

Company Name: Synchronoss
Company Ticker: SNCR US
Date: 2017-03-06
Event Description: Raymond James Institutional
Investors Conference

Market Cap: 1,219.42
Current PX: 26.51
YTD Change(\$): -11.79
YTD Change(%): -30.783

Bloomberg Estimates - EPS
Current Quarter: 0.388
Current Year: 2.521
Bloomberg Estimates - Sales
Current Quarter: 172.778
Current Year: 814.889

Raymond James Institutional Investors Conference

Company Participants

- Daniel Harlan Ives
- Daniel Ives

Other Participants

- Tavis C. McCourt

MANAGEMENT DISCUSSION SECTION

Tavis C. McCourt

All right. I think I'll get it going here since it's 1:40. So, good afternoon. This is Tavis McCourt, senior technology analyst for Raymond James. I'm very pleased to have with us today, Daniel Ives, who is the Senior Vice President, Finance & Business Development, at Synchronoss.

Synchronoss is undergoing a reasonably substantial transformation of its business. In the last several months, sold off a legacy business process outsourcing business and purchased a software company called Intralinks. So, it's kind of déjà vu with the stock, was in a very similar position last year at this time with this conference for a lot of similar reasons.

And so, this is going to be mostly a Q&A session. I'm going to hand it off to Dan initially to kind of have some initial thoughts on the business, and then I'll pepper him with Q&A after that. Go ahead, Dan.

Daniel Harlan Ives

Yeah. Thanks. And hello, everyone. So, instead of doing a normal presentation, I thought it'd be a better serve to I'm just going to speak for a few minutes and do more of Q&A. I think there's a lot of confusion since December 6 when we divested a major part of our activation business as well as we bought publicly held Intralinks.

So, I really wanted to use this, and Tavis and I talked about this. This is really more of a Q&A and really to go through not really just the past year but more of the sort of the vision as well as any questions in terms of why we did what we did, any questions about the acquisition, the divestiture, what we have left, growth, whatever may be.

So, I think, it would maybe serve everyone, especially ones that don't know us, about a year-ago when we sat here, we had really two businesses. There was a traditional activation business which that was our original business.

Think about it like AT&T, iPhone started in 2007, the activation process, that's essentially what we did. That was outsourced to us. We got paid per handset. That was a big major – I will call it a growth business that really started to see sluggish growth the last few years, and I would characterize margins in that business that also started to come down. But that was our original business on activation, 40%.

Starting 2012 is where we moved to cloud. And when I say move to cloud, view us like we're essentially an iCloud for Android. Verizon was the first major carrier to go with us in terms of Verizon Personal Cloud. That's a white-label solution where we really power that solution, and the best way to think about it is that carriers face increased competition today with churn and over-the-top providers, and this is something that – especially with Verizon getting them back [indiscernible] (02:56) on this cloud start off as zero in revenues, and since then, it's done over about \$1

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billion over in revenues since 2012.

And we sat here a year ago, Verizon, we just had them on personal cloud. Today, on Verizon, we're not just personal cloud, but we're enterprise, as well as we're a big part, a major part [indiscernible] (03:19) of Exponent, which got announced in conjunction with Mobile World Congress.

American mobile, today, now we have on cloud BT. We talked about AT&T as well as Japan, which we really got original through the Openwave acquisition. That's something that we took now to what's over \$100 million in bookings.

So, in late 2015, we had an enterprise business that we started off. That was through strategic partnerships with Goldman as well as Verizon. The thing about that like BYOD mobile security trend. And now it's going to be something where there was going to be a third leg of the stool. We start to see a lot of success with that last year and starting in about mid-2016 is where we really decided that we need to go from a scale and scope perspective on enterprise, especially through an acquisition, and that's where we started our process ultimately which would Intralinks which we could go into more in terms of the merits of the acquisition.

But at the same time, our traditional activation business, which at one point was primarily software driven was becoming much more, I'll call it, BPO services driven. And what was happening there is that business model was changing and we're in – as we went through that strategic process, we decided to really divest that piece of that activation business, we'll call that BPO business, as well as some other non-strategic businesses.

Through 1Q, 2Q and 3Q as everyone saw, since, call it going back to a year ago, we had what I would call a pretty strong performance, especially on cloud as that was ramping. And I think where a lot of the confusion actually start is on December 6 when we divested a major piece of our activation business, really that BPO piece choose sequential technologies, which we could go into. And then at the same time, we acquired publically-held Intralinks and to add more, we'll call it – to add more moving parts, our CEO became active chairman, and the CEO of Intralinks became CEO of Synchronoss, Ron Hovesejian. And since that our CFO is also changed and John Frederick was announced CFO last week.

So, I think this will be an important form to sort of answer questions about not just where we've been but where we're going, the evolution, and I think it really started with – at Analyst Day in mid-2016 quarter, seven, eight months ago. We talked about our business at that point was 95% plus carrier. It was 10% international. We had two customers which were 70%, 75% of revenue, Verizon and AT&T. And we talked about in our past \$2 billion in terms of diversification getting less than 50% from two customers, and we could say our top three customers today are 35% international, 10% now north of 25% and an enterprise which was \$10 million of revs will now be, say, close to \$300 million. We talked about being north of \$100 million.

It was a major evolution of our business. It's a lot of moving parts. As you could see by the reaction from – from investor reactions since. And there's a lot of confusion. I think some understand the vision. And also, others that have been through with us and perhaps has been there, when we went from activation to cloud, people thought we are – that was the smart move and the stock reacted accordingly.

Ultimately, that was probably one of the best strategic moves we did on cloud. When we went from cloud to enterprise, I think there was a similar move in terms of the joint ventures of the strategic partnerships. And here it is, we – I think we're back in one of those situations where we really need to prove ourselves out, answer any questions, and really again investors are comfortable with the Synchronoss 3.0 vision where we are today and why we did it.

So, Tavis, I'll stop there.

Q&A

<Q - Tavis McCourt>: Can we start out – maybe you want to talk about [indiscernible] (07:44) first one on the back that a [indiscernible] (07:45) it was kind of the pro forma number, it doesn't look like a whole [indiscernible] (07:49) decision, kind of forward-looking cost, kind of 20%, 25% operating margin. [indiscernible] (07:52-07:55) but we sold this for like 3.5 times, 4 times EBITDA. So, tell us why [indiscernible] (07:59)? What was the logic behind that? Tell

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me, on the surface, [indiscernible] (08:04)?

<A - Daniel Ives>: Yeah. And, I think, it's a fair question. I think what was also happening is that that was becoming much more services-based, right, where that was going to – especially going to this next year or two is going to be one that was going to require a lot of central CapEx. We would have to really build out potentially some more call centers, potentially in third world countries. And it was one of those two where there was a lot of expenses associated with that business that you see in 2016 that subsequently has been taken out of the business.

And, I think, that's something that's very important to understand about this business is that there is the BPO business. We have some other remaining pieces of activation that were classified as activation which, per our 10-k, we've sort of broken out in terms of cloud analytics as well as some activation APIs. But, I think, really to your point, that was one where the expense profile there was continuing to go south in terms of the amount of expense we're going to have to put in there. And fundamentally, strategically, it was really a decision by the company where we are heading.

We felt like we are in a position of strength on cloud in terms of where we were a year ago versus today, where a year ago is basically Verizon. Today, we have tremendous amount of more what I would call shots ongoing. I think anyone that was with us last week in Mobile World saw that. And it was one where, on enterprise, there was a view like that was going to be an opportunity for us if we made the right acquisition and, obviously, Intralinks is what we thought and I can walk through the merits there in terms of why that made sense.

<Q>: Great. And talk about sequential...

<A - Daniel Ives>: Sure.

<Q>: [indiscernible] (09:50-09:53)

<A - Daniel Ives>: Yeah. So, this is something – and I know for investors here on the webcast that might not know the story. It's an important point I want to get across. So, sequential technology who we sold that this BPO piece was originally Omniglobe.

Now going back, Omniglobe in 2003 was our founder now Steve Waldis, as well as a number of other, let's say, tech-focused partners put together Omniglobe. And Omniglobe was really a BPO in 2003. We were small start-up. We fell like we went to another BPO. We really couldn't control our destiny. So, that really started that Omniglobe starting in 2003, 2004, 2005 as we are going into the IPO process. It all lose any relation to Synchronoss and Omniglobe was that anyone at Synchronoss sold at-cost basis their shares to Omniglobe.

So, there was no related party between Synchronoss and Omniglobe. Omniglobe ultimately did a merger with an Indian outsourcer. They had other new investors that came in. There was no relation. 2006 was wasn't really a party. For 10 years, Omniglobe ultimately became a big BPO, add AT&T there were partners of ours when we went through the strategic process of selling the activation business. And I think there's been a lot of questions out there in terms like why sell it to a cheaper, in terms of the view there. I think what's important to understand that was a process where we shop that out there around. We had multiple banks. We had a fairness opinion. We also as we shop that around, we had some that declined that they had no interest and others where we felt it was obviously a price that was less. Now, when you look at the why would it be that value, that, with the vast majority of that asset is one customer, AT&T, with a contract that renews in 3Q 2018, that was primarily BPO based. I remember this is a [indiscernible] (12:17) process. It had to be AT&T approved or the AT&T driven process. So, when it came to Sequential which ultimately through new investors formed Omniglobe, formed Sequential. We have a 30% ownership in Sequential where we plan to sell that piece as we've discussed ideally in 2017.

That's what's important to understand about that process, is that it was not a related party. I remember it hasn't been a related party since 2006, arm's-length transaction. There is a history there with Omniglobe and I think from an investor perspective, it's very important to everyone understand that especially in the telco world between AT&T, Verizon ourselves, there's a – it's a very small society. Omniglobe is a big BPO of our, big BPO of AT&T. It made sense not just strategically but financially for us to sell it. And I know there's been disappointment in terms of that price. But the only thing I could tell you is that we ran that process, that's a process through our board and into the [ph] fairness

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(13:26) opinion.

<Q - Tavis C. McCourt>: Great. And let's talk about the pro forma number in 2016, 2017. So, as you look at it, what did the cloud business, the traditional [indiscernible] (13:39) on cloud business [ph] throughout (13:40) in 2016, rough number [indiscernible] (13:43) guidance was \$530 million [indiscernible] (13:47).

<A>: Yeah, let me hear another point here where acquisitions are a key part of our success. I mean, this is something that's important to understand. You go back to the FusionOne acquisition that we did in 2010. Verizon and their cloud initiative which is worth of \$1 billion so far that we've done plus of that. That was – a core of that was in that acquisition. You'll get app secure in the AT&T relationship. You will get open way this past year. In terms of Japan, we are nowhere with Japan. Now it's 100 million plus bookings. So before gains to growth, it's important to understand in terms of organic, in terms of acquisitive growth. We view it as – think about our distribution channels, our partners, our products that they touch.

We're constantly looking at assets to put in there. And if you look historically, those have been a key part of our success. So when you look at just core growth for 2016, and this is something where we went to great lengths in the 10-K to kind of put a bridge together. Because I think there's been a lot of confusion and a lot of it is – and I would say some are self-inflicted in terms of what's personal cloud, what's traditional activation that's left, and what's analytics?

And when I say analytics, we acquired a company called Razorsight. And the best way to think about what we do, we sent 3.5 billion subs and this is a big opportunity over the last year and a half where we built out and initiative, more of big data analysis pool. That really helped us in activation as well as cloud. And these analytics piece is something that, it's not just that we're keeping it. It's going to be a big initiative going forward. When you look at personal cloud growth, 2016 over 2015, the best way is apples-to-apples to think about it which we did about \$310 million in 2015. And in 2016, that was essentially, call it, \$378 million, non-GAAP. The one thing I would point out is that enterprise is roughly about \$10 million in there. So, you could take that out just to do a full, a true growth rate, on that personal cloud.

And the one thing I'd also point out is that activation, we had about 86 million of activation left. And that's our traditional activation business. We sold – which was SpeechCycle. We also sunset or are not pursuing some low margin or non-strategic pieces. So, of that 86 million, about 50 million will not be in 2017, roughly about 36 million, 37 million is what will be in 2017.

<Q>: And so, if I do the math on that, it's kind of pro forma, that \$378 million will, in 2017, [indiscernible] (16:41) the activation business. [indiscernible] (16:43) activation that is sitting around roughly the service fee and license fee, some sequential [indiscernible] (16:51) about \$450 million or so?

<A - Daniel Ives>: Yeah. I think it's \$441 million.

<Q>: And that's where the \$530 million in 2017 is the guidance?

<A - Daniel Ives>: Yeah. And what I would say about the – that's true. That's true. And what I'd also say is that, there's a number of moving parts that we talked about. And, I think, going forward, when you think of our businesses, we have a core cloud business, which is not just Verizon and those multiple initiatives, but it's also – we talked about América Móvil, BT, and what we're doing in Japan, which we hope we could talk more about in the second quarter.

When you think about Synchronoss and cloud, don't think about it like traditional. Think about it, we're continuing to significantly evolve that platform and, I think, anyone that was in Mobile World Congress saw that last week. And, I think, as you look at cloud initiatives going forward and to carry us around the world. That's where I think we're going to be playing.

<Q - Tavis C. McCourt>: Right. And can you remind us how [indiscernible] (17:50) the overall [indiscernible] (17:52)...

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<A - Daniel Ives>: Yes. So, overall guidance was between \$810 million to \$820 million in terms of revenue. And [indiscernible] (18:00) normalized growth 13% to 15%. Gross margins were 70 to 71. The important thing to note on the gross margin is that we were really trending before [indiscernible] (18:11) somewhere about 60% gross margin. The nature of their business [indiscernible] (18:16) characterizes a high gross margin business in the upper 70s, so that benefit us in the gross margin side. And then we have upped margins 25% to 27%, and we talk about 245 to 260 bps.

The other thing that's important to note, we took a cash flow – operating cash flow on a forward run rate business about \$200 million for the combined entity. So, I think when you look at the merits of the model and [indiscernible] (18:46) what you have before you do the deal and what you did after the deal, you went from [indiscernible] (18:51) that was 95% plus to call it 65% customer contribution came down, and obviously dramatically. And when we feel what we got in Intralinks when we looked out there at acquisitions, we thought that Intralinks was typically known for their M&A business. That's where they really established their brand name.

But what you have is really essentially \$300 million of ARR recurring revenue in financials, in life sciences, they were building out through their VIA platform a very significant enterprise platform, we had pieces of our enterprise platform on the mobility side. But importantly, we had a major distribution channel with Verizon, and I think it's one of those where we felt like their product, through our distribution channel with what we already had, it was one where we were going to be able to sort of transform a vision here in terms of becoming a legit enterprise player which is something we couldn't have done as a standalone.

<Q>: So, strategically, I've always thought about Synchronoss is like, you're a company that kind of helps a lot of carriers from becoming commoditized. So, [indiscernible] (20:02) be able to see or not but they clearly are spending a lot of money on this. And so, if I roll the clock back two years ago to the kind of the [indiscernible] (20:10) the cloud business was why we're not spending any money on cloud [indiscernible] (20:15). It's becoming a little more clear now [indiscernible] (20:21) from Mobile World Congress that the monetization is that carriers have [indiscernible] (20:26). So, you're hoping [indiscernible] (20:32). Can you talk about that [indiscernible] (20:32)

<A>: Yeah. It's really a two-factor approach because you're not just storing the data in a seamless fashion and the scalability that we proved with Verizon, that's how we've gotten the success with other carries around the world. But you're really helping carriers reduce their churn, compete in an ever-difficult environment.

And from an analytics perspective, it's taking that data and helping carriers make sense of it in terms of customer data, buying behaviors, whether it's on the activation side or on the digital platform side. And that's why it's one where we felt, going into this year, we had 3.5 billion subs, personal cloud subs. As we talked about our Analyst Day, it's about 33 million going to 50 million by the end of 2017. And there was a major opportunity that we were, in mind, passing.

Now, even though we've accomplished that and now, in terms of the products and in terms of being in the right position, I think now, we have to prove, especially to investors yet again, that our vision will take hold similar to what we saw from activation to cloud or from cloud to enterprise and some of the other acquisitions and organic initiatives that we've done.

<Q>: Got it. And then on the follow-up to 2017 guidance. On your acquisition for, I guess, one is that there are acquisitions that you haven't announced yet that are included in that guidance. And number two, I feel like sometimes investors are a little confused to take [indiscernible] (22:06-22:11). So, talk a little bit about the visibility of licensed deals into the future.

<A - Daniel Ives>: Yeah. So, if you think about our business, 65% to 75% historically was recurring, 25%, 35% was licensed. Now, technically, based on new models, you could say maybe that would be upward by just based on some of the volatility that goes away on the activation side.

But what's important to understand is that large license deals are a part of our business. We view that as carriers work to invest from a CapEx perspective as they do those investments that usually signifies a bigger recurring stream that's going to come after that. If they do not typically invest upfront in some of these significant license deals, usually that might not be the best predictor of how successful that deal could come.

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So, what I would view is that historically, CapEx was a predictor where we build our CapEx. CapEx at one point is 18%, 20% of revenues. It's come down significantly because of our virtualization now called it in 8% to 9% range. But large license deals, we do expect, as we've talked about, a large license deals could come into any given quarter. It's a part of our success. It's been a part of our DNA.

Now, the goal, if you look at our model going forward and you get this [indiscernible] (23:36) as well is that you won't have [indiscernible] (23:39) is going to increase, cash flow conversion. We talked about [ph] ARR (23:43). Bookings will be something that we're going to be talking about as well.

But it's a process, and what's important to understand is that, last year, again, in the third quarter, we had a, let's say, \$25 million one-time license deal. When that comes in, it's one where that's viewed that that's something that's a key part of our business model, and it's something that usually is the indicator, like in that case that a bigger recurring stream is to follow.

So, don't view large one-time licenses when they come in as negative. And I think – and Tavis have seen it – we [ph] specialized (24:23) year and a half. It's actually been an indicator of future success.

<Q - Tavis C. McCourt>: [indiscernible] (24:28-24:38)

<A - Daniel Ives>: Yeah. I mean, look, we always have a pipeline of large deals, and what I would say is that if you look over the last year, and you've seen it in our results, we have a lot more, what I'd call, [indiscernible] (24:49) just in terms of – if you really look what's happened to the market, like Verizon was really the only one supporting our cloud initiative. If you [indiscernible] (24:59) back 18 months, give or take 12 months. Since then, as that model has proven itself out at Verizon, it's given us now a huge runway to a lot of these other customers that we talk Móvil, BT, AT&T, and especially Japan.

The one thing I'd focus on in Japan, we – and let's even go back to the Japan opportunity. International for us, that's probably been something that's been slowest to develop if you look historically. Japan, we viewed over a year ago, given the ARPU, given homogeneous consumers, given what was happening in the end market. There was a major opportunity on next-generation messaging, as well as cloud initiatives. We bought openly last March. When we did it, we bought a customer base. We bought some existing business, and that's something that we done if you look since the beginning of time when Steve started in 2000.

But openly, we talked about the major Japanese deal 100 million in bookings. We talked about that throughout the next few quarters, and ultimately we talked about winning that deal during – on the third quarter, our conference call and then subsequently in early 4Q.

<Q>: [indiscernible] (26:12)

<A - Daniel Ives>: Well – this goes to one of the things that you have to either understand about our model. That our model and part of how we started going back to 2000 is that we have phenomenal relationships, gateways, as well as products into major carriers around the world. The beauty of that is that if you take the right products, customer distribution and you acquire it and you do it right that could actually turn something into multiples of what is, which we saw with the Verizon cloud deal.

And I think you saw that openly. When we did openly year ago, people had to look two or three times the press release to make sure that we actually we're buying [indiscernible] (27:01) messaging. And subsequently now I think the biggest deal that we've won since the Verizon deal going back 2012, I would characterize this as landmark Japanese deal which we look forward talking more about in the next few months.

<Q>: [indiscernible] (27:21) if we could dive in to that a little bit more on the cloud side. So, in round numbers, about a \$100 million quarter, growing around 40% plus. That was traditionally all of Verizon business. You mentioned several others kind of world-class carriers that you guys have been talking about for several quarters. Can you give us a sense of the magnitude of kind of what's involved with the primary customers and some of those shifts? And then, what's the opportunity? Can anyone approach the scale of Verizon or is that just really a [indiscernible] (28:03).

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<A - Daniel Ives>: Yeah. I think that's a great question in terms of Verizon and the scale and scope of that deal. If you look at what happened at Verizon, Verizon from the beginning viewed cloud as that was going to be one of their major beachheads and ultimately, if you work from – as we talked about customer churn, separating, keeping customers within their network. And as that scaled, the one thing that's important to understand with Verizon, is that Verizon, we went from that initial cloud deployment to now something that's embedded in their handset and we've gotten success not just on Android as well as on iOS.

I think it's sort of been the door opener for now what we're seeing around the world. And now, we talked about helping sell Verizon to international markets with Exponent because carriers around the world have significantly looked at what Verizon did with cloud. You look at over-the-top providers, over-the-top providers, just so we're clear, when we go up against over-the-top providers, it's about we build solutions for carriers that can scale. If you look at what's a similar competition like Dropbox and others that are not white label, they don't sell into carriers. Carriers are looking to control the data, while label solutions. And, we believe, as we've talked about that Verizon is the tip of the iceberg from broader cloud deals, not just at Verizon, but around the world. In terms of cloud 1.0, 2.0, 3.0 from monetization to other ways to penetrate the customer.

<Q - Tavis C. McCourt>: [indiscernible] (29:45) some of the best carriers having their own platforms [indiscernible] (29:50) their customer data. Can you [indiscernible] (29:50) what we'd see as the value prop for consumers who've been using carrier [indiscernible] (29:54) platforms like Google or iCloud?

<A - Daniel Ives>: Sure. Sure. So, that's – the question is in regards to carriers. Why would carriers as a consumer go to a carrier cloud versus just traditional iCloud or Google or anything else. What I would say there is that the evidence that we've seen in cloud is that carriers and especially when you look in areas like Japan, the trust with carriers. There's actually more of a trust to go within the carrier network than actually some of the over-the-top providers.

I think here in the U.S., I think what you've seen you saw the Verizon, but I think what starts to happen is that once customers over years, especially some of the traditional customers have their data in that cloud. If you look at the statistics, the statistics is that there's a very good likelihood. They're not just going to stay in the cloud, but they're going to stay at customer for that carrier given that's where their information is.

And that's – look, and that's one thing and [indiscernible] (31:01) last week. I mean you see the shift from hardware to software services where really it has become like how can you enhance experience of consumers, how could you reduce churn, and that's why when carriers around the world are looking at software and services, and you look at what's happened at Verizon with that cloud initiative, that really started the trend and now we're seeing.

And what I'd also hit on just another point. I think we get asked a lot of questions about, okay, like, look what happened in activation. Activation five, six years ago it was a key part of your growth. Now, ultimately what happened in activation is that you kept a small piece but a lot of it was becoming more services and you really had to sell it because of it wasn't strategic and the margins was starting to decline. Why can't that happen to cloud, right?

[indiscernible] (31:49) rhetorically ask that. What I would say is that if you look over the last year, if we stood still that would be a problem, as we've talked about it. This is not a company that sits there on its pedestal and just continues to just do what it's doing. It continue to evolve, which is why the company went from, we call it, \$5 million revenue \$800 million plus this year.

And I think that's what we're doing on the cloud that's [indiscernible] (32:17) around monetization. That's what we're doing when it comes to some of these international messaging cloud deals. And when you look at enterprise, we – we're very well versed in the enterprise market. It's a competitive market. We know that there's a lot of vendors there. We felt that the Intralinks product through our carrier distribution with our existing mobile product was really the one-two punch that could make us a legitimate enterprise player over the next few years.

Tavis C. McCourt

Great. Thanks. I think we'll take it to the breakout room which is [indiscernible] (32:49).

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Current PX: 26.51
YTD Change(\$): -11.79
YTD Change(%): -30.783

Bloomberg Estimates - EPS
Current Quarter: 0.388
Current Year: 2.521
Bloomberg Estimates - Sales
Current Quarter: 172.778
Current Year: 814.889

Daniel Harlan Ives

Thank you.

Tavis C. McCourt

Thank you.

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