



Q3 2022 Earnings

Prepared Remarks

November 3, 2022

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This document also includes certain non-GAAP financial measures. Reconciliations between our GAAP and non-GAAP results and further information related to guidance can be found in our earnings press release.



Jeff Lawson, Co-founder and CEO

With our Investor Day taking place today during our SIGNAL customer and developer conference, we're going to provide a condensed version of our prepared remarks this quarter. With that in mind, let me quickly touch on a few of the recent highlights.

We just wrapped SIGNAL today with some exciting product announcements, furthering our leadership in customer engagement software. We also hosted conversations with leading customers like Toyota Connected, for whom Flex powers roadside assistance across North America, as well as the Red Cross who uses messaging to help displaced people with cash assistance. These customers highlight for our next generation of upsells and prospects the art of the possible with Twilio's Customer Engagement Platform.

At the event, we announced several exciting enhancements and products including:

- The general availability of **Twilio Engage**, which is a meaningful milestone for us. Not only does Engage introduce an exciting new market for Twilio's CEP, Engage is our first software application that natively brings Segment's leading customer data infrastructure and Twilio's scalable communication APIs together into a single platform. We believe this native combination is what differentiates Twilio from anyone else in the market. Brands like Discovery Education, Harry Rosen and EasyHealth, are building personalized marketing campaigns as part of the Twilio Engage Pilot. By bringing Engage to General Availability, we will begin selling it more broadly into our base of customers who already buy channels (such as Messaging or Email) and data (Twilio Segment CDP). Upselling customers from channels to Engage can represent a substantial increase in revenue and gross profit for us, so the GA milestone is important.
- The public beta of **Verify Silent Network Authentication (SNA)**. By partnering with over 50 mobile operators across 30+ countries, Twilio is able to verify the device and phone number with an operator without the need for additional authentication requirements like pin codes or visual tests from users to create a seamless user experience. Gojek, an Indonesia-based ride share, delivery and shopping app, implemented SNA and reduced customer login time from 20 seconds to five seconds – all with no user intervention and increased security. By bundling SMS, WhatsApp, SNA, and Fraud protection into one software product,

Verify is driving more value for our customers and more gross profit for Twilio.

- A new native integration between **Twilio Voice and Google Dialogflow CX** that can equip virtual agents with advanced AI capabilities in Flex and IVRs. This integration automates self-service use cases to better help customers and decrease frustrating IVR experiences that damage customer relationships and increase the cost per call. Machine learning-based agent coaching and self-service automation is becoming a must have, so partnering with Google can help accelerate our penetration of Flex as a cloud replacement for customers' legacy workloads.

Our highly diversified customer base serves us well, but we are not immune to changes in the macro-economic environment. While we delivered a strong quarter of results, our Q4 guide is below where I'd like it to be. Like many software companies, we are seeing a more pronounced impact from the macro environment on our business than in prior quarters. As we noted on the Q2 call, certain verticals, such as crypto, consumer-on-demand, and social have been more heavily impacted in day-to-day usage. This trend persisted in Q3, and has also extended to the retail and eCommerce verticals.

Additionally, unlike prior years, Q3 and Q4 largely exclude a political spike because we made the decision to offboard a lot of that traffic from our platform after 2020. That traffic was from customers who did not intend to honor our Acceptable Use Policy with regards to consumer opt-ins and therefore we refused their business in this election cycle. We presume they went to other providers. To us, the short term revenue benefit in the election cycle is not worth the friction with consumers who do not want their traffic, or with carriers who have raised repeated concerns about this traffic.

That all said, we're still closing incredibly exciting new software deals. We signed one of our largest Flex deals for the second quarter in a row – an 8-figure expansion deal with a Fortune 100 insurance provider, deploying Flex for more than 20,000 agents! We continue to see strength in other verticals, such as financial services, but we have also seen some instances of longer sales cycles. The diversity of our customer base is an asset, but under this macro-economic umbrella, we think it prudent to be conservative in our business planning and guidance.

In light of the challenging macro environment, we have made and will continue to make changes that will allow us to continue to deliver strong topline growth while balancing it with profitability. Earlier this year, we committed to delivering non-GAAP operating profitability in 2023. That commitment is not changing and we will deliver improvements

each year thereafter as we balance growth and profitability. We're not just building a big business, we're building a great business.

While Twilio is facing the same short-term headwinds as many other companies in this environment, we believe our long-term opportunity is massive. Every company needs better customer engagement software, and we're eager to deliver on that opportunity. I'm extremely confident that we have the right team, plan and products to take advantage of this market opportunity in the long term, all while delivering profitable growth.



Elena Donio, President of Revenue

Today marks the final day of SIGNAL 2022, our annual customer and developer conference, and I'm walking away from it with a renewed sense of excitement about Twilio and our future. Talking directly with customers in person and connecting with thousands of them virtually reminds me of the immense influence our solutions have around the world and our ever larger opportunity for growth.

These conversations also solidified for me the changing dynamics in our customers' needs today and how Twilio can help them in the current environment. The new challenges they're facing make it even more crucial that they create quality customer experiences with efficiency and scale, bring in new business with innovative new tools, and retain them over the long term through personalized interactions at just the right moment, with just the right message, over the right channel.

This quarter we made some significant changes to our go-to-market team to better position ourselves to acquire and serve customers as they evolve their customer engagement strategies. We're scaling up our strategic software selling muscle, increasing our sales capacity on our Segment and Flex teams, and driving efficiency across our communications portfolio. Across the board we're investing in our products and services with more precision and putting the weight of our human-touch efforts behind landing new software deals and cross-selling to existing customers.

Some customer wins from the quarter include:

- We signed a new 8-figure deal with a Fortune 100 property and casualty insurance provider. They were struggling with their existing on-premise contact center platform that didn't offer the flexibility to drive modern, omnichannel engagement with their customers. They selected Twilio as our platform and roadmap best supported their long-term strategy, and they will be leveraging Flex, Messaging, Conversations, and more to power their next generation of customer engagement.
- We entered into a new relationship with Guardian Life, a 160 year old insurance provider with more than 29 million customers. They were looking for a solution to help them gain a real time 360 degree view of their customers, and selected Twilio Segment to accelerate their Customer Centricity initiative.

- We expanded our relationship with Jack Henry, an industry-leading financial technology company that prioritizes openness, collaboration, and user-centricity – offering banks and credit unions a vibrant ecosystem of internally developed modern capabilities as well as the ability to integrate with leading fintechs. Already a great Twilio Messaging customer, Jack Henry was looking for a solution to help reimagine the virtual banking experience. They selected Twilio Video to build a new solution to help their customers create personalized, one-on-one video interaction to drive higher levels of customer engagement.
- We continue to enhance our GTM efforts to meet our customers' contact center needs. On October 13, we announced Twilio Flex as a Google Chrome Enterprise Recommended solution, optimized for Google ChromeOS. Additionally, we are excited to announce a native integration of Twilio Voice with Google Cloud CCAI and Dialogflow CX to enhance the virtual agent experience. These innovations allow our customers to provide their call center agents with the tools they need to enhance their customer experience.

These are just a few of the wins Twilions have secured throughout Q3. They landed these deals while the economic situation worsened globally and buyer hesitancy increased. Our job in the coming quarters is to demonstrate the ROI of better customer engagement. This is an investment that businesses can't afford to ignore.

We're already seeing some momentum on that front. Just a few days after the start of Q4 we closed our first new Engage account after testing it with customers in the beta program over the past year. This customer initially came to Twilio through a simple SendGrid email API use case but as their business grew, they struggled with the time and resources it took to manually maintain customer journey flows and gather data to inform their campaigns. In fact, they were about to hire dedicated employees to manage this process. Now with Engage's advanced journey orchestration and omnichannel campaigns, they can cost-effectively scale their customer acquisition strategy and provide a better customer experience, without needing to scale their team.

Our software solutions are unlocking new value for Twilio customers – providing them with the data and insights they need to truly engage their customers – and our communications products allow businesses to deliver the right message at the right time, built off of those insights. I'm excited about the opportunity ahead to expand our existing customer relationships and reach into new businesses.



Khozema Shipchandler, COO

Our third quarter results were strong, despite seeing continued degradation in the macroeconomic environment. Following our recent restructuring actions, we're driving more focus throughout the company to accelerate our software sales, while driving operating leverage across the business to deliver non-GAAP operating profit in 2023 and beyond.

Third quarter revenue was \$983 million, up 33% year-over-year, including:

- \$35 million from Zipwhip, including \$17 million in 10DLC A2P fees; and,
- \$2 million from all other acquisitions closed after July 1, 2021.

Excluding these items, third quarter organic revenue growth was 32%. As a reminder, we have lapped the anniversary date of the additional U.S. 10DLC A2P fees being put in place on our core messaging product, so those are now considered to be organic revenue.

Our third quarter dollar-based net expansion (DBNE) rate was 122%. As a reminder, Zipwhip and all other acquisitions closed after July 1, 2021 are not included in our DBNE this quarter.

Revenue from our top 10 active customer accounts represented 13% of revenue in Q3, compared to 12% last quarter, and 11% in the third quarter of 2021. International revenue was 34% of total revenue in Q3, compared to 35% last quarter and 33% in Q3 2021.

Third quarter non-GAAP gross profit grew 25% over last year, and non-GAAP gross margin was 50.8%, roughly flat to last quarter. Reported Non-GAAP operating loss was \$35 million, inclusive of a one-time, non-cash charge of approximately \$29 million related to the implementation of our sabbatical program for tenured employees. Excluding that charge, non-GAAP operating loss was approximately \$6 million. This was better than expected primarily due to the implementation of a more focused hiring plan.

Our GAAP operating loss was impacted by \$72 million related to the restructuring we announced in September, as well as \$98 million related to the impairment of several of our real estate leases as part of our “remote first” policy.

While we delivered solid results in Q3, we're mindful of the evolving macro environment and as Jeff mentioned, we started to see a broader impact from the macro environment on our business throughout the quarter. We remain confident in the long-term opportunity as companies continue to prioritize investments in customer engagement; however, in light of the current environment, we made the difficult decision to undertake a restructuring in September in an effort to right size the company. We're continuing to focus our hiring efforts on Segment, Engage and Flex, while moderating both new hiring and backfills in other areas as we monitor the macro environment and impacts on our business. We'll continue to closely monitor the returns on our investments, and make adjustments as needed, in an effort to recognize further efficiencies as we scale.

Turning to guidance, we've incorporated the impact from the dynamic macro environment into our guidance for the fourth quarter, and we're initiating revenue guidance of \$995 million to \$1.005 billion, for year-over-year growth of 18%-19% for both reported and organic revenue. As a reminder, Zipwhip and its associated A2P fees are considered to be organic as of Q4. For the full year, this guidance implies revenue growth of approximately 29%. I recognize that this is below the 30% revenue target we laid out two years ago, but we're also facing a very different and rapidly evolving external environment today. As Jeff mentioned, like many of our software peers, we're seeing negative impacts on our business from the macro environment, and we've taken that into account in our guidance. As a result of the worsening macro situation, we also feel it is prudent to pull the 30%+ revenue target today. We still believe we'll deliver attractive levels of growth going forward, but in the current market, we don't believe 30%+ is achievable. We expect a fourth quarter non-GAAP operating loss of \$5 million to \$15 million, which includes expenses associated with our 2022 SIGNAL event.

In closing, we're pleased with our results in the third quarter, and the continued growth that we've delivered. Despite the current macro environment, we remain very optimistic about our long-term opportunity as we continue to help companies develop more meaningful relationships with their customers.