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PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to TomTom's First Quarter 2020 Earnings Conference Call. (Operator Instructions) We will be facilitating a Q&A session towards the end of today's prepared remarks. (Operator Instructions) Please note that this conference is being recorded.

I will now turn the call over to your host today -- today's conference, Claudia Janssen, Head of Investor Relations. You may begin.

Claudia Janssen - TomTom N.V. - Group Controller & Head of IR

Thank you, operator. Good afternoon, and welcome to our conference call during which we will discuss our operational and financial highlights for the first quarter of 2020.

With me today are Harold Goddijn, our CEO; and Taco Titulaer, our CFO. We will start today's call with Harold, who will discuss the key operational developments, followed by a more detailed look at the financial results from Taco. We will then take your questions. As usual, I would like to point out that safe harbor applies.

And with that, Harold, I would like to hand over to you.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Thank you very much, Claudia. Welcome, ladies and gentlemen, and thank you for joining us today.

The start of 2020 has brought unprecedented times to all. COVID-19 has impacted how and where we work, but it has not changed the focus of our company. Taco will provide further information on financial highlights later during this presentation, and I will now discuss our response to the pandemic and our key operational highlights for the quarter.

The COVID-19 impacts our Automotive and Consumer revenue, but we do not expect a material impact on our Enterprise business. Automotive revenue arises principally from vehicle sales, and they are sharply impacted by factory closures. Consumer revenue is impacted by a steep decline in demand, and that is caused by a combination of closed retail stores, retailers reducing inventory and people not driving. Recovery will depend on how quickly economic normality is restored, including vehicle production and end-user demand, which is currently uncertain.

Given the nature of our business, nearly all of our employees can perform their work from home. With health and safety of our employees and partners as the highest priority, we acted fast to enable remote working, and that has enabled us to sustain our engineered development activities

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and customer service levels. Our employees have responded well to the new situation. We are maintaining productivity, and we are fulfilling customer commitments.

The year has started well for Automotive and Enterprise orders, including new business expansions of and extensions of existing contracts, and we believe that our investments to improve our location technology products are delivering to plan. Because of our strong debt-free balance sheet, we have the resilience to maintain our course despite the current uncertainties. We are, of course, carefully looking at our cost base and avoiding expenses where possible.

In the next slide, I want to give you a short overview of our operational highlights for 2020. As I mentioned, we're excited with the progress we've made in both winning new deals and expanding on existing partnerships. One of the deals we could announce today is for our Maps APIs business in an expanded collaboration with Verizon. Verizon is integrating our Maps APIs in SDKs in location service offerings and it powers a broad range of applications and a substantial developer community.

Related to our Automotive driving -- Automated driving activities we announced early in the quarter, a successful demonstration of fast, high-definition map-building methods in a joint effort with Toyota and DENSO. At the outbreak of the pandemic, we opened up our traffic reports and APIs to governments, researchers, financial analysts and journalists to better understand the effects of the lockdowns in various geographies. The data were widely used and reported on.

This concludes my part of the presentation. I'm now handing over to Taco.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Thank you, Harold.

Let me make a couple of comments on the financials and outlook, and then we'll go to the Q&A.

In the first quarter of 2020, we reported group revenue of EUR 131 million, which is 23% lower compared with last year. The lower group revenue is mainly due to the impact of COVID-19 and the anticipated decline in Consumer. Location Technology business, which represents roughly 70% of our group revenue, decreased 11% on year to EUR 91 million. Let me go through the details one by one.

Automotive reported revenue was down by 24% to EUR 50 million in the quarter, and operational revenue was down by 2% to EUR 85 million. The year-on-year reported revenue decline is as a result of higher deferral rates in the quarter in combination with lower operational revenue following factory closures. For some Automotive customers, revenue is recognized over time based on the estimated total contract value, which has decreased based on the anticipated impact of COVID. This has led to higher deferral rates.

Enterprise revenue was up by 10% to EUR 42 million in the quarter, reflecting increased revenue from new and existing customers.

Consumer revenue was down by 40% to EUR 40 million in the quarter. Retail closures and factory closures during March accelerated the anticipated decline in Consumer, reflected by declines in both consumer products as well as automotive hardware revenue.

Gross margin was strong at 78% during the quarter, an increase of 6 percentage points year-on-year, a result of larger proportion of high-margin software and content revenue versus hardware in our revenue mix.

Total operating expenses in the quarter was EUR 180 million, an increase of EUR 46 million compared with the same quarter last year. Of this increase, EUR 40 million related to the increased amortization expense resulting from the change in the estimated useful life of the map database implemented from Q2 2019.

The free cash flow from continuing operations was an inflow of EUR 14 million in the quarter. The inflow is driven mainly by cash inflow from a stronger collection of receivables during the quarter, combined with a lower payout of variable employee expenses compared to last year.

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Our deferred revenue position is now EUR 395 million compared with EUR 369 million at the end of 2019. Automotive deferred revenue increased by EUR 37 million. Releases in both Enterprise and Consumer partly offset this increase. The deferred revenue balance in automotive is now at EUR 315 million. At the end of the first quarter of 2020, we reported a net cash position of EUR 432 million.

The share buyback program announced with our Q4 and full year 2019 results, began in the beginning of March. As a precautionary measure in the current economic environment, this program was suspended at the end of March until further notice. By that date, we have purchased approximately 2 million shares or an amount of EUR 17 million.

I would now like to comment on the outlook. As previously communicated, given the uncertainty in the market, we have withdrawn our full year 2020 guidance. Automotive and Consumer revenue were both negatively impacted in the first quarter, and we expect this trend will worsen in the second quarter. We plan to continue executing our long-term strategy and associated R&D activities, but we will take some measures in the SG&A area.

Overall, we expect that 2020, the free cash flow will be negative. We'll provide updated guidance when we can reliably estimate the duration and consequences of the current situation.

With our Q4 press release, we reiterated our midterm guidance for our Location Technology revenue and our free cash flow. At this point, it is too early to make amendments to this midterm guidance.

Operator, we would now like to start with Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we have a couple of questions that came through, sir. And we'll now take our first question. This comes from the line of Francois Bouvignies.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

I have a couple and maybe one for Harold and one for Taco. The first one for Harold is, you mentioned in the release and your remarks as well that you had a good start of the year in terms of orders. So I just wanted to know what kind of products you're talking about. I mean do you think you are gaining shares? Just to get more color around this kind of good start of the year, would be very helpful. That's my first question.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. Francois, thank you very much. Yes, we've seen substantial interest in our new navigation products for the Automotive industry. So traditionally, we serve -- our technology was mostly embedded. We're in the process of moving all of our services online for online delivery for connected vehicles, but importantly, also with an off-line full back facility. That technology is maturing nicely. And we found traction in the market for those products, and that has resulted in some deals in the first quarter of this year. And that is -- we're very happy about that and is a confirmation that we are on the right track with our product development road map.

But it's not just in Automotive, we also saw -- seen some activity in Enterprise business as well. I think the importance of the Verizon deal is not to be underestimated. It's a breakthrough deal for us. Verizon has been a customer, but they're now taking our APIs instead of uncompiled map content. I think that's an important one as well. And we see further traction for our APIs Enterprise business, especially on the West Coast. We're very encouraged by that as well. All that, in combination with long-term strategic accounts traction again in Automotive, take up of our new

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technology products that will be ready somewhere next year, for which we are writing orders already, gives us all the confidence that we need to continue our investments in the areas that are -- that we think are strategic.

Now the COVID situation, of course, is a tough one because we don't know how long it's going to take and how long it will take to fully recover from the current -- from the levels of business that we've seen before the pandemic. But the underlying business is solid and sound. And that has made us also decide to keep going where we're going, avoid cost where we can, but not compromise our ability to deliver against the product road map and our strategic priorities.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

That's very helpful. Just a follow-up on that before asking Taco my second question is, in terms of Enterprise, I mean, it's always very difficult to model, like the long term. It seems that in the last few years, you have been successful with Microsoft, Verizon, and a couple of new deals. My question is, what changed in the last 2 years after this acceleration of this within Enterprise, what makes you gaining more deals in your view?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Well, it's a number of things. They are partly commercial. I think we have good partners. We work well with our partners, collaborative, commit to, I think, that's an important part of the success. But I think fundamentally, it's the underlying technology that gives our customers the confidence that they're choosing the right partner. These are important deals. They're lasting for a long time. It's not easy to switch. So you need to deal with partners that are transparent, reliable, but are also deploying modern software technology principles and have a kind of a modern stack. And I think our map-making platform is one of the things where we have a lead that inspires confidence. There's real end-user benefit from that to be gained as well. You add it all up, and we are successfully expanding our business, both in America and in the -- and globally in the Automotive industry.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

And within Automotive, I mean, do you think you are gaining market share? And...

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes, yes, yes.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

Okay. And HD Maps, any...

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. HD Maps, it keeps going and we keep working, and we announced that some R&D work with Toyota and DENSO, where we do online, on-the-spot, immediate map making based on video and cameras on board of cars. So very, very cool stuff. That's happening and where we are maturing the pipeline and so on and so forth. But the introduction of fully automated cars has been pushed further out. So the applications that carmakers are looking for now are closer to more an increment of what we're already doing with cruise control and lane guidance and those kind of things, where HD Maps will start playing a role. But the fully automated driving car is going to take longer than we all have hoped, but the business for HD Maps will continue to develop gradually over the next 2, 3, 4 years.

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Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

That was great. And maybe Taco quickly. On the free cash flow guidance that you gave, I mean, just that it's going to be negative in 2020. I understand there is a lot of uncertainty, and I totally, yes, understand. Could you run through the different scenarios that you may experience in 2020? So without giving like a clear target, just to help us run through the drivers of the free cash flow for 2020 would be great.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes. So as Harold already explained, it's that the Enterprise revenue is relatively not affected by COVID. For Consumer, it is different because it is related to end-user demand, people driving less and not going on holiday or less than normally. And the retail closure is also limiting the accessibility of our product. For Automotive, there's a direct correlation between factory closures. The royalty reports that we receive are coming from the factory. So when cars are being shipped out of the factory, the OEMs report those royalties to us. And yes, in a period where factories are closed, our revenue stops. And if factories are producing on lower capacity, our revenue is lower. So the modeling for Automotive is directly correlated based on the number of weeks that these factories are closed or not operating at full capacity.

Yes, that's all I can say about it. And we can -- you can model every single scenario you like, obviously. But we -- yes, we are hopeful that during Q2, we see an uplift again in the Automotive production volumes.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

Okay. And any range you could give for free cash flow, like a range even if it's wide, could you provide that? Or...

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

I don't want to go there at this point, no.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

Okay. Okay, that's fair. But do you expect, for example, Q2 to have a big negative in Q2 and then unknown later? Or is it going to be more like unknown through the year, but not necessarily bad in Q2, if you understand where I'm going?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Well, Q2 will see negative cash flow. And Q4 will probably see a positive cash flow. And yes, the Q3 is a bit of a question mark.

Francois-Xavier Bouvignies - UBS Investment Bank, Research Division - Technology Analyst

Okay. You said Q2 negative, right? Sorry, I didn't get it.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Q2 is negative. Yes.

Operator

And we will now take our next question, and this comes from the line of Marc Hesselink.

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Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Firstly, I would like to come back on that strong order intake or on the strong momentum that you've seen since the start of the year. On the other hand, you also have the negative effect of where you have to adjust your backlog a little bit because of the lower car volumes. Could you indicate what currently is stronger? Is your backlog still growing since the beginning of the year? Or is it in decline at the moment?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Sorry, I didn't get your question. Could you repeat that, please?

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Yes. So if I'm correct, there are 2 things driving the backlog. One, actually, the order intake, which you already elaborated on, that's pretty strong. But there's also a negative effect on the backlog, if I'm correct, that because there are lower volumes at the moment, you also have to decrease the expectations of car volumes in the future. What is a stronger trend at the moment?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

The former. [Harold] Yes, so growing...

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

So the order intake is a lot bigger than the reassessment of the current order.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

And the big push behind that, is that new contracts or the extension of the contracts or the expansion of the contract, which 2 of those?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

All of the above. Yes, so order intake is strong that leads to a growing backlog order book.

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Yes. So there are -- so if you look at the backlog, there are 3 elements. One -- if you look at the delta of the backlog, there are 3 elements: One is the reported revenue in the period. Now that was quite modest. And then you have the reassessment of the future revenues. And then you have new order intake. Now the last one, the new order intake, is by far the biggest.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Okay, that's clear. Then, on Automotive operational revenue, to get a little bit of a feel to help us with our own modeling. What is the run rate, rough numbers, post COVID and pre COVID? Are we down like 50%? Or what kind of magnitude should we think at the moment?

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Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

For Automotive?

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

Yes, for Automotive -- the operational revenue in Automotive?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Well, the way to think about the operational revenue is that when factories are closing down, the whole thing stops. So all car factories or nearly all car factories producing cars with our software and content stopped producing cars in March -- at some point in March, and that has a direct impact on our billings. When -- so there's now talk that car factories will start producing again, albeit at a lower level. We see news from Renault, a couple of other carmakers, who are either preparing to bring their machines and their production lines online or are committed to do so already.

So we expect that manufacturing will start, not in April even at some factories, that in May it will continue. We don't expect those factories to run at full capacity, but they will slowly ramp up their capacity. We don't know to what extent the whole supply chain is affected. It's not just ours -- our components that go in, but also a lot of other manufacturers need to bring their supply chain online.

So there will be a gradual restart of production capacity. Once that is at full capacity, then we need to look at the end-user demand effects that come into place. And those are harder to predict. And what the economy will look like in 2021, of course, is still all-defining question. So from a financial perspective, 2020 will not be good, let's face it. It's impossible to call it a good year. But on product development, on order intake, long-term outlook, we still believe that we can produce a good year from that perspective, and we're fully in position to pick it up in 2021, when we hope everything is back to normal. But what the state of the overall economy will do to car demand is, of course, the \$1 billion question that we cannot answer at this stage.

Marc Hesselink - ING Groep N.V., Research Division - Research Analyst

That's very clear, thanks. Final question is the part that actually you have the feasibility on Enterprise. It seems to have a good start of the year and a nice contract with Verizon. What kind of growth rate, rough numbers, should we think for the full year?

Taco J. F. Titulaer - TomTom N.V. - Member of Management Board & CFO

Well, I think the revenue that we reported in Q1 was a good indicator for the further quarters in the year. So it's quite stable sequentially as well. And year-over-year, we see a bit of increase compared to the increase that we saw also Q1-Q1. So EUR 41 million in Q1 that is the run rate. And maybe at the end of the year, we are a couple of million higher, but it will be -- it will start with a 4.

Operator

And we will now take our next question, and this comes from the line of Wim Gille.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

Sorry, if I ask questions that have been asked before, but my line got cut off a few times earlier in the call. First of all, on the contract wins in -- with OEMs, you're referring to new or contract extensions, but more importantly, also new deals with both new applications as well as new clients, i.e., new OEMs. Can you give us a bit more granularity on where you have been winning these contracts without naming the actual client, obviously? But can you give us a bit of feeling on what type of product? Is it mainly the new software applications that you've launched earlier in the year? Or

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is it Maps? Is it Traffic, Europe versus U.S.? So that we have a bit more feeling on what it's actually -- which corners you're actually winning at this point in time.

Secondly is on Enterprise. Obviously, a lot of questions already about the growth. But indeed, it appears that you've past the inflection point here, growing double-digit rates in Q1 already coming from a strong or a high base. So what's been driving this growth? Is it the Verizon extension and some other kind of new deals? Or is it existing clients that do more work? Is it in compiled Maps or is it Map APIs? And maybe on the Map API, I've got a few follow-up questions, but let's start with these 2 questions.

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. Wim, thank you very much. Yes, it's difficult to give you a lot of detail. But I think the most important thing for us, and I think for TomTom is that those -- that we see significant deal flow now on the new technology and that is -- I referred to it earlier in the Q&A session. So we have -- in fact, we have 2 type of customers. We have West Coast customers who are kind of pulling us ahead in terms of our technology. And then we have a more conservative Automotive customer base with embedded applications, broad variety, little standardization. And generally speaking, high cost to serve per contract. Now what we see now is the new technology and these carmakers are moving online as well. They have now kind of come to the view that it is harder and harder to deliver a good end-user experience if you're only running embedded software. So we have initiated a change more than a year ago. It is time that we switch gear and put all of our efforts on online delivery of our products. And that is -- that was in time. We are now sufficiently developed in our products, that we're winning significant deals on that technology.

Longer term, this is very important because the cost to serve will go down. We get more uniformity in our product offering. The difference in what we need to build for Maps APIs and automotive applications will get narrower. There will be more commonality in our APIs and our product offering. And that prepares us for more engineering and software-driven approach to innovation with less variety, more uniformity, and generally speaking, better products. And the fact that we won those contracts in the beginning of the year for that online delivery of our product portfolio is very encouraging because it will prepare the way for better products, more mature, better user experience, lower cost to develop, more benefit of the scale we have in Automotive and Enterprise will come through as a result of that. So we're very happy that we have those early proof points. We believe that it'll help other OEMs to follow the same trajectory. And as a result, we will be looking at a business that will be simpler and with a more uniform product portfolio going forward.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

And does it also make you more effective in basically competing against Google in this particular case?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Absolutely. Absolutely. We started that development was a -- I'm not going to sugar coat it, it was a direct reaction to developments in the market. OEMs had to follow through as well. They've long been preventing us from delivering our products online because of cost. They now accept that there's no longer a strategy they can stick to and need to follow the mainstream in order to satisfy their end customer with experiences that are compatible to what you get on the mobile phone.

Now we started that development. It's taken up. There's good proof points and it's all working. And now we also have the commercial proof points that carmakers are coming to us for online products as well.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

Very good. And then maybe on APIs and Enterprise. At the Capital Markets Day, you already alluded to the fact that API is kind of the, let's say, future revenue stream for Enterprise. At least, it's a new area for you guys during the Capital Markets Day. The revenues you generated from Map APIs were still relatively limited compared to the revenues you're generating in compiled Maps. So can you give us a bit of feeling where you are

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now in that transition? When can we expect Map APIs to become a meaningful revenue stream? Can you maybe share some data points? How many Map API calls do you get on a monthly basis? And at which rate is this growing?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Yes. So the -- I think we're doing very well in the Enterprise business, and there's proof for that with deals that we did with Microsoft, of course, who are using our APIs for their Location Technology products. The new contract with Verizon is not a proof point. But there's a long way to go, especially in the independent developer route, that's where we're lacking strength. We need to improve there. And that's one of the areas that we have on our to-do list is to also make product offerings that are compelling for the independent and developer community. We have a little bit of traction there. That's clearly an area where we can and will improve.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

Very good. And then maybe on lastly, the widely publicized Huawei contract. Basically, developers on the Harmony OS platform can access your APIs now. Do you see any traction on the developer community on that particular platform?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

I cannot answer the question. I need to refer that to Huawei to answer that. It is commercially sensitive. So I am not in position to answer that, Wim.

Wim Gille - ABN AMRO Bank N.V., Research Division - Head of Research & Equity Research Analyst

All right. I understand. And then maybe lastly, with respect to HD Maps, is there any indication, or do you have any feeling on whether or not this crisis, which obviously is leaving deep scars in the automotive industry, if this crisis will have an impact on the OEM's road map towards autonomous driving? And in a similar fashion, will it impact the road map for HD Maps? And can you just remind us on kind of when the first, let's say, level 2 vehicles will enter the market in generating meaningful revenue streams on the HD Map side?

Harold C. A. Goddijn - TomTom N.V. - Co-Founder, Chairman of the Management Board & CEO

Well, I think the -- I think you cannot underestimate what will happen to the car industry at this stage, and fighting -- for carmakers to fight their way back out to position they're holding in at the moment is priority #1, 2 and 3. There's limited bandwidth now to think about the wider, longer-term strategic implications of what has happened. I think it will take some time before for the dust to settle and then to analyze what the impacts are on the longer-term road map and product development cycles for carmakers. But it's clear that this comes at a bad moment when there's a lot of transition going on already in the car industry and this is not helping. We can only hope that production will resume relatively quickly. I think there is indications that, that will happen. It will take a couple of weeks, maybe months for the whole supply chain to get adjusted to the new normal. But then we will start to get visibility on end-user demand and on the more longer-term strategic implications. I think it's a bit too early to call at this stage.

Operator

And no further questions have come through at this time, you may continue.

Claudia Janssen - TomTom N.V. - Group Controller & Head of IR

Since there are no further questions, I would like to thank you all for joining us this afternoon. Operator, you can close the call.



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Operator

Yes, ma'am. Thank you. That concludes our conference for today. Thank you all for participating. You may now disconnect.

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