Riskified Third Quarter 2023 Earnings Transcript *Edited*

Corporate Participants

Chett Mandel, *Head of Investor Relations*

Eido Gal, *Chief Executive Officer*

Agi Dotcheva, *Chief Financial Officer*

Analyst Participants

Ramsey El-Assal - *Barclays*

Brent Bracelin – *Piper Sandler*

Timothy Chiodo – *UBS Securities*

Bob Napoli – *William Blair*

Terry Tillman – *Truist Securities*

Reggie Smith – *J.P. Morgan*

Chett Mandel
Head of Investor Relations

Good morning and thank you for joining us today. My name is Chett Mandel, Riskified's Head of Investor Relations. We are hosting today's call to discuss Riskified's financial results for the third quarter of 2023. Participating on today's call are Eido Gal, Riskified's Co-Founder and Chief Executive Officer, and Agi Dotcheva, Riskified's Chief Financial Officer.

We released our results for the third quarter of 2023 earlier today. Our earnings materials, including a replay of today's webcast, are available on our Investor Relations website at ir.riskified.com.

Certain statements made on the call today will be forward-looking statements related to our operating performance, business and financial goals, outlook as to gross profit margin, Adjusted EBITDA profitability, and expectations as to positive cash flows, which reflect management's best judgment based on currently available information and are not guarantees of future performance. We intend all forward-looking statements to be covered by the Safe Harbor provisions contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements reflect our expectations as of the date of this call and except as required by law, we undertake no obligation to revise this information as a result of new developments that may occur after the time of this call. These forward-looking statements involve risks, uncertainties and other factors, some of which are beyond our control, that could cause actual results to differ materially from our expectations. You should not put undue reliance on any forward-looking statement. Please refer to our Annual Report on Form 20-F for the year ended December 31, 2022 and subsequent reports we file or furnish with the SEC for more information on the specific factors that could cause actual results to differ materially from our expectations.

Additionally, we will discuss certain non-GAAP financial measures and key performance indicators on the call. Reconciliations to the most directly comparable GAAP financial measures are available in our earnings release issued earlier today, and also furnished with the SEC on Form 6-K, and in the appendix of our Investor Relations Presentation, all of which are posted on our Investor Relations website.

I will now turn the call over to Eido.

Eido Gal
Co-Founder, CEO & Director

Thanks Chett and hello everyone.

Before we dive into a discussion on our financial results and outlook, I would like to first briefly touch on the evolving situation in Israel. Then I will share some commentary from the third quarter, and end my remarks discussing why I remain as confident as ever in the positioning of the company. As part of this discussion I will provide some color on how we were able to efficiently adapt our workforce and enact our Business Continuity Plan to ensure uninterrupted service to our merchants in the wake of the October 7 events. Then, Agi will walk you through our third quarter financials, and what to expect in the fourth quarter.

First and foremost, we condemn the horrific attacks in Israel and we send our thoughts, and support to all affected. The loss of innocent lives resulting from this unforgivable terrorist act and the war that ensued is truly devastating. To our customers, partners, and shareholders who have reached out to support us during this difficult time, on behalf of everyone at Riskified, we sincerely thank you.

I am relieved to report that all of our employees are accounted for. I am proud of everyone in the organization for stepping up their efforts and for their hard work in a time of need and I believe this speaks loudly to the strong culture at Riskified. This level of focus and flexibility has meant that we've seen no material impact on our ability to maintain day-to-day operations across all critical functions.

Moving now to our third quarter results. Once again, our revenue growth during the third quarter was primarily driven by the successful execution of our "Go-to-Market" strategy, which contributed to 14% year-over-year revenue growth, and 17% for the first nine-months of the year.

We are growing more confident in our ability to add new merchants, retain and upsell existing ones, and expand our market share despite an uncertain and challenging macroeconomic backdrop.

Our competitive win rates remained high during the quarter, and we have onboarded more new merchants versus this point last year. We have generated over 20% more leads compared to this point last year, which is contributing to a large and growing pipeline.

We are working diligently on maximizing revenue opportunities, leveraging our machine learning capabilities to positively impact the business while prioritizing investment in the areas with the highest return. I'm excited that we've grown topline revenue by 17% while simultaneously decreasing total operating expenses by 6%, which drove an improvement in Adjusted EBITDA performance by over 50% in the first nine months of 2023. We believe that these results are testament to the overall strength of the business, and our ability to execute and find leverage in the model.

Next, allow me to spend some time talking about the isolated fraud event that we discussed on our last earnings call.

As a reminder, one of our largest merchants experienced a significant fraud event in July. This event was contained over the course of a handful of weeks, and as expected, the impact caused by this event contributed to a non-GAAP Q3 gross margin of 44%. We do not anticipate any further impact to our gross margin going forward as a result of this event.

While we are disappointed by this one-time event, we did learn valuable lessons. For example, we have updated and solidified various go-live processes, improved some of our chargeback monitoring tools and added new detection capabilities. I should also mention that our relationship with the impacted merchant remains very strong, and this isolated example underscores the overwhelming reason why we believe that chargeback guarantee is a superior model that delivers the most value to merchants.

Overall, we remain encouraged by our underlying gross margin performance. I believe that our commitment to continuously invest in our machine learning capabilities through feature enhancements and model improvements continues to strengthen our market leading technology.

Now, back to the Israel conflict and how it relates to our business. Our core focus since the events of October 7th has remained the safety of our employees and continuity of services to our merchants. To support the well-being of our teams in Israel, we have provided flexible working arrangements for those who are not yet back to their normal office schedule, assisted those employees and their families who have been called on reserve duty, and expanded our existing mental health and wellness offerings.

To support our merchants, we've been working diligently as part of our Business Continuity Plan to leverage our global network of employees to fill temporary capacity needs. Although we've experienced minor delays in a small number of long term initiatives, there has not been any material impact to our current productivity. We remain 100% engaged with all our customers through increased communication efforts, and have not seen loss of merchant volumes, as a result of the October 7 events. This is a testament to the deep relationships that we have cultivated with many of our merchants, high retention rates, and our track record of being a reliable and trusted partner.

Before I turn to Agi, I want to emphasize that I believe the DNA of our company positions us well as we work through the current situation. While we are proud of being a company founded in Israel, we are truly a global company with business functions spread through eight locations around the world, and with merchants in nearly 40 countries.

Our goal remains to maximize revenue and profit with our AI-powered fraud and risk management platform to all of the world's largest enterprise eCommerce merchants, and I am very confident in our ability to continue executing on that mission through all environments.

Now, I will turn the call over to Agi

Aglika Dotcheva
Chief Financial Officer

Thank you Eido, team, and everyone for joining today's call. I echo Eido's thoughts on how incredible the team and organization have been in the face of a difficult situation in Israel.

Our GMV for the third quarter was $29.7 billion, reflecting a 17% increase year-over-year.

We achieved third quarter revenue of $71.9 million, up 14% year-over-year, and year-to-date revenue of $213.5 million, up 17%.

Our GMV and revenue growth during this quarter was primarily driven by the continued expansion of our platform across new merchants and upsells, similar to recent quarters.

"Tickets and Travel" remained the largest overall category, with year-over-year growth in the mid-teens. The step down in growth from previous periods was primarily driven by the lapping of a large merchant in this category that was onboarded in the third quarter of 2022.

Encouragingly, for the first time in eight quarters, all industries outside of "Tickets & Travel", in the aggregate, contributed more than that single category, or approximately 60% to our quarterly growth. In particular, this quarter we saw solid performance in our "Home" category, primarily driven by upsell activity.

Similar to the first half of the year, third-quarter growth in one of our largest categories, "Fashion & Luxury Goods," remained relatively flat year-over year. We continued to see softness in particular within our luxury brands and sneakers sub-segment. In addition, our "Electronics" category declined further from their second quarter levels during the third quarter, as demand for goods in this discretionary category slowed.

Finally, we also saw revenue growth across all geographies. Our third quarter revenue in the United States, our largest region, grew by 9% year-over-year and we experienced 12% year-over-year growth in EMEA. Our Americas and APAC regions each grew approximately 40%, primarily due to momentum in new and upsell activity. We believe that our continued revenue growth from regions outside of the United States demonstrates market share gains, and validates our decision to invest in these regions.

Moving on to gross margin. As Eido mentioned, our Q3 margin was negatively impacted by the isolated fraud event announced at our last earnings call. The impact of the event was in line with expectations and our non-GAAP gross profit margin for the third quarter of 2023, reflective of this impact, was 44%.

As a reminder, gross margin is best analyzed on an annual basis as gross margin may fluctuate on a quarterly basis. However, given the unique nature of the third quarter margin, allow me to provide clarity on the annual range as we approach year-end.

As of today, we anticipate that our annual non-GAAP gross profit margin will be at the mid-point of our range of 50.0% to 51.5%, or 50.7%, which translates to a fourth quarter gross margin of approximately 54%.

Moving to expenses. Total non-GAAP operating expenses were $40.2 million for the third quarter of 2023, a 5% decrease year-over-year as a result of our continuous focus on optimizing our expense base. Our third quarter expenses represent the lowest absolute quarterly level since our IPO over two years ago.

Our non-GAAP operating expenses as a percentage of revenue improved year-over-year, from 67% to 56% reflecting leverage in the business model.

For modeling purposes, we anticipate a modest step up of approximately one million dollars in expenses in the fourth quarter.

Adjusted EBITDA for the third quarter was negative $8.4 million, and negative $18.2 million for the first nine months of 2023. Even with the one-time impact of the aforementioned merchant fraud-event, we have been able to improve our Adjusted EBITDA performance year-over-year for the fifth consecutive quarter and have improved our Adjusted EBITDA performance performance by 50% Year-to-date.

As previously mentioned, we continue to anticipate profitability on an Adjusted EBITDA basis in the fourth quarter of 2023, and on an annual basis in 2024.

Moving to the balance sheet: we maintain a very strong liquidity position and generated positive free cash flow during the quarter.

We ended the third quarter with approximately $482 million of cash, deposits, investments and accrued interest on the balance sheet, and we carry zero debt. This amount represents a sequential increase of approximately $2 million.

We remain confident in the business's ability to generate positive operating cash flows over the long-term as was demonstrated during the third quarter, and we continue to believe that our balance sheet and strong liquidity position are underappreciated assets.

Related to our capital allocation initiatives, as we announced alongside our second quarter earnings, our Board has authorized a share repurchase program of up to $75 million, subject to approval from the Israeli court, which is required by law. Due to the events of October 7, Israeli courts are currently operating under rolling Emergency Orders, and certain court processes are delayed. We anticipate receiving a decision from the Israeli court in the next several weeks and we will announce the court's decision promptly once it is obtained.

We expect to leverage this program to take advantage of opportunistic repurchasing opportunities, and manage share dilution. At valuation levels well below that of companies with similar financial profiles, we believe that we have a great opportunity to repurchase our stock at attractive prices. We believe our strong balance sheet enables us to continue driving shareholder value by investing in the growth of the business while maintaining significant capital to continue pursuing M&A opportunities.

Now moving to our guidance, which assumes no further worsening in consumer spending patterns, or material changes to the macro-economic environment. As we approach year-end we have more visibility on the timing and ramp-up of the onboarding of certain merchants, and expect a more muted than originally anticipated T&T season, especially in the tickets and live event vertical for the remainder of the year. As a result, we are refining our full-year 2023 revenue range to be between $297 - $300 million.

That being said, as a result of our ongoing expense discipline in the first nine-months of the year, we are improving our full-year 2023 Adjusted EBITDA guidance to be between negative $12.5 million and negative $14.5 million, an improvement of 7% from the midpoint of our previously disclosed guidance range.

Overall, from an operational perspective, I believe that we are executing from a position of strength, even in a challenging environment. And despite the evolving geo-political situation in Israel, and the continued challenging macroeconomic landscape, we remain excited about prospects for long-term growth and our ability to deliver value to shareholders.

Operator, we're ready to take the first question please.

Question and Answer

Ramsey El-Assal
Barclays

This is Owen on for Ramsey. I appreciate you taking our question this morning. Wanted to ask specifically about your sales pipeline, and was wondering if you could provide any more color on the portion of new sales that's being driven by cross-sell compared to net new logo growth and if you're seeing any difficulty in one versus the other? Any clarity there might be very helpful.

Eido Gal
CEO, Riskified

Hey, Owen. Sure. So we feel great about the pipeline. I think we mentioned it's about 20% larger than this point a year ago, and that's really across the board, both in the newer products around policy and dispute, also from a geographical perspective. So the pipeline increase, I would say, is relatively broad-based.

Ramsey El-Assal
Barclays

Understood. I appreciate that. Also wanted to follow up, if I may, on your take rate and kind of longer term expectations there and how you expect that to trend relative to the business. Is there any sort of point in which you might choose to favor new logo growth by passing along some expense savings to customers? Any kind of update there might be interesting as well.

Eido Gal
CEO, Riskified

Sure I would say, look, take rate is always risk adjusted, right? So depending on the risk of thesegment or the merchant or the category, that informs our pricing, and that means that there's really variance within take rate based on those profiles. To be just a bit more specific, if we work with a digital goods merchant that sells high risk products internationally, the fee would appropriately be higher than a merchant that sells domestically in the US with low risk products, and that would influence the take rate. Our pricing philosophy is to make sure that there's always value to merchants when they start using Riskified, right? So our pricing, which impacts our take rate, would always provide them savings relative to their existing cost.So that's how we think about pricing.

Bob Napoli
William Blair

Thank you for taking the question. And we're probably thinking about you all going this time. Glad to hear everybody is accounted for. As we think about your turning to profitability and maybe a longer term picture, Eido, Agi, how do you think about the glide path to getting to your long term targets of EBITDA margins?

Eido Gal
CEO, Riskified

Look, I think the things that are within our control, right, are around OpEx discipline, around executing on the sales side. Like we've been focused on them for the past eight quarters, we'll continue to focus on them as we march towards those longer term margin targets.

Aglika Dotcheva
CFO, Riskified

I mean, for the last couple of quarters, I think that we've been able to improve our OpEx line and ultimately going to pass this to adjusted EBITDA. We're still expecting Q4 to be profitable and next year to be profitable. It's very much of a focus and something we're executing on.

Bob Napoli
William Blair

Thank you. And from a geos perspective, I mean, great to see the strong growth out ofAsia. Just over the next – where do you see the bigger opportunities? Are you just scratching the surface in those markets or those international going to become a much higher portion of the business over time? And is the international business, the profitability, is there any – are there any differences geo-wise in the profitability of the business?

Eido Gal
CEO, Riskified

I think we're all very proud of the GMV gains and kind of the market share we do have. Having said that, we still feel we're scratching the surface of the overall eCommerce market and penetration. So we still think there's significant growth definitely in some of these newer regions where we're seeing higher growth rates, like you mentioned, but also in the more traditional industries and regions. So when I think about growth outlook, it's continuing to focus on our existing categories and geographies. It's strengthening some of these international markets, APAC, LATAM and moving more towards a platform sale where policy and dispute resolved have a more pronounced impact. So I think all those will help us with the growth moving forward.

Tim Chiodo
UBS

Thanks for taking the question. So my question is around the Plaid partnership that you announced for ACH payments. Can you provide us any update on how the partnership has contributed to your business so far? And where do you see most of the use cases among your verticals?

Eido Gal
CEO, Riskified

I think ACH is a growing and evolving payment method, and we see more merchants want to offer it as an alternative to credit cards, either to build recurring payments, less the interchange fee, or to take care of high amounts or different verification statuses. So we do see it as a growing consumer payment option. And what we've heard from our merchants is because the risk there is slightly different than traditional credit card fraud, but they still need help solving those problems. So really the partnership with Plaid is aimed at offering merchants an end-to-end solution that includes a way to accept guaranteed payments via ACH, and it has been meaningful in building some of that pipeline that we discussed earlier.

Tim Chiodo
UBS

Got it. That's really helpful. And a quick follow-up on – of new products, in addition to chargeback guarantees. So it was encouraging to see the pipeline growth and the cross-sell opportunity that you highlighted in the release. So how does the momentum look like with Policy Protect contributing to your new revenue bookings? And do you see any difference in terms of product adoption between the US and the international side?

Eido Gal
CEO, Riskified

We feel great about the pipeline, the way it's building. We feel that the merchants are – that are live, it's solving a very meaningful and significant pain point for them. I'm not sure that I can differentiate between the global and kind of local markets, but we definitely don't see a difference in the ROI that it's providing to either. So we look forward to continuing to update you on the progress.

Terry Tillman
Truist Securities

Eido, Agi and Chett, good morning. And also my thoughts are with everyone impacted by the conflict. I had two questions. Maybe the first question, Eido, I think in your prepared remarks, you talked about having increased confidence I think just in general in the business and in monetizing new logos. I hope I didn't misrepresent that. The Top 10 new customer deals in the quarter, particular strength in the US. What I'm curious about is what's driving the increased confidence? The macro isn't any better, so it can't be that. Is it stuff on the sales side with leadership? You've got a new CMO. Is the market just, from 12 months prior, based on the RFP activity, just starting to come around to these advanced ML decisioning engines? I'll stop with my rambling and maybe you could just put a little bit more meat on the bone in terms of the increased confidence in just winning new business.

And then I had a follow-up for Agi.

Eido Gal
CEO, Riskified

Sure, happy to do so. I think – so let me – tighten that up, I have increased confidence in the things within our ability to control, right? So when I think about some of the initiatives we started probably two years ago, about the increased investment in additional products in our platform, additional investments into a global enterprise salesforce, sitting here today, I think we're starting to bear the fruit of some of that, right, and some of that reflected in some of these products being fully deployed and in the hands of merchants and generating value. Some of that is reflected in the growth rates in APAC and the pipeline that's building. Some of that is reflected in the ML platform and the performance that it's been providing to us and our merchants. Also you mentioned Jeff , our new CMO from a few quarters ago, also very confident and happy with our current leadership team. So I think all those things are definitely helping me become more confident in the business longer term. Like you said, macro, I have not seen inflect meaningfully this quarter like you mentioned.

Terry Tillman
Truist Securities

Understood. Thank you for that, Eido. And then, Agi, in terms of the fourth quarter outlook, I know the comp was tougher in 3Q, so that made sense on maybe kind of growth year-over-year. But in 4Q, it is an easier comp. I think I'd love to just get a little bit more perspective on, is there an incremental degree of conservatism? You did say tickets and travel. Maybe that's the sole factor. But I did hear that, well, maybe there's –some of the rollouts will take a little longer. Just a little bit more in terms of maybe some of this is timing. And then actually once you – there's some incremental benefits from some of the rollouts. Just a little bit more on the roughly 7% growth of the midpoint comment. Thank you.

Aglika Dotcheva
CFO, Riskified

So in terms of the fourth quarter and what's changed is that some of our perspective since we last reported, I'll say some of the nuances and trends specifically about the ticketing sub-vertical in tickets and travel, mostly in live events, is something that we saw a little bit softer coming out at the end of the quarter and kind of like early in October The way I look at it, it's mostly coming off of a really busy season, starting from the beginning of the year, but also through the summer, and a little bit of a different seasonality in this industry than what we saw last year. So that's one of the aspects related to Q4. And the other aspect is more around new deals coming in. Looking at 2023 growth, it's primarily driven by new business, and it's a very, very strong driver for us. Looking into Q4, I think there was some slight delay in a bit of deals still coming in, just a little bit in the back half of the quarter, which may get pushed into maybe early next year. But all of them are really strong deals. All of them are still in the forecast, just a little bit later in the cycle.

Eido Gal
CEO, Riskified

Yeah, I would just add to that. Again, I think, like you've seen throughout this year, sometimes there can be fluctuations between quarters for us because of underlying eCommerce trends across our different categories. And it is important to point out that we don't feel that the Q4 rate is reflective of what we would anticipate next year.

Reggie Smith
J.P. Morgan

Thank you. Good morning. I guess most of my questions have been hit. Just a point of clarification.vDid you guys size the actual impact of that fraud loss during the quarter? And I have a quick follow-up.

Aglika Dotcheva
CFO, Riskified

Thank you for the question. So it landed up within the range of what we expected, more precisely around $4.5 million. And the gross margin that we expected based on this fraud event is also 44%, aligned with our expectations.

Reggie Smith
J.P. Morgan

Perfect. Thank you. And then – and I'm not sure to what extent you guys can provide color on this, but I'm just curious if there's – maybe you can kind of walk us through eComm trends in general throughout the quarter and maybe through the first month, month-and-a-half of 4Q. Anything you're seeing there worth calling out?

Aglika Dotcheva
CFO, Riskified

Yeah, of course. So, as I already mentioned, I think the biggest kind of change from prior expectations is around live events in the tickets sub-industry. It's been a little bit softer, but overall it's still a very strong growth driver for the year and still overall performing well. The other trends, I'll say there's some strength in the food and home category, the latter one primarily driven by some of the upsells that we were able to execute. And electronics has been a little bit soft. I think it was soft last quarter, but continued softness in this quarter. These are probably kind of like the biggest highlights.

Reggie Smith
J.P. Morgan

So are you suggesting that tickets and travel weakened toward the end of the quarter and into this fourth quarter? Just trying to clarify the comment there. I guess that would coincide with the Beyoncé concert, if I'm thinking about that correctly.

Aglika Dotcheva
CFO, Riskified

It's hard to say. We just see it in more than one merchant. I don't see exactly what's driving it, but it's really like across geos and in more than, I would say, like probably two, three of the merchants in this category.

Eido Gal
CEO, Riskified

You're right to highlight that it's more specific to live events than other types of ticketing.

Brent Bracelin
Piper Sandler

Thanks for taking my questions and glad to hear all your employees are accounted for. Just wanted to echo my support for you, your colleagues and your families here. Eido, in a previous answer, you mentioned moving more to the platform sale. Iguess can you talk about your ability to land new merchants with more than just chargeback guarantee upfront and how that's evolved?

Eido Gal
CEO, Riskified

Sure. Thank you for that commentary. Look, I would say that when we sell chargeback guarantee, we're solving for chargebacks related to fraudulent reason codes, right? And that leaves a lot of pain points and inefficiencies for our merchants such as chargebacks related to non-fraud reason codes, different forms of financial loss related to policy abuse. Right now we have the ability, whether it's through a new sale or a cross-sell or upsell, to solve a wider set of problems, right? So sometimes merchants are saying, hey, that's great.I don't just have a chargeback issue, I have issues with some of these other problems and that's helping us advance conversations with the platform sale initially. It's actually also helping us, even when a merchant might say, you know what, I'm not ready to make a change on my fraud platform right now, we can actually start with policy or dispute, which has been showing great traction and is a really easy and good initial sale. So we feel good about the opportunities and conversations with new merchants from that more platform approach.

Brent Bracelin
Piper Sandler

Okay. Super helpful. And then, Agi, in terms of upsell strength, are you seeing more strength on the volume side or the cross-sell side, and how do you expect that to trend over time?

Aglika Dotcheva
CFO, Riskified

Upsell has been a strong driver. It's coming from a lot of different areas. Definitely the ability to expand both – a higher approval rate or also to kind of expand more of GMV and from existing customers have been a factor.

<End of Q&A>

Eido Gal
CEO, Riskified

Thank you, everyone, for the support. We look forward to updating you in the coming months on our next call.