

SNAP INC. Q4 AND FULL YEAR 2019 TRANSCRIPT

OPERATOR

Good afternoon, everyone, and welcome to Snap Inc.'s Fourth Quarter and Full Year 2019 Earnings Conference Call. At this time, all participants will be in a listen-only mode. After the prepared remarks, there will be a question and answer period. If you would like to ask a question during that time, please press star, then the number one on your telephone keypad. This call will be recorded.

Thank you very much. Mr. David Ometer of Investor Relations, you may begin your presentation.

DAVID OMETER, INVESTOR RELATIONS

Thank you, and good afternoon, everyone. Welcome to Snap's Fourth Quarter and Full Year 2019 Earnings Conference Call. With us today are Evan Spiegel, Chief Executive Officer and Co-Founder, Jeremi Gorman, Chief Business Officer, and Derek Andersen, Chief Financial Officer.

Earlier today we made a slide presentation available that provides an overview of our user and financial metrics for the fourth quarter and full year 2019, which can be found on our Investor Relations website at investor.snap.com. Now I will cover the Safe Harbor. Today's call is to provide you with information regarding our fourth quarter and full year 2019 performance in addition to our financial outlook. This conference call includes forward-looking statements. Any statement that refers to expectations, projections, guidance, or other characterizations of future events, including financial projections or future market conditions, is a forward-looking statement based on assumptions today.

Actual results may differ materially from those expressed in these forward-looking statements, and we make no obligation to update our disclosures. For more information about factors that may cause actual results to differ materially from forward-looking statements, please refer to the press release we issued today, as well as risks described in our quarterly report on Form 10-Q for the quarter ended September 30, 2019, particularly in the section titled Risk Factors. This information can be found in our other filings with the SEC, when available. Our commentary today will also include non-GAAP financial measures and we believe that the use of these non-GAAP financial measures provides an additional tool for investors to use in evaluating ongoing operating results and trends. These measures should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with GAAP.

Reconciliations between GAAP and non-GAAP metrics for our reported results can be found in our press release issued today, a copy of which can be found on our Investor Relations website. Please note that when we discuss all of our expense figures they will exclude stock-based compensation and related

payroll taxes as well as depreciation and amortization and non-recurring charges. At times in our prepared remarks, or in response to questions, we may offer additional metrics to provide greater insight into our business or our quarterly and annual results. This additional detail may be one-time in nature, and we may or may not provide an update in the future on these metrics. Please refer to our filings with the SEC to understand how we calculate our metrics.

With that, I'd like to turn the call over to Evan.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Hello everyone, and thank you for joining our call.

2019 was a transformative year for Snap. We saw momentum across the board as we grew our community, accelerated our revenue growth, and made progress towards profitability and free cash flow. We continued the momentum we developed early in the year through the fourth quarter, and we are excited about growing our business into 2020 and beyond.

Our community grew to 218 million daily active users in Q4, we accelerated year-over-year revenue growth to 44 percent compared to 36 percent in Q4 of 2018, and we generated \$42 million of Adjusted EBITDA. Throughout the course of 2019, we added 31 million daily active users, largely driven by investments in our core product and improvements to our Android application. Our full-year Adjusted EBITDA improved by 65 percent year-over-year, and we are working towards full-year Adjusted EBITDA profitability in 2020. The strength and momentum in our underlying business fundamentals gives us confidence in our long-term growth and profitability as we invest in growing our business for the future.

We've recently completed our 2020 strategic planning process and have aligned our teams and resources around our goals of supporting real friendships on Snapchat, expanding our service to a broader global community, investing in our AR and content platforms, and scaling revenue while achieving profitability in order to self-fund our investments in the future.

We have always believed that supporting real friendships and creating products to serve our community are core to building a long-term, sustainable business. On any given day, most people have something to share with their family and close friends, and using Snapchat allows them to communicate together in a way that is efficient and expressive. This means that our camera has become an important tool for maintaining relationships through visual communication and storytelling, creating a distinct competitive advantage for our company. Supporting daily self-expression, while harnessing the richness of visual communication, gives us a broad and unique long-term opportunity that will serve us well into the future.

Beyond empowering new ways of communicating visually, Snapchat allows our community to nurture close friendships, which plays a vital role in health and happiness. The growth of our Snapchat community underscores people's desire to communicate with one another through technology that feels natural and similar to face-to-face friendships. We want to build technology for humans that is supportive of the ways we have interacted for centuries, long before the creation of the smartphone.

Our fourth quarter engagement demonstrates the power of friendship and self-expression. As our community came together to celebrate the holidays on Snapchat, we saw more than 200 million Snapchatters creating Snaps on Christmas Eve and Christmas, sending an average of nearly 30 Snaps each. We are particularly excited to note that the number of people creating a Snap with our camera every day is growing faster year-over-year than our overall DAU growth, meaning that existing and new members of our community continue to use our camera frequently to express themselves. We are encouraged by the way Snapchatters worldwide have adopted visual communication, and we are excited to empower even more creativity by making it faster and easier to express yourself on Snapchat.

As we work to grow our community around the world, we believe that the best way to build a global business is to invest in products and partnerships that are locally relevant and reflect local culture, while reducing the barriers to using Snapchat. Visual communication is a high-bandwidth activity that can be burdensome in markets with limited and expensive cellular internet. We have now partnered with over 70 international carriers to help our community manage these costs, and our ongoing investments in the efficiency of our service helped cut Snapchat's median cellular data usage in half in the past six months. We are also working with local partners to provide content and AR experiences that are tailored to the diverse cultures of our community, and now offer hundreds of locally relevant international Discover channels, the majority of which were launched in 2019. Going forward, we will continue to invest in our team, technology, and partnerships to fully realize our vast opportunities for growth around the world.

Our content and augmented reality platforms have continued to grow and provide value to our community and partners. Discover, our curated content platform, has grown year-over-year in both reach and time spent, especially as content viewership continues to transition from linear television to mobile. We have dramatically expanded our product and content offerings through partnerships, including our Snap Original Shows. While our investments up to this point have been selective and measured, these Original Shows are already being watched by more than half of the US Gen Z population. This makes our Original Shows, ranging from early hits like the Dead Girls Detective Agency, now in its fourth season, to new franchises like our recently-launched "Vs the World" docuseries, some of the largest premium ad-supported titles for this audience. As we continue to increase our investments in Originals and other premium content offerings, we are excited to see Discover evolve into a top destination for mobile content consumption, with the number of people that

watch more than 15 minutes of premium Discover content every day growing by nearly 50 percent year-over-year.

We have also worked hard to provide value to our community through our camera with augmented reality. This year, we are focusing our efforts on expanding both the variety of Lens experiences available to our community and the value that augmented reality is able to deliver beyond entertainment and self-expression. For example, our growing Lens Studio platform is dramatically increasing the number of AR experiences available to our community, which in turn is driving more engagement on Snapchat. On New Year's Eve alone, more than 200 million Snapchatters engaged with augmented reality over 13 billion times, up over 50 percent from the prior year. Lens Studio contributed meaningfully to this increase, with more than 20 percent of the Lenses sent on New Year's Eve built and submitted by our community, compared to just 5 percent the year before. We've also made it easier to find and experiment with different AR experiences on Snapchat using Lens Explorer. In Q4 2019, five times as many people went to Lens Explorer to search and browse AR experiences every day when compared to Q4 2018, with more than 10 percent of our community using Lens Explorer every day on average. We are also excited to be working with partners to expand the value of our camera. Shazam has helped Snapchatters identify over one billion songs using our camera, and we are adding new partners like Photomath to help people learn how to solve math problems without using a calculator.

As we continue to scale our content and AR platforms, we are also making significant progress against many other long-term opportunities, including Snap Kit, Maps, and Games. While these newer offerings are at a much earlier stage than our content and AR platforms, we are excited by the engagement we are seeing from our community. Today, these platforms enable people to share a new song they discovered on Spotify, see what their friends are up to around the world, hang out and chat with a group of friends while playing games, and personalize their Fitbit workout routine and watch face with their Bitmoji. We can't wait to continue expanding these offerings across a wider variety of experiences for our community, some of which we will be announcing at our Snap Partner Summit in April.

Given the substantial long-term opportunities ahead, we are working hard to scale our revenue so that we are able to self-fund our investments in the future. We believe that our platform is still extremely under-monetized given our massive reach among a differentiated and growing community, the high levels of engagement on our service, and our proven advertising products that drive measurable ROI for our partners. This means that we have a large volume of high-quality advertising inventory and the potential to meaningfully increase our average revenue per user over time, even in advance of monetizing our longer-term investments like gaming, and maps. In 2020, we will continue to evolve our advertising products and go-to-market strategy for both performance and brand-oriented budgets.

We have started investing heavily in our ranking and optimization efforts this year to increase the scale and return on ad spend that we are able to deliver to performance advertisers. As these early investments are starting to bear fruit, we are getting better at increasing the value and relevance of each ad impression. Not only does this increase the return that our advertisers receive from their investment in our platform, but it can simultaneously reduce the number of impressions we show for a particular campaign. This frees up inventory for additional campaigns while improving the user experience by reducing the number of ads shown that are not relevant to a particular individual. As with any new technology platform, we expect ongoing improvements to be steady but incremental, and we plan to significantly increase our investment in product and engineering talent to build upon the gains we have made in this area.

Given our massive reach among young people, we also believe we have a strong value proposition for household brands that want to reach our audience at scale, but find it increasingly difficult to efficiently access our audience on linear television or other online platforms. We have seen early success with many brands, and believe there is a significant opportunity to scale their success across more advertisers, especially as television and desktop budgets represent three times the total mobile ad spend in the US, but advertisers are increasingly unable to reach our unique demographic on those platforms. Building trusted, long-term relationships and further developing our advertising solutions for specific verticals takes time, and we are investing in a multi-year strategy to address this massive opportunity.

We are focused on growing our revenue and achieving profitability so that we are able to accelerate both our near-term investments in our products and business as well as the realization of our long-term vision for the camera. We continue to see tremendous opportunity in defining what it means to be a modern camera company because the camera has seemingly infinite untapped potential. Historically it was difficult and expensive to create a photograph, and people used cameras infrequently to document and save treasured memories. The past decade brought smartphones with an internet-connected camera in everyone's pocket, empowering people to use cameras for daily communication, with over 1.3 trillion Snaps created on Snapchat in 2019. This decade promises to bring yet another revolution in terms of camera usage with augmented reality, as people begin to experience the world around them through Lenses that inspire creativity, provide real utility, and understand context in ways that have never before been possible.

I'll now turn the call over to Jeremi to discuss the progress we have made in growing our advertising business.

JEREMI GORMAN, CHIEF BUSINESS OFFICER

Thanks Evan.

We are so excited with the progress we made in 2019 and see significant opportunities for our business moving into 2020. Our teams are well aligned, enabling our business to grow revenue alongside our community through performance improvements on Android and iOS, world-class augmented reality experiences, and engaging made for mobile content.

Over 2019, we generated full year revenue of \$1.7 billion dollars, an increase of 45 percent year-over-year, compared to 43 percent in 2018. In Q4 2019, we generated revenue of \$561 million, an increase of 44 percent year-over-year, compared to 36 percent in Q4 2018. These results are a byproduct of the hard work being done across all teams at Snap, and validate decisions we've made around the structure of our sales teams and the products we have built for our advertisers and our community. As a result, we believe that we have the opportunity to continue growing annual revenue at a pace significantly faster than our peers.

We are fully focused on making progress against our ARPU opportunity, which we believe in the short to medium term will be largely driven by advertiser demand. We have significant headroom in our business given our high levels of engagement and ample supply of available impressions globally. As a result, we are focused on driving demand from advertisers to improve CPMs in our self-serve auction. Looking at our current ad products and applying comparative industry CPMs to our own inventory, we are in a position to meaningfully close the ARPU gap relative to our peers. In addition, not only does demand growth increase contestation in our auction, driving up CPMs, but it also increases the number of ads available to choose from for each impression, improving relevance per impression and ultimately yielding higher ROI for our advertising partners, even at increased prices.

To achieve our ARPU goals, we remain focused on our three key priorities: First, improving our measurement, ranking, and optimization to drive relevance and deliver ROI. Second, building out our sales and marketing functions to support the needs of our advertising partners globally. Third, creating innovative ad experiences around video and augmented reality that deliver real business value. Our three priorities—along with our growing, global audience—will allow us to drive performance at scale for businesses around the world.

Our business growth is enabled by our large, growing, unique, and unduplicated audience. For example, in the US, we reach more than 90 percent of 13 to 24 year-olds and more than 75 percent of 13 to 34 year-olds. In addition, our reach is expanding outside of the US as a result of ongoing product improvements that allow us to grow our business and community around the world. Our community engages with our service for over 30 minutes per day on average, and our advertisers have unparalleled

reach with the valuable 13-34 year old demographic that makes up the majority of Millennials and Gen Z.

Our first priority is investing heavily to improve our measurement, ranking, and optimization to drive relevance and deliver ROI. In 2019, our investments enabled performance advertisers to scale on our platform. For example, at the start of the quarter, our pixel purchase optimization goal comprised less than 5 percent of self-serve revenue. Over Black Friday and Cyber Monday, however, this optimization goal that allows advertisers to bid explicitly on a purchase activity on their website, grew to over 10 percent of self-serve revenue globally. We enter 2020 with multiple investments in Commerce from the past year ready to scale to new advertisers. Our self-serve tools, lower-funnel optimization goals, video ad formats, and advanced solutions—such as product catalogs and dynamic ads—work together to reward advertisers who invest in our platform with ROI at scale.

For example, Ralph Lauren started testing Dynamic Ads in October 2019, as product-based ad formats have been amongst the tactics that have worked for their business. After initial testing proved to be extremely successful, they increased investment by 3x in Q4 2019, during one of the most competitive times of the year for shoppers. This solution not only helped them drive relevance during the holiday period, but they've shared this will be a key performance driver throughout the course of the year.

Our second priority is to grow demand via better service for our advertising partners. As we continue to scale our advertising business across all geographies, we expect to build out teams in different verticals to support our rapidly growing ad business. This includes building a Global Partners team to work with our largest global advertisers to create seamless global planning, hiring more sales operations experts to continue to improve operational rigor in our sales teams and pipeline planning, and generally mature the ways our Sales organization operates as we scale over the coming years. We're encouraged by the early success with many of our verticals, most notably Tech, Restaurants, Entertainment, and CPG.

For example, PepsiCo's Mountain Dew looked to Snapchat to leverage our innovative ad products and drive sales for the Mountain Dew brand. Snapchat worked with Mountain Dew to run two campaigns for their DEWnited and VooDEW product lines. The DEWnited campaign leveraged Snap Ads and Filters to highlight the classic Mountain Dew logo, and helped drive incremental sales returns above PepsiCo norms primarily through a lift in household penetration. The VooDEW campaign leveraged Snap Ads and Lenses to target Halloween fans and candy buyers, which resulted in a significant lift in ad awareness and brand favorability for Mountain Dew's limited-time VooDEW product.

Our third priority is to continue to lead the way with innovative advertising products and services. As brands focus more on incremental reach and depth of engagement, rather than just clicks and impressions, more advertisers are employing innovative formats that drive real customer interactions. Snap is the ideal place for these brands, because our advertising products are built on the same foundation that makes our engaging consumer products successful. We continue to invest heavily in

innovative solutions that leverage our content and augmented reality platforms in order to drive better outcomes for advertisers and delight our Snapchat community.

Video is a top priority. For example, we started to scale Commercials—our six-second, non-skippable, full-screen video format—and Snap Select, which enables fixed CPM buying of Commercials in pre-packaged, premium inventory. Combining this engaging ad format and easy-to-buy model within premium content placements has seen early success with high quality brands.

Recently, we rolled out the capability for Snapchatters to engage more deeply with our Commercials product, and have already seen success stories. For Black Friday 2019, GOAT, the global platform for style, featured a week-long Black Friday raffle that included over 3,000 prizes, 35,000 sneakers and \$10,000 in GOAT credit. They ran a Commercials campaign that swiped up to the promotion landing page which lead users to download the app. Snap accounted for 95 percent of all traffic to that landing page, and GOAT saw a cost per install of just 20 cents from Snapchatters downloading their app to participate in the Black Friday raffle. Amanda Sun, Senior User Acquisition Manager, said, “We’ll continue to leverage Commercials annually with our Black Friday raffle, as well as with other similar campaigns to not only broaden awareness but to reach a highly engaged audience.”

Long-term brand building on mobile remains a challenge for marketers and no one is better positioned to deliver solutions than Snap. We have a huge opportunity with our camera-first functionality and our Sponsored AR Lens formats. We are at the beginning of building out our AR ecosystem for brands and providing additional value beyond paid media. For example, this quarter we announced that McDonald’s and Coca-Cola are the first brand partners to utilize our Scan camera search technology. Our Scan feature combines visual search and augmented reality by recognizing images through the Snap camera and providing AR lenses related to what the camera is focused on—in this case, the well-known logos of McDonald’s and Coca-Cola. These initiatives complement our existing marketing campaigns and link digital content to the physical world.

Any brand can now utilize our Scan technology for free via Lens Studio, our public AR creation tool, and submit it to the Snapchat community. Turning physical products that are a part of Snapchatters’ everyday lives into conversation starters through immersive AR is a unique way to connect with our audience and an important milestone for this technology. We believe we are poised to continue growing advertiser adoption of AR ad formats as augmented reality marketing becomes more widely adopted by businesses.

We are also seeing that when brands utilize a portfolio approach of combining Sponsored Augmented Reality Lenses with Snap Ads, they result in stronger ROI and lower costs per outcome. This is leading to brands deepening their investment with Snap over time.

For example, our partnership with MGM Resorts International started with brand-focused campaigns, including a Lens in Q4 2018 to launch their new Park MGM hotel in Las Vegas. This drove a 10pt lift in Ad Awareness and a 5pt lift in Consideration Intent. Given the upper funnel success they saw, they implemented the Snap Pixel and expanded into running direct response efforts to drive room bookings across their entire portfolio of properties using Snap Ads, Story Ads, and Collection Ads. These generated an 18x blended ROAS across all ad units. Most recently they came full circle by combining the best of their direct response learnings with Snapchat's augmented reality opportunity by applying AR for direct response to drive Park MGM and expanded portfolio bookings in Q3 2019. This activation drove ROAS in-line with direct response-focused Story Ads and Snap Ads units, proving augmented reality is an effective tactic for achieving cost-efficient room bookings.

We enter 2020 with a full-featured ad platform and a sales team structured to support our business. Looking forward, our strategy for growth is to continue to invest in new products and marketplace improvements to help advertisers scale, build focused relationships with brands and agencies across many of our verticals, and to improve our direct response products for performance-centric businesses. Based on the size of our audience, their levels of engagement across camera, content, and communication, and our overall opportunity in the growing digital advertising market, we are in a position to meaningfully close the ARPU gap relative to our peers.

Our team is incredibly excited about what the future holds for Snap and we look forward to growing and building deep relationships with our partners over the longer term.

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

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Thanks Jeremi. Our Q4 financial results reflect our priorities of making focused investments in the future of our business, and scaling our operations efficiently in order to drive towards profitability and positive free cash flow.

As Evan mentioned earlier, our community grew to 218 million daily active users in Q4 2019, which represents an increase of 31 million or 17 percent year-over-year. We are pleased to see that the year-over-year growth rate of our community accelerated from 13 percent in Q3 2019 to 17 percent in Q4 2019, and that the sequential growth in DAU exceeded our expectations entering the quarter. We continue to benefit from the cumulative impact of improvements we have made to our application, which are contributing to higher levels of engagement and the sustained retention of new Snapchatters.

The growth in our community continues to be broad based, with year-over-year and sequential growth on both iOS and Android platforms, as well as year-over-year and sequential growth across each of

North America, Europe, and Rest of World. As we are now lapping the period when DAU stabilized near the end of 2018, we are focusing once again on the year-over-year growth rates in DAU, which tend to better illustrate the underlying trends within the community compared to the sequential growth patterns that are often skewed by seasonality within regions. In North America, DAU grew by 7 million or 9 percent year-over-year, up from 5 million or 6 percent in the prior quarter. In Europe, DAU grew by 7 million or 12 percent year-over-year, up from 6 million or 9 percent in the prior quarter. In Rest of World, DAU grew by 17 million or 36 percent year-over-year, compared to 13 million or 28 percent in the prior quarter. We are pleased to see that a pattern of solid year-over-year growth has developed across all regions, and that the rates of year-over-year growth accelerated across all regions in the current quarter. We believe the accelerating growth of our community, in an increasingly competitive market for attention on mobile, clearly demonstrates the value of our differentiated platform.

We exceeded the top end of our guidance range in Q4 and generated total revenue of \$561 million, an increase of 44 percent year-over-year. As expected, our rate of revenue growth decelerated versus the prior quarter reflecting a tougher comparison period in Q4 relative to recent prior quarters, and the impact of a shorter peak holiday period in the current year. Recent prior quarter growth rates have been elevated by the impact of growing always on demand for our goal based advertising products, which has helped to fill in valleys of demand within our self-serve auction ecosystem. We are now lapping the launch of our goal based advertising capabilities in the prior year, which resulted in a tougher comparison period this quarter relative to recent prior quarters. In addition, while we experienced elevated holiday driven ad spending throughout the period between Black Friday and Christmas, this window of time was approximately one week shorter in the current year compared to the prior year, and this factor also contributed to the deceleration in year-over-year revenue growth rates in the current quarter.

In North America, revenue grew 42 percent year-over-year in Q4, compared to 52 percent in Q3, while ARPU grew 31 percent year-over-year, compared to 43 percent in Q3. This relatively lower rate of growth in North America in Q4 reflects the impact of the shorter holiday period being concentrated in this region as well as the tougher comparison period. In Europe, revenue grew 47 percent year-over-year in Q4, compared to 36 percent in Q3, while ARPU grew 31 percent year-over-year compared to 24 percent in Q3. We were pleased to see European growth accelerate following the completion of our sales team re-organization in the prior quarter. In Rest of World, revenue grew 49 percent year-over-year in Q4, compared to 55 percent in Q3, while ARPU grew 9 percent year-over-year, compared to 21 percent in Q3. The deceleration in Rest of World revenue growth reflects the steep ramp in the prior year when Rest of World revenue grew 47 percent sequentially following the launch of more sophisticated goal-based-bidding capabilities. Our goal based advertising products gained traction quickly in the Rest of World region a year ago and helped to drive the growth of our always-on advertising business worldwide throughout the course of 2019.

We continue to see broad-based improvement in advertiser demand and strong adoption of our ad products including Story Ads revenue that doubled year-over-year in Q4, and Commercials ad revenue that more than tripled year-over-year in Q4. We continue to view the Camera as a significant long-term monetization opportunity and were pleased to see year-over-year revenue growth from AR Lenses and Filters accelerate by 21 percentage points in Q4, driven by strong adoption of our self-serve Reach and Frequency AR products and strong demand from advertisers seeking to build their presence in the carousel at key moments.

Total impressions doubled year-over-year in Q4 while cost per impression continued to stabilize with a year-over-year decline in eCPM of 24 percent in Q4, an improvement over the 27 percent decline observed in the prior quarter. The ongoing growth in engagement, combined with optimizations to our self-serve platform to utilize our inventory more efficiently, are driving continued expansion of our available supply, which allowed us to grow revenue 26 percent sequentially with just a 7 percent rise in yields over the same period.

Gross margins were 56 percent in Q4 2019, up 8 percentage points year-over-year and 5 percentage points sequentially, as we continue to focus on scaling our operations efficiently. Infrastructure costs per DAU were \$0.72 in Q4, flat versus the prior year but up two cents sequentially reflecting seasonal trends in user activity. We continue to make significant progress against our goal of driving down our underlying unit costs over time, including the cost to deliver a Snap, the cost to deliver an impression, and other key drivers of infrastructure costs. In Q4, our efficiency improvements fully offset the year-over-year increase in user activity, resulting in flat cost per DAU year-over-year. On the content side we have been doubling down on our investments in premium content, and we are pleased to see these investments yield more than 50 Shows with monthly audiences of 10 million or greater in Q4, which contributes to our ability to grow Story Ads revenue and Commercial Ads revenue at the rapid rates noted earlier. The focus on scaling our infrastructure costs efficiently has allowed us to make these investments in premium content, while continuing to expand our gross margins, which reflects our overall approach of scaling our operations efficiently while making investments in the future of our business.

Operating expenses were \$271 million in Q4 2019, up 14 percent year-over-year and flat sequentially. We shared last quarter that we intended to invest in the future of our business by growing our talent base and we have begun to do so. Full time headcount grew 11 percent year-over-year in Q4, with the growth in headcount focused on monetization and engineering, and this was the primary driver of our year-over-year operating expense growth. While there is typically a lag between investing in talent and improved output metrics, we are pleased with the momentum we are seeing from the investments we have made over the past year and expect to continue to invest productively in the growth of our business going forward.

Q4 marked our first quarter of Adjusted EBITDA profitability at \$42 million for the quarter, an improvement of \$93 million over the prior year, and \$85 million over the prior quarter. Consistent with our prior guidance, this was the seventh consecutive quarter that we reported a year-over-year improvement in Adjusted EBITDA. In Q4, we delivered Adjusted EBITDA leverage of 54 percent, which as expected was down from 65 percent in the prior quarter as we continue to invest in the future of our business, while making progress towards profitability and positive free cash flow.

Net Income was negative \$241 million in Q4, a decline of \$49 million over the prior year, and \$13 million over the prior quarter. The decline in Net Income largely reflects a one-time legal settlement, which offset the improvement in Adjusted EBITDA in the quarter.

Free Cash Flow for Q4 was negative \$76 million, an improvement of \$73 million year-over-year, and \$8 million quarter-over-quarter, primarily driven by the improvements in Adjusted EBITDA that were partially offset by seasonal changes in net working capital between Q3 and Q4.

We ended the quarter with \$2.1 billion in cash and marketable securities, down from \$2.3 billion in the prior quarter, which largely reflects investments in working capital as well as cash investments related to M&A activity during the period.

As we look forward to Q1, we expect to continue to invest in the future of our business, to scale our operations efficiently, and to make additional progress towards full year profitability and positive free cash flow. To begin, I will share with you that our financial guidance for Q1 assumes DAU of 224 million to 225 million, implying year-over-year growth of 18 percent. For revenue, we are guiding to a range of between \$450 million and \$470 million for Q1, which includes the potential for modest acceleration in year-over-year revenue growth relative to Q4 at the higher end of the range. For Adjusted EBITDA in Q1, we are guiding to a range of between negative \$90 million and negative \$70 million with the sequential decline reflecting the seasonally higher revenue in Q4 and our plans to invest in the future of our business while continuing to achieve positive Adjusted EBITDA leverage.

Thank you for joining our call today and we will now take your questions.

OPERATOR

Thank you. That concludes the prepared remarks for today's earnings call, and we will now begin the question-and-answer session. To ask a question, you may press star, then one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then two. In the interest of time, we ask that you please limit yourself to one question. After your initial question is asked, your line will be muted. At this time, we will now pause for a moment to assemble our roster.

Our first question comes from Ross Sandler of Barclays. Please go ahead.

ROSS SANDLER, BARCLAYS

Hey guys, just a question on revenue trajectory in 4Q and 1Q. Jeremi, you flagged how the ad load is pretty low and that there's plenty of available impressions on any given day, given the engagement here. So, the question is more on the demand side. How much of the growth that you're seeing in the fourth quarter, the 44%, is from new versus existing advertisers, and then, I guess, what's the team doing to increase the pace of onboarding new advertisers onto the platform?

Then, looking at the 1Q revenue range, Derek, you mentioned there's acceleration at the high end. We can all see that. So, I guess, what's giving you the confidence that the revenue growth is going to pick up in 1Q? Thank you.

JEREMI GORMAN, CHIEF BUSINESS OFFICER

Thanks for the question, Ross. A couple different things. From the advertiser count perspective, as we don't break it out specifically, we are continuing to see strong demand for down-funnel bid optimizations, such as app install, and then increased demand for our premium ad units for brand advertisers, like Commercials and AR. Our advertisers are generally retaining well and increasing their spend, as we continue to demonstrate meaningful ROI, which is really critical in terms of advertiser growth.

I'm pleased to let you know that in Q4 of 2019, we did have our highest number of active advertisers ever, and there's still a lot of room to grow there. We have a lot of opportunity to get new advertisers, primarily through education of the market through our sales teams, and our work with our agency partners, as well. In addition, in Q4, we started a deliberate approach to buying B2B marketing, to reach the media planning community, and that's still early days, but we really like what we're seeing.

So, all in, we continue to deliver ROI. We're really, really focused on the market, ensuring that we bring the best solutions to them, and have the right products to continue to grow the advertiser base.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

It's Derek speaking, and thanks for the question, Ross. I'll take the second half of it, with respect to the Q1 guide. You know, I think a couple things. One, when I look at the growth rate in Q4—obviously, we pointed out some one-time factors there that are impacting the revenue around the timing of the holiday season, and whatnot. One of the things, I think, when we think about the revenue going forward, we're really confident in the trajectory of the business, fundamentally, for all of the reasons that Jeremi just mentioned.

In terms of our personality around guiding, we want to make sure that we're factoring into our range not only the things that we're optimistic about or that we're seeing materializing in the business, but

also the potential for some risks to materialize in the environment. Our guide tries to reflect both the momentum we see in our business and the confidence we have about our long-term trajectory, but also the potential for risks to materialize throughout the course of the quarter.

Hopefully, that gives you a little bit of a sense of why we point a little bit optimistically to the higher end of the range and the potential for us to bounce off that Q4 number.

OPERATOR

Our next question is from Michael Levine of Pivotal Research Group. Please go ahead.

MICHAEL LEVINE, PIVOTAL RESEARCH GROUP

Thanks for the question, guys. I wanted to understand how big of a driver for 2019, and conceivably in Q4, native direct-to-consumer advertising has been for the business. It's definitely a question we get a lot of inbounds from investors.

JEREMI GORMAN, CHIEF BUSINESS OFFICER

Thanks for the question, Michael. I would say that we're very, very fortunate to have both a strong brand-based business and a strong DR-based business, so we're not concerned, relative to the fact that we have that diversification and a suite of products that's meant to serve advertisers of all types. We love what we're seeing in the verticalization efforts and that broad-based swath of success across verticals, like entertainment, tech, CPG, and more. We are not as heavily reliant on that D2C group, because we have products and services that are as diversified as possible.

OPERATOR

Our next question comes from Heath Terry of Goldman Sachs. Please go ahead.

HEATH TERRY, GOLDMAN SACHS

Great, thank you. When you look at the improvements that you're seeing in ARPU in the quarter, how would you disaggregate that between usage and monetization? There was a lot of great detail about monetization in the prepared remarks, but can you quantify the contribution from the investments that you're making in advertising technology, better targeting, and measurement, and are there specific components in that ad tech that you'd call out as contributing, whether it's specific ad formats or specific tools that you're seeing advertisers use?

Then, just when you mentioned that ARPU gap in the transcript, can you quantify what you see as the right measurement of that gap between sort of where you are and who you're using—not necessarily who, but the level that you're using as the benchmark?

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Hi Heath, it's Derek speaking, and thanks for the question. There's sort of two components there. I'll take them in reverse order. The first one was just about the ARPU gap and what gap are we trying to close. I think, when we think about our ARPU opportunity near term and longer term, we're really looking at the audience we have, the engagement we have, the ad products that we have today, and the yields that we see in the marketplace for the inventory that we have. What we're really excited about is the opportunity to just continue to drive demand into our ecosystem and get market-based eCPMs and yields for the inventory and the audience that we have. So, we're trying to drive towards that.

Of course, we look at our peers in the marketplace in near term, like a Twitter, which we think is a benchmark we want to drive towards, and obviously we've got opportunity to go beyond that, and that's where we get into some of the discussion about how excited we are about the improving engagement on the user side.

We pointed in some of the prepared remarks and highlights that the growth that we're seeing in engagement on Discover, with the time spent being up there, growing our engagement with premium Shows, and, in general, the health of the ecosystem. And of course, when we see the growth in our DAUs accelerating year-over-year versus the prior quarter, all of that just adds to our opportunity. So, when we think about closing the gap, that's the kind of stuff we're looking at.

Then, to your other question, which is how much of the ARPU growth is being driven by usage versus say, optimization, I think at this point, because we are not supply-constrained, we're looking at predominantly just trying to build absolute demand into the ecosystem, and so what you see, when we're able to improve our optimization and serve the right ad to the right user at the right moment, and we can bring more diversity of advertisers into the ecosystem, that just allows us to use our inventory more efficiently and it takes some of the pressure off yields, which is great for our advertising customers who benefit from really low yields in the ecosystem today because we are not supply-constrained.

So, that's how we see the marketplace yielding out, and hopefully that gives a little bit more color to your question there.

OPERATOR

Our next question comes from Mark Mahaney of RBC. Please go ahead.

MARK MAHANEY, RBC CAPITAL MARKETS

Okay, two questions, please. One, Evan, a quarter or two ago, you called out the impact, particularly, of some of the new features on the gender filters, on the DAU growth, and this last quarter you had this nice innovation in terms of Cameos. Was it just not as material, so there wasn't a need to call it out, if you'll talk about that?

Then, you talked about a full year EBITDA profitability, but, Derek, you didn't mention that at the end, so just is that a goal, is that—not wishful thinking, but is that like a nice-to-have-goal, or is that actually you're trying to run the business to generate full year profitability, if one or two of you will address that? Thank you.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Hi, Mark. Yes, a lot of exciting innovation for us, Cameos included. It's very early for Cameos. They are a part of our Chat service. So, I think, over time, as more and more members of our community discover Cameos, they'll get really excited about them, and I think that has a lot of potential to drive growth in the future.

But I think one of the really interesting things that's happening in our business is that as we start turning our products into platforms—for example, whether that's our content business or augmented reality business—we see a lot of opportunity for durable innovation. One of the things we're seeing on the augmented reality side is the community-created Lenses are really growing in engagement and popularity, and what's great about that is that we don't have to come up with all the ideas here at Snap, our community is coming up with great ideas every day, and they're actually building them and then sharing them with everyone, and that's driving a lot of recurring engagement and growth for us, and so we're excited about that going into the future.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Then, Mark, thanks for the question, and obviously, on the full year profitability side, look, obviously, Evan and I are a thousand percent aligned. This is an objective for the company. We don't guide beyond the current quarter, but, as you can see, we've been investing in the company in order to accelerate our revenue growth, try to close these ARPU gaps faster. And as we pour those investments on, we liked the returns that we're seeing, and so we're driving the scale in the business in order to make that possible. So, it's obviously an objective that the entire Leadership Team is pushing towards. We just don't guide beyond the current quarter and that's why you don't see me talking to it in my section there.

OPERATOR

Our next question comes from Rich Greenfield of LightShed Partners. Please go ahead.

RICH GREENFIELD, LIGHTSHED

Hi, and thanks for taking the questions. I guess, just kind of maybe to start with, for Evan, kind of philosophical. I think if you looked back a year ago, kind of the quality of Discover was something we spent a lot of time harping on, and I think if you look a year forward, you've made a lot of progress in improving the quality of the content that's there. But I'm just wondering, as you think about the tension between what the algorithm wants to suggest to drive the most clicks versus improving the quality, how does that battle take place at Snap every day, and is some of it—what we're seeing in terms of revenue growth or ARPU growth—is part of it constrained, in that you're improving the quality of the experience and it takes time to onboard all the advertisers to benefit from the improvement in quality?

Then, just kind of a follow-up to the question that was asked earlier about the number of advertisers. Facebook disclosed, I think, over 8 million advertisers now, up from 7 million. Jeremi, is it fair to say that you're still in the hundreds of thousands of advertisers? I guess the biggest single question that everyone is thinking about is, is that the single greatest driver of closing the gap, is just bringing on more advertisers to build up competition in the auction? Is that what gets you 50-60 percent revenue growth, relative to where you are now? Thanks.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Thanks for the questions, Rich. We're really excited about the momentum we're seeing on the content side of the business and I think there's still a lot of room to improve the service. There's going to be some announcements we're making later this year around new innovations, to that effect. I think that tension is always going to be there, but one of the really unique things about Snap is that all of that content in Discover is curated, and so we're really defining the pool of content that's served to our community. And that's how we try to get the right balance between content that's really relevant, but also content that's high quality. I think that's sort of the right trade-off to make for now, but we're doing some experimentation around merchandising, things like our Shows, more effectively. You see that if you swipe over from Discover, one page over, we're doing a lot of experimentation there, and we're learning a lot. We hope to bring some of those learnings more broadly to our community as we go forward.

JEREMI GORMAN, CHIEF BUSINESS OFFICER

Then, I'll take the second part of your question, Rich. Yes, absolutely, definitively, advertiser count is the single best way to grow demand, including onboarding new advertisers of all types. We have products for all of them and we are very comfortable with how we're onboarding those, but tons and

tons of opportunity ahead. We do have fewer than 8 million advertisers, but a lot of headroom to grow. We have the supply to do it and the products to do it and bring on advertisers of all types. So, yes, that is where we are myopically focused on the sales team, to ensure that we have a breadth of advertisers to close the ARPU gap relative to our peer set.

OPERATOR

Our next question comes from Doug Anmuth of JP Morgan. Please go ahead.

DOUG ANMUTH, J.P. MORGAN

Thanks for taking the question. I just want to follow up on Discover, Evan. You talked about the 35 percent increase in time spent, and more than that among users 25 plus. Can Discover help Snap age up more over time here? Then, can you just talk more about what the shift in usage toward Discover means for monetization and closing that ARPU gap? Thanks.

EVAN SPIEGEL, CHIEF EXECUTIVE OFFICER AND CO-FOUNDER

Well, at a high level, there are really interesting shifts happening in content consumption overall, as you know, as the viewing behavior moves from linear television to mobile content consumption. And I think the content offerings, really, across the board have not caught up to this behavioral shift, and that's why we see so much opportunity here and why we're continuing to invest in creating new shows, creating new content types, because we see so much demand from our community.

That behavior shift, I think happened first with young people, and it's increasingly happening with older folks, as well, and we're excited about the growth that we're seeing there. I do think it plays an important role in closing the ARPU gap, but, frankly, the ARPU opportunity is so broad at Snap. Given the current level of advertiser demand and the amount of inventory that's available, I think we'd have to grow something north of 50 percent full year revenue for several years just to get close to a Twitter level of ARPU. So, we're very focused on accelerating revenue growth, which we think is possible.

OPERATOR

Our next question comes from Justin Post of Bank of America Merrill Lynch. Please go ahead.

JUSTIN POST, BANK OF AMERICA MERRILL LYNCH

Great, a couple questions. First, you are guiding to possible acceleration in Q1. I know the comps get tougher both on DAUs and revenue growth as the year progresses. How do you feel about the year and your revenue initiatives, and just kind of the setup for the year, if you can help with that at all?

Then, secondly, I thought it was interesting that your revenue share costs were up 49 percent year-over-year, but your Commercials, I guess, were up 3x. So, maybe you could just help us a little bit about the gross margins of the Discover business, if those are really attractive to you, and the operating margins there? Thank you.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Hey Justin, it's Derek speaking, and thanks for the questions. In terms of a setup for the year on revenue, and just our momentum heading into it, I think we've really been focused on our long-term opportunity. Both Evan and I have touched on it here today, around the longer term ARPU opportunity. We've been investing in the business in a lot of different ways around monetization, in terms of our sales teams, the engineers that support those teams on optimization, and then, of course, in the product. And so, we feel like we've been putting the inputs into the business in order to set ourselves up. I think we are really pleased with the momentum we're seeing in the business and the absolute revenue growth opportunity there. You're going to see us continue to invest in the business in order to make it possible to close that gap faster.

In terms of the scaling on cost of revenue, there's really three big components of the cost structure there. Obviously, infrastructure, which you can see separately, and then, of course, the content side, and then, of course, serving costs on ads. When I think about scaling there, we do report that within revenue share, so it probably gives you a little bit of a sense of the structure of a lot of that cost, but we're also investing in our own shows, in our own content. Some of that structure is a little bit different and scales, frankly, quite well for us, as our audience grows and as the engagement grows, and so that also contributes to our ability to expand our margins as we scale the business. You're seeing a really good flow-through there. The eight-percentage-point expansion is really healthy, and we expect that we can continue to scale efficiently. Having that infrastructure cost number get more efficient on a unit cost basis over time really opens it up for us to invest in the future of the business on the content side, which expands our monetization opportunity, while still growing those margins. That cost structure has been working nicely for us and we're going to stay focused on being operationally efficient, so we can make those investments.

OPERATOR

Our next question comes from Steven Ju of Credit Suisse. Please go ahead.

STEPHEN JU, CREDIT SUISSE

Thank you. Evan, some of the RoW regions have lower GDP per capita, so your ARPU may ultimately be lower, but would you say that the cost to serve in those regions may be that much lower, as well, given the data cost constraints you called out, and the use case for the app might be different?

Derek, your DSOs are down every quarter this year, relative to the prior year, so can you talk about the shift in mix between revenue that is more self-service versus agency-driven, and ultimately where that DSO can ultimately go as the advertiser base continues to shift? Thanks.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Hi, Stephen, thanks for the questions. To the first one, in terms of us managing our infrastructure cost per DAU, and any of the long term around the cost per DAU by region, relative to ARPU, obviously, we've got a lot of opportunity to grow ARPU, as we've been talking about. And we've been able to grow ARPU much faster than our cost per DAU. You can see that this quarter with the growth in revenue and flat cost per DAU. That's allowing us to expand our efficiency, overall, in our margin.

Typically, as you're thinking through the cost of infrastructure, user engagement is obviously a driver, the cost to deliver impressions are also a factor, and, of course, it's going to vary based on user engagement. It's going to vary based a little bit on ARPU because of the impressions being a component of that. Generally speaking, there's some alignment there between your ARPU and your cost per DAU when you look at different regions, and so that helps you a little bit as you've got your ARPU varying by country. Importantly, we're getting better and better at managing those costs and getting them scaled appropriately. That's been working pretty well for us, and I think you can see that coming through in the margins. Even as our Rest of World DAU's been growing a little faster than our more mature markets, the margins have still been expanding. I think you can see that coming through in the outputs.

In terms of DSO, yes, we've put a lot of attention on just scaling our business efficiently and making sure that we're managing our DSO efficiently, and working capital, making sure it scales well. Obviously, Q4 working capital was a drain quarter-over-quarter. Seasonally higher revenues, we've got to collect those in. But, generally speaking, we've been able to expand the working capital structure pretty efficiently over the course of the last year, and you can see that starting to come through in the output.

OPERATOR

Our next question comes from Eric Sheridan of UBS. Please go ahead.

ERIC SHERIDAN, UBS

Thanks. Maybe two topics, if I can. On the shorter holiday period there, I just wanted to know if you could quantify how that might have impacted Q4, and whether that outperformed or under-performed versus your expectations that we knew the calendar was going to be less days?

Then, the always-on-demand, and thinking about the valleys built into the self-serve auction, you're calling that out as a headwind in Q4. Looking back over Q1 to Q3 of '19, as we look at year-on-year comparisons going forward, are there any comparisons we should be aware of that create either tougher comps or easier comps now, as we look forward over the next couple of quarters, that we should be aware of, just versus the way you'll be communicating on the business going forward? Thanks so much.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Hi, Eric, thanks for the questions. Yes, shorter holiday period, I mean, the way I think about that is I look at the revenue through the quarter. Similar to what we've seen in prior years, we saw elevated holiday spending in the period between Black Friday and Christmas. That period is just a little shorter for us. One of the things that's really important to understand about our business is, because we're not supply-constrained, we're more sensitive to fluctuations in demand. Whereas other platforms, if you're more dense, when you have that kind of demand fluctuate in, it's going to trade off against yield a little bit more. The expectations that we had for that impact in Q4 pretty much lined up with what we saw, so it was as expected, which is why you saw us come in real close to our guide.

Then, in terms of the impact of the always-on going forward. For sure, we saw the business accelerate throughout the course of 2019, and, of course, that just makes the expectations higher, but as we were seeing our business improve over the course of 2019, we were investing in the business, and you can see that, where we were investing in our Sales Teams, in our Engineering and Product organizations that support the business overall, and content, and so on, and so as our business has improved, we've been investing in the business. Typically, you'll see a lag effect between the investments that you put into the business and the monetization that results from all of that. We're pleased with the early results that we're seeing from those investments and we're doubling down on what's working. That's what's making us optimistic about our ability to realize our ARPU opportunity as we move forward, because of those investments, you know, appear to be looking good.

Thanks for the question. I hope that helps to illustrate.

OPERATOR

Our last question will come from Brian Nowak of Morgan Stanley. Please go ahead.

BRIAN NOWAK, MORGAN STANLEY

Great. Thanks for taking my questions, I have two. The first one—Jeremi, I appreciate the detail on your key strategic priorities. I guess, sitting in your seat now, what do you think are sort of one or two of the most important aspects to really improve, to improve the direct response advertiser adoption and the

pace at which DR dollars can flow over the platform? What's the biggest area of friction you need to improve in 2020?

Then, the second one, for Derek. I thought it was interesting to hear sort of your guidance philosophy, where you're sort of assuming some risks for the upside and downside. Just as we're thinking about the first quarter guide, maybe talk us through some of the potential risks to the downside that are incorporated into the guide, that could perhaps go better or worse? Thanks.

JEREMI GORMAN, CHIEF BUSINESS OFFICER

Thanks for the question, Brian. We are absolutely focused on optimization and ranking, alongside improvements to our advertising tools and products for our more sophisticated advertisers. There are not a lot of huge hurdles remaining in the business. I think we're structurally sound, but I think really importantly, one of the things is that advertisers really just want us to win, they want us to succeed. They want options, they are looking for brand-safe environments for their messages. They want to reach Gen Z and Millennials, where they're forming lifelong habits. They want performant media, they want video and they want creative canvases. And we have all of those things. So, I think, in terms of fundamentals, we have everything we need in the building to reaccelerate revenue, and we're extremely optimistic about our ability to do that, and so we're looking forward to a great 2020.

DEREK ANDERSEN, CHIEF FINANCIAL OFFICER

Brian, it's Derek speaking, and thanks for the question. The Q1 guide, I think, when you're thinking about risks and opportunities, a lot of that really comes down to our execution and how quickly we can capitalize on our opportunity. Obviously, we talk about keys to growth being bringing more and new demand into the platform, diversifying our advertisers, and continuing to deliver optimizations that allow us to use our inventory more effectively and deliver ROI for our advertisers. That's really the focus, and how quickly we can execute on that and how quickly our customers react to the ROI that they're seeing.

We're really excited about our opportunity and the momentum we have in the business, and we're trying to give you a good estimate of where we think things can come out. Obviously, when you're growing at the rates we are, there's a little bit of a range around what that possibly is. We're trying to deliver in the short term, but also keep our eye really focused on investing for the long term, so that we're accelerating the business to capture the longer term opportunity as quickly as we can, and the Q1 guide reflects that and the range around what we think the execution could be.

Thanks for the question. Hopefully, that helps explain.

OPERATOR

This will conclude our question-and-answer session, as well as Snap Inc.'s Fourth Quarter and Full Year 2019 Earnings Conference Call. Thank you all for attending today's presentation and you may now disconnect your line.