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Unity Software, Inc. (U)

Q1 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Welcome to Unity's First Quarter 2024 Earnings Call. My name is Daniel Amir, VP and Head of Investor Relations. After the closing of the market today, we issued our Shareholder Letter. That material is now available on our website at investors.unity.com. Today, I'm joined by Jim Whitehurst, our Interim CEO; and by Luis Visoso, our CFO.

But before we begin, I want to note that today's discussion contains forward-looking statements including statements about goals, business outlook, industry trends, market opportunities, expectations for future financial performance and similar items, all of which are subject to risks, uncertainties and assumptions. And you can find more information about these risks and uncertainties in the Risk Factors section of our filing at sec.gov. Actual results may differ, and we take no obligation to revise or update any forward-looking statements.

Finally, during today's meeting, we will discuss non-GAAP financial measures. These non-GAAP financial measures are in addition to and not a substitute for or superior to measures of financial performance prepared in accordance with GAAP. A full reconciliation of GAAP to non-GAAP is available in our shareholder letter and on the sec.gov website.

Great. So, what we'll do now is similar like what we've done in previous quarters, we get a number of inbound questions during the quarter, and we will start with two key questions here. The first is to Jim, and then the next is to Luis.

QUESTION AND ANSWER SECTION

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

So the first question to Jim is with the recent announcement of the new CEO and your new role as Chairman of the board, how do you see Unity going forward?

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Let me start off with saying, I am thrilled to have Matt Bromberg, joining us as Unity's CEO. He starts next Wednesday. Look, we conducted a super thorough search, and really, I'm thrilled with him. He has a great combination of – he is super strategic. He really has a sense of the industry, what are the trends, what are the subtleties, what are the disruptions happening. So, I think he'll be a great strategic steward of the business.

But in addition, he is a down in the weeds operational leader, who I think can continue to drive improvements in our execution. And finally, he knows the business extremely well, both the development – kind of game development side, as well as the monetization side. So, I think he will be a great leader for the company going forward.

Secondly, I'm not going anywhere. I'm remaining as Executive Chairman. And what I'm really excited about working on is the industry side of the business. I am – obviously, an area where I've spent a lot of time, and I continue to be super excited about the opportunity we have there. I'm probably biased, but I still think that's a bigger opportunity in the long run than the gaming business. And I'm looking forward to partnering with Matt to help however I can and ensure the success and growth of that business.

In terms of how I see the business today, I guess let me address that in the short term and the long term. I'd say in the short term, I am even more confident in our ability to deliver the plan this year. The reason I say that is several fold as things have unfolded.

First off, we are seeing customers, who were a bit ruffled at the end of last year, feeling much more confident with us. We've gone from the what and why of runtime fee to, I think, a recognition that the industry wants to make sure that we invest in the runtime. And so, it's a matter of how, and let's kind of work through that. So, we're having super productive conversations with our large customers. We had a phenomenal GDC, really, really great engagement across the board. So, also makes me feel good about our relationships with developers and where those are moving.

On Unity 6, obviously, that doesn't release until later this year. But if we look at the leading metrics, both the downloads and usage, but importantly, our measures around quality and our timelines, it's the highest quality release at this stage that we've ever had and the timelines have pulled in. We're not necessarily saying we're going to pull the release date in yet, but the timelines are coming in, that's generally a really, really good sign of good execution.

And finally, we talked a lot about interventions we're doing on the data and analytics side on the monetization business. Obviously, those have not manifested in the numbers yet. We've done a lot of the work. We're starting to get the results of the testing. It looks very encouraging. Those will roll out through the quarter, and you'll start to see that in Q3. So, you put all that together, I'm highly confident in our plan for the remainder of the year. We,

obviously, were confident last quarter, but all the indicators over the last three months make me even more confident in our ability to deliver.

In the long run, again, I continue to be super optimistic about the business. We are essential to gaming. There are a number of trends in gaming, where I think our position can help our customers be even more successful, which makes us essential and we'll continue to obsess over our customers' success and I feel really great about that piece of the business.

And frankly, on the industry side, as I said, it is still a relatively nascent opportunity for us, but the more I'm out talking to customers, the more opportunity I see there. So, overall, both the short term, I feel much more confident and in the long term, I remain super excited about.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

Great. Thank you, Jim. So the second question is to Luis. What is your overall take on Q1? And what are the plans to accelerate revenue growth here in the second half of the year?

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Hey, thank you, Daniel. I believe that we accomplished a lot in Q1. You think about it, we delivered in line with expectations with strategic revenue up 2%. Create, in particular, grew strategic revenue 17% with our core subscriptions up 13%. And we're making very good progress expanding profitability. EBITDA was up \$50 million year-over-year, and if you look at our like-for-like net income improvement, it is close to \$100 million year-over-year. So, great progress on profitability as we continue to drive revenue growth.

And very importantly, this resource were achieved while successfully completing a very large and complex cost and portfolio reset that will position us much stronger going forward. As Jim mentioned, customer engagement with the Engine and retention rates are healthy, industry continues to be our fastest growing business, and we continue making progress with AI tools, particularly Muse and Sentis. So I would say, a very good quarter.

Now looking ahead, which is kind of your second part of your question, overall the plan is unchanged from our conversations last quarter. With the portfolio and cost interventions behind us, we're now focused on the Engine, the Cloud, our Monetization business, where we believe that we can sustainably create value for our customers and generate a good return for our shareholders.

In Create, we expect the second half to continue to come from growth in subscriptions in both games and industries. And in Grow, we expect the second half acceleration to be driven by improvements in performance in our Monetization solutions and better usage of data to train our models and deliver that return on ad spend for our customers.

And very importantly, we continue to make progress on something we talked last quarter, which is to integrate, Create and Grow, to better serve our game customers more holistically, which is something that Unity can uniquely do better than anybody else. So in summary, I would say that we believe that we're very well positioned, and our focus now is to execute our full potential.

Now before we go to other questions, I would like to remind you that our revenue guide is for our strategic portfolio only. And we're doing this to help investors really focus on the business that we're driving while we exit

the non-strategic business. So you will see our guidance for strategic revenue. When we report actuals, we're obviously giving you both numbers, the numbers for our strategic portfolio as well as our non-strategic portfolio.

On adjusted EBITDA though, we're guiding for the total company. This is to avoid allocation issues. And as we know, the non-strategic portfolio adjusted EBITDA is not meaningful, which is one of the reasons we're exiting those businesses. So hopefully, that is clear, and we can go back to the questions.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

Great. Thanks, Luis. So with that, why don't we open it up to questions here. [Operator Instructions] Okay. So the first question, Andrew Boone from JMP Securities.

Andrew Boone

Analyst, Citizens JMP Securities LLC

Q

Thanks so much for taking the questions. I wanted to go back in terms of the growth drivers that you just talked about for the second half acceleration. I think for Grow, you talked about monetization of solutions and then better usage of data. Can you just unpack that a little bit more in terms of what we should actually expect. And from the product perspective, what exactly are you guys doing to be able to drive that growth? Thank you so much.

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Do you want to take that, Jim? Or...

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Well, I mean, I can start and you can kind of break that out. So it sounded like you said, more on the Grow side of the portfolio. So as we said before, we're operating with, frankly, two different data science departments. So we weren't fully kind of integrated in what we were doing. This year, as part of kind of completing the ironSource merger, we've kind of brought those organizations together, whether it's data engineering or data science, there was frankly a lot of data we just weren't fully using. We are now training our models using substantially more data.

We also, by combining forces, we're able to kind of roll out incremental analytics against those things. And there are multiple, there's like one for iOS, there's one for Android, there's one around different sets of kind of behavior in these various data sets, data we're getting from MMPs. And so each one of these, you kind of continue to tweak models and test and compare and run A/B tests, et cetera, et cetera. And then as you see those results and you kind of tweak and you kind of get where you see material uplift, you then do the full training on all your data and you start to roll those things out.

So that's what we're doing. Obviously, some of those things are competitive, so I don't want to go into very, very specifics. But we have at least about eight or nine I'd say major kind of things that we contemplated at the beginning of the year. Literally, I think all of them look pretty good. I think six or seven of them, we actually now have some initial results that look super positive. The others just take longer. And so, we will be rolling those out more at scale through the rest of this quarter, and it will lead into July as well, which is why we see the back half of the year as we've projected kind of sequential improvement in the back half of the year there.

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Totally. And maybe just to add, when we talk about more data, as we said last quarter, there are two components of more data. The first piece is just using more data that we already have. There is nothing we need to do. We just need to consume it. We need to train our models, and that's what we're doing. And the other piece is to get more data, which we think we can, based on our total portfolio so that we can actually improve and create a competitive advantage. So those are two components of the data. And as Jim said, we're working very hard to improve our models. There are very clear interventions that are coming in. We're testing, tests are looking encouraging. And therefore, that gives us confidence that we'll see improvements in the back half.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Thank you. The next question, Jason Bazinet from Citi.

A

Jason Boisvert Bazinet

Analyst, Citigroup Global Markets, Inc.

Thanks so much. I just had a question on the share count. I don't – maybe I have my notes wrong, but did the share count guidance for the full year increase a bit? And if so, you mind just unpacking the drivers of that? Thanks.

Q

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

Yeah. Jason, it did go up a few million. It's just driven by all the changes, all the restructuring we're doing, nothing significant. I think it went up less than 1%, 0.5% or something like that. So, that's the increase you see there.

A

Jason Boisvert Bazinet

Analyst, Citigroup Global Markets, Inc.

So I thought – maybe my numbers are wrong. I thought it went up like 3%, 492 million versus 476 million or something. Maybe I have the wrong note.

Q

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

Yeah, I'll come back to you, Jason. I think it was a small increase driven by all the restructuring we're doing [indiscernible] (00:13:47) the year. But that's really the change, nothing else.

A

Jason Boisvert Bazinet

Analyst, Citigroup Global Markets, Inc.

Okay. Thank you.

Q

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Great. Thank you, Jason. So the next question is Michael Funk.

A

Michael J. Funk

Analyst, BofA Securities, Inc.

Hey, guys. Thank you for the questions tonight. Jim, you mentioned interventions on the monetization side and not in the numbers yet. But can you give us more clarity, maybe some quantification on what you're seeing in initial testing expectations for return on ad spend relative to the industry standard today. AppLovin commented

Q

last night, they believe they have an insurmountable advantage on the monetization side. And so, I would love to hear your thoughts on what you're seeing with the initial testing and where you are or believe you are return on ad spend and where you believe that you can go and close that gap?

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Well, I'll give you two observations. Then, Luis, if you want to kind of add in here. So, first off, some of these tests, as we then kind of talk to partners, they have been extremely positive, and we've actually had some people moving some more to LevelPlay with the results of some of the things we're doing. And these are large MAX customers. And so that leads us to believe that the interventions actually closed much of the gap versus AppLovin.

These things are kind of relative to share, so a lot of share moving back our way. Are we equal to them or not in ROAS, it's hard to exactly say on these. But the customer feedback has been actually extremely positive. And we are seeing share shift. And we think when we roll these out, we will continue to see that.

The other thing I would say just broadly is, look, nothing against AppLovin. I think they're doing an amazing job. They're executing on all cylinders. I think one of the benefits as we look at ourselves right now, and we hear this over and over and over again, no one wants to have one partner, right? That scares people. You don't want to be reliant on one partner, especially given the ability if you have a lot of share to just increase your margin, i.e., what you pay a publisher versus what you charge. And so, people want competition there. And so, we've had a number of customers just say we're being patient. We're expecting to catch up. We're here for you. You got to deliver, but we're here for you. So, it's not a situation where a company can run away with this and everybody is excited.

People are wanting us to close gaps and win. So there's a lot of patience there. And as we're working through these, again, where we've worked with a couple of partners specifically on these things, we've seen really good results against those things. So, whether we close the gap to 100% or to 70% or 80%, it's really hard to say just as we're kind of running through because you don't actually see the ROAS numbers across. But what we're seeing is very positive trajectory, which will impact spend with these various advertisers. So, that much I can say. It's hard to compare benchmark to benchmark exactly.

Michael J. Funk

Analyst, BofA Securities, Inc.

Q

Thank you for that color, Jim. And by the way, very nice speaking with you last few quarters and good luck to you in the new role.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Thank you. Appreciate it.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

Thank you. So the next question, let's open the mic for Clark Lampen, at BTIG.

W. Clark Lampen

Analyst, BTIG LLC

Q

Hey. Thanks for taking the questions. Jim, I wanted to start with the Plus to sort of Pro transition that's underway. Anything that you could tell us around early signal with customers sort of moving up to more expensive Pro plans? Have you seen that sort of happening the way that you expected?

And then, Luis, a bit of a micro question on 2Q. But understanding that you guys don't guide at the segment level, I was curious if you could give us some directional commentary around both sort of Create and Grow. Should we expect both segments to be up? Is one sort of up and one is flat? Just curious if there's any one bucket that's going to be driving more of 2Q than the other. Thank you.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Look, on the Plus to Pro, Luis, I don't know if you wanted to add some commentary. I, honestly, couldn't tell you versus our expectations on where that stands. I think we're pleased with it, but I'm not sure how that plays out versus, Luis, what you would...

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Yeah. No...

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

... [ph] probably guide (00:18:13).

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

...we're very happy with how customers are migrating. Particularly, we're seeing some of our customers migrate all the way to enterprise, which is obviously better for us, better for our customers. So, we're seeing a good migration of customers up and that comes on top of the price increase we took about 18 months ago. So, we're seeing all of that flow through the bottom line.

I think to your second question, I really want to be careful and not guide between the two businesses. I do expect Create to do better than Grow on the quarter, and also on the year, so Create should be growing faster as you would expect, but Grow will be sequentially improving, particularly in the second half as we fix some of these gaps that we have.

W. Clark Lampen

Analyst, BTIG LLC

Q

Thanks very much.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

Thanks. Next question comes from Parker Lane at Stifel.

Jeffrey Parker Lane

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Yeah, hi, guys. Can you hear me okay?

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Yeah.

A

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

Very well.

A

Jeffrey Parker Lane

Analyst, Stifel, Nicolaus & Co., Inc.

Perfect. Jim, how significant or material is the Capgemini partnership been in delivering successful projects around industries? I know this is something that you guys really wanted to emphasize with a third party. So, is that shortening the time for people to deploy industries' products, improving the scope of those projects? What is that looking like?

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Well, we closed April 30. So in the last nine days, I mean, honestly, we haven't had a chance to see a lot there. What I will say is having kind of lived this movie before, I think if you look, most enterprise, or I'm talking about enterprise software, the infrastructure companies accelerate their business when they have partners who take that infrastructure and deliver bespoke solutions for customers.

A

I don't think it will be any different for us. We offer an extraordinary solution to visualize real-time kind of Interactive 3D, whether that's creation through viewing. The use cases, there are a few standardized ones taking all your PLM tools and having a common viewer. That's more of a true product thing, but the vast majority of this will be kind of custom applications that are delivered by SIs. So I have high confidence in it. I think we're excited about it. But literally, we just closed April 30. And so again, beyond high confidence, nothing's changed in the last nine days enough to kind of give you an indication on deal sizes or lengths in those things, but we continue to be optimistic.

Jeffrey Parker Lane

Analyst, Stifel, Nicolaus & Co., Inc.

Totally fair. Got it. Thank you.

Q

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Thank you. So next question, Josh Tilton from Wolfe.

A

Joshua Tilton

Analyst, Wolfe Research LLC

Hey, Guys. Can you hear me?

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Yes.

A

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Yes.

Joshua Tilton

Analyst, Wolfe Research LLC

Q

Great. Thanks for taking my question. I just want to – I kind of want to follow-up on a question I think that was kind of asked a few different ways in the beginning, but just very directly. And what I'm just trying to understand is, is your confidence around the second half acceleration in growth coming strictly from the improvements that you're making and your expectation for these improvements to help improve growth, or is it because you've made these improvements and you're already seeing it somehow change customer behaviors today? And if it's the latter, can you just help us out, give us a sense, give us a flavor, just an example of how these improvements are already changing customer behaviors to use these products?

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Yes. I mean at the end of the day, they are not yet showing up in revenue, right? Otherwise, you would be seeing it in Q1. And what we're telling you is that it's not going to happen until the back end of the second half of the year. So our A/B testing is encouraging. We continue to show – particularly we're improving the sophistication of our complex machine learning models and infrastructure and using more data, as I mentioned just before. So we're seeing those benefits, but they are just not yet at a scale where it's showing up in our revenue.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Yes, I'll try to give you just an example. And it's a lot of little things. So, we did some work on the performance of our Playables ads, made a tremendous improvement. And so we have a couple of customers in particular who are really excited to see that and are working with us to want to kind of scale this out much more broadly. And so as those things where they're small, but they are real – on real data, live experiments that we've done are bigger than kind of trials that we've done that have shown real material results. And we have no reason to think that that won't continue when we roll these things out at scale. So, like Playable ads would be one. I want to be a little cagey because we don't want to talk about details of the various areas we're working relative to competitors.

But it's areas like that where it is real things, real tests run for multiple weeks, where you see the results. And [ph] everyone else is (00:23:17) run a test and say, oh, let me throw it out there is, you run a test and you tweak because you want to get it as optimized as possible before you roll it out at full scale. But what we're seeing in several areas like Playables has been extremely positive. And so we expect as we roll these out that we'll see material positive results from them.

Joshua Tilton

Analyst, Wolfe Research LLC

Q

Super helpful. Thank you.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

So, next question, Matthew Cost from Morgan Stanley.

Matthew Cost

Analyst, Morgan Stanley & Co. LLC



Hi, everybody. Thanks for taking my question. So I guess, you're obviously having a lot of conversations with customers right now. I think you stated that kind of at the beginning of the script. One thing that Unity as an institution has talked about historically is how your customers are paying you less than 1% as a take rate of their revenue? And mathematically, given how much value you provide, they should be able to pay more.

I imagine you're probably in those conversations with advertisers right now kind of testing and going back and forth about what they are willing to pay you, kind of along the lines of what you're saying. They understand that it's important for Unity as a product you invest for the good of the industry. So I guess how should we in the financial markets think about what your customers are willing to pay you? How are you dimensioning that in the conversations that you're having with them right now? And how should we think about it? Thank you.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.



I'll start on that. Look, I've been frankly trying to stay away from those conversations. To talk about a fixed pie and the fact we're not getting our fair share in a fixed pie is a really lousy conversation to have, because that means you're talking to your customer about kind of giving some of their pie to you.

I think the better and broader way to think about it, and Luis alluded to it before, we're not talking about Create and Grow internally, and we're not talking about with our customers. We're talking about what can we do in what is a very difficult market for our gaming customers. How can we help drive their success by what we can bring to bear? Whether that's about how to build games that are more immersive, so better games, how to build games faster, how to build games with lower development costs, how to accelerate the ability to monetize against those games.

And when you have conversations around that, where you start talking about how do we improve your success, how we get paid becomes a little bit less kind of important kind of in that. And I think it's an area where because we cut across development through monetization, we have a unique ability to talk to them.

So, Matt, I know I'm not directly answering your question because we're not asking it that way. But I'm very confident about how positive the conversations have turned in the last few months, I think partly bluntly just runtime fee having sunk in and kind of gotten behind this. But I think part of it is people seeing us talking in a much more productive and proactive way, not saying, we're only getting 1% and we deserve more. But, hey, how do we make this industry more profitable. And in doing so, yeah, we'll find a way to get a little bit of that.

Matthew Cost

Analyst, Morgan Stanley & Co. LLC



Great. Thank you. And then in terms of...

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.



Overall, I really do feel like the conversations are so much more positive than they were kind of coming in with that attitude.

Matthew Cost

Analyst, Morgan Stanley & Co. LLC

Q

No, no, that makes perfect sense. And then I guess in terms of those conversations with customers, I think one thing that you've mentioned over the course of the past quarter is the idea of maybe more data sharing with customers as a means of providing inputs for the Grow business. I guess, how are those conversations going? Are you seeing any uptake or even any early testing with that right now?

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

We actually have a product launching called [ph] CoreStats (00:27:10) over this summer. And so, frankly, we've been kind of – we want to kind of get that solidified before we actually start having some of those conversations. So, I personally haven't had a lot of those conversations, because we didn't want to make it too theoretical. So, I don't know, Luis, have you had any of those? Do you have any color there?

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

No.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

No. I think [indiscernible] (00:27:29).

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

I agree with what you're saying, Jim.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

But our belief, just in our broad conversations is, again, when you start talking about how do we make you more profitable across the portfolio, obviously, doing a better job of identifying kind of users that are going to be profitable, so part of that.

And so, I think of it less as kind of somehow giving data to Unity as much as like how do we work together to kind of whether it's improved ad spend or improve monetization, data is a part of that, but I think of it as more how we're helping them use that data for their benefit. And I think when you kind of articulate it that way, it makes sense to people.

Matthew Cost

Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

Thank you, Matt. Next question, Martin Yang from Oppenheimer.

Martin Yang

Analyst, Oppenheimer & Co., Inc.

Hi. Thank you for taking my question. Can you hear me okay?

Q

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Yes.

A

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Yeah.

A

Martin Yang

Analyst, Oppenheimer & Co., Inc.

My first question is regarding runtime fee and its implementation. Do you still intend to use that fee to help the Grow segment in any way? In the past, I think using a runtime fee to offset some of the advertising expenses was part of the plan. Do you still have similar designs by the time you launch runtime fee later?

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Yeah, that's still part of the plan. I don't look at it that way. I mean, I look at it as more we need to make the runtime sustainable, and that requires a revenue source. And whether that revenue source is, I'll call it, direct kind of pay us based on usage or indirect, use our monetization, our ad stack, and therefore we get some degree of monetization on that, I don't really care, right?

A

But I think the key is for us to be able to continue to invest and build the runtime to be extraordinary and long-lived, et cetera, et cetera> We need the revenue stream. And again, whether it's direct or indirect, I don't think we care as much. So, I don't think it as much as a subsidization as much as choose the way you want to help ensure that we make the runtime sustainable for all our customers.

Martin Yang

Analyst, Oppenheimer & Co., Inc.

Got it. Thank you.

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

So I guess, yes, I guess in a sense that if you're using LevelPlay, yeah, you don't have a runtime fee.

A

Martin Yang

Analyst, Oppenheimer & Co., Inc.

Makes sense. Next question is on [ph] CoreStats (00:30:05). Can you maybe give us more information on that? Is that going to be a product that sits in Create, or Grow, or something entirely different?

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Well, it is in Create because it is – I would call it more of a service than a product that we offer to help our customers better understand how users are engaging with their games. And so, it's anywhere from crash data all the way through to kind of various measures around engagement. And of course, that data is also can be valuable on the ad side as well.

So it's – I guess you could argue it's a product feature that can be enabled, but it's not like a separate line item. It is not something we're charging for. It's kind of a benefit to customers if they're willing to kind of engage with us to see that data to help also help them better monetize their games.

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

And I think this is a great example where we're no longer thinking about Create and Grow, but we're thinking about the game customer, right? And how do we create more value to them and more value for us by thinking about these customers more holistically.

Martin Yang

Analyst, Oppenheimer & Co., Inc.

Q

Got it. Thank you very much.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

A

Great. So our next question is Gili Naftalovich from Goldman Sachs.

Gili Naftalovich

Analyst, Goldman Sachs & Co. LLC

Q

Hey, everyone. Just checking if you can hear me here?

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Yeah.

Gili Naftalovich

Analyst, Goldman Sachs & Co. LLC

Q

Perfect. So thanks, Daniel and team. And I have one for Jim and a follow-up for Luis, if I may. And this is really off of Luis, on the comment that you just made. Are you guys seeing any different trends around customers that are using both Create and Grow? Or is this something that we should expect more in the second half on the back of the roll-off of Unity 6 and Unity monetization engine?

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Yeah. I would say, it's really going to come together in the second half on how we create the synergies between the two. We're not seeing a lot of that yet. But we think that we have unique assets where we can actually do that. And that's something that only Unity can do. So we should expect that to come in the back half and then to continue to increase the years thereafter.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Yeah. In part, it's not just around Unity 6, it's just time, right? I mean, we literally just did this reorg and started acting this way in January. So, yeah, we're starting to engage. Again, I hear positive feedback. But engagement to behavior will take a bit of time.

Gili Naftalovich

Analyst, Goldman Sachs & Co. LLC

Q

Got it.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Kind of like got a slack from our marketing people. We actually feel very good about kind of ahead of plan on the migrations up to higher priced versions of Unity.

Gili Naftalovich

Analyst, Goldman Sachs & Co. LLC

Q

That's great to hear.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

A

Luis, our staff is listening.

Gili Naftalovich

Analyst, Goldman Sachs & Co. LLC

Q

I mean, I guess on that line of thought, too, like as it pertains to EBITDA, Luis, you came in very strong this quarter. How do you evaluate investment opportunities and get comfortable with the allocation of capital in each one of the business initiatives and business line items that you have in the pipeline?

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

A

Yeah. I mean we're being very choiceful on where we invest, and we're particularly investing in things that make – this is going to resonate because it's in line with everything we're saying. So where are we investing? We're investing in data. That's one of the – I was expecting you guys to ask why is our EBITDA kind of not improving significantly in Q2. And one of the reasons is because we're investing in cloud consumption to drive that data that will help us on our Grow side.

So we see the benefit of the savings, the benefit of the restructuring on cost on the portfolio and it flows through the bottom line, but then we're investing particularly on two things: cloud consumption to drive more data; and data scientists, because that's an area where we need to continue to improve and that just pays out very quickly. So that's kind of where we're going.

On capital allocation, as you know, we've been buying shares. We also reduced our debt significantly at a good discount by the way. We had a \$61 million gain, as you saw. And we'll continue to evaluate what we do based on whatever the market is going. So we're constantly looking at that, Gili.

Gili Naftalovich

Analyst, Goldman Sachs & Co. LLC

Perfect. Thank you.

Q

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Thank you, Gili. And the last question is from Bernie McTernan from Needham.

A

Bernie McTernan

Analyst, Needham & Co. LLC

Great. Thank you for taking the question. Can you guys hear me all right?

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Yes.

A

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

Yeah.

A

Bernie McTernan

Analyst, Needham & Co. LLC

Great. Thanks. Jim, can you just unpack some of the comments you made about the runtime fee? Just thinking about why customer sentiment has improved so much. And then also on Grow, just any impact on – or any thoughts on macro impact on the business and how you expect it to progress throughout the year? Thank you.

Q

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Well, so a couple things. I think in the cold light of day, when you sit down with customers and you're talking about kind of our existing contracts and what this really kind of means and where those dollars get spent, I think people have realized, a, it's not as dire as they thought it was depending on the game and how it get monetized as it kind of varies around whether it's an app purchase or ad or whatever.

A

So I think people have now are moving from worst case to a realistic view of what a runtime fee would be because we can sit down and work that through with them. And then it does create an opportunity, and I actually saw this a lot even as far back as UNITE about, let us talk about the engineering effort that goes into the runtime, forget about the engine, the runtime and building the most performant run time, keeping it performant and continuing to drive value into that as we go forward.

And people start to say, okay, I get it. A, I'm not like immediately saying, oh it's 2.5% of all of my revenue, it depends, right? There's a lot of – and you kind of work through that. And then you kind of work through but here's the value and what we can drive with that. People kind of come down and you start to have more rational conversations.

I wish I could say it's more than that, but I think some of it is just from kneejerk reaction about, oh my god, it's not a great time in the market you want to charge me more to, well, here's what we're doing, here's the relationship,

here's the value you're actually getting. And here's what it looks like it's really going to cost you. And the conversations kind of softened and they become much more kind of productive for how we work together.

I don't know if it's a lot more than that. It's just, I think, a little bit of sobriety after a while and a combination of moving from kind of thinking the math in worst case to actually see what it's likely to be.

Daniel Amir

Vice President-Investor Relations, Unity Software, Inc.

Great. Thanks a lot. So with that, we're going to wrap up the call. Thank you for dialing in today, and we're looking forward to meeting you during the quarter at various investor conferences. Have a great day.

Luis Felipe Visoso

Executive Vice President & Chief Financial Officer, Unity Software, Inc.

Thank you.

James M. Whitehurst

Interim Chief Executive Officer & President & Director, Unity Software, Inc.

Thank you.

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