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NortonLifeLock, Inc. (NLOK)

Stifel Cross Sector Insights Virtual Conference

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MANAGEMENT DISCUSSION SECTION

[Abrupt Start]

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

...from the cybersecurity research team here at Stifel. Thank you, all, for joining this virtual event. I have the pleasure of also virtually welcoming Norton CEO, Vincent Pilette; and then President as well, Samir Kapuria is going to be joining too.

Before starting, if you'd like to ask a question, you can do so via the webcast link or you can also just shoot me an email at gtalpaz@stifel.com. Vincent and Samir, thank you, both, for joining us.

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QUESTION AND ANSWER SECTION

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

So let's start high level as we usually do with these things. I think most of you have familiarity with the Norton brand, but obviously a lot has changed over the last year. I think for those perhaps less familiar, maybe you could provide us with a brief overview of the core business today, and the overall growth strategy? I think a lot of investors have familiarity with the prior iteration of Symantec, but how should we think about Norton as a standalone consumer story going forward?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. Thanks for the question, Gur, and I met with a few investors this morning, was surprised to hear that a few were new to the story, which was actually delightful, but surprising. So we are NortonLifeLock, we come out of the separation of Symantec between consumer cybersecurity business, and the enterprise business. The enterprise business last November was sold to Symantec for $11 billion and we returned the cash to shareholders in the form of special dividend.

When you talk about the division, we see really November as kind of our IPO, if you want, under NLOK, NortonLifeLock brand. It comes from the Norton security business, software security business for Consumer part of Symantec, and the acquisition of LifeLock identity protection and restoration business that Symantec acquired two years ago.

At the time of the acquisition under the leadership of Greg Clark, they built a vision of developing a Cyber Safety plan for consumers. As the life of consumers more and more moved online, as your identity becomes more and more digital, and as your identity actually explode into multiple identities, and lives online, the need for an overall Cyber Safety protection plan if you want. The same way that you have protection and safety in your physical world would only grow. And the combination of an integrated portfolio coming out of the merge of Norton and LifeLock enabled us to launch last April, Norton 360 which is an integrated platform offered for a membership fee, fixed level of membership, and giving us the ability to add new features as we build this vision towards a digital Cyber Safety plan for consumers.

Since then, we've said that we would increase our investment in marketing since we're 90% direct-to-consumer business selling through our ecommerce platform. Ecommerce and marketing is basically our sales engine. We've increased our overall marketing investment to roll out Norton 360 and build up the message of Cyber Safety for consumer. And we've seen early signs of success. We've been growing at 4% booking rates for two quarters. A customer account that had been in decline for many years has turned now to be growth, granted slow growth, sequential growth, but we'll continue to build and roll that Norton 360 features to our installed base and to new consumer across the world.

So that's where we are today as we close the fiscal year. We have a midterm model in place from a financial perspective, growing mid-single digit, delivering operating profit of 50% margin, both of which we're almost there. At that level, delivering an EPS of $1.50 and generating $900 million of free cash flow, supporting then all of that division towards the Cyber Safety company.

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Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That's great. Thank you for that. And, Vincent, you've been tasked with handling the separation of the Symantec Enterprise piece from the Consumer piece. Can you maybe just talk about where we are in that transition? I think if you go back even a year plus ago, there was sort of this discussion of whether such a separation could even happen given shared technology, yet it's been incredibly smooth. Maybe can you just kind of walk us through the underlying reasons why that's been the case and where we are today as far as that separation?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. And I think that's correct, a pure separation in two stand-alone businesses could have been really hard. We had the opportunity with the board, the management team to sell the enterprise business in a very unique manner for this case, which is an asset sale. Broadcom bought all of the enterprise revenue and only the necessary assets for them to integrate into their already formed software division, which then left behind about $1.5 billion of annualized stranded costs at the time.

And we told the board that we would eliminate 100% of those stranded costs over a 12 months' period. While at the same time, we would reinvest into the Consumer business that was a little bit trending like a cash cow division, if you want, invest first in marketing, and then invest in R&D to accelerate the innovation cycle. We bifurcated both processes and we accelerated the transition.

We've almost done – I told on the last earnings call that by this quarter would be the last of materials stranded cost. And then in July and August, the following quarter, we'll have the remaining ERP and data center, the commissions are a little bit of remaining costs, by September, we will be done with that transition. We also saw the portion of our underutilized asset, still have a little bit to do in that area, and we then embark on to really focusing on building that Consumer business.

When we reinvest in R&D, there are two areas that we're looking at. The first one is SaaS prototyping, so creating more bandwidth in the R&D organizations to accelerate the development of new features for Norton 360 as we constantly evolve the portfolio, and the second one is rebuilding some of the layers that moved to Broadcom for which we have a long-term partnership with and sharing data across the two companies. They focus on their enterprise, we focus on Consumer, but there are some layers that we want to have in-house that we are rebuilding.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That makes a lot of sense. And I do want to drill in a lot of Norton 360 in a second, but I'll ask the obvious elephant in the room question get out of the way first, which is you gave some good detail on the last call regarding the impact of COVID, which was actually fairly minimal as far as what it meant for retention rates. As things are fairly fluid out there, the world is changing by the day, perhaps you could give us your updated thoughts on where we stand today as far as how you're thinking about that overall impact, and if you've seen any sort of change here over the past few weeks?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. So, when COVID-19 happened, obviously like any leadership team and working in collaboration with the board, we went back into analyzing multiple scenarios, and say what would happen if. And we developed all of

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those. We went back also to 2008 and 2009, and see what happened at that time. We concluded that we have a very resilient business and that we have plenty of P&L and balance sheet flexibility with by that excess cash and plenty of variable spend to navigate through short-term impact in the economy.

Now every crisis is unique, and this one definitely comes with the fact, if it's an economic crisis may be now, short-term or long-term, nobody knows. But it comes with the fact that more of your life is moving online. More of your identity – more of your identities are moving online and from old cohorts, new cohorts that maybe my mother who never really went online and now is going online to do some orders. And all the way to my 12-years old son that does all of his school through video conferencing and other.

So the digital life has taken a bigger proportion, and that is our underlying structural growth story which is as more and more of your life as a consumer, over the long-term we have 7.5 billion of consumer to touch, you will develop a need for Cyber Safety enablement and protection plan if you want as you do that. That long-term view of us has just been more validated by COVID-19. And we haven't seen like a jump of multi-percentage point overall, but we've seen very good solid interest for our products, our portfolio from members that wanted to make sure that they have all data right in our system to ensure proper renewal. All of that if you want, has been a validation of our message.

Now the question I get from investors is saying, hey maybe the pandemic is behind us, maybe. And the economy may be in a V-shape in term of a recovery, maybe. What does it mean for you and my point of view is always the same. We have a long-term structural growth. We have not changed our long-term model or metrics. And I think we're marching towards that. In between COVID-19 has been just one more angle for us to drive our message and awareness with consumers.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Let's drill into that in the context of Norton 360, right? If you look at the history of the consumer security space, it's been, I would say fragmented in a lot of ways, right? Maybe how to play on mobile, maybe how to standalone VPN play, and it's a patchwork of different solutions. You're really sort of making the play for a consolidated sort of simplified type of solution. What do you think the appetite is right now for a solution like that? How should we think about present-day penetration? And what are you thinking about, in terms of longer-term penetration, do you see COVID simply as a catalyst, and sort of in the wake of greater digitalization, and more folks moving online, more folks doing things online or the need for a more holistic solution might be more impactful in today's world than it was last year?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. And, of course, you will want, and I will want to stay very practical and not fragmented, but allow me to step back first. When consumer security started, it was really mainly along the antivirus to compensate for security weaknesses of certain operating systems. That need by itself obviously has diminished tremendously as the operating system have increased. It's still there because I think a certain level of protection is an absolute plus, but it's not by itself the main driver.

Then all provider of those solutions have increased their portfolio and have tried to eliminate some pain points, password managers, may be VPN when you connect. All of those features, in my mind, are still very device-centric. You move maybe from one device to multiple device; from one operating system to multiple operating system; but you're very device-centric.

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Two years ago, when we bought LifeLock, we became user-centric. We also wanted to protect and restore your identities. Everything that went online that could be stolen from you or misused from you from an ever-evolving cyber criminality is something we want to address as a pain point from consumers. And so moving from what I mentioned, one device to multiple device, from one operating system to multiple operating system, moving towards user-centric what applications do you share information with that could be a risk from a cyber-criminality is what we're trying to address.

And I would say, if you fast forward now to the future, that's even evolving the same way the device has evolved from one identity that you could now have physical and digital to multiple identities, even the definition of a digital identity could continue to evolve and be broad based. All of those are offering us opportunity to build that overall Cyber Safety plan. And within that of course, now you want to come back to the practical view, which is you still have standard market. Do you have a market defined as security in which you have multiple players with the leader in it, and will continue to roll up and add new functionality. You have a market for identity and that's growing at mid-single digit.

You also have multiple players in that. And there the technology underneath will constantly evolve. Then you have new emerging markets. What does privacy mean? What does the right to be poking around on the Internet means, etcetera, etcetera? And all of those are opportunities that we believe we have both the brand and the capabilities to address under an integrated umbrella of Norton 360.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

So I think, I think you answered the question, but I'll drill in a little bit. When you think about that conversation, how do you sort of view your current appetite for pushing into relevant adjacencies? And when you take that a step further, how do you think about the potential impact to ASPs which have been trending up, should you make kind of these further push into relevant adjacencies?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. So let's just be clear, we are at the early stage of our new life under NortonLifeLock, right, and building up an operating system, a leadership team, a company that can operate with credibility was very important. I think after two quarters operating standalone, we've earned the right to be considered that way, but we'll continue to improve

The second immediate initiative that we launched was to make sure we have the marketing engine, which is really our sales engine if you want, behind to push that awareness, [indiscernible] (00:14:16) of Norton 360, making sure that there is an overall demand and awareness for our products out there. That's the investment in marketing we've made and you'll see more of that.

It goes without saying that at the core, we are a technology product company. And so, constantly investing in that technology space is the next step of initiatives. We've definitely launched a few new features, and the Dark Web Monitoring, the Home Title Alerts are all inputs that we get from our vast installed base and many other inputs that then build into the overall R&D engine. As we continue to create operational efficiencies, we're going to increase both the velocity and the bandwidth of that R&D engine to be able to do fast prototyping and test some of the new features and push them along.

So you'll see more of that as we continue and progress. You'll hear more about the new features we're launching and that's absolutely a critical avenue, if you want, in our long-term future.

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Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That makes sense. And I guess in the context of that conversation, how do you think about potential appetite for M&A? I think there have been a lot of chatter out there right now in the security world. Just given the environment we're in, given some of the challenges that smaller private companies perhaps are facing in raising capital is the question we ask everybody. But when you sort of look out there, does this make you want to be perhaps more aggressive or less aggressive, and looking outside of the core R&D base to perhaps grow the TAM and expand it to other areas?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

I think we want to be ambitiously aggressive to build toward that vision, which is a Cyber Safety plan for Consumer. And again, if you go into pretty mature industries, you always have one or two top brands that come to mind. If I go to Consumer today and I say Cyber Safety, you won't have that. And we have both, the brand and capability to go and define that overall market for Consumer. So that's an exciting place to be. You need to have a vision and we have that.

Then you need to have a strategy and an operating system and that's what we're building and I think we've earned the right now to say that we've had early success in both the operational side and also the growth side. We added a few functionalities not yet to where we want to be but it's getting there and we've returned to stabilizing and maybe slightly growing sequentially customer count. Both are very good signs.

Then you want to say, okay, what else you want to do? And you continue on the strategic framework and you say, what are the adjacencies I want to build on? And as we do that, we identified some. Obviously, we have and then you analyze, say, do I want to invest organically there because I have a shot, I have the ingredients, nobody has been there yet or you look at the competition say, hey, as a product already being de-risk from a prototyping perspective or is it already a full business who is paying customers.

And you look at all of that and you want to make a financial tradeoff between your organic investment and your tuck-in M&A strategy. I think we are at the stage today that we have the right to do that, not that we will do it, because as always in acquisition it depends on so many stars, cultural people, process, timing, et cetera. But in terms of aggressively pursuing our vision whether it's organic or inorganic is absolutely, not only a must, but something that drive all of us on the leadership team here.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That makes sense. And the context of that conversation, how do you think about the competitive environment today? And if you kind of – if you go back two to three years, the viewpoint was that Consumer was just sort of going to be a part of an Enterprise story, a way to kind of make margins and then ultimately fed the engine. Obviously, the viewpoint has changed pretty dramatically today.

When you look out there, you still have some players that still kind of [indiscernible] (18:15) hybrid model. You still have some stand-alone players, but when you kind of take a step back, how do you think about that environment? And then, you talked about some that are device-centric, maybe you could elaborate a bit on that, whether you see that that being still kind of an undercurrent across the broader space?

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Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. So to be clear, the competition evolved, the view of Enterprise and Consumer evolved, but also, the consumers themselves have evolved with their habits and what's happening as well. I think that's an important one. I cannot speak for the competition, but I can tell you for us, managing the requirement of an Enterprise Security business and managing the speeds, velocity and different angle of the Consumer business has been pretty challenging. I think, we made the right decision by selling the Enterprise and focusing on the Consumer.

And maybe that thesis, when it was mainly around engine and [indiscernible] (19:09) an endpoint device, which is by the way is an Enterprise term, made sense. But as you get closer to the Consumer, integrated, past the device security needs and go into the user needs and embraces different needs around like for example, your identity restoration or your protection, you have also different business model, more services oriented. And I think that an opportunity by itself that has enough complexity. When it comes to competition, we address all pillars mainly, right. So still the traditionally defined security pillar, the identity pillar, privacy and maybe connected home in a fragmented way.

On the security side, there are three main players that together and with the leader own about 60% of the market, the rest is still fragmented. And we compete in that environment obviously is proposing an integrated solution that not only protect the device, but protect the usage and use digital identities online.

When it comes to identity, we also have – mainly competing against the credit bureaus, if you want. We offer a broader set of the portfolio and then you lean back to the technology software security angle, which is not only will provide your identity element, but we do it in the digital world, thanks to our software enablement platform.

And then on privacy and connected home, I would say, those are emerging fragmented market for which we absolutely have the right to play and need to be very innovative.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That makes sense. And maybe just going back to comments you made earlier, you talked about the growth in subscriber count here for two consecutive quarters. Maybe let's elaborate a bit on that, the underlying drivers of that growth, despite all the changes happening within the business, you're still able to kind of get good growth here on the subscriber levels that I also think surprised a lot of people especially in this environment. If you take a step back, how you think about just the funnel, if you will, of customer growth? And where do you ultimately get the confidence of durability in that metric?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. And it's an interesting one. I get that question very often. So first let me tell you about the growth itself then we'll talk about the confidence and the future. It's important to recognize that over the last two, three years the Consumer division Symantec really spent most of their energy integrating their offerings into that one platform and they have done a great job at it.

In the meantime, they also increased their engagement with their installed base and increase the retention up to 85%, which is an industry leading standard metrics. But at the same time, did we not invest really in marketing because you need to tweak marketing down and let the customer count glide down for many, many quarters. I would say, even many, many years.

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So when we launched Norton 360, [indiscernible] (22:15) the room to invest in marketing, we became a Consumer pure play. So every dollar we invested in the business is made for that business, and we launched or increased our marketing spend from roughly $200 million to $300 million at the same time that we Norton 360.

We also directed those dollars into new form of marketing from the long and short form, traditional forms, the TV and radio and mailing into the new forms like paid search, social media and moved those dollars more US-centric to also being international. We've seen an early sign of success. I would call it, customer stabilization with of course broad based as I mentioned performance there. Not only the traditional side, the security side which we call Norton 360 value customers, but also continued growth into the premium side, which is more identity driven of Norton 360.

A little bit more in Europe and Asia than in the US, but broad based, still low broad base. A very good first sign than getting there in the market with our new offering and our unique approach was well-received. Obviously, we're going to continue to do that. With COVID-19, we saw marketing spend actually, on a rate basis, being lowered and we reused some of those dollars to continue to accelerate our penetration in those market and new cohort.

When you talk about confidence for the future, I get most often the question around say, hey, there will be less and less device or less and less need for security and people you've lost – you lost them forever. All of which for me is very different in the way that we look at the world, which, as I mentioned, at the risk of repeating myself, when we move from device to user-centric and maybe you were a customer of Norton Antivirus five years ago and you don't need it anymore. But tomorrow, you're going to have a need for privacy or the right to be forgotten not the experience.

And as we continue to build up the portfolio toward the Cyber Safety, we're going to continue to increase the addressable market, if you want, or the number of customers who can go and reach. And so, it's a mix for me of goods marketed, e-commerce engine, coupled with constant development of the portfolio, a new feature innovative technology.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That's really interesting. Maybe you could kind of elaborate a bit on the threat environment that you just kind of touched on and the evolution of that threat environment as it pertains to consumers. When you think about sort of this – I would say [indiscernible] (24:53) but this transition, if you will, from more device-centric type of risk on the AV side to maybe perhaps more user-centric, how do you think about the broader threat context around that? And then maybe more importantly, how do you think about the consumer willingness to pay for security around that? Is it heightened relative to [indiscernible] (25:12) AV or it's the same? Is it different? Is it too early to tell?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. So, it's an interesting one, right, because in this world of cyber community, it's an ever-evolving threat, if you want, right? And while the consumer constantly evolve, they need, their practices, their usage, the community adjust to that as well. And so new needs emerge and we need to address them. A small but perfect example is from a Consumer when we heard the need to understand what did they have for their home title.

Because, as you know, some home titles could be misused and against which some loans could be taken. And nobody really knows what's happening against their home title until they try to sell their home or do something

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differently and so they realize, oh, my god, that something has happened. And so, we quickly integrated into a Norton 360 platform if you want [indiscernible] (26:10), which is kind of a new need that came from Consumer and we built into our overall environment. That is constantly evolving platform and need.

And, again, if you go back to device-centric and [indiscernible] (26:26) centric, that needs maybe will not be growing and also we never know, but when you think about, hey, I want to have my identity protected, and it's not just online it's also the service that go with it [indiscernible] (26:40) easy to restore our future needs like the right to be forgotten, how much would you pay to have all of the information you don't want to have on the Internet that you may have posted when you were a teenage, right? And so all of those things will constantly evolve and our portfolio, which is a mix of software technology coupled with services will enable us to address those things.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.
Q

That's great. It makes a lot of sense. And we've got time for maybe two more questions. I'm going to ask one from the webinar Q&A. I've been asked what is an example of a competitor device-centric product strategy and how does Norton address that differently?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.
A

Well, I can mention [indiscernible] (27:30), right? So, first, I will start with us. We've embarked on a platform to integrate everything under an app, Norton 360. You a pay a level of membership, call it level 1, and from that you have an antivirus, a regular back storage, you have VPN, and then you can move up a level and you can have password managers and other things still device-centric or value-centric. And you move at the next level of membership, let's say level 3. Now, you have some identity protection and you could have the dark web monitoring, you're your password and users being sold or used in the deeper layers of the Internet.

Then you can move another level, and you have – you've used your identity somewhere on the Web to buy a car maybe and now, your identity is being stolen, your credit is being attacked and the next level of membership could have a services of restoring that identity all the way to, kind of a protection services if we can't restore the damage.

So that's our way of approaching it and we can constantly move features up and down, depending if they're being commoditized or innovated and that's our strategy. We've seen from competition some mimicking behaviors, such as offering bundled products or offering discounts if you go on auto renew your membership structure. And those small points for us are our proof point that we are on the right path. Also as I said, when we started this call, this is uncharted territory and we are about to redefine a market for consumers.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.
Q

That makes sense and maybe we have time for one more question, if you're okay with that...

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.
A

Sure...

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.
Q

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...just high level. We talked a lot about direct customer acquisition. Maybe we could talk a bit about indirect channels as well. You've had IST relations in the past, some new, some old that you inherited. How do you think about those just more broadly in the context of the evolution of the company?

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

A

Yeah. So, definitely direct-to-consumer, 90% of our business all acquired through our e-commerce platform, support by marketing engine and of course a great product portfolio, this is a fantastic asset. You can evolve that e-commerce platform in many different ways for the consumer and we see that as a strong value. At the core of it, it's not really the e-commerce tactics it's not really just the marketing dollars. It's our brand. Our brand calls for trust in the value in Cyber Safety. The trust that it [ph] embodied (30:09) allow us to think about many different adjacency for which we have the right to play. Either we have the capabilities with that brand or we can acquire the capability or have the right to play. 10% of our business is indirect, which means directing these products through partners to push the message and the brand of Cyber Safety.

The various form and shape of those partnerships. In my mind, they could be a lot bigger. They allow us to scale and combined our brand with other brands to have validity in certain sub-market or vertical market. So it's a very important one. We still have to make sure we can bridge between direct-to-consumer and that partnership and don't become an indirect business. But there are huge assets for us to continue to push that brand value in different shape and form to the vast amount of consumers that would be interested to buy Cyber Safety.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

So, that's helpful as always. And, Vincent, I want to say thank you so much for your participation here.

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

Sure.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

And for the insightful answers to all my questions. It was a great pleasure catching up with you again. And if any of you have any questions on the line, feel free to shoot me an e-mail. I will get them to the company or you can [indiscernible] (31:27) directly as well. Again, thank you to Vincent...

Vincent Pilette
Chief Executive Officer & Director, NortonLifeLock, Inc.

Thanks, Gur. Appreciate it.

Gur Yehudah Talpaz
Analyst, Stifel, Nicolaus & Co., Inc.

...Yes. Take care, and talk soon.

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Vincent Pilette

Chief Executive Officer & Director, NortonLifeLock, Inc.

Thank you.

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