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NortonLifeLock, Inc. (NLOK)

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MANAGEMENT DISCUSSION SECTION

Patrick Colville
Analyst, Deutsche Bank

Hello, everyone. I appreciate you join us today. I am Patrick Colville, a senior analyst at DB's covering the cybersecurity and the infrastructure software space. This session with NortonLifeLock will be a fireside chat with listener Q&A. There's a chat boxes where you can ask questions, but any questions will be anonymous, so we will not mention your name or your company affiliation. I guess the place to start is to have some introductions, so we got Vincent Pilette, the CEO of NortonLifeLock with us today. NortonLifeLock, as you all know is a pioneer in consumer cybersecurity and arguably one of the most recognized and trusted brands in the space. Vincent, thank you for joining us.

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

Yes. Thanks, Patrick. Thanks for inviting me.

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QUESTION AND ANSWER SECTION

Patrick Colville
Analyst, Deutsche Bank

Q

So I guess, given time constraints, let's jump straight into the questions. I think the – probably the most obvious place to start, the elephant in the room really is that cybersecurity risks have been increasing, we all know that, but how has the coronavirus pandemic affected that trend?

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

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Yeah. We're going to talk about that. Let me step back a little bit and really talk about what NortonLifeLock is about, right. As we sold the Enterprise Security business that was part of Symantec to Broadcom, we became NortonLifeLock cybersecurity company as you mentioned, solely focused on consumer. And our mission is really to enable and protect consumers to live their digital lives in a safe environment, protect them against cyber criminals, but also enabling them to conduct their digital operations that could be ecommerce, that could be now talking to friends, schooling, many different activities and conduct that in a safe environment.

As we came from the Norton side, the security on your endpoint device to combine with LifeLock, which is more user-centric, really focusing on the overall ecosystem of the consumer. Now, of course, with the pandemic as you know, more and more of the activities that we used to conduct in a physical environment, my kids going to school are now doing it virtually, my mother was going to the shopping [indiscernible] (02:33) everything online. So, more and more people got into that overall digital environment and with that, of course, cyber criminality adapted, increased, changed and people have the need to be protected against that. So, I would say, the pandemic has accelerated the understanding that as a consumer, you will need a Cyber Safety umbrella to protect you against cyber criminals.

Patrick Colville
Analyst, Deutsche Bank

Q

Interesting. And I guess the kind of anecdotal evidence you are pointing to is, we have seen in your numbers, the recent results suggest an increase in new customer adds. So I think across your portfolio in device security, identity protection, digital privacy, where has the kind of strength been most concentrated? It's probably the most – the first question. And then the....

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

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Yeah.

Patrick Colville
Analyst, Deutsche Bank

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....and then the second question is, is this strength a sustainable tailwind in your view?

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

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Yeah. So a year plus ago in April 2019, we launched the first integrated platform to address the Cyber Safety needs of a consumer. So, that's an integrated platform for membership fee, you can have access to the various functionalities of our portfolio, you mentioned, at the bottom we have some device endpoints, securing the core, antivirus, password managers, we have VPN and then you go up and up of functionalities and at the highest level of membership, you have full identity protection plus every other service, including insurance services or restoration services. And I think that integrated approach to address and build up on what Cyber Safety is for consumer is at the core of our vision if you want.

If you will subscribe to a Cyber Safety protection, the same way that today without thinking when you buy a car, you buy an insurance or when you buy a house you take a physical protection of that house, you will do the same online, but the functionalities that's made up of Cyber Safety will continue to evolve. If 10 years ago it was really around protecting your multiple devices, today it's about protecting your multiple digital identities, pushing into the new frontiers, you mentioned privacy as one example, and definitely people are very conscious about their data being on the web and being able to better control their own data.

Through the pandemic crisis, what we've seen is a pretty broad-based growth as we know – as you know we've reinvested into marketing to kind of drive this message of the integrated platform for Cyber Safety to the consumers and we've seen a pretty broad-based growth on the bottom side of the portfolio, which is more value-based security based, but also on the higher side of the portfolio which is pushing into the identity and privacy based. It was growth in the US and it was growth international. So, we've seen a good reception, if you want, of our overall message, vision and supported by the launch of Norton 360.

Patrick Colville
Analyst, Deutsche Bank

Q

Nice one. And I guess I mean – and do you think this is sustainable, I mean it's your view that the world is now more digital and so these kind of – this – we're in a new paradigm and this is, I guess, a sustainable tailwind is that how we should think about it?

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

A

First, let me share how we think about it right. More and more consumers will be moving their lives online and there will be actually an overlap between your physical life and your digital life. And today when we talk about cybersecurity in 90-plus-percent of the cases people think about enterprise security or vendor specific security for their specific application. But when you're a consumer you don't really worry about which vendor provides what type of security, you want to be fully protected overall the same way that you have an insurance for your entire set of assets and you want to have it that way.

As we return to growth, we know that the potential is basically that every consumer on earth and we citizen on earth has that ability to live their digital lives in a safe environment and safe includes protection upfront, education and prevention all the way to restoration and insurance protection. And today with 7.5 billion on earth and we only have 20 million consumers, so we feel that the structural growth opportunity as we develop our portfolio, as we launch into new market will enable us to continue to grow.

Now you first need to walk before you can run, the division for 10 years under Symantec was run more as a profit maximization division as we became a company launch Norton 360 we invested into marketing, we've returned the company to what we call a low to mid-single digit growth rate that is still our view that as we build up the portfolio we are on that path. Last quarter with COVID-19 was a little bit of boost, and frankly at least a structural step in term of understanding the need to have cyber protections when you're a consumer out there.

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Patrick Colville
Analyst, Deutsche Bank

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Got it. That's very clear. I just want to make this to our listeners as interactive as possible, so if you've got any questions please post them to the chat boxes or alternatively why not email me, if that's easier just patrick.colville just C-O-L-V-I-L-L-E at DB.com so patrick.colville@db.com or the chat boxes any of our audience have you any questions? So switching gear, I think the kind of key question on many people's minds is NortonLifeLock versus McAfee a vast and competitive environment. So I think it's kind of key to for us understanding that what differentiates NortonLifeLock versus those other vendors?

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

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Yeah. So let me go back and how today the market is being described and no one is really backward looking and how we look at the market, right. So you still have part of the overall market dysfunction, the core pillar of security and that's very endpoint-centric protecting you from endpoint perspective, maybe expanding from antivirus to maybe a password manager and a few other functionalities with endpoint-centric.

Then you have a second pillar, which is identity, and the identity it's not more user-centric, it's about giving your ability to understand the attributes that matter to your identity, in the US it could be a social security number, it could be a credit report, digital identity numbers [indiscernible] (09:45) those are attributes and you want to make sure, they're fully protected and that you can control them.

Then you have fragmented and new emerging pillars around privacy, connected home and families and those have new fragmented applications that could become big or not and there will be a lot of innovation in those spaces. So with the approach we have is we're really building up an integrated portfolio that addresses all of those pillars to build our vision of Cyber Safety. The day those four pillars which I think they are going to start merging, where we could add new pillars to that overall platform. So, our vision is really to run as fast as possible to offer a fully integrated solution to have Cyber Safety or peace of mind from a cyber-perspective for every consumer and citizen on earth. That's our objective.

Now, when you compete day-to-day, if you're someone that's more obviously focused on security, you're going to maybe compare Nortaon, McAfee and Avast. If you're more focused on identity, you may compare one of the Equifax or Experian and us. If you're focused on privacy, there's a few applications. If you're focused on connected homes, there's a lot of products. And I think the way we differentiate it is towards that integrated platform.

Patrick Colville
Analyst, Deutsche Bank

Q

Okay. That's very clear. I got a question from one the audience members about specifically these kind of competitive dynamics with the freemium models, I mean is there any color you can give us around, how you see NortonLifeLock will compete against those premium vendors would be interesting?

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

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Yeah. Well, at the end of the day, every company has to be able to charge for the innovation and make a profit and that's the capitalist system and then they reinvest that profit to continue to grow their innovations and build up on the R&D and build up on the portfolio. How you get to your funnel whether you use marketing dollars and get the consumers to download the applications on your platform, and then, immediately subscribe, which is the

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Norton model. And it's one way. And we continue to invest into R&D and we have a premium from a functionality perspective.

You have another distribution model, as you know, which is more like OEM, you partner with OEMs and you load your applications on hardware manufacturers, and then, at a time of you getting an endpoint device, you can convert or not. And that's the McAfee model and it works well when PC is up, it works less well when PC is down. And for us, it takes a little less well because we've become really user-centric versus pure hardware-centric.

And then, you have another model there could be freemium, a lot of startups are offering the application for free. It's about touching more people, but you still have then to convert them into the premium subscription or the premium price to be able to support and fund your innovations. So, at the bottom of the market in the value, you will always have functionalities that become more and more commoditized, and that becomes free. We offer those functionalities in the lowest level of our membership, but we always add a few functionalities that are innovative and competitive to be able to have our customers that pay for solutions.

Patrick Colville
Analyst, Deutsche Bank

Q

Okay. That's very clear. And another question we've got and it's about something you mentioned earlier that you have increased marketing spend, both I guess in the US and internationally. And so, the question is, what you've seen your competitors do to react to that – have you seen your competitors change their strategy as it relates to marketing and take similar actions?

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

A

Look, we're not really obsessed by what our competitors do, we're obsessed about the building up the portfolio to address the consumer needs towards that new vision of Cyber Safety as one membership fee you get fully protected in all of your digital activities. So that's our core focus. As you know and as I mentioned, the vision NortonLifeLock as part of Symantec kind of reduced their marketing spend as they were maximizing their profit and focusing on other priorities within the company when we became NortonLifeLock a standalone company, we basically returned to the level of marketing there were pre-acquisition of LifeLock. And with that as you've seen for the last three quarters, we returned to growth, we turned around the customer decline to a customer count growth and are really focused on that.

For sure, for years probably our competitors we're enjoying the fact that in the consumer space we're not as dynamic as we could have been and now they see the difference. We are somewhat reinforced towards our vision when we see that many competitors are trying to bundle functionalities or are trying to create an integrated platform. We kind of know that we underwrite that.

Patrick Colville
Analyst, Deutsche Bank

Q

Got it. Yeah. And so, another question has come, again, time in double-clicking what you mentioned earlier, it's about – the customer adds, there was 400,000 customer adds last quarter and the investor is asking can you provide us some context ideally quantitative on how much of that was COVID, and is this one-time effect, and how much was it – is it possible to quantify how much you think is, I guess, other factors that you talked to?

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

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Look, I've been a CFO for 10 years, so I can model and spreadsheet and put numbers behind every reality. So I can do that if you want for last quarter. We said when we became NortonLifeLock back in November, that we would reinvest in marketing supported by the launch of Norton 360 in 43 countries, we would return to first low-digit growth rate on the bookings level, and then, post-transition, a mid-single-digit growth rate. And then, for the first two quarters, we delivered a booking growth of about 4% and a customer account growth of around 100,000. Last quarter, Q1 – fiscal Q1 for us, we delivered a building growth rate of 7% in constant currency and a customer account growth of about 400,000.

And so, we believe that our changes will take time – over time to get the maximum productivity from a marketing perspective to support those marketing investments by continuously innovating into new functionalities and converting more members to Norton 360. We believe at this point in time from what we can see that we can sustain a mid-single-digit growth rate. And we guided the Q2 quarter, the current quarter, [ph] back at (16:55) earnings, we guided 3% to 5% on the top line revenue guidance.

And so I would say, that's our structural improvement [indiscernible] (17:06) you may have plus or minus 1%, but we are on that path. And therefore, if last quarter had a boost on COVID, you take whatever number you want, four or five or three, minus the seven we delivered, and I would say that was the impact from COVID.

Patrick Colville
Analyst, Deutsche Bank

Q

Yeah. That's very clear. And going along with that chain of thought, has COVID led to any noticeable share shift, deltas, or competitive dynamic changes that are worth calling out?

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

A

Yeah. I don't think we've seen a change in competitive dynamic. I think the COVID awareness if you want or the COVID – the awareness created by the COVID pandemic and more of the activities moving online has realized from a consumer standpoint that we need to fully protected from a cyber-criminality perspective. And I think various companies benefit different ways and you saw our results. I don't think that has changed the competitive environment.

I do want to step back again. I'm not trying to avoid the direct questions, but none of our competitors or us are really competing on the core AV market, right? We all are moving towards more of that cyber safety vision and we feel really good about the integration of our portfolio, our ability to add new functionality to that [ph] input integrated (18:43) platform, and based on what's happening in the market, the ability to then tailor the marketing messages to the new functionality we launched.

Earlier this year, we launched the ability to have a home title alert in the US. And we saw 1.8 million of our members actively looking at those alerts. And now, the ability to message that functionality at different levels of membership to the consumer is a new one. And as you know, the housing market is getting very strong and finding new areas where we can educate the consumer on that functionality is a new one.

In July, we launched a gaming edition. And gaming edition is not for the core AV characteristic that you may hear from some of our competitors. For us, it's really about now providing gamers the ability to have their gaming identities to which they have attached virtual asset that they bought with real cash. To have those gaming identity being monitored in the dark web and alerting the gamers, when their credentials might be compromised in the dark web.

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And so, as you see, the real race, if you want, is to build up that cyber safety portfolio. We have tons of ideas in our labs, in our R&D teams, in our product teams continue to build up on that overall. And ideally, at one point in time, people buy a cyber-safety membership the same way that you buy an insurance when you buy a car.

Patrick Colville
Analyst, Deutsche Bank

Q

Yeah. Okay. And I guess, that's pretty clear. So probably worth talking about the channel strategy, you alluded to this earlier, but there are numerous channels in this space that direct that's kind of via telcos, that's via PC and device OEMs. So just talk me through to help me understand, I guess, audience how – which channels you think are most, I guess, the richest scenes and has that changed? Will that change? I mean, color there on the channel would be fantastic.

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

A

Yeah. So the first one to understand is we have about 21 million customers that directly download their applications from our website in that we are directly in touch with. We support that with marketing materials to educate them on the various value of the product, if you want. And that's a very important one, because it's enabled us to be very much user-centric application-based, something that matters to you like, for example, understanding which one of your personal data is on a website or on the Internet being sold by data brokers.

Upgrading then that functionality with the ability for you to delete those or automating the deletion of those data and part of your membership having the ability to keep those records clean at all times, that has nothing to do with your endpoint or which device you use, it has to do with you, your data, your digital identity being on the web.

And I think that direct relationship with our consumer is a very, very important one [ph] as we go through (22:08) our vision. Then, we have about 30 million of customers that are in touch with our products, with our brand through an indirect channel, whether it's, as you mentioned, telcos, it could be employee benefits. So employers can offer that as a basic benefit as part of the benefits programs. And so we have a set of partnership, if you want. We signed TELUS in Canada to push NortonLifeLock in Canada. We signed a marketing partnership with ARP and are providing an upgraded level of support for senior people that may need more help as they understand or learn about the product. And I think building up more on those partnership will be an important part of our strategy to be able to scale faster.

Patrick Colville
Analyst, Deutsche Bank

Q

So, yeah, that's all very clear. So, I guess, let's probably switch gear to more of the numbers now. You were CFO for a long time, [ph] so you'd be doing (23:18) injustice not talk about the numbers. So the elimination of the stranded costs was, I guess, something that was a major, I guess, [ph] if you want,(23:28) an investment cases for NortonLifeLock, how is that going? And how are also the proceeds from the sale of underutilized assets coming along?

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

A

I think, Patrick, when we met in November in London a while ago, you did not believe we would take all of this stranded cost out. So you're now nine months later, yeah, that's a on record. And you were like many investors saying, hey, you know, there will be these economies of scale, if you want, reduce the scale of the company economies; all of the costs you have to absorb, some of the infrastructure. We have taken all stranded cost down

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to the penny out of the company. We were very disciplined in doing that. To be totally [indiscernible] (24:12) it was easier because as I had told you, we sold the revenue [indiscernible] (24:17). So it was a question of just discipline and making sure you can handle the risk that you took the cost out of [indiscernible] (24:24) to the enterprise business.

So in August, we wrote off the last ERP or eliminated the last ERP that was in duplicate. And we're now done from a stranded cost perspective. And so this quarter, Q2, we'll have the last write-off and we expect Q3 to be a thin quarter. How do you measure it as investors? Very simple. We committed to return the company to 50% operating margin. And they were driving the consumer business at 50-plus-percent margin. We still had a little bit of stranded cost in the last reported quarter, and will be done by Q3, that is the December quarter.

We'll be done with the transition. We also transitioned all of the executives that were not directly linked to the consumer business. And we've upgraded the leadership team, if I can use that term with people coming from the consumer space. So we have a new Chief Commercial Officer who is coming from PayPal, Robert. We have a new CFO, as you know, Natalie coming from eBay. We hired a new CPO Gagan who is coming from Avast, and myself from Logitech. And we have a few other executives around that have all consumer background. I think there will be a very good – great team to drive towards the vision I described.

The last piece of this overall transition, if you want, was to reduce the assets that we had on the balance sheet. And the biggest of those were the buildings. We sold a few assets, sold one building and we still have about $600 million of real estate that we are selling. Obviously, there COVID-19 slowed down as you know in commercial real estate market dried up at one point in time back in March or April. In July, we sold the first building in Los Angeles and we are in discussions with various interested parties for our various buildings here in Mountain View.

So that's – we'll find the right balance between value of price, if you want, and timing. Those buildings do not impact the cost out of P&L. They are held for sale on the balance sheet. And we'll make sure that we consider both time and value.

Patrick Colville
Analyst, Deutsche Bank

Q

Good. And I think we're running out of time. So I've only got chance for one more question. But it's around the capitalization, and so paying down debt versus paying dividends, any color you can give there on your – on the way that your thinking about the capitalization and the financial profile.

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

A

Yeah. When we talk about capitalization, let's first recognize, I know many investors know that we're very – at a high margin very low CapEx intensive. We really generated a lot of cash, $900 million free cash flow on an annual basis. We have about a third of that free cash flow assigned to our regular dividends, which at the time of the separation, we doubled from $0.25 a year to $0.50 a year.

And at that point in time we said, hey, we're going to have a buyback in place opportunistic buyback as we see disconnect between our short-term, midterm forecast and the value – discounted cash flow value, we'll buy more stock. And then, of course, the number one priority now that we have finished the transition and we've shown that our strategy is working, our execution has improved, I think we now have the right also to look at tuck-in acquisitions and completing the portfolio both, of course, organically but inorganically as well.

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Patrick Colville
Analyst, Deutsche Bank

You heard it here first. So with that, thank you so much for your time, Vincent Pilette, CEO of NortonLifeLock. Thank you for joining us today at the DB Tech Conference. Really appreciate your time.

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

Thank you.

Patrick Colville
Analyst, Deutsche Bank

Have a great day. All the best.

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