

Upwork Q2'24 Prepared Remarks

Hayden Brown, President and CEO

Welcome everyone to Upwork's second quarter 2024 earnings call.

Upwork's strong and durable business continues to deliver compelling growth characteristics on both the top and bottom lines. Our second quarter revenue reached \$193.1 million, marking a 15% year-over-year increase. Our continued commitment to enhancing profitability was demonstrated by our highest-ever quarter of GAAP net income, at \$22.2 million, while adjusted EBITDA was \$40.8 million, a 21% adjusted EBITDA margin, up from 8.5% in the second quarter of last year. We delivered this revenue growth and outperformed our profitability goals while operating in a dynamic macroeconomic environment that has become more challenging for businesses large and small.

This challenging environment showed through with softer top-of-funnel activity than expected in the second quarter. A leading indicator of this softness that we track internally is "clients seeking work," which is a measure of the number of clients engaging in an action that leads to a new contract. In Q1, this number accelerated 11% quarter-over-quarter, while in Q2, this number decelerated 6% sequentially, with particular impact in May and June along with a mix shift of active clients towards very small businesses. While we applaud the resiliency of smaller businesses outperforming other cohorts on our platform, small businesses' historical characteristics of lower spend per contract and fewer contracts per client lead us to have more caution about performance expectations for the remainder of the year.

We believe it's prudent to assume that the changes in client activity due to macroeconomic conditions that we observed in Q2 will remain for the rest of 2024, and we have factored those changes into lowered 2024 full-year revenue guidance while reiterating our 2024 full-year adjusted EBITDA guidance.

Upwork's profitable marketplace model and our continued disciplined execution provide us with a distinct competitive and financial advantage, which we are continuing to leverage. Our advanced technology platform and global, two-sided marketplace enable us to serve as the singular online destination to connect highly skilled freelance talent with clients in the full range of ways they want to work.

Our numbers also evidence our continued success in winning share from offline, analog and digital hiring and staffing sources, as we outperform broader market trends. Upwork benefits from the ongoing, enduring secular shift towards a high-quality, cost-effective, flexible alternative to traditional full-time and contingent staffing approaches. We are in a position of continued strength both on an absolute and relative basis, with growing profitability and free cash flow dynamics that reflect the fundamental advantages of our business model.

Innovation for growth continues to be paramount for Upwork, positioning us for peak performance once the macro rebounds. We continue to invest in multiple revenue and GSV growth levers to maintain our position as an industry leader and translate that leadership position into top and bottom line growth, supported by continued healthy take rate expansion. These levers include:

First, continuing to leverage Upwork's intrinsic ability to shape-shift to wherever the market demand for skills is, with a current focus on making Upwork the preeminent destination for **AI talent and work**.

Second, improving customer productivity, engagement and work outcomes in our products by infusing AI-powered features and user experiences built on Uma™, Upwork's Mindful AI.

Third, our continued expansion into our Enterprise TAM, through the right products, partnerships and integrations.

Fourth, acquiring new clients cost-effectively and at scale, by launching new distribution channels through partnerships.

And fifth, continuing to drive marketplace quality, efficiency and adoption of value-added services via our ads & monetization efforts.

I'll touch on progress for each of these GSV and revenue enhancing levers.

Based on a long track record of serving clients with access to the talent that is always most relevant for the skills they need today, clients are coming to us for professionals skilled and knowledgeable in transforming their AI dreams into realities, from building and deploying GenAI chatbots to training and tuning data and prompts for LLMs to delivering marketing or back office projects that integrate the latest AI-enabled capabilities.

Businesses are realizing the need to supplement their internal capabilities and know-how by looking externally to find talent and solutions that deliver on the promise of AI-driven productivity and innovation. This is where Upwork has a tremendous structural advantage. Compared to studies that show only 15% of corporate employees have the AI-related skills and training they need, more than half of freelance professionals on Upwork are already familiar with and using AI tools to deliver high-quality outcomes. It's no surprise, then, that a recent [report](#) from our Upwork Research Institute found that nearly half (48%) of C-suite executives have already brought in freelancers to get delayed AI-related projects back on track.

Upwork is serving a range of businesses, including leading companies like Scale AI, with the expert talent they require for their AI initiatives, and evolving our offerings to meet this growing market demand. While GSV from AI-related work was up 67% year-over-year in Q2, what excites us most is the opportunity ahead for this business and our customers.

The tangible benefits for talent on our platform who are leaning into these opportunities are compelling. As just one example, freelance professionals working on AI-related projects earned 47% more per hour than those working on non-AI-related projects in Q2.

Our second ongoing growth lever is improving customer productivity and enhancing engagement through our AI-powered product features. During the second quarter, we announced Uma™, Upwork's Mindful AI, to underpin key steps in the hiring and matching process and serve as an always-on, indispensable work companion. Our vision for Uma™ is to transform the way work is done on Upwork by more seamlessly augmenting the power of people and AI working together. Although this product is still in its early days and has launched only in select use cases, we've seen demand growing, with a 23% quarter-over-quarter increase in users interacting with Uma™ in Q2. Over time, we see Uma™ changing the game for customers, both making our platform easier to use and improving the quality of work outcomes.

We also continue to innovate our offerings on behalf of our Enterprise clients. The large Enterprise market is not a monolith, but is comprised of multiple large sub-segments with clients that prioritize their needs differently, so we have been strategically addressing that diversity of business needs. This quarter, we successfully began testing a new bifurcation of our solutions for Enterprise clients, in which we ringfenced existing functionality and pricing in one offering, and winnowed down a more limited set of functionality and alternative pricing to target a subset of enterprise buyers. During testing, this approach yielded higher total conversion for our sales team, with 46 combined Enterprise deals closed in the quarter — 27 for the new offering and 19 for our traditional Enterprise Standard and Compliance products. This dual-track approach is giving us good insights on how to move forward with modifications to our pricing and packaging to reaccelerate Enterprise growth, and we will have further updates in the coming quarters. During the second quarter, Labelbox, Builders FirstSource, and Guidepoint were among the new Enterprise Solutions clients we added.

Further advancing our existing Enterprise Solutions partnerships, this month we [announced](#) a new partnership with Beeline, one of the largest and most familiar VMS providers. We've also built on our MSP partnership with KellyOCG by enabling our first joint clients, including Nasdaq, to incorporate and access the high-quality talent pool on Upwork. These steps indicate our agility and further lay the foundation for unlocking this large market opportunity.

Historically, Upwork's primary method of acquiring and converting clients has been on our website and mobile apps, attracting them through word of mouth, SEO and paid acquisition channels. With our broad partnership strategy, we see a new avenue for cost-effectively attracting and converting new clients at scale, by embedding Upwork experts and innovative experiences for businesses in the third-party ecosystems where those prospective clients encounter the need for expertise in real time. Upwork is home to huge communities of experts in everything from GoDaddy, WordPress and website development to Shopify, BigCommerce and other ecommerce platforms to social media management, project management and a massive middle and long tail of knowledge work specialties. Our strategy is to

light up these communities of experts inside third-party ecosystems in the places where they can enable partners and their customers to succeed. The starting point of engagement does not need to be on Upwork for significant value to be created.

In the past quarter, we more than doubled our number of partner deals, and May brought the highest monthly revenue derived from partnerships that we have seen to date. Today, partnerships' combined contribution to our GSV is small, but it is growing. As we further accelerate this partner program over future quarters, we will reach orders of magnitude more businesses in prime position to leverage Upwork for their work needs.

Finally, a critical lever for us as we continue to lean into building more value-added services for customers that improve the overall quality and efficiency of the marketplace while also expanding our take rate are our ads & monetization features, including subscriptions. Q2 was a quarter of record experimentation velocity for us in this area, and we saw notable success in updates to our pricing and packaging. In the Marketplace, we added more Connects and our AI-powered Upwork Chat Pro app to the Freelancer Plus subscription, while increasing our price point to align with the additional value we are delivering. These changes contributed to our highest take rate ever, 75% year-over-year revenue growth in ads & monetization products, and a 68% quarter-over-quarter increase in Upwork Chat Pro daily active users in Q2. Ads & monetization products continue to be one of our fastest-growing revenue streams. This is another area where the progress made is significant and yet the runway ahead is even more promising.

Upwork is demonstrating our position to capture long-term growth from secular tailwinds, even while navigating a choppy environment in the near term, staying the course and executing unwaveringly on our profitability goals. We are excited to drive this business to tremendous scale, building on our formidable assets and momentum, continuing to invest in growth, and creating meaningful leverage increases every year towards our 35% five-year adjusted EBITDA target. We are thrilled to be in a position to innovate work with and for our customers, using our distinct differentiators of talent, technology and know-how.

With that, I will turn it over to Erica to review our financials.

Erica Gessert, CFO

Thanks, Hayden.

As Hayden outlined, we're excited about the strength of our business model, the opportunities ahead for Upwork, and our ability to generate durable, profitable growth in a tough macro. Our model is highly profitable, with gross margins over 77% in the second quarter, expanding adjusted EBITDA margins, and increasing free cash flow. We are steadfast in our goal to reach 35% adjusted EBITDA margin in the next five years, while increasing our operating leverage every year along the way.

Now, I'll review a few highlights from our most recent results. Revenue grew 15% year-over-year to \$193.1 million in the second quarter, and was driven in part by the flat fee pricing structure we started last year as well as sustained momentum from our ads & monetization products. Marketplace revenue was \$166.8 million and grew 17% year-over-year. In our Enterprise business, total Enterprise revenue remained flat at \$26.3 million in Q2. Within our Enterprise Solutions products, customer spend and behavior remained consistent with Q1 trends and with the current high interest rate environment which is impacting corporate spending. Managed Services revenue showed strength in the quarter, growing on a year-over-year basis, reflecting increasing demand for work product delivery and the signing of six new Managed Services MSAs in the past few quarters.

While Q1 of this year saw strengthening top-of-funnel activity on Upwork, in Q2 we saw a softening in these trends as well as a mix shift to very small businesses, which affects our average contract size. This activity is a flow-through from broader macroeconomic trends. As a result, Upwork's GSV declined 2.7% and GSV per active client declined 5% year-over-year. In spite of these temporal, macro-related challenges, we're pleased with our ongoing ability to perform better than many traditional staffing, temp services and job board companies, due to our differentiated, tech-enabled marketplace business model.

Even with these pressures, active clients were up 6% year-over-year to 868 thousand, with both new acquisition and retention benefiting us on a year-over-year basis.

Our Marketplace take rate was at an all time high of 18.0% in Q2, up 30 basis points from Q1. We are confident we have additional capacity to grow our take rate, and our approach to this is focused on pricing to value. We continue to test and experiment with a wide variety of monetization strategies on the platform, and these tests are supporting our belief that we have significant opportunities to increase our take rate in the future. As we do this, we will always balance the opportunities we see to monetize the unique platform experiences we enable with marketplace health and growth. In Q2 we saw sustained momentum from our ads & monetization products, with Freelancer Plus subscriptions growing 28% year over year, contributing to what continues to be our highest growth revenue stream.

Non-GAAP gross margin continued to improve both on a year-over-year and sequential basis to 77.6%. Non-GAAP operating expense was \$112.2 million in the second quarter, representing 58% of revenue, compared to \$115.7 million, or 69% of revenue, in the comparable prior year period as we continue to successfully reduce operating costs. For the second quarter, non-GAAP R&D expense was \$44.0 million, increasing 21% year-over-year, as we continue to accelerate our pace of innovation and invest in technology. We expect R&D to be higher in absolute dollars year-over-year, but decline as a percentage of revenue throughout 2024. Non-GAAP Sales & Marketing expense of \$43.9 million declined 22% year-over-year, and we expect to maintain a similar level of spend as a percentage of revenue for the remainder of the year. Our provision for transaction losses, or PFTL, remains low at \$1.8 million for Q2, approximately 1% of total revenue.

Adjusted EBITDA was \$40.8 million in the second quarter, representing adjusted EBITDA margin of 21.1%. Our profitable business model generated our highest quarter of GAAP net income ever and continues to

generate GAAP earnings per share growth, which includes the impact of stock-based compensation. For the second quarter of 2024, GAAP net income was \$22.2 million and fully diluted GAAP earnings per share was \$0.17 cents. Free cash flow for the second quarter was \$33.5 million, the result of the high free cash flow yield inherent in our business model. We also returned \$33.1 million to shareholders through share repurchases, representing nearly 100% of the free cash flow generated during the second quarter. Cash, cash equivalents and marketable securities were approximately \$497.7 million at the end of the second quarter.

Turning to guidance. We are providing a more tempered revenue outlook for the remainder of the year, based on the data points we have seen since May and no expectations of improvement to the current macro environment. By maintaining our adjusted EBITDA guidance for the year, we are increasing our margin outlook. This is due to the strong focus on cost discipline across our business. Our ability to produce growing margins in this environment gives us confidence in our long-term adjusted EBITDA margin goals. We believe our balanced focus on growth and profitability, and growing margins with a high free cash flow yield will produce strong shareholder returns over time.

For the third quarter of 2024, we expect to produce revenue in the range of \$179 to \$184 million, representing 3% year-over-year growth at the midpoint. For adjusted EBITDA in the third quarter, we are guiding to a range of \$36 to \$39 million, which represents an adjusted EBITDA margin of 20% at the midpoint.

For the full year 2024, we anticipate revenue between \$735 to \$745 million, representing 7% year-over-year growth at the midpoint. Contemplated in our revenue guidance are some near-term headwinds from anti-circumvention initiatives, which we expect will help improve customer experience and platform quality while stimulating long-term growth of our marketplace. We expect our take rate for the rest of the year to remain stable with what we saw in Q2. As a result of our ongoing cost discipline and the strength of our model, we expect full-year adjusted EBITDA within a range of \$140 to \$150 million, increasing our adjusted EBITDA margin outlook. As a reminder, GSV and revenue growth, and consequently adjusted EBITDA margin, are affected in the fourth quarter of this year by the fact that there are fewer Sundays in the quarter this year versus last year. Because of the timing each week when our clients are billed, the number of Sundays in any set period affects our revenue and GSV recognition in that period. Excluding this structural impact, our GSV growth rate for the year would be approximately 1 point higher. We expect full-year 2024 non-GAAP diluted EPS to be between \$0.90 and \$0.94 cents, up from our guidance last quarter of \$0.88 to \$0.92 cents. For the full year, weighted average shares outstanding will decline to a range of 139 to 143 million, down from our prior guidance last quarter of 140 to 144 million.

Our profitable marketplace enables us to achieve durable, profitable growth in the near and long term. We can increase profitability and free cash flow while continuing to invest in innovative solutions that will unlock new S-curves of growth for Upwork. Regardless of the macro environment, we will continue innovating and strengthening our position as a market leader while producing steady and significant operating margin and free cash flow on an ongoing basis. As always, I want to close by thanking our

incredible team at Upwork for their contributions this quarter and their unparalleled creativity, focus and pace of execution. I am proud to be a part of this great team.

With that, we would be happy to take your questions.