

UNITY Q3 EARNINGS SCRIPT

Richard Davis - Safe Harbor statement

Welcome to Unity's third quarter 2022 Earnings call.

After the closing of the market today, we issued our earnings press release and earnings presentation. These materials are now available on our investor website at investors.unity.com.

Today, I am joined by John Riccitiello, our CEO, President and Chairman and by Luis Visoso, our CFO.

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. You can find more information about these risks and uncertainties in the Risk Factors section of our filings at sec.gov. Actual results may differ, and we take no obligation to revise or update any forward looking statements.

As in prior quarters, we are providing both GAAP and non-GAAP financial measures. Unless noted otherwise, we will be speaking to the non-GAAP financial measures when describing our results. The earnings presentations and the press release are available on the Unity Investor relations tab as well as sec.gov and includes full GAAP to non-GAAP reconciliations.

And in the fourth quarter, we plan to present at investor conferences with BTIG, Credit Suisse, and Barclays. Full details are also available on our website.

With that, I will turn the call over to John.

John Riccitiello

Thank you Richard.

I want to start the call welcoming everyone at ironSource to Unity. The merger closed on Monday, as expected. We will report consolidated results starting in the fourth quarter of 2022.

Together, Unity and ironSource will write the next chapter of Unity's journey as we capture the large real-time 3D opportunity in front of us. In fact, we feel more positive about the merger now than we did when we announced the deal on July 13. Today, only a fraction of creators succeed in the creator economy. We are passionate about changing this reality because we believe that the world is a better place with more creators in it. By joining forces, we believe Unity and ironSource will transform the

industry and increase creators' success by replacing luck with science. We expect to achieve this through an end-to-end platform that enables creators to build better games and better user acquisition and everything in between by solving our customers toughest problems. And as a result, we expect to be a highly profitable company operating with positive cash flow.

Moving on to the financial performance of the third quarter.

Unity delivered a good quarter with revenue and non-GAAP operating income in line with guidance. Create posted a strong quarter and our internal performance challenges in Operate are behind us.

Total revenue for the third quarter was \$323 million, up 13% year-over-year. Create delivered \$129 million in revenue this quarter, an increase of 54% year-over-year. Operate delivered \$172 million, down 7% year-on-year and up 8% as compared to the previous quarter. Strategic Partnership revenue of \$23 million this quarter is up 28% year-over-year. Non-GAAP loss from operations of \$37 million came in at the better end of the guidance range as we continue to make progress with our cost structure on our way towards break-even by the end of the year.

Let's dive into **Create**.

Q3 was another strong quarter for Create Solutions. We continue to have strong customer pull in our core Unity engine and in our newer segments of digital twins and artistry. We are enabling our customers to create extraordinary real-time 3D experiences in games and across industries which we believe will accelerate our growth.

Innovation is the foundation of everything we do at Unity. A great example of this is our Data Oriented Tech Stack or DOTS. DOTS allows creators to get more performance and more scene density on any device they target by optimizing real-time 3D experiences in ways that take better advantage of modern chip architectures. This quarter we released our Entities 1.0 Experimental release. This release includes critical functionality to allow creators achieve native code performance with the ease of C# development, support massive data streaming through all Unity rendering pipelines with significant improvements in rendering performance with our updated occlusion culling system. It is encouraging to see compelling examples of creators using these tools to deliver spectacular games of all types – from open world MMOs, to strategy, to racing. Some recent games that use DOTS include V Rising by Stunlock Studios, Zenith: The Last City by Ramen VR, IXION by Kasedo Games, and Detonation Racing by Electric Square.

Another good example of the end-to-end focus on enabling creators to build, launch, and scale terrific games is our work with Marvel:Snap, developed by SecondDinner. SecondDinner developed their game using Unity and are also a Unity Game Services customer. We love the success they are seeing with their new launch – currently #1 on the IOS and Android app store in their category. As Aaron Brunstetter, Senior Director of Software Engineering at SecondDinner said: "Unity is a very close relationship for us. It feels like we're one team, with a shared purpose, taking on challenges together. That's thanks to everyone here who has joined us on this journey which, in all reality, is only just getting started." We couldn't agree more.

Outside of games, we are seeing similar results. This quarter has continued our strong momentum in digital twins. A few examples: Tilbury Douglas just launched their Connect Configurator. This enables them to bring forward insights and better decision making with their clients earlier in the construction process - eliminating delays, materials waste, and re-work. The Orlando Economic Partnership is working on the initial phase of the world's first immersive 3D regional digital twin. This project combines 80 different existing data sources over an 800 sq mile region to provide an immersive 3D experience and provides companies looking to expand their businesses to the Orlando Region with a much more effective and engaging way to understand the region, infrastructure and demographics.

I also want to talk about our progress with Parsec and SyncSketch, which together make up our Create Anywhere business. We continue to see very strong demand as companies around the world reconfigure and make permanent investments to support creators collaborating and creating in hybrid work scenarios. The combined ARR of the businesses in Create Anywhere grew north of 100% year-over-year through product innovations that continue to help scale our product-led growth and accelerated our enterprise sales. In fact, in the third quarter, we closed our largest Parsec enterprise deal-to-date, which was over \$1 million ARR. In Create Anywhere, we now have 25 customers contributing over \$100,000 of annual recurring revenue. SyncSketch has become the go-to collaboration tool for creators in the media and entertainment industry.

Recently, *Raised by Wolves*, an HBO Max show from Executive Producer Ridley Scott, which has a very high bar for visual quality in their futuristic sci-fi world, relied on SyncSketch to collaborate on nearly 3,000 complex visual-effects shots with a geographically distributed team. The *Raised by Wolves* team was able to work with executives, vendors, and the production team for review sessions throughout pre and post production. Putting all of this collaboration online made it easy to meet deadlines and deliver a world-class production.

Last quarter, we announced and launched a significant pricing and packaging change with our Unity Pro, Unity Enterprise and Unity Industrial Collection offerings. We raised the price between 13% and 25% across these offerings – the first significant price change in three years. More importantly, we aligned these offerings to better fit the needs of sub-segments of creators.

This means adding functionality – like MARS, our XR authoring environment and Havok, a high performance physics engine often used in the creation of advanced games, as well as optimizing support and customer success for Unity Pro, Unity Industrial Collection and Unity Enterprise offerings. Unity Enterprise customers will also receive read only source code to enable more rapid debugging and optimization, and an extra year of Long Term Support (LTS) for enhanced stability, both highly demanded by these customers. These are foundational changes that we will continue to build from to improve our take rate significantly by adding value our customers are happy to pay for.

We also continue our shift towards the cloud, enabling ratable revenue. This quarter, we released a private alpha of our cloud-based digital twin solution. This platform is designed to enable the end-to-end creation and use of real time, interactive, and 3D digital twins with capabilities across any industry all powered by cloud services. The platform is in private preview internally and with select customers in information technology, energy, and construction. We will have more details on this platform as we move beyond our alpha stage.

Across Artistry, Digital Twins, and Games – we are encouraged in the momentum we see, the customer demand, and the large market opportunity across short, medium and long term with Create.

Moving on to **Operate**.

Again, I want to welcome team ironSource to Unity. From here, we are merging ironSource and Operate, and the combined teams will come together under Tomer's leadership. We will refer to this larger combined business as Grow Solutions. Ingrid and her team will form a key part of the new team, as will the founders and teams at ironSource.

With that I will now speak to Unity Operate in Q3.

Operate delivered sequential progress in the third quarter with 8% quarter-on-quarter growth. This quarter, we increased competitiveness in our core product and as a result, we are growing our share of wallet with several of our largest advertisers. With increased trust comes increased spend on our platform. We continue to improve our models and have a healthy pipeline of ongoing initiatives. We also saw an increase in new publishers partnering to integrate advertising placements with Unity.

Looking at 2022 as a whole, there is no doubt that the ads side of Unity Operate has experienced a challenging year. Between 2019 and 2021, the team navigated essentially flawlessly through complexities that would have tripped up many others and grew revenues at a 55% CAGR. We undoubtedly benefited from COVID stay at home mandates. But in 2022, we experienced the operational challenges we have well described on prior calls. These problems have been addressed and are now in our rear view mirror. Our teams have rallied and executed well to begin the process of regaining market share and position.

Moving onto Unity Gaming Services or UGS. We are pleased with the uptake for UGS since going general availability this summer. UGS unifies, in a single suite, more than a dozen analytics tools, cloud orchestration, and embedded voice and multiplayer functionality. UGS is an example of how we address acute needs, reduce complexity for our customers. We priced these services on a consumption basis so studios only pay for what they use and we scale as they succeed.

UGS also unlocks added synergy in our model. Create, Operate and UGS, working together, solve more of our customers' key challenges. A great example is how developers at SecondDinner used our editor to build Marvel:Snap. Our editor seamlessly connects to our UGS services, which made it a simple decision for SecondDinner to self-provision our Cloud Content Delivery and Cloud Build modules that are part of UGS. The result was a blockbuster game as brilliant design combined with exceptional user experience delivered by UGS. That is our mission for every creator.

In September we introduced Multiplay and Matchmaker self-serve. The mobile game market is evolving will evolve to player versus player, much in the way that the market for console and PC games has. Multiplayer games have proven to realize much greater player engagement. Players enjoy them more. And, with more engagement comes more opportunity for revenue. But until now, building multiplayer functionality for mobile games was too complex. With the launch of these two self-serve products, we solved this difficult networking challenge, and made the technology easy to provision and manage at scale for developers and studios of all sizes.

With that, I'll step back and look at the games ad market overall. The current softness in the ad market weighs on my mind. I want to address this with you to put future performance and plans into context. One key question – what has happened in the games ads market overall in recent years in light of Apple's changes in privacy programs which began in Q2 2021? While we did see some change in spend between iOS and Android, the overall ad market had an incredible year in 2021, partly fueled by higher player engagement due to players being at home during COVID. Looking at 2022, Q1 2022 was strong for the in-games ad sector with year-on-year growth in the teens. We estimate overall in-game ads growth was up approximately 10% year-on-year in Q2 and slowed to low single digits in Q3. We currently expect that the sector will be flat year-on-year in Q4.

In terms of player engagement, as the first half of 2022 unfolded, we began to see some softness in overall player engagement versus the elevated COVID levels of 2020 and 2021. It is important to note that engagement was up cumulatively a full “three-years worth” versus pre-COVID. And, when we look at daily active users, or DAU, we're actually seeing an increase in Q3 this year versus Q3 of last year. Despite macro market conditions, users continue downloading and playing games, proving the sticking power of this entertainment segment. This speaks to the long term resilience of the games business.

What was new starting in late Q3, is that CPMs have declined, on both mobile operating systems. The timing here is clear: the declines take place as the world's banks increased interest rates and the specter of recession was everywhere in the press. Not earlier when privacy changes took place. When we talk with our advertisers, the sense we get is clearly one of caution, and reticence to commit to the aggressive campaign spends that would crowd out competition and at the bid, elevate CPMs.

The market for ads is experiencing recession sentiment. As you will hear from Luis, we have factored this sentiment into a lowered Q4 guide. And, while we don't know when it will end, strong consumer engagement will ultimately bring back growth to this dynamic ads market.

With ironSource, we become the leading end-to-end platform in the market, supporting the developer throughout the entire development lifecycle, from opening a project in the Unity Editor all the way through to making it a successful business and supported by our data science. As such, we are positioned to lead the market and be the main beneficiaries of a market recovery. While market conditions are challenging, we have a unique opportunity to gain market share and invest in positioning ourselves to grow rapidly once macro conditions improve. Our end-to-end platform will be a critical enabler in helping creators thrive *even* in a challenging market. By enabling more game creators to build successful businesses, ultimately we'll be growing the market overall.

LevelPlay becomes Unity's mediation offering, delivering unparalleled reach to creators to help tap into a combined global network of players with more than 3 billion monthly active users. Unity LevelPlay will have plug-in integration into the Unity Editor and deliver superior performance for the Unity Ads and ironSource Ads networks, while Supersonic will add critical publishing capabilities to our offering, helping even more developers successfully launch and scale their games. We believe the new Unity Grow platform can and will materially out perform the industry, gaining share due to our ability to drive success for our customers.

Before turning the call over to Luis, I want to reinforce a few points that we have made before.

First, Unity is well positioned to capture what we believe is a very large opportunity as the world moves from linear 2D to real-time 3D. We have a strong position in games and are making strong progress across industries.

Second, we believe that Unity with ironSource provides a unique end-to-end platform that solves more of our customer's toughest challenges, enabling us to accelerate our revenue growth and making Unity cash flow positive and adding new capabilities and amazing leaders. We believe the new Unity Growth platform can and will materially out perform the industry, gaining share due to our ability to drive success for our customers.

Third, advertising is an integral part of the games business model. Gamers are highly engaged and only a small minority pay directly for the games they play. Advertising and in-app-purchases are the ways creators monetize their games. And most players welcome ads as a way to discover new games to play. And while we are in an advertiser sentiment recession, we believe that the ads market will remain resilient even with last year's changes to privacy.

We expect Unity to sustainably grow at a 30% growth rate. As we have said in the past, this will not be the case every single year but is the compounded growth rate that we expect to deliver. We will guide 2023 on our year-end earnings call when we have a better view on the economy and, in particular the in-games ad spend trends. At that point we will have a much better handle on advertiser sentiment. We will have clear plans for Create to continue to deliver strong growth and for Growth to outpace any ad market we experience. Given what we know today, we expect to guide lower than the 30% sustainable growth target.

Finally, a word about profitability and cash flow. Luis will dive into this in more detail, but in the fourth quarter we will be positive. This has always been important to us, and it's even more important in challenging times. This strong financial position is further testament to our ability to capitalize on the opportunity ahead of us. With that, let me turn the call over to Luis.

With that, let me turn the call over to Luis.

Luis Visoso

Thank you, John.

The third quarter came in line with guidance for revenue and non-GAAP operating income. Create continues to perform strongly and our internal performance Operate challenges from the beginning of the year are behind us.

In the third quarter of 2022, we delivered revenue of \$323 million, up 13% year-over-year and in the middle of our guidance range. Create continued to execute well with revenue of \$129 million, up 54% from a year ago. Despite the challenging economic environment, Operate delivered \$172 million in revenue, up 8% quarter-on-quarter and 7% below year ago. Strategic partnerships and Other delivered \$23 million in revenue, up 28% from a year earlier.

At the end of the third quarter, we had 1,075 customers with trailing 12 months revenue above \$100,000. This compares to 973 customers at the end of the third quarter of 2021. This lower rate of growth in our customer count above \$100,000 is driven by Operate.

Our 12-month trailing net dollar expansion rate came in at 111%, down from 142% last year. The drop in our net dollar expansion rate is driven by Operate.

Our third quarter non-GAAP gross margin was 74%, down from 81% a year ago. The year-over-year gross margin decline is mainly due to lower mix from monetization, which has a higher gross margin than the average as well as the impact of Weta as engineers supporting the business are charged to cost of goods sold.

Non-GAAP operating expenses increased 16% versus last year's third quarter, and 4% sequentially as our cost containment efforts continued to take hold. We expect to significantly over-deliver against our \$100 million cost savings plan discussed at the end of the second quarter. We closed the quarter with 6,244 employees, as compared to 6,246 employees at the end of the second quarter.

Non-GAAP operating income for the third quarter was negative \$37 million or negative 12% of revenue. This compares to guidance of negative \$35 million to negative \$50 million. Cash flow from operations was negative \$70 million, which includes an \$18 million payment to a publisher that had not collected their pay-out for several years and a \$10 million M&A cash payment that is excluded from non-GAAP operating income. Unity had 301 million basic shares outstanding and 403 million fully diluted shares at the end of the third quarter. The difference in fully diluted shares compared to our Q2 guidance of 375 million is entirely due to the lower share price which impacts the conversion of the convertible notes.

Moving on to fourth quarter guidance. Our guide includes ironSource financial results as of Monday this week and our best estimate of the impact of the economic environment. Unity and ironSource are operating as one company as of Monday.

For the fourth quarter, we expect revenue between \$425 million to \$445 million, an increase of 35% to 41% year-on-year. We expect full year revenue between \$1,365 million and \$1,385 million, an increase of 23% to 25% year-on-year. Let me break down the details. First, this is down approximately \$60 million from the time adjusted prior guide for the combined companies. Second, within this, we expect Create to continue to perform strongly. With regard to ads, we have taken a conservative view this quarter given that we have not yet seen the seasonal rise in CPMs that typically happens during the holidays. We have reasons to be optimistic given our recent gains in mediation and the expectation that this can result in share gains.

For the fourth quarter, we are guiding non-GAAP operating income between \$5 million and \$15 million. Implied full year non-GAAP operating income is between negative \$88 million and \$98 million. For perspective, we expect Unity to break-even and be cash flow positive at the end of this year. We will build from that base in 2023.

With the Ironsource merger, we issued approximately 113 million shares. In addition, we issued \$1 billion of convertible notes with a 2.0% interest rate and a \$48.89 conversion price. We expect to have 416

million basic shares and 562 million fully diluted shares at the end of Q4, which includes 46 million shares to convert the convertible note and 29 million shares to convert the PIPE investment.

We will provide full year guidance for 2023 with Q4 Earnings. Our guidance will factor in the very large opportunity in front of us, the synergies from the ironSource merger and the near term impact of the potential economic recession. We remain committed to our \$1B EBITDA run-rate goal by the end of 2024 and to deliver significant EBITDA and free cash flow progress in 2023.

Near term, we are cautious given the potential for recession. While we expect to expand market share in 2023, as long as the ads market sentiment remains one of recession, we expect to guide revenue growth lower than our sustainable growth target.

To close, we believe that the real-time 3D opportunity is very large and we are well positioned to capture it given our strong capabilities in Create and Operate.

In Create, we enjoy a leading and growing market share position in games. We have best-in-class artist tools with Weta, Ziva and SpeedTree, and strong customer pull with over 750 leads generated at SIGGRAPH. We are making strong progress to scale our digital twin business with the launch of platforms that automate services such as Presence, Annotations, 3D Data, Identity, Data Workflows and Live Streams Data. And we are evolving our business models to be cloud-based and ratable. We are very optimistic on the Create business.

Within Grow, Ads remains a critical part of the games industry. The ironSource merger strengthens our position with the best mediation platform out there; Unity LevelPlay, the leading game publisher; Supersonic, three Ad Networks with Unity Ads, ironSource and Tapjoy, and the leading device management partner with Aura. We are optimistic about this business, and our ability to build market share, yet tempered by market expectations.

With that, let me turn the call over to Richard who will coordinate the Q&A.