first-of-its-kind Contextual advertising product. It's built with the best of Criteo AI to merge content classification with 1st-party transaction data to close the loop between what cohorts of consumers buy and their affinity for specific content. In the very early going, we've seen incrementality for our clients, and believe this product will thrive in a post-3rd party cookie world. It's also important to note that our Shopper graph data proves particularly relevant for Cohort advertising use cases to drive higher relevance for consumers and performance for marketers. We believe this positions us well ahead of testing Google's FLoC and FLEDGE proposals over the coming months and quarters.

In short, our team has delivered steadily, thoughtfully and with discipline across our strategic priorities in early 2021. Looking ahead, we remain laser-focused on **<u>the same 3 priorities</u>.**

- First, **<u>on growth</u>:** accelerating the momentum we've built, focusing on strong secular trends in ecommerce, making the right thoughtful decisions on investments and continuing to attract and retain the best and brightest talent out there;
- Second, **<u>on execution</u>**. By sticking to a strict "we do what we say we'll do" discipline, we nurture a culture of high performance and accountability in everything we do;
- And third, **<u>on 1st-party data</u>:** using our competitive moat of protected 1st-party data across our advertiser and publisher network, and focusing on the various techniques we have available to us, we feel good about our position in the market post-cookies.

In closing, I'm very proud of our team's solid delivery, achieved with grit and conviction. I feel good about the momentum we've created in our Commerce Media Platform and how we're tracking against our Transformation plan to turn our business around. To discuss our strategy and execution plans in more details, we are excited to host you all at our **2021 Investor Day which will take place, virtually, on June 3**. During this event, our extended leadership team will explain why the New Criteo we are today is best positioned to offer the World's leading Commerce Media Platform to brands, retailers and publishers. All details will soon be available on our IR website. I hope you'll all be able to join.

With this, and looking forward to seeing you all attend our Investor Day, I'm pleased to turn it over to Sarah who'll take you through the Q1 performance and outlook for the rest of 2021. I'll be back for the Q&A session. Sarah?

Sarah Glickman – Chief Financial Officer

Thanks Megan - and yes, it's exciting to see our momentum unfold. Good morning everyone. I'll discuss the operating and financial drivers of our Q1 performance. And I'll share our financial outlook for Q2 and 2021.

Let me start with the headline numbers. Revenue grew 7% in Q1, or 4% at constant currency to $541 million. We beat expectations for Revenue ex-TAC and Adjusted EBITDA, due to our overperformance across retargeting and our new solutions.

On a non-GAAP basis, Revenue ex-TAC was $213 million, up +4% or +0.5% at constant currency, and $13 million above our expectation. Adjusted EBITDA of $76 million, up 21% at constant currency, drove our 36% margin. This resulted in adjusted diluted EPS of 67 cents. Free cash flow was $64 million, representing 84% of Adjusted EBITDA. Even with Q1 seasonal uplift in cash collections, this was the highest level for 21 quarters.

We estimate that COVID had an incremental impact to early 2020 of negative $18 million, or about 9 points year-over-year. Excluding this estimated incremental COVID impact, our Revenue ex-TAC grew close to +9%. Incremental identity and privacy impacts drove a $5 million reduction in Rev ex-TAC. And, our Revenue ex-TAC margin was 39% of revenue, down 150 basis points YoY, in line with expectations due to the evolving product mix of our business and our go-to-market strategies.

Our performance was strong across Criteo's entire business. Revenue ex-TAC growth improved about 7 points compared to the rate in Q4.

We continue to operate Criteo as a single operating segment. In our financial reporting, and to provide additional transparency, we have disaggregated Revenue and Revenue ex-TAC to show both Marketing Solutions and Retail Media.

Marketing Solutions Revenue ex-TAC declined 5% compared to Q1, 2020, largely related to an estimated $18 million impact from COVID. Close to 90% of this impact was in Travel. Excluding this estimated incremental impact, Marketing Solutions Revenue ex-TAC was up +4%, driven by better performance in retargeting across all regions and Audience Targeting growth of 14%. Growth in our Omnichannel product accelerated to over 160% due to continued strong demand in Retail.

In Q1, Retail Media grew 122% on a Revenue ex-TAC basis, driven by strong momentum across existing clients and onboarding new retailers and brands. Overall, our New Solutions across Criteo, including Retail Media, grew 60% to 21% of total Revenue ex-TAC.

Same-client Revenue ex-TAC growth of +3% improved 4 points relative to Q4. In Marketing Solutions, Retail was up +9% this quarter. Both metrics highlight **healthy momentum** that we anticipate will continue into Q2 2021.

For our regions, Revenue ex-TAC in the Americas grew 6% or 8% at constant currency, improving 13 points of growth compared to Q4, driven by Retail trends across retargeting, audience targeting and Retail Media momentum with large retailers and brands. In EMEA, Revenue ex-TAC grew 5% on a reported basis but declined 2% at constant currency, driven by continued weakness in Travel offsetting Retail new business. We saw strong traction in Retail Media, including our preferred deals offering. Revenue ex-TAC in APAC declined 2% or 5% at constant currency, improving by over 12 points compared to Q4. This was impacted by the Travel vertical, an improving classifieds vertical, offset by the return to growth of our Retail business in Japan and Korea.

We added over 120 net new live clients in Q1 as commercial momentum built on across all solutions. Over 75% of these new live clients related to Retargeting with about 25% upsold to New Solutions campaigns as well. In Q1, our client metric, which is a lagging indicator counting all clients that have been live with us over the preceding 12 months reflected the annualized impact of client churn that peaked in Q2 2020 when COVID started to impact the global economy.

We continue to invest in growth while wisely managing the expense base. We are seeing returns from investments in our Commerce Media Platform including expansion of our Retail Media sales team and new product launches in Commerce Insights and Contextual advertising. Our G&A costs increased as we invest in back-office capabilities and tools to support new products. Our growth investments are largely funded through productivity and cost savings, enabling top line leverage as we commercialize new products and capabilities.

In Q1, non-GAAP expenses were $137 million, down 8% at constant currency. Non-GAAP opex reduced by $8 million or 8% at constant currency, declining -13% before the impact of our higher stock price on social charges. On that same basis, we reduced employee costs by $7 million or 12% at constant currency after investing in R&D, Product and Retail Media. We continue to work with strategic partners to accelerate innovation and expand our capabilities, particularly in Contextual advertising, Retail Media and the build out of our First-Party Media Network. These partnerships are reflected in the evolution of our R&D opex line.

As you can see in our non-GAAP reconciliation, we incurred just shy of $12 million of pre-tax restructuring and transformation costs, largely related to real estate and severance costs. We anticipate expenses of $20 to 25 million in pre-tax restructuring costs in 2021, split between real-estate portfolio reductions and employee severance.

Moving down our P&L, our D&A expenses reduced 9% and share-based compensation expense declined 7%. This, combined with our business performance and good cost management, drove a 44% increase in income from operations and a 43% increase in net income, reflecting flat financial expenses and a 30% GAAP effective tax rate. Our weighted average diluted share count was 64 million, up 3% as a result of our increasing stock price over the period. Diluted EPS was 35 cents, up 40% and adjusted diluted EPS was 67 cents, up 29%.

Our strong cash generation and cash position continue to provide ample flexibility for execution. Our Free Cash Flow grew 41% to $64 million in Q1, 2021 reflecting strong cash collections, offset by payout of the 2020 bonus and some restructuring payments. In Q1, we purchased approximately $5 million worth of shares, as part of our new $100M share buyback program. Our balance sheet continues to be very strong as we closed Q1 with $566 million in cash and marketable securities. We look to maintain flexibility in our capital allocation to pursue organic and potentially inorganic investments, and have an active M&A pipeline focused on our growth areas. As of March 31, we had total financial liquidity of around $1 billion, providing strong flexibility for investments as well as enabling the execution of our $100M share repurchase over time. In the quarter we repurchased 150,000 shares at an average cost of $32.87.

I'll now provide our guidance and business outlook for Q2 2021 which reflect our expectations as of today, May 5. This guidance reflects our views of secular trends sustaining in ecommerce, expectations for more Retail reopening and slower than expected recovery for Travel retargeting. We continue to monitor the impact of iOS14 changes over the coming weeks and months.

As we head into Q2, we continue to see good traction in our Commerce Media Platform, with continued strength in Retail, strong momentum in Retail Media and solid growth across our new solutions. We do not anticipate any significant rebound in the Travel vertical given extended lockdowns. We do expect growth in retargeting in Q2, partly driven by the favorable comp in Retail and Classifieds from the trough of the COVID impact in Q2 last year. As we had a very strong comp in Q2 2020 that was helped by Covid, we expect our Retail Media business to grow in the high 30's.

Taking all this into consideration, we're guiding for **Revenue ex-TAC in Q2 of approximately $208 million**, **or about +14% growth at constant currency**. This includes $11 million of incremental identity and privacy impacts relative to the 2020 run-rate. On the profitability side, we expect **Q2**

Adjusted EBITDA of approximately $60 million, and anticipate expenses to increase low single-digit year-over-year at constant currency after increased investments in our growth areas.

For fiscal 2021, we maintain our guidance of **mid-single digit growth in Revenue ex-TAC** at constant currency and an **Adjusted EBITDA margin above 30% of Revenue ex-TAC**. We refined our assumption on incremental identity and privacy impacts to $55 million in 2021 relative to the 2020 run-rate, mostly as a result of the later than expected release of Apple's ATT in iOS14.

In closing, I want to thank our customers and our Criteos for the steady momentum our business is enjoying, powered by disciplined execution and strong, lasting commerce trends. We are laser-focused on our transformation and our plans to offer the world's leading Commerce Media Platform. We work to drive sustainable and profitable growth and create long-term value for our shareholders. As an advocate for diversity and inclusion, and as a female CFO, I am very proud to work for a company that ensures gender pay parity.

We are looking forward to hosting you all online at our **June 3 Investor Day**. We will share our views on our opportunities, insights on our Commerce Media Platform strategy and provide you an opportunity to meet our team. We will not be sharing a formal financial outlook. We remain committed to continue to be transparent and share updates with our investors on our transformation, new solutions and on Chrome mitigation as the industry and strategy evolves into 2022, and as we continue to launch new products. With that, I'll now open up the floor to your questions.

[…Q&A…]

Edouard Lassalle – SVP, Market Relations & Capital Markets

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