



Will Wong, RingCentral, Inc. – Vice President, Investor Relations

Thank you. Good afternoon and welcome to RingCentral's second quarter 2022 earnings conference call. I'm Will Wong, RingCentral's Vice President of Investor Relations. Joining me today are Vlad Shmunis, Founder, Chairman, and CEO, Mo Katibeh, President and Chief Operating Officer, and Sonalee Parekh, Chief Financial Officer. Our format today will include prepared remarks by Vlad, Mo, and Sonalee, followed by Q&A.

We also have a slide presentation available on our investor relations website that will coincide with today's call, which you can find under the Financial Results section at ir.ringcentral.com.

Some of our discussions and responses to your questions will contain forward-looking statements, including our third quarter and full year 2022 financial outlook and our assumptions underlying that outlook. These statements are subject to risks and uncertainties. Actual results may differ materially from our forward-looking statements. A discussion of the risks and uncertainties related to our business is contained in our filings with the Securities and Exchange Commission and is incorporated by reference into today's discussion. RingCentral assumes no obligation and does not intend to update or comment on forward-looking statements made on this call. Unless otherwise indicated, all measures that follow are non-GAAP with year over year comparisons. A reconciliation of all GAAP to non-GAAP results is provided with our earnings release and in the slide deck. Please visit our Investor Relations website to access our earnings release, slide deck, our GAAP to non-GAAP reconciliations, our periodic SEC reports, a webcast replay of today's call, and to learn more about RingCentral. For certain forward-looking guidance, a reconciliation of the non-GAAP financial guidance to the corresponding GAAP measure is not available as discussed in detail in the slide deck posted on our Investor Relations website.

With that, I'll turn the call over to Vlad.



Vlad Shmunis, RingCentral, Inc. –Founder, Chairman, and CEO

Thanks Will. Good afternoon everyone and thank you for joining our second quarter earnings conference call.

While we are not immune from the current macro environment, we delivered a strong Q2. Let me start by giving you five fun facts.

1. We are a \$2B ARR company.
2. Contact center is now over a quarter billion of ARR, and is a key growth driver for us.
3. We are now at more than 5 million paid seats in our base.
4. We matched our quarterly record of \$1M plus TCV deals, bringing the total to almost 500.
5. We delivered a record operating margin in the quarter of 11.3%, up 110 bps year over year.

These results demonstrate RingCentral's leadership position in UCaaS, driven by our product innovations and unique go to market strategies.

We have been able to achieve these milestones through consistent execution. Q2 was no exception. Sonalee, who I'd like to welcome to her first earnings call as RingCentral's CFO, will share with you more details about our financial results shortly. Let me first give you the highlights.

Subscription revenue grew 32% year over year, and 33% on a constant currency basis. Total revenue grew 28% year over year, and 30% on a constant currency basis. Both were above the high end of our guidance, even taking into account the stronger dollar.

Operating margins of 11.3% were a quarterly record and well above our guidance, with free cash flow margins expanding 220 basis points year over year to 6.0%.

Following solid margin expansion in Q1, these results give us confidence in our ability to deliver-sustainable growth while expanding our margins.



Our success to date is grounded in four global megatrends. These are:

1. The cementing of hybrid work in the post COVID era, which in turn reinforces the need for cloud-based communications platforms.
2. The ongoing adoption of Mobility by businesses worldwide, which drives the need for solutions that enable work in any mode, on any device, from anywhere. Mobility is a friend, not a foe.
3. Teams in the Enterprise, which creates a meaningful opportunity for well-integrated, enterprise grade UCaaS and CCaaS solutions. We believe Teams is a growth driver for RingCentral.
4. Preference from CIOs to purchase an integrated, cloud based Unified Communications and Contact Center from a single provider, consistent with historical on prem buying behaviors.

Voice remains a key mode of communication for consumer to business interactions across a vast array of industries. These include healthcare, professional services such as insurance and finance, logistics, government and education, to name a few. We continue to win in all these verticals.

Another fun fact. We recently engaged a third party to conduct a survey of key technology purchase decision makers. 85% of respondents consider voice to be very to extremely important to customer engagement. 80% noted that voice is very to extremely important to revenue generation.

We continue to win because of our core corporate values: trust, innovation and partnerships.

First, Trust. For our customers, this marked the 16th consecutive quarter of 99.999% uptime, which is a key competitive differentiator. Our customers need to know with certainty that when their customers need to reach them, or when they need to communicate with any of their stakeholders, the technology will work. Time and again customers tell us that one of their top reasons for picking RingCentral is our proven reliability. And underpinning everything we do is our dedication to security and data privacy. Simply put, we treat our customers' data like our own. We also embed state of the art capabilities such as end-to-end encryption into our portfolio.



And speaking of Trust - we are proud to announce that yesterday we released our 2021 Impact Report, which highlights our commitment to our customers, our people, our shareholders and the communities we operate in.

Second, Innovation. RingCentral is committed to leading with innovation, creating features and functionality that customers want and need.

To highlight a few of our significant innovations in Q2, we launched new enhancements with our Salesforce and HubSpot integrations, making it easier for our customers to reach and engage with their prospects and customers.

For large international deployments, we introduced a Smart Dial Plan and a new bulk number management capability. These innovative features make it easier for international enterprises to connect their employees and customers across the globe.

We have also enhanced RingCentral Rooms with new seamless integrations with hardware partners like Avocor, Jabra and EPOS. This allows customers to enhance their ability to work from anywhere - whether in the office or remotely.

And last but not least, Partnerships. We had a good quarter with our strategic partners, led by Mitel and Avaya. On that note, we would like to welcome Avaya's new CEO and reiterate our commitment to this unique partnership that paves a way for the world's largest installed on-prem customer base to move to the world's leading UCaaS solution. Our unique global partnerships have contributed to our growth as customers transition from on prem to the cloud, and we are still relatively early in this journey.

Looking ahead, we are firmly focused on durable growth, improving profitability, and stronger free cash flows. We have the industry's leading UCaaS platform, and a talented management team in place to drive our continued success as we address the large, untapped opportunity still ahead of us.

With that, let me hand the call over to our President and Chief Operating Officer, Mo Katibeh.



Mo Katibeh, RingCentral, Inc. – President and Chief Operating Officer

Thanks Vlad. Q2 was a strong quarter, with strength from our direct business and our partners. We won close to 50 deals with a TCV of over one million dollars. Our integrated, market leading UCaaS and CCaaS offering also performed very well - with continued increase in the attach of CC on UC for our up-market teams. And we were able to achieve these results while driving revenue and operating margin growth. In short, we executed well.

Now - let me give you some examples of how we benefited from the 4 megatrends that Vlad outlined.

First, Hybrid work. Companies are enabling their people to work from anywhere. And RingCentral helps them be productive wherever they are.

As an example, C&S Wholesale Grocers, a US industry leader in supply chain solutions and wholesale grocery supply, recently selected RingCentral to replace their legacy PBX infrastructure. Here's what C&S had to say. "As we researched cloud solutions to replace our PBX infrastructure, we saw that with RingCentral, we could integrate a whole suite of communication features in one platform, connect our dozens of offices across the country for the first time ever, empower our employees to communicate from anywhere—and still save a million bucks a year."

Second, Mobility. One of the largest real estate brokerages in the United States needed a solution that seamlessly allowed their offices to back each other up and securely route calls to their thousands of agents whether in the office, at home, or in the field. And beyond creating a truly Mobility centric solution - the brokerage was able to recognize meaningful ROI by selecting RingCentral, with \$2M of savings over 5 years via a transparent and predictable cost structure. As a bonus this also freed up their IT team to focus on other key initiatives.

Third, Microsoft Teams which continues to be a growth driver for RingCentral. Second quarter was the single largest quarter of growth yet.

The vast majority of Team's customers are on E1 or E3 licenses, which do not include any sort of phone or telephony service – a key part of any business identity. This creates an immediate opportunity to complete the cloud communications suite by adding a well-integrated UCaaS solution like RingCentral. And as to the minority of Team's customers who have an E5 license, first - they still require an incremental calling plan to make calls outside



of their company. And even more importantly - they often need a richer feature set, 99.999% reliability, an integrated contact center option, and a larger geographical footprint – all things that RingCentral can offer.

In short, customers are benefiting both from a feature and cost perspective when adding RingCentral to their Teams environment. For example, a global provider of professional services purchased Avaya Cloud Office this quarter. The customer used Teams for messaging and video, but required a telephony option that provided 99.999% reliability and global reach. In evaluating their different options, they concluded that adding telephony to Teams was more costly - and offered less reliability and functionality - when compared to RingCentral. These cost savings are in addition to the ROI that the customer will realize as they reduce resources that supported several legacy systems.

And last but not least, customers want an integrated UCaaS with CCaaS solution.

RingCentral is currently the only company offering a fully integrated solution combining market leading UCaaS and CCaaS on a single bill, and leveraging a highly scalable and reliable global voice network.

Preferred Risk Insurance, a professional services company, highlights the benefits of our integrated UCaaS and CCaaS solution. Preferred Risk Insurance encountered significant challenges during the pandemic using legacy communications technology, which caused call quality issues and broken customer experiences. It became vital for the company to upgrade to a cloud solution that would allow their employees to call, message, and meet in one app, from the home or in the office. They also required a cloud contact center that would provide innovative features. For example, with RingCentral Contact Center, they will now have the ability for their Claims Agents to take a recorded statement that can be added to the insurance claim, while also ensuring that they can still leverage end-to-end, automated call recordings for compliance purposes.

Net - RingCentral is continuing to benefit from the four megatrends that we outlined- and we see this in our pipeline and our partnerships.



Regarding our pipeline - we saw 3 key trends this quarter. First, sales cycle times from opportunity to close have reverted to historical pre-COVID trends, which we expected. Second, and demonstrating demand - we saw an increase in leads quarter over quarter and year over year. Third, opportunity size for small business has remained consistent. However we are seeing cautiousness from larger customers in their buying decisions - focusing on smaller, initial deployments. What is clear is customers ranging from small business to enterprise and across all verticals continue to see the value of our offerings - while also being mindful of broader, near term market forces that is influencing buying behavior.

As part of our diverse vertical go to market approach we are focused on how moving to UCaaS from an on premise solution generates a strong return on investment for our customers.

In the current environment where many customers are looking more closely at their spend, we show value very quickly, with an average customer payback period of about 9 months. Customers that move to RingCentral MVP on average are also able to reduce their telecom costs by 23%, their hardware costs by 20% and their IT spend by 16%.

Turning to our partnerships, we continue to see growth from our Strategic Partners and the GSP community. Seats from our Strategic Partnerships are up almost 100% YoY. Mitel continues to gain traction, as endpoint compatibility remains on track and we continue to onboard their channel partners. Avaya also continues to consistently add seats to our growing base with another sequential growth quarter. We continue to believe that there is a meaningful opportunity for ACO as a destination for Avaya's customers, which represent the world's largest installed on-premise base. Partners remain part of our differentiated go-to-market strategy, and are contributing to our million dollar plus wins in the enterprise market.

Lastly, international continues to be an area of opportunity. In addition to recently launching with Vodafone in Germany, we closed multiple million-dollar TCV wins outside of North America, and launched services in new geographies. We continue to build up our efforts globally as we are still early in our opportunity.

To summarize, we had a strong quarter. We win because of our unmatched, best in class product, go to market motion - and our ability to address customer needs and pain points with clear value and ROI. Now, I'll pass it over to Sonalee to discuss financials and our guidance.



Sonalee Parekh, RingCentral, Inc. –Chief Financial Officer

Thanks Mo.

It's a pleasure to be here on my first earnings call as RingCentral's CFO. I've met some of you since I joined in May, and look forward to spending time with more of you in the coming weeks and months.

I chose to join RingCentral because I saw a compelling opportunity to join a category leader in a high growth space - operating at scale. Importantly, RingCentral is one of the few high growth SaaS companies with a \$2B revenue run rate, expanding operating margins - and - free cash flow. My first few weeks have reinforced my belief that RingCentral is still in the early innings of a tremendous market opportunity, and I look forward to sharing our progress with you in future quarters.

As RingCentral's CFO, my top priority will be driving efficient growth. This includes expanding operating margin and free cash flow while investing in and driving our future growth. I will be firmly focused on creating value for our key stakeholders, which include our customers, our employees and our shareholders.

With that, let me turn to our Q2 highlights. Q2 was a strong quarter. All key metrics came in above the high end of our guidance, and we delivered a record operating profit margin.

- Subscription revenue rose 32% year over year to \$463 million, above the high end of our guidance range of 28-29%. Adjusted for constant currency, which represented a roughly 1.5 point impact, subscription revenue rose over 33%.
- As we highlighted last quarter, balancing growth and profitability is one of our core tenets. I am particularly pleased with the improvement in our non-GAAP operating margin of 11.3%, which was meaningfully above our previous outlook of 10.4%. This was up 110 basis points year over year and continued the expansion we delivered last quarter.
- Additionally, we ended the quarter with \$306 million of cash on hand and generated non-GAAP free cash flow of \$29 million. This represented a free cash flow margin of 6.0%, up 220 basis points versus last year.

Now let me share with you some commentary around the key drivers of our results.



Firstly, growth. During the quarter, we benefited from strong upsell into our base, as customers continue to move to higher value and higher price point SKUs, as well as expand their seats with us.

Additionally, contact center continues to be a strong growth driver for us and is outpacing our overall growth. Many CIOs want to buy a Unified Communications and Contact Center as an integrated global solution from a single provider, and we are well positioned to benefit given our leading product and integrations.

Importantly, overall ARPUs remained stable quarter over quarter and year over year and are north of \$30. Also, new customer acquisition ARPU remained steady and over \$30. Customers buy RingCentral because they see the value in our global, integrated message, video and phone and contact center platform, with advanced features including analytics and AI, and our consistent 99.999% reliability. We save customers money and improve their productivity.

Regarding new bookings, we saw a \$15 million impact from the stronger dollar. Adjusted for currency our implied new bookings would have been over \$100 million and consistent with last year's sequential trend.

Now let me turn to profitability. Our solid operating margin starts with our industry leading subscription gross margin of 82.7%. Additionally, margin improvement during the quarter was driven by realizing efficiencies such as more disciplined hiring and vendor consolidation while prioritizing investments in our core innovation and growth vectors. We will continue to take a balanced view of investments, ensuring they meet our return criteria. Additionally, we will be looking at all aspects of the business to evaluate further opportunities to drive efficiency and continued growth.

Now turning to guidance. I will provide you with an outlook that is reflective of what we see in the market today. Regarding the current macro backdrop, as Mo stated, we saw three key trends in the quarter. These were:

1. Sales cycles reverting to pre-Covid norms.
2. Sales leads increasing quarter over quarter and year over year, and
3. More cautious buying behavior from larger customers, manifesting itself in smaller initial deployments.



We recognize that companies are navigating through a more challenging backdrop than what we saw even three months ago, as well as the impact of a stronger dollar. Taking this into account:

For the third quarter, we expect:

- Subscription revenue growth of 23% to 24%. Adjusted for constant currency, we expect subscription revenue growth of 25% to 26%.
- Total revenue growth of 21% to 22%. Adjusted for constant currency, we expect total revenue growth of 23% to 24%.
- Non-GAAP operating margin of 12.5%, and
- Non-GAAP EPS of \$0.50 to \$0.51 per share

For the full year 2022, we are reiterating our top line guidance.

- We continue to expect subscription revenue growth of 27% to 28%. Adjusted for constant currency, we expect subscription revenue growth of 29% to 30%.
- We continue to expect total revenue growth of 25% to 26%. Adjusted for constant currency, we expect total revenue growth of 26% to 28%.
- On profitability, we are raising our full year non-GAAP operating margin outlook to 12.0%, up from prior outlook of 11.5%. This reflects 180 basis points of year-over-year improvement at the midpoint.
- And, we are increasing our non-GAAP EPS outlook range to \$1.91 to \$1.95 per share, up from our prior range of \$1.83 to \$1.87 per share.

We have guided to 180 basis points of margin expansion this year despite the strong dollar. Looking forward, we are committed to ongoing margin expansion and are reiterating our target of achieving at least a 20% operating margin with continued growth in our free cash flow.

To summarize, we had a strong quarter marked by solid execution. We are well placed to navigate the current environment and we will continue to invest in a disciplined manner where we see the highest return and potential for growth.



Finally, I'd like to thank RingCentral's team and our Board for their warm welcome and support during my first few weeks here, as well as for their ongoing hard work and dedication to our shared vision. I believe we have a large opportunity in front of us and the right team to deliver sustainable, profitable, growth and to create value for our stakeholders.

With that, let's open the call for questions.