Veritone Second Quarter 2023 Prepared Remarks

Stefan Norbom, Investor Relations

Thank you, and good afternoon.

After the market-close today, Veritone issued a press release announcing results for the second quarter ended June 30, 2023. The press release, and other supplemental information, are available on the Investors section of Veritone's website.

Joining us for today's call are Veritone's CEO and President, Ryan Steelberg and CFO, Mike Zemetra who will provide prepared remarks and then open up the call for a live question and answer session.

Please note that certain information discussed on the call today, including certain answers to your questions will include forward-looking statements. This includes, without limitation, statements about our business strategy and future financial and operating performance. These forward-looking statements are subject to risks, uncertainties and assumptions that may cause the actual results to differ materially from those stated. Certain of these risks and assumptions are discussed in Veritone's SEC filings, including its annual report on Form 10-K. These forward-looking statements are based on assumptions as of today, August 8th, 2023, and Veritone undertakes no obligation to revise or update them.

During this call, the actual and forecasted financial measures we will be discussing include non-GAAP measures. Reconciliations of these measures to the corresponding GAAP measures are included in the press release we issued today. Also, when we reference pro forma measures, such measures are presented on a combined pro forma basis treating Broadbean as owned by Veritone during fiscal year 2022.

Finally, I would like to remind everyone that not only has this call been produced with Veritone Generative AI, but it is also being recorded and will be made available for replay via a link in the Investors section of Veritone's website at www.veritone.com.

Now I would like to turn the call over to our CEO and President, Ryan Steelberg.

Ryan Steelberg, CEO and President

Thank you, Stefan.

Good afternoon (English and Spanish), good evening (German) and good morning (Chinese).

As Stefan noted, this call is being powered by our AI-driven and multi-award winning offering, Veritone Voice.

I'm pleased to share our second quarter earnings results which demonstrate Veritone's progress against the strategic pillars we presented earlier this year, despite a challenging macroeconomic backdrop. Before turning to results, I want to discuss the attractive opportunity that Veritone is uniquely positioned to capitalize on through disrupting target vertical markets.

Over the last year, artificial intelligence has transitioned from a niche area of R&D, to a catalyst for transformation expected to boost global productivity and GDP by over 14% in 2030, representing a contribution of approximately $16 trillion according to PwC. The global technology landscape has experienced immense innovation over the past decades, and, consequently, we have seen a rapid increase in data creation foundational to consumers and businesses. With unstructured data comprising the overwhelming majority of data created globally, there is a clear demand for solutions that extract value and actionable insights from this sea of unmanaged data, as well as act upon it. While structured data can show you what is happening, the programmatic use of unstructured data allows you to realize the full potential of this asset. **Data is the lifeblood of predictive, end-to-end automation and commercialized artificial intelligence.**

Through Veritone's enterprise AI software and solutions, we are enabling companies to integrate and orchestrate their disparate data sources and workflows to drive operational efficiencies and productivity gains. A consequence of enterprises centralizing vast amounts of structured and unstructured data is the opportunity to infuse existing applications or build new applications with AI-based generative models.

Veritone's purpose-built applications powered by aiWARE have been enabling disruptive efficiency and productivity in the market verticals we believe are most attractive: talent acquisition, media and entertainment, sports and government and regulated industries. These purpose-built applications provide a best-in-class ecosystem of AI models as well as an intelligent data lake and workflow tools that help companies acquire, analyze and act on unstructured data sources for greater business efficiency and insight. With Veritone's aiWARE operating system, developers are able to rapidly build, scale and operationalize AI-enabled applications.

The AI paradigm has shifted and it's important to remember we are still in the early innings. While companies continue to ramp adoption, the underlying AI models themselves will not be differentiated. Rather, differentiation will come from the application of the AI and large language models with unique data on a job specific-basis. For almost a decade, Veritone has demonstrated its ability to weave together data and a vast array of cognitive and generative AI models for industry-leading customers. These capabilities allow Veritone to double down on attractive market verticals and expand our proprietary data moats. I can confidently state that Veritone, through aiWARE and our unique data and workflow capabilities, is strategically positioned to capitalize on the opportunities that lie ahead.

To understand my initial strategy as CEO, I want to reiterate Veritone's pillars of focused execution, operational excellence and fiscal responsibility. The entire team remains committed to strengthening our foundation while streamlining operations to accelerate our mission of achieving sustainable and profitable growth. I'm excited to share with you the progress on Veritone's transformation initiatives and unpack operational updates which enforce management's focus on driving long-term shareholder value.

Inline with our strategy to pursue existing market verticals where Veritone has clear differentiation resulting in efficiency gains for customers, Veritone's acquisition of Broadbean this quarter marks an inflection in growth trajectory for years to come, accelerating our leadership in the global talent acquisition and HR technology market which is projected to exceed a valuation of $196 billion by 2028.

Within this expanding opportunity, Veritone is amplifying recruitment and positioned to benefit from generative AI in HR, which alone will grow from $413 million in 2022 to over $1.6 billion in 2032.

The combination of PandoLogic with Broadbean, or Veritone HR Solutions, will leverage aiWARE to orchestrate cognitive, predictive and generative AI workflows across the talent acquisition ecosystem. Notably, Broadbean provides us access to nearly 3,000 customers, direct integration with over 100 ATS providers, millions of applicants and resumes and billions of valuable data points globally. This transaction is immediately accretive to Veritone and, on a standalone basis, is projected to generate SaaS and GAAP revenues of over $35 million on an annualized basis, of which about $30 million is subscription-based with attractive margins. Veritone HR Solutions will be the leading provider capable of offering universal talent acquisition and AI-driven data solutions to its global set of customers, leading to significant growth opportunities beginning in 2024.

In the near-term, the platform synergies accelerate growth of programmatic adoption with diversified customers across the globe, drive efficiencies of scale and enhance recruitment insights. As we look ahead, this solution will allow customers to evaluate the return on hiring investments in real time, from job acquisitions and recruitment to down-the-funnel attribution, improving the quality of applicants. Moreover, the recurring subscription-based revenue streams generated by this acquisition aligns with our long-term strategy for growth, earnings stability and strong customer retention. There are a number of additional strategic initiatives currently in flight, and we look forward to providing an update in the back half of the year.

As Veritone pursues operational excellence across all aspects of our business, achieving profitable growth through reshaping the organization to more efficiently support the needs of our customers remains a priority. Our integration of Broadbean is just the beginning; Veritone has been strategically evaluating opportunities to deepen our exposure to the industries we believe are the most attractive. As mentioned previously, we are committed to diversifying our customer and revenue base, and we expect that, for each quarter moving forward, earnings will become more stable and less susceptible to the actions of a single customer or end market.

Notably, we are seeing meaningful traction, with near 100% year over year growth for 2023, from new and existing government & regulated industry solutions, or GRI customers that want to benefit from Veritone's industry leading applications, as evidenced by cloud-based Veritone Redact which accelerates evidence redaction workflows. During the second quarter, Veritone deployed a series of product enhancements for its award-winning, aiWARE-powered Veritone Redact and Contact applications for its customers in the legal and law enforcement sectors, delivering greater customization capabilities to enable users to operate with a higher overall degree of efficiency, effectiveness and seamlessness. Hundreds of law enforcement agencies are actively using Veritone's AI-powered technologies and applications to improve the way they respond to crime, collect and analyze data, while maintaining safety within their respective communities. One customer that I would like to highlight is the Beverly Hills Police Department, led by its data-focused Chief, Mark Stainbrook. Mark is developing a state-of-the-art, real time watch center, that is ingesting and orchestrating thousands of data sets, including real-time drone video, officer body and dash cam video, as well as CCTV footage from across the city. His goal is to protect his citizens and real property, and this real-time visibility is providing the data and information to not only react quickly to crime, but potentially to prevent it. This infrastructure is already producing results, but Mark and his team understand that to keep up and process all this data, AI must be at the center of his stack. We are excited to be working with Chief Stainbrook, who is setting the standard for modern law enforcement agencies.

Not only are our customers fans of our products and solutions, but the industry is also taking note. Veritone's Generative AI platform won two prestigious awards at the NAB Show 2023, including the NAB Product of the Year in the AI and Machine Learning category and the IABM Broadcast and Media Award in the Monetization Category. Winning these two awards is a testament to the power of Veritone's generative AI platform, and validates our efforts to create solutions that deliver meaningful results for our customers. 2023 is the fourth year Veritone has won the NAB Product of the Year.

A recent example of how we have incorporated Generative AI into an established product line is Digital Media Hub, or DMH. Used by hundreds of media & entertainment customers today, DMH provides the ability to use AI to ingest, index and automate your metadata creation process, allowing users to easily find content via metadata tags, such as object, facial or logo recognition. Synthetic data enhancement uses generative AI, natively within DMH, to fill in those gaps by using existing asset metadata to create and apply new metadata in order to improve the cataloging and accessibility of that asset. This is a productivity enhancer, and provides users the ability to save countless working hours in data management.

Warner Brothers and other prominent media companies are already using these generative AI features within DMH. We believe these examples underpin Veritone's ability to deliver powerful, orchestrated cognitive and generative solutions across a variety of industries that include: sports, advertising & entertainment, law enforcement and talent acquisition.

And most recently, in the media, entertainment and sports vertical, I wanted to spotlight our recent partnership with Major League Baseball to distribute short-form video content through SPORTX, which is powered by aiWARE and supported through DMH. Veritone's Sports and Media Licensing offering, SPORTX, is a premier intelligent marketplace for sports federations and content producers, which enables media buyers direct access to sports video from around the globe, maximizing additional revenue streams and increasing visibility for rights holders.

Turning to fiscal responsibility. Today, Veritone's cost saving initiatives have translated into $17 million in annualized savings year-to-date. We have already exceeded our annualized savings target for 2023, which highlights management's commitment to right-sizing our cost structure. With the recent integration of Broadbean, we will continue to evaluate opportunities to unlock further operational efficiencies. On June 30th, we officially divested our Energy Group, in line with our strategy to divert resources to Veritone's target market verticals. Furthermore, we have secured an AR credit line of up to $30 million, providing additional liquidity on our balance sheet. The net result of these actions is that Veritone is more capable, focused and efficient in its operations and our go-to-market strategy is more tightly aligned as we drive value and progress towards profitability.

Before we turn to second quarter operating results, I'd like to re-emphasize the product demand and broad-based growth opportunities for Veritone as artificial intelligence continues to gain traction. Since 2014, Veritone's AI mission has been to augment the human workforce by transforming concepts into industry-leading applications and solutions. We remain confident in Veritone's long-term strategy which will propel us into our next phase of growth.

Now, I would like to hand the call off to Mike Zemetra, our CFO, to go through the financial results and guidance.

<u>Mike Zemetra, CFO</u>

Thank you, Ryan.

I am pleased to report Veritone made great progress in the second quarter headlined by the acquisition of Broadbean, the divestiture of our energy group, the closing of a $30 million revolving AR facility to improve our liquidity position and balance sheet and increased annualized cost savings to over $17 million while closing the quarter with solid customer and operating metrics.

I would like to highlight a few items before I begin. With the June 2023 acquisition of Broadbean, we have updated our key customer metrics, on a pro forma basis, which assumes we owned Broadbean since the beginning of fiscal year 2022. In addition to ending customers and gross retention, we are introducing ARR, or Annualized Recurring Revenue, as a new key performance indicator.

During my prepared remarks, I will discuss our:

- Second quarter financial and operating performance;
- The acquisition of Broadbean and its financial implications;
- Progress on 2023 cost savings initiatives;
- Q2 cash flow and liquidity sources, including our $30 million credit facility;
- And, our Q3 and fiscal 2023 outlook.

Starting with Q2 2023 performance.

Revenue was $28.0 million, down 18% or $6.3 million year over year, driven primarily by Software Products and Services and Managed Services, which decreased 23% and 13%, respectively. The year over year decline in Software Products and Services was attributed to certain one-time software revenue in Q2 2022 of $5.7 million, which did not recur in Q2 2023, coupled with the previously announced decision by Amazon to reduce consumption of our HR products and services mid-May, the impact of which was between $4 to $5 million. Offsetting this was Government and Regulated Industries, which collectively grew 84% to $1.6 million in Q2 2023. Included in our Q2 GAAP results was approximately $1.7 million of revenue from the Broadbean acquisition completed in mid-June 2023. Overall, Amazon represented approximately 14% of our consolidated Q2 2023 revenue, down sequentially from 18% in Q1 2023. All to say, each quarter Veritone's revenue base is becoming increasingly diverse.

The Q2 2023 decline in managed services versus the comparable quarter in 2022 was driven by advertising, which was impacted by lower ad net revenue contribution, combined with a shift of campaign budgets from the first to the second half of 2023 due to the challenging macro environment, offset by a slight improvement in licensing. We believe advertising softness will reverse itself into the second half of 2023, due largely to our customer mix, new customer activation, seasonality on spend and improved economic outlook. Our optimism here is also supported by the fact that, despite our lower net revenues, gross current ad bookings are higher at this point, as compared to the same point in 2022.

On a pro forma basis, and assuming we owned Broadbean as of the beginning of 2022, Q2 2023 revenue was $34.7 million as compared to $42.5 million in Q2 2023, a decline of 18% driven by the previously discussed one-time software revenue benefit in Q2 2022, coupled with the decline in Amazon. On a pro forma basis, Broadbean was relatively flat quarter over quarter with Q2 2023 revenue of $8.5 million as compared to $8.3 million in Q2 2022. During 2022 and the first half of 2023, Broadbean spent a lot of its efforts on moving existing customers off its legacy Career Builder platform in preparation to be sold. This effort shifted sales focus on maintaining existing customers versus new customers, particularly in North America. Despite this challenge, Broadbean did grow slightly year over year, which highlights the stability of its subscription-based business.

As Ryan indicated, we are very excited about the future synergies and revenue growth opportunities of our combined HR Solutions products and services. On a pro forma basis, Broadbean adds close to 3,000 subscription-based customers, with over $30.0 million of Annual Recurring Revenue or ARR. On a consolidated basis, our software products and services now have a combined ARR of over $100 million, with over 44% coming from recurring-based subscription customers versus consumption based. From a strategic perspective, Broadbean is integrated in over 100 Applicant Tracking Systems, with global customers across the EMEA, North America and APAC and is integrated with over 2,500 global job board providers – accelerating our previous product road map by years.

With the addition of our programmatic advertising solutions, we expect to realize significant revenue and cost synergies beginning in the first half of 2024 as we finalize our go to market and sales strategies. Most importantly, our HR Solutions will now benefit long term by leveraging our AI with fully integrated ATS data sets. Based on our conversations with Broadbean customers, there is a lot of excitement around the long-term potential of data migration across top of the funnel talent through the employee life cycle.

We remain highly confident in the strength of our hiring solutions platform. Excluding Broadbean, our hiring platform customers exceeded 25% year over year growth. While Veritone has faced a number of external headwinds due to the macro environment, strategically we have made improvements in diversifying earnings streams and we are focused on moving towards future net retention growth across existing customers, starting first with ATS partners and customers in North America.

As an industry leader, Veritone remains encouraged by the growing number of opportunities as companies seek to boost operational efficiencies given the challenging market. We continue to see meaningful traction from new and existing commercial enterprise and GRI customers that want to benefit from Veritone's industry leading applications, hiring solutions and new offerings, such as cloud-based Veritone Redact which accelerates evidence redaction workflows. Our future pipeline remains strong with ample cross-selling opportunities, particularly in GRI where we expect significant growth in the near and long-term. Our partner-driven channel strategy continues to deliver results, with new bookings of $8.4 million in Q2 2023.

In Q2, we delivered strong key performance metrics, on a pro forma basis:

- ARR of $108 million, including over $47 million from subscription versus consumption based customers;
- Total New bookings were $8.4 million on a pro forma basis, down from Q2 2022 largely due to Amazon's reduced spend;
- Gross revenue retention continued to be in the high 90th percentile

- And, Total Software Products & Services customers of 3,705, which were relatively flat year over year given Broadbean's focus over the last 18 months on customer retention as it transitioned off its legacy platform.

In Managed Services, Q2 advertising gross billings per active client decreased to $576,000, down 22% from Q2 2022. Consistent with the drop in revenue, the decline was due to the challenging macro environment that impacted customers' spend and planned campaigns being pushed to the second half of 2023. Given our performance and bookings through today, we expect significant improvement heading into the second half of 2023.

Q2 2023 GAAP loss from operations was $28.2 million as compared to $3.6 million in Q2 2022, driven by a decline in non-GAAP gross profit, coupled with a non-recurring non-cash benefit of $13.8 million in Q2 2022 associated with a change in estimated value of contingent purchase price consideration.

Q2 2023 non-GAAP gross profit reached $20.2 million, down $7.3 million or 27% from Q2 of 2022 largely due to the decrease in one time software revenue. Overall Q2 non-GAAP gross margins were 72.2%, as compared with 80.4% in Q2 of 2022. Software Products and Services non-GAAP gross margins benefitted from the inclusion of one time software revenue in Q2 2022, which generated non-GAAP gross margins in excess of 90%. In addition, our managed services benefits from advertising revenue with non-GAAP gross margins in excess of 90%. We expect consolidated non-GAAP gross margins to trend towards 80% by year-end 2023, with sequential improvement each quarter consistent with the seasonality of our business.

Q2 non-GAAP net loss was $13.0 million, as compared to $7.2 million in Q2 2022 driven largely by the decline in revenue and corresponding non-GAAP gross margins, which negatively impacted our Core Operations.

Turning to our balance sheet, at June 30, 2023, we held cash and restricted cash of $63.5 million, compared to $185.3 million at December 31, 2022. The $121.7 million decrease reflects net cash outflows from operations of approximately $58.5 million, driven principally by the timing of payments in Managed Services and by our non-GAAP net loss. In addition, we had net cash outflows from financing and investing activities of $63.2 million, driven by the net $50.2 million acquisition of Broadbean in June 2023 and deferred purchase price consideration of $10.5 million attributable to Pandologic's 2022 earnout and certain 2022 acquisitions.

Turning to the Broadbean acquisition. Total purchase consideration paid was $50.2 million net of cash acquired, or a little over 1.4 times 2023 forecasted revenue. Before synergies, the acquisition is expected to be immediately accretive to Veritone and, on a standalone basis, is expected to generate SaaS and GAAP revenues of over $35 million on an annualized basis, contributing over $30 million in ARR from its subscription-based customers with attractive margins.

Of the total $62.7 million in cash, $52.7 million of our reported cash is essentially held for payment to third parties from our Managed Services, down from $93.1 million at December 31, 2022. The decline in cash held for third parties is partially reflective of the seasonality of our advertising services coupled with certain catch-up payments made in Q1 2023 from delayed payments as we migrated onto our new Oracle ERP system in the second half of 2022.

Turning to our liquidity. I am happy to report that we closed a revolving AR credit facility allowing us to initially borrow $30 million over a three year term. Interest is set at prime plus 1% with a floor of 9.5%, with a minimum of $250,000 of interest per year if we choose not to draw down on any funds. The facility will be senior secured against a portion of our domestic receivables, allowing us to periodically draw down on the credit line at our discretion and up to 90% of such receivable balances. Outside of standard covenants, there are no financial covenants or restrictions and no dilution.

In addition, we are currently in the process of completing a strategic transaction, which will further improve our liquidity position on a non-dilutive basis. We hope to have an update for you on this before the end of Q3 2023.

We ended June 30, 2023 with 36.9 million shares outstanding and convertible debt of $141 million principal, 1.75% interest due November 2026.

Turning to our cost savings update. In February of this year, we announced $12 to $15 million of annualized cost savings initiatives, which included optimizing our cost structure along with the divestiture of our energy group. I am happy to report that in Q2, we fully divested our energy group in exchange for a minority interest in Grid Beyond, a privately held company that delivers intelligent energy solutions. To date, we have executed over $17 million of annualized savings, well above our initial range. We are in the process of evaluating additional material cost savings targeting over $10 million annually, including planned synergies from the Broadbean acquisition, which we will update in the latter part of Q3 2023. These cost synergies are all part of our strategic plan as we look towards more vertically integrated growth opportunities in 2024, with a much more efficient cost structure.

Turning to our financial guidance for Q3 and Fiscal 2023. Fiscal 2023 continues to be a challenging year, with increased uncertainty amplified by recent Fed rate increases, inflation and customer impacting decisions – including Amazon's recent decision to reduce spending. With the addition of Broadbean, and assuming Amazon continues its reduced spend throughout the remainder of 2023, we are providing a more conservative 2023 outlook, with heightened discipline around costs as we march towards profitability heading into 2024.

With that backdrop, we are guiding:

Q3 revenue to be between $35.5 and $37.5 million, flat year-over-year at the midpoint. Included in this is Broadbean, which is expected to contribute $8.5 to $9.0 million in revenue in Q3. Excluding Broadbean, organic revenue is expected to decline overall largely driven by our conservative outlook on Amazon spend in Q3 2023, coupled with a slight projected decline in advertising, offset by continued improvement in GRI and other services.

Risks to our Q3 revenue guidance include the execution of new Enterprise deliverables, namely across GRI which can be unpredictable, advertising concurrent with current economic environment and any strategic transaction executed in the period, offset by potential for upside from Amazon as usage of our hiring platform can vary.

And…

We expect Q3 quarterly non-GAAP net loss to be between $6. 5 million and $8.5 million, which is relatively flat versus Q3 2022 at the high end.

For full year 2023, we are tightening our revenue outlook to be between $128.0 million and $135.0 million, representing a year-over-year decrease of 12% at the midpoint. As a reminder, and given the current economic outlook, we are forecasting our revenue conservatively throughout the remainder of 2023, including a material decline from Amazon in the second half of 2023, certain one-time software sales revenues in 2022 not recurring in 2023 and the impact of the Broadbean acquisition. Risks to our annual revenue guidance reflect the macro economy and the results of continued inflation and higher interest rates on our customers, hiring patterns, execution of new enterprise deliverables, namely across GRI, and continued customer growth and retention metrics from our Software Products and Services. 2023 revenue guidance also excludes the impact of any strategic transactions executed going forward.

In summary, our efforts in 2023 have been focused on streamlining operations to build a strong foundation for Veritone's next phase of disruptive growth. Despite external challenges in the current environment, we are excited by the improvements we have made year-to-date. Considering the impact of previously stated headwinds, we expect full year non-GAAP net loss to be between $28 million and $33 million, with Q4 approaching profitability. As previously discussed, we will be implementing additional initiatives that will translate to annualized cost savings of $10 million, which is incremental to the $17 million executed in 2023 to date. As these cost reductions flow through the P&L, we expect they will have a much larger impact in 2024, which will be when Veritone pivots back towards vertical growth from existing software and services, with a clear path towards profitability.

That concludes my prepared remarks. Operator, we would like to now open up the call for questions.