Riskified Ltd.

presentation delivered at the J.P. Morgan 2021 Ultimate Services Investor Conference on Thursday, November 18, 2021 at 2:30 PM

Tien-Tsin Huang: Thanks, everyone for joining. My name is Tien-Tsin Huang. I'm the payments and IT services analyst at J.P. Morgan. You're joining the Riskified session here at the Ultimate Services Investor Conference.

From a format standpoint, we are taking questions from the Ask a Question portal. If you have any questions, happy to take them there. I've got a list of questions that I fielded from investors, so thank you for that. We'll go through it in the next 30 minutes or so.

Eido Gal, the co-founder and CEO of Riskified has been gracious enough to join us. I know there's been a lot of interest and activity in the stock. I'm hoping to cover all of that here in our discussion. I didn't want to go right into the quarter and some of the details, if that's OK. Thank you for being with us.

I want to start with the basics, if you don't mind. Go back to basics. Tell us about the founding of the company and what problem you are trying to solve. Let's build up to what we've learned recently, if that's OK. Thank you again. Appreciate it.

Eido Gal: It's great to be here. Hey, everyone. You can see I'm in our windowless board room at the Riskified HQ.

Why do we start the company? I'm not sure everyone is exactly familiar to all just briefly recap. If I steal your credit card engine while we're speaking, order a bunch of stuff online, you see it on your statement. You call the bank, you say. "Hey, I did not place this order." You're just filing a charge back. The merchant is liable in that event.

Merchants basically what they have to do e-commerce merchants, they screen every single incoming transaction to understand if it's fraudulent or not. The reason they do this is that they have the liability.

When we started Riskified, every Merchant was building and managing this process internally, and they were using external vendors and internal teams. We said we think we can build the world's best solution for identifying fraudulent e-commerce transactions and provide that as a service to these merchants.

I'm replacing the entire structure that they have internally, and that was the basis of Riskified. That's how we started.

Tien-Tsin: Perfect. A lot of focus on chargebacks and fraud, we hear about that quite a bit from an economic perspective. It's interesting that you provide charge back guarantee. Let's discuss that. Why charge back guarantee as the focus? Why not also do scoring as an option for some of your merchant clients?

I ask this because I think back to covering some of the check verification, check guarantee companies like TeleCheck and Certegy back in the day. Not to date myself, but I think back to that where there was two sides of it. One was guarantee and one was verification. Tell us about why only chargeback guarantee.

Eido: Sure. Going back to that original model, before Riskified, an enterprise e-commerce merchant, you would have a team of 5 to 10 analysts, data scientists. They would be using some of the tools, whether it's CyberSource or Accertify.

They would be using these platforms to build rules or maybe even smarter machine learning models. They would be deciding what to accept or what to reject. They would basically make mistakes, and accept bad transactions, and receive chargebacks.

They would be declining some good customers, so some false positives there. There was a lot of friction in that process.

When we started Riskified, we said, "How do we replace that entire scenario, because we don't want to be a tool that they're using? We think that we can provide more value by doing the ultimate decisioning."

We believed that the way that merchants would trust us to manage their business, we would have to provide them with an approval rate guarantee, so they knew exactly the performance on an ongoing basis and a chargeback guarantee.

Now, it's a different product, the product that optimizes performance on an ongoing basis for fraud with approval rates and chargeback rates than a product where you give the merchant the score and the ability to decide on his own.

Very early on, we believed, and we still believe, that the ultimate value that we can provide when we manage the entire process and have the direct feedback loop of the chargebacks and the approvals, versus creating a tool that the merchants can use internally with their own teams is going to be much greater.

The thesis was that even in the largest e-commerce retailers, the largest ones, at some point they're going to say, "Hey, I have so many things to do, why am I building and managing a team to solve the problem of e-commerce risk? I have a million other things that are much more important to do. I'm not the best in the world at it."

We're the best in the world at doing that one thing. Today, to your question, or it was a previous question in a discussion we had, is this more SMB? Is this enterprise? We believe it's enterprise.

We have three out of the world's 10 largest Internet retailers on the platform today. It's not a question of do they have the capabilities. If they decide to go to the moon, they could put their focus on that. It's not their core competency.

When you think about the network effect demo platform, the engineering resource we have, it's vastly larger than any single merchant can. We believe, again, that the ultimate value's in the chargeback guarantee model, which is inherently different than the scoring model, which is where merchants manage it in-house.

Tien-Tsin: You've got some skin in the game as well, so that's got to buy some confidence in with the merchants.

Given everything you said makes sense around getting rid of the cost and the burden and the headache of dealing with something that's not core to them, what's the value proposition for the merchant? What do they typically see from a cost or savings or ROI? What do you pitch when you go out and you talk to prospects?

Eido: Three main value props, number one is around increase in sales. That's the number one proposition.

Today, merchants proactively decline a large percent of transactions, because they do not want to receive chargebacks. There, we're saying that we've seen results up to 20 percent increase, average closer to the range of 8 percent increase, and this is across our top 10 largest clients.

Second dimension is around cost reduction. If you think about the cost of managing fraud, the cost of tools, the cost of chargebacks, the cost of staffing pre-to-post Riskified, 40 percent reduction in cost. We're getting massive incremental sales uplift, significant cost reduction.

Third one is around customer experience. Pre-Riskified, you might have done a lot of manual checks calling the customer. You weren't able to offer same-day shipping, because 10 percent of volume is in a manual review queue, so third one is around enabling better customer experiences.

Tien-Tsin: Every time I hear those stats, it's really compelling to the merchant. The sales cycle, I've always been surprised how long it takes, but I also understand that you're placing an internal operation, and it takes time to learn and build that trust. Tell us more about the sales cycle and what a typical onboarding process looks like.

Eido: I would say that a typical sales cycle is 9 to 12 months for our larger enterprises, with the integration cycle being an additional 2 months. That's fairly long. We think we can shorten it, but it would still be a multi-month process.

When you think about working with a large enterprise, getting historical data, running a PoC, going through legal, going through procurement, there's a natural cadence to this. We think we're good and we're comfortable with it.

We think that the upside to this is that it's very sticky once you're in, and that's a combination both of the value that we highlight, but also of that challenging process to integrate and embed within these enterprises. When you have that combination of a sticky solution that creates a lot of value, we think that the retention characteristics are great.

Tien-Tsin: Got to make money, of course, so the pricing model and how you benchmark pricing in general, what's the right way to think about it?

Eido: It's risk-adjusted pricing. What that means is based on the level of risk in a certain population of transactions we receive, that's the fee that we price. For example, same merchant, we can start working with a merchant, and he can say, "Hey, you know, what Riskified? I want you to work on all my international volume. It's 10 percent of my volume. It's higher-risk categories."

We would analyze that, and we would come to the merchant and say, "Hey, you know what? We could provide you for a 50-basis point fee and 92 percent approval rate, and that would be the fee for this segment."

Later on, that same merchant would come and say, "Hey, you know what? I want you to do all my domestic US. It's a safer population." We'd say, "Hey, you know what? The pricing for this segment would be 20 basis points." It's risk-adjusted pricing.

The great thing about that is that it enables us to work with much, traditionally, safer categories. Basically to mention some of the names are like Wayfair, we work with the largest online retailer of pet food in the US, so traditionally safe industries we work with, because we have a lower risk-adjusted fee.

While we can also work with higher-risk industries, whether it's categories like remittance, like digital wallets, sneakers, where the risk-adjusted fee is high.

Tien-Tsin: Let's get to the numbers a little bit. You've talked about longer-term growth targets of, what, 25, 30 percent plus on an organic basis. Build us up to that.

The same store, the term, the new sales contribution, however you want to build. I know you've given some NRR figures in the past, too. How do you build up to that?

Eido: Yeah, so the framework we just recently provided to help give more clarity around how we think and run the business on a multi-year horizon, it's to say we're positively leaver to e-commerce. When we look at GOAT analyst reports of e-commerce growth and what we anticipate from our existing base, we're building up to a 10 to 15 percent organic growth motion.

That's how much our existing clients are growing, net of any upsells are cross-sells. When we think about new business upsells to existing clients and cross-sells, we think that's adding an additional 15 percent. That's how we got to that 25 to 30 percent longer-term algorithm.

Within that, obviously some fluctuations when merchants go live for some share percentage there, but that's the framework.

Tien-Tsin: This quarter, you grew revenue 26 percent right in that zone, but the gross profit was up 10 percent. Walk us through the variance there. What drove that?

Eido: Right. I'd say this quarter, we're starting to see the impact both of PSD2, which is the regulation in the EU which is reducing some of the volume that is submitted to Riskified, so that's impact number one. Impact number two is that we're starting to see some change in the organic behavior as re-openings happen, some of the shift away from traditional e-com.

Those two factors are in play, and together with a different merchant mix, we saw a different risk category. We had higher amounts of travel. We entered new categories around payments and remittance, so a lower gross margin quarter. We're 100 percent fine and OK with that.

We manage the gross profit on an annual basis. We anticipate some fluctuations within a quarter, and we do not see any meaningful impact on our longer-term gross margin trajectory, or on the performance of the algorithms, or on same merchant performance.

When we think about Q4, again, let's talk an annual basis because that's how we think about it. We feel this is a 50 plus gross margin this year as well. Those would be the annual ranges we would give.

Tien-Tsin: Got it. I don't know, like I said, we get caught up in the quarter sometime, but we're trying to learn as we go and as we get more familiar with the business of, so thank you for that.

You did mention a little bit softer e-com, we heard that throughout the sector. You also mentioned a supply chain issues that you're watching that not a surprise. We've heard that through the earning season as well.

The question I have, and I field it from a lot of investors, is that do you over-index to higher-value resalable goods that might be more impacted by supply chain? May be a source more from Asia, etc., so what's your response to that?

Eido: I think it could be. It could be we're over-indexed to consumer goods relative to services for sure, things that are more easily resellable. I haven't done a smart enough analysis around shipping patterns within our existing client base and to match that.

I can tell you, and what we're basing this off is the public reports of some of our portfolio that people know our clients, whether it's Peloton, Wayfair, Foot Locker, some other sneaker industries. We also work with more private companies in these categories, so just based on what they're projecting is giving us a more cautious spend, just how we get SIC.

Tien-Tsin: Fair enough. I think, look, SIC county's part of every business, but I think we...That's helpful to hear some of the exposure from the end market standpoint. Before we go into PSD2, because I know it's a complicated subject that we can talk for at lengths, I know you and I talked about this quite a bit.

We have this at our keynote speaker event earlier as well. Alternative payment methods, buy now, pay later, all the different pays. PayPal, Alipay, Shop Pay, you pick it. What does it mean for Riskified?

Eido: Risk or opportunity, it's a bit of both when you think about commerce volume. Going away from credit cards and so these alternative forms of payments, the question we ask is, "OK, what does that mean from our perspective? We can work with an e-commerce merchant. Can we work with a buy now, pay later provider? OK, can we work with a digital wallet?"

For us, the answer is clearly, yes. They're going through the same issues, the same problems that enterprise e-commerce merchants are having. All right, they're managing fraud and risk on their own. They're building their own systems and platforms, and we believe that we can facilitate and help them manage that process just like we can the world's largest e-commerce merchants.

We definitely work with remittance and some digital wallets within the BNPL space. We feel we have a healthy pipeline in that category. Just the highlight when we talk about buy now, pay later, we're talking about underwriting transactions for fraud, fraudulent credit cards. We're not talking about, "Will this user default on a two-year loan?" That's not our specialty.

Tien-Tsin: Right. It's if this is a legitimate transaction flow-through. You're not trying to take a view of the credit.

Eido: Sure.

Tien-Tsin: Understood.

Eido: Now, look, it's interesting because all these different payment methods. There's definitely more confusion, I would imagine, for the merchants, but there's probably more opportunity for fraud and bad behavior as well.

Yeah, I think we'll keep asking you, but I guess we should think of those as those genotypes is just another merchant as well that has to deal with the same problems that a traditional version would.

Tien-Tsin: Let's shift gears and do Europe and PSD2, what was 15 or so percent of your volume before. For those less familiar, maybe you should go into PSD2. A strong customer authentication, and it shifts the liability away from the merchant which makes the chargeback guarantee product less relevant in Europe. How do you frame the risk, and what are the offsets?

Eido: We obviously frame the risk as the European volume that is now under PSD2 is no longer...They no longer need a chargeback guarantee, so that volume is removed from risk. If we see that as a one-time reset, and when you think about it, you mentioned the amount of volume from the EU.

When you start to look at it, some of it is eligible for exemption. For example, if a transaction is below a certain amount, it does not have to go through strong customer authentication. If a transaction is initiated in the EU but maybe the credit card was issued elsewhere, then it also doesn't have to go.

There are like different pockets that can help you build up an exemption list, but the main thing to remember is that PSD2 is a bad consumer experience. It creates drop-off. It forces people into strong customer authentication, and it's a bad thing for merchants.

We believe that merchants will try to find a way to build as many exemptions, and work around from the strong customer authentication as they can. That's led us to develop a set of solutions to optimize for PSD2.

What is important to remember is from a timing perspective, as PSD2 is coming into play in Q3 with a fuller impact into Q4, meaning will cycle out of that, 12 months following. It will take more time between the implementation and the time that merchants will onboard a new solution.

Just think about it naturally. You're impacted by something in Q3. You start to analyze it in Q4. You optimize for solutions in Q1, and you go live with them in Q2. While we do think that there is a significant opportunity to recapture some of that PSD2 volume with our solutions, it would be at a different time frame than one of the regulations goes into effect.

Strategically, we do not believe this impacts our European capabilities or volume or market. That's mostly at around PSD2.

Tien-Tsin: Well said. Just to be clear here, you have a product that helps with the experience side of it in the [inaudible] . Can you spend a minute on what that is exactly on how you monetize it?

Eido: That's a great question. Thank you. The main product is what merchants are allowed to do. As long as they are able to keep chargeback levels below, a certain rate, they can send a subset of transactions to be excluded from strong customer authentication.

When you think about who is the best in the world, we believe it's the best in the world at maintaining approval rates up to a certain chargeback rate, it's us. If a merchant on his own or any other competing solution would be able to approve 20 percent of transactions before reaching that 10-basis points limit, we would say that risk if I can reach 60 percent while reaching that limit.

60 percent that does not go through SEA creates higher acceptance rates. I always feel it it's incredibly complex whenever we get into PSD2. I just hopefully the audience that part was clear.

Tien-Tsin: No I get. It is complicated, and it's new for all of us, even though I feel like we've been studying it for years now, if not a decade, but it's finally here.

Tien-Tsin: Last one, I think you said on the call recently that the impact should peak in the first half of '22. You explained it very well that it takes time to digest, understand it, eventually, do something about it. If we're thinking about peeking, we could see first half growth be quite depressed.

I don't know what you can tell us about how to frame the downside to growth in relation to another 25 to 30 talked about is we're going to be below that. Next year, obviously, I think street was well below that. How do we frame the bottom here on the on the first half '22?

Eido: Let me just be a bit cautious because we're not providing guidance yet.

Tien-Tsin: Understood.

Eido: We haven't fully analyzed and made sure that our models and we want to have a bit more runway into February when we do announce that we have very smart and concrete numbers, but we did want to give everyone the anticipation because we do believe that the overall trajectory will be a reduction into H1 followed by a resumption into that framework, that we share.

Going in that direction into page two. I think directionally what you're saying is obviously correct. H1 would be below that type of framework guidance that we shared.

Tien-Tsin: We'll cross through the holiday. We'll hear from you probably sometime in February. I would imagine at that point, if I'm correct, that you'll you should have a pretty good grasp of where trends, unless there's some other delays or some other shock. I would imagine at that point, the visibility should be very high on this topic. Fair?

Eido: Very fair. Again, just to reiterate, obviously, of course, changing market conditions. The reason we decided to share some of this is invent is to give people the opportunity to understanding, to be as transparent as possible. We're relatively new to the public markets. That's been our approach internally and externally to share what we see. Hopefully, we'll continue to do that.

Tien-Tsin: We value that so we'll be sure to stay on top of hopefully asking the right questions and learning as we go, learning as we go. I think we've got seven minutes left. I have a few more things I want to hit. We've got a couple questions here from the investors too. I'll try and put them all.

Policy protect deco, it sounds like policy protect has had some good outcomes recently. How do you feel about those products in the demand for those in the short-term midterm here?

Eido: I think policy protect his awesome. I love it. When you think about the value that it can create and how the technology underpinning it is similar to what we do as charge back guarantee I think it's amazing.

Policy Protect, what happens is there are multiple use cases, but one significant use case is when you initiate a refund request with the merchant. You say, "I didn't receive my package, it's the wrong size," whatever. You do not believe how easy it is to create a false claim and receive money, even though you shouldn't.

Merchants are not even close to being aware of how much loss is going on in those categories. For us, it's the same type of fraud and detection in identity technology to understand the good versus the bad.

We've built a very robust solution. We're scaling it up with significant enterprises this coming year. We mentioned we went live with an e-commerce merchant that does over 10 billion in GMV, so I'm very excited about that opportunity.

When you think about Account Secure, it's also very meaningful and has a great interaction with our core chargeback product. We look at account creation, at logins at account, and share that data between the two products, so also more security-oriented, and Deco which helps optimize payment failures, which every enterprise tries to optimize.

They don't like these payment failures. This is a great, great buyer. We're not modeling out, and we've shared these historically meaningful numbers for these cross-sell opportunities in 2022. We believe that in 2023 and beyond is when you will start seeing that. That's it, then.

Tien-Tsin: That covers it then, that's good. A couple questions from the audience here about the holidays and how that impacts implementations. Do you see a natural slowdown in the fourth quarter into the new implementations or product sales, and then that picks up again in the first quarter?

Of course, there also will be higher holiday sales, in general, but you do understand the question? I'm reading it live. [laughs]

Eido: Yeah, yeah. I know that's clear. Look. We're seasonal businesses, and not all businesses are seasonal. We have a wide portfolio.

They definitely hunker down around Black Friday, Cyber Monday -- December, they're usually, between the holidays, back to business as usual. Some segments are more hesitant to go live during this timeframe, others, like tickets and travel, it's not so much an issue.

Tien-Tsin: Then the other question just here was, do you have any large implementations that are underway that are going into the fourth quarter that were not present in the prior year? That was the other question here.

Eido: In the prior year, yes, we always have ongoing implementations, and definitely during this quarter as well, of course.

Tien-Tsin: Nothing unusual to call out there. You've come public, you talked about investing heavily in talent, hiring people, R&D. I know you guys are all engineers at heart here. What can we expect on the returns on some of those investments?

I know we need to be patient with spinning the go-to-market quickly, but how about from a product side? Could we see more product launches here, as we roll into 2022?

Eido: We definitely can. We believe at heart we're a product-led company, and we think that product innovation that solves meaningful problems for our customers is the way to create long-term and lasting and differentiated company, and increase the TAM and the stickiness. A lot of good things to come from that.

We also believe that we're good at solving hard and complex problems, so we think it sometimes takes times and capabilities to solve those problems. That's our approach.

We think about, "OK, what could be the total opportunity if we penetrated with this new product? What revenue can we generate?" and based on that, decide how many resources to allocate there.

That's our thinking on the product side, and we’ll definitely be happy to share more about some of the newer products, but once they're more mature. We don't see a lot of competitive value in talking about them very early in life.

Tien-Tsin: We've about three minutes left here. How about working with non-merchants, working more with issuers, merchant acquirers, networks, other players of the ecosystem?

Eido: It makes sense, doesn't it? There are so many different players, and there are so many working links between the card issuers and the merchant side that it would definitely make sense to think about it.

Tien-Tsin: When you prioritize partnerships, how do you go about working with the right players or deciding not to work with another? How do you prioritize the partner model?

Eido: Let me take a step back, by the way. On the previous question, it was more creating unique solutions to solve the problems for those different audiences, right, for the banks.

Now talking just about partnerships, it's, "Hey, what's a great distribution strategy, maybe mid-market? I don't want to build a salesforce, so maybe a good distribution strategy is an integrated partnership through someone who does serve the mid-market."

" We want to go deeper into, you know, a geography like Japan. We think that the easiest way to market is through like a significant partnership there." It really depends on the use case, and for us, it helps solve different parts of the go-to-market equation.

Tien-Tsin: Just from a geo expansion -- I know people are asking this, too -- is that another growth vector that maybe could surprise the short or mid-term, and you need to do it? Can you do it organically, or is that maybe where an M&A focus might be?

Eido: Let me answer it in two parts, first the geographic and then the M&A. In geographic expansion, a hundred percent, we need to be everywhere globally tomorrow -- yesterday, sorry, not tomorrow.

The reason we say that is we've seen that there's demand for the product, we've seen that there's capabilities of the product. We believe that over the next few years, most of the merchants in the world will migrate from their existing tech stack to a newer tech stack, which includes a newer way to manage fraud.

We just want to be front and center as part of that change, so we're trying to expand globally very, very quickly, which, to your point, might add cost in the near term. We believe it's a fundamentally effective model.

When you think about building out a new geography, you have a few AEs some BD, some AMs, some marketing capabilities. That scales for a multitude of years when you're talking about dozens or hundreds of that region's largest merchants. You don't need to create a massive salesforce, and the investment in year one is very, very beneficial.

The example we shared was that the 8 million we spent on sales and marketing in 2017, which we attribute to the cohort of merchants that went live in 2018, that generated 40 million in billings the prior four fiscal quarters, so we think it's very effective in the long term. Sorry, that was a very lengthy answer. That was on the global expansion piece.

When we're just thinking about M&A, it can be different things, and we're actively looking to find the right type of M&A. It could be either an expansion of the product portfolio if we can find something nice. Maybe it's buying into certain merchants or geographies, although we're not that focused on market consolidation.

We don't think there's a ton of value there, but I'm sure there's opportunities for smart M&A across a various range of use cases.

Tien-Tsin: Sorry, I have to rush through to the end here. I just want to make sure we can get all of my list. We're out of time. Let me let you go on one last question, if you don't mind.

I try not to let the stock influence our thinking at all. I hope it doesn't do that for you either too much. What do you think is misunderstood, in a nutshell, in 10 seconds or less. What do you think is misunderstood about Riskified today?

Eido: We do something that's core for every single e-commerce transaction. We do it, we're the best in the world at doing it. When you think about chargeback guarantee and the enterprise space, that's what Riskified is.

We believe that chargeback guarantee provides more value than any other type of solution, and that the opportunity is ours to win or lose. That's how we view it.

Tien-Tsin: Very good. Let's close out on that. Eido, thank you for the time. It was really busy times these days, and look forward to catching up with you soon at the next event.

Eido: Thanks, Tien-Tsin. Really appreciate it.

Tien-Tsin: Have a great week.

Eido: Bye.