

Semrush Q2 2024 - Earnings Call Prepared Remarks

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Good morning and welcome to Semrush Holdings second quarter 2024 conference call. We will be discussing the results announced in our press release issued after market close on Monday, August 5th. With me on the call is our CEO, Oleg Shchegolev, our President, Eugene Levin, and our CFO, Brian Mulroy.

Today's call will contain forward-looking statements which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, statements concerning our expected future business and financial performance and financial condition, expected growth, adoption and existing and future demand for our existing and any new products and features, our expected growth of our customer base and specific customer segments, the continued development of our products, the expansion of our ContentShake tool, industry and market trends, our competitive position, market opportunities, sales and marketing activities, acquisition activity, integration and results of recent acquisitions, future spending and incremental investments, our guidance for the third quarter of 2024 and the full year 2024, and statements about future pricing and operating results, including margin improvements, revenue growth and profitability, and assumptions regarding foreign exchange rates. Forward looking statements are statements other than statements of fact and can be identified by words such as expect, can, anticipate, could, plan, believe, seek or will. These statements reflect our views as of today only, and should not be relied upon as representing our views at any subsequent date and we do not undertake any duty to update these statements.

Forward-looking statements address matters that are subject to risks and uncertainties that could cause actual results to differ materially from these forward-looking statements. For a discussion of the risks and important factors that could affect our actual results, please refer to our most recent quarterly report on Form 10-Q and our annual report on Form 10-K, filed with the Securities and Exchange Commission, as well as our other filings with the SEC.

During the course of today's call, we refer to certain non-GAAP financial measures. There is a reconciliation schedule showing the GAAP versus non-GAAP results currently available in our press release issued yesterday after market close, which can be found at investors.semrush.com.

Now, let me turn the call over to Oleg.

Oleg Shchegolev, CEO and Co-Founder

Thank you and good morning to everyone on the call. I am excited about our results- we had a very strong second quarter, delivering revenue of \$91 million, up 22% year-over-year and ARR growth of 25% year-over-year. We reported income from operations of \$3.4 million and non-GAAP income from operations of \$12.2 million in the second quarter. Non-GAAP operating margin increased to 13.4%, compared to non-GAAP operating margin of 3.1% in the prior year period.

We exceeded our prior guidance and I am pleased to say we are raising our full year 2024 revenue guidance. We are expanding our leadership position in online visibility and are succeeding in combining strong durable growth with improving profitability and free cash flow generation.

Our strong financials are the result of the solid foundation we have been building since 2008. Semrush started as a small group of SEO and IT specialists united by one mission—to make online competition fair and transparent, with equal opportunities for everyone.

Now, we are well positioned for the next leg of growth with the leading software platform that enables marketing professionals to build, manage, and measure campaigns across all major channels to improve their online visibility.

Our edge over the competition comes from our strong culture and history of leveraging our differentiated data to elevate the digital marketing activities of our customers.

Semrush's unique data sets are born from our own intellectual property and historical customer knowledge and the data our customers share with us. This data generates invaluable predictive insights and opportunities for customers to drive significant ROI. As we enable new ways for customers to use our data, this use itself generates additional data, and as these data sets get larger, they also grow in power, accuracy, and trust.

In the early years, we gained a strong reputation offering a single SEO product to SEO specialists and small to medium-sized businesses. Over the years, we have evolved our product suite into a comprehensive Marketing Platform focused on Search Engine Optimization, Search Engine Marketing, Content Marketing, social media, Competitive Intelligence, Local Marketing and Digital PR leveraging AI, and advanced analytics. During the course of this evolution, we believe that we have created one of the most comprehensive digital marketing data sets available in the market. And while we started our journey focused on specialists and small business owners, we now have over 116,000 paying customers, and approximately 1.1 million free active users, over 150 countries, across all industries and all market segments.

This shift from a single SEO product tailored to specialists and small business owners to a multi-product platform has been the driving force behind our growth and ability to significantly expand our Average ARR per Paying Customer by over 50% since the beginning of 2021. And we expect to continue to expand average ARR over the long term.

We believe our brand, competitive moat, data set, product offering, efficiency and profitability, and customer loyalty are stronger than ever and we continue to make new investments that we expect to further strengthen the business.

This year, we continued on our journey and focused on initiatives we expect to drive the next phase of growth for Semrush.

In May, we launched our enterprise SEO product, and we are pleased with the initial traction and demand. Prior to the launch, we already had been successful in acquiring 8,000 enterprise accounts, with over 500 employees.

In a few short months, we have closed new deals with Digital Ocean, HSBC, Royal Bank of Canada, and many more. We believe the demand for our innovative Enterprise SEO product is strong, and we are encouraged by our early traction in the market.

In addition to expanding our portfolio, we have a disciplined capital allocation approach around M&A and we believe we are well positioned to take advantage of new opportunities given our cash position.

In the second quarter, we made a small acquisition by taking a majority stake in Brand24, which we expect to extend our capabilities in Social Media and Brand Marketing.

And most recently, in Q3, we acquired Ryte, which extends our capabilities with Technical SEO, and we believe will significantly increase our average ARR per paying customer potential.

With our strong start to 2024, I feel even more confident that we have built the foundation for the future. We plan to leverage our profitability to invest in new products to extend our reach, impact and cross-sell/up-sell capabilities. These moves in concert are designed to solidify Semrush as the Marketing Platform of choice across all industries, segments, geographies and now evolving across all marketing disciplines and leadership levels. We look forward to showcasing this strategy in more detail at our Analyst Day in New York City on October 1st. I am excited to see many of you there.

I will now turn the call over to Eugene and Brian to discuss the results of the quarter and our outlook in more detail.

Eugene Levin, President

Thank you, Oleg.

We delivered another solid quarter and continue to scale, innovate and accelerate growth. Our platform is very powerful and helps marketers all over the world grow their online visibility. We are expanding our product portfolio into a comprehensive marketing platform - leveraging our innovative internal development teams, partnerships and M&A.

In the second quarter, we acquired a majority stake in Brand24, an impressive company with a strong team, and a leading SaaS platform, with a global reach, providing metrics measuring brand awareness, sentiment analysis, and collecting customer insights. The acquisition strengthens our portfolio of upmarket media monitoring products and enhances our data analytics capabilities and insights into market trends.

In July, we acquired Ryte, which is a SaaS platform that helps businesses optimize their websites to improve user experience and organic search performance. Ryte can scan websites of any size and highlight important technical and performance issues. And these insights are used by both marketing and engineering teams. They have strong traction with large companies, and we believe that virtually any large company that generates customers through their website can benefit.

We believe Ryte enables us to expand our Enterprise portfolio footprint beyond SEO and content marketing by engaging website developers within our current and prospective customer base. It is our expectation that over time, these additional features will further increase our average ARR per paying customer. We talked previously about our Enterprise SEO product increasing our average ARR for enterprise accounts by 10 to 15 times and we estimate Ryte could further extend that increase by 15 to 20 times.

We are gaining traction with both our SEO enterprise product and our enterprise go to market strategy. We are increasing the number of dedicated enterprise reps, have signed new deals with some of the largest companies in the world, and we are building out a strong pipeline that gives us confidence that our platform is resonating in the market.

In addition to enterprise products initiatives, we continue to leverage AI in our platform. This quarter, we leveraged AI to give our customers truly personalized recommendations. In keyword research, we use AI to calculate personalized metrics such as keyword difficulty. Our AI engine takes into account characteristics such as relevance, topical authoritativeness, ease of navigation and other relevant factors to create a truly personalized experience. This new feature enables our customers to identify topics that create the best potential for success to enhance their online visibility.

In ContentShake AI we can now generate different content based on the location of the business. For example if your business is near Boston you might want to highlight your special offers for Celtics fans.

These new features demonstrate how the value of AI can be dramatically increased when it is combined with proprietary Semrush data.

And of course as Google added new AI powered search engine page result elements such as AI overview, we were one of the first companies to support this feature. Now our clients can monitor their presence in AI overview snippets using Semrush tools such as Position Tracking and Semrush Sensor.

I am confident in our position in the search market and our extensive portfolio. We are seeing increased adoption of our AI products and continue to innovate and launch new offerings into the market. We are expanding both our revenue and portfolio in the Enterprise segment which helps fuel higher average ARR per customer and strong net retention. I am very excited about our ability to service enterprise customers and continue to expand our portfolio of offerings.

I will now turn the call over to Brian who will provide a more detailed discussion of our financial performance and guidance. Go ahead Brian.

Brian Mulroy, CFO

Thank you, Eugene.

We had a solid second quarter across the board. Our revenue was \$91 million, growing 22% year over year. Growth was driven primarily by an expansion of our average revenue per customer as we continue to execute on our cross-sell and up-sell strategy.

Annual Recurring Revenue for the quarter grew 25% year over year to \$377.7 million. The acquisition of Brand24 contributed approximately 2% of our reported ARR.

Our calculated ARR per paying customer grew 12% year-over-year and is now up over 50% since the beginning of 2021, with the cross-sell and up-sell benefits that come with our comprehensive Marketing Platform focused on Search Engine Optimization, Search Engine Marketing, Content Marketing, Social Media, Competitive Intelligence, Local Marketing and Digital PR.

During the second quarter, we added approximately 4,100 net new paying customers. Roughly three quarters of those came through our acquisition of Brand24.

Our dollar-based net revenue retention for the second quarter remained at 107%. We continue to believe our dollar-based net revenue retention will remain strong and increase as our more sophisticated accounts increase as a percentage of our mix, since these customers have higher net retention than our company average.

Moving down the income statement, during the second quarter we had positive non-GAAP operating income of \$12.2 million.

We reported another significant improvement in our Non-GAAP Operating Margin of 13.4%, which was up over 1000 basis points year-over-year and surpassed our second quarter guidance.

Cash flow from operations in the second quarter was \$12.1 million.

Turning to the balance sheet, we ended the quarter with cash and cash equivalents, and short-term investments of \$231.5 million, down \$11.6 million from the previous quarter as we used approximately \$10.7M of our cash balance to obtain a majority share in Brand24 and reserved another \$11.7 as restricted cash to purchase the remaining shares of Brand24 throughout the second half of 2024. We will report approximately \$9M in cash outflows in the third quarter for the Ryte transaction.

Turning now to guidance.

For the third quarter of 2024, we expect revenue in a range of \$96 to \$97 million dollars, which at the mid-point would represent growth of approximately 23% year-over-year.

We expect our third quarter non-GAAP operating margin to be approximately 11%.

For the full year 2024, we are raising our guidance and expect revenue in a range of \$373 to \$375 million dollars, up from our prior range of \$366 to \$369 million, which translates to growth of 21% to 22%. We expect the combination of Brand24 and Ryte will contribute approximately 200 basis points of growth, which would mean our organic growth would be in the vicinity of 20% year over year at the midpoint.

Moving to our guidance for full-year operating margins....while we are ahead of our full year guidance in the first half, we are maintaining our Non-GAAP Operating Margin guidance for the full year of 10.5% to 11.5% and our Free Cash Flow Margin of approximately 8% due to the following reasons:

1. First, because we are off to a very strong start to the year, we expect to make several focused go-to-market investments to help drive future growth in our enterprise business.
2. Second, although Brand24 and Ryte both have margins that are inline with our corporate average, we plan to accelerate our integration efforts to more rapidly incorporate their products into our portfolio. To do this, we expect to incur some temporary, one-time integration expenses that we have built into our updated operating margin guidance. We expect these expenses to abate as we get into next year, and we also plan to extract some synergies which should help their operating margin improvement as we progress through 2025.
3. We had some expenses originally planned in the second quarter that pushed into the second half of the year. This, is part of what allowed us to over-achieve our second quarter guidance
4. And finally, the increase in our stock price combined with changes in our affiliate ownership structure means we will transition to large accelerated filer status under SEC rules. As a result, we anticipate higher general and administrative expenses as a result of increased compliance costs.

I'd note that holding our operating margin guidance still implies that our operating profit guidance in dollars will increase, despite these components.

To help you with your modeling, I'd make a few additional comments:

- 1) We expect that the combined total of Brand24 and RYTE will have a revenue growth rate similar to our corporate average over the near term, before our cross-selling efforts kick-in.
- 2) The difference between our non-GAAP operating margin and our free cash flow margin is the result of interest income offset by capital expenditures, cash taxes and acquisition related expenses for the Brand 24 and RYTE transactions.
- 3) As a reminder, we enacted a core price increase during Q3 of last year, which we don't expect to repeat this year. This could put some pressure on the year-over-year growth rates we've been experiencing in our ARR per paying customer.

And finally, our guidance assumes a Euro exchange rate of 1.08. Approximately 30% of our expenses are denominated in Euros.

In closing, we are very pleased with our performance in the first half. We have executed well to overachieve on our top line growth and profitability, advance forward our strategic priorities and place Semrush in a strong position for our next phase of growth. We continue to remain confident in our ability to grow and scale our business, are pleased with the traction of our most recent investments and remain committed to efficient and profitable growth that drives long-term value to our shareholders.

With that, we are happy to take any of your questions. Operator please open the line for questions.