Doug Garber (00:01)
Welcome to Pitch the PM. My name is Doug Garber and today I'm here with Sean Emery from Avory & Co. We're going to be discussing Zoom video communications, ticker ZM. Sean is one of my go-to contacts for anything tech related. He runs a concentrated equity portfolio and today we're going to go through the pitch of Zoom. With that, I'll turn it over to Sean and he could give you a brief introduction of himself and his firm.

Sean Emory (00:28)
Doug, what's going on? Thanks for having me today. Avory & Company, that's the name of our firm. We're based in Miami, Florida. Our firm is, we have an ethos around our investment process, which is where's the world headed? We do that in a concentrated manner, very data-driven in the way we articulate our views. And we have a portfolio that ranges from anywhere from eight to 25 holdings, usually around 14.

So again, there you can see some of that conviction at play. I think, know, very briefly, we try to fight two tales of, you know, the investment landscape, which are kind of these structural winners, who's really winning in a category that we think will define the future. And then companies that are also transitioning their business to better realign to where the world is headed. And ultimately, that's how we facilitate our views and put those into our high conviction equity strategy at Avory.

Doug Garber (01:26)
Great. Thanks, Sean. And just the title for today's episode, so everyone knows it's growth acceleration, a catalyst to unlock value at Zoom. It's a contrarian high conviction value with Sean Emory from Avory & Co. And I just want to give a quick shout out to our sponsors and partners really, and sponsors. InSync Analytics helps build our models and does our work with their outsourced custom analyst team. If you want a copy of the Zoom model, please just contact me at

learn@pitchthepm.com. I'm happy to share the model that we built together. And also AlphaSense has been very helpful by sharing their product and gives us access to their search engine, their lead in AI that helps, you know, helps shave a lot of time off our process. And also their expert network that really lets us dig into what former experts on Zoom have to say and gives us lot of insight and extra conviction in our thesis. So.

big thank you for them for providing and sharing their leading edge research with us that allows us to put on what we believe is the best video podcast. With that, Sean, we're gonna go into our 10 step variant view process. The first question here is what actions do you want your PM to take?

Sean Emory (02:45)
Yeah, you know, obviously, you know, we have pretty high conviction on Zoom. You know, anything in our portfolio we have high conviction in. So I think that's, you know, speaks for itself when you run a concentrated book. You know, the view there is simply we think Zoom is a best

in class enterprise software business. And the today's valuation does not reflect that. It reflects something, you know, quite the opposite. Enterprise software historically, you know, gets somewhere between, you know, a

15 at the very low end at a low growth company on a cashflow basis, enterprise-valued free cashflow, say, to anything north of 30, 40 times. Now, that's partially an extreme when you start to lump in some of the best-in-class enterprise companies like the Microsoft that also incorporate their cloud business, which is fast-growing and high margin.

But generally speaking, our view is that Zoom is an accelerating growth story. I don't mean accelerating to 20% plus, but something that is much more manageable and fruitful for investors going forward. There's a lot to it. It's going from a single point solution to a product or to a platform. And I think that's ultimately how you get from A to Z in this investment.

Doug Garber (04:01)
Great, thanks. And just a quick overview for everyone. The price, it's December 24th here, the day before Christmas. The price is about $85, $86. The market cap of Zoom is about 26, 27 billion. Enterprise value is about 19 billion. They've got 7, 8 billion of net cash and it trades 3.26 million shares a day. So a lot of liquidity there and that's just a quick overview. You know, one of the reasons I decided to go with Sean on

for Zoom is when you look at the shareholder owners list, and this is something I usually look at at the end of the process, but I decided to bring this slide up to the beginning is Sean has, he runs a concentrated portfolio and as a percent of his holdings, he had the highest conviction and not by saying it with his words, but by showing it with his actions, his percent of portfolio is very levered to Zoom.

The founder obviously owns about 7%, 8%. There's a couple other concentrate active funds that own a good amount. Lane Generational is about 7. Newland Capital owns about 2 % of their portfolio is in this. And then you have the diversified active players, the Fidelities, the T-ROs who own a lot more, but it's a tiny percent of their portfolio. 20 bips at T. Rowe, 0.05 at Fidelity. And then like most stocks, the passive index guys are most of it are the quads who don't know too much about the actual products.

but are just buying it. So from a fundamental perspective, you know, Sean really stood out to me on his conviction on his weighting in his portfolio. That's really, at the end of the day, the most important thing is, you putting your money where your mouth is? And that showed me his conviction. So that's why I thought Sean would be a great candidate to talk with here. And I also just want to give a quick, quick background here on the next slide. We're kind of just going through the overall chart.

Sean, do you want to walk us through kind of what happened to Zoom over the last five years into the pandemic and then out and what's going on now?

Sean Emory (06:04)
Yeah, know, lots happen. Obviously, you know, this was a story that was a, you know, COVID darling. You know, it really took over, you know, mainstream in terms of, you know, the product itself, but also the brand. You know, some of this was big benefits to Zoom. You could argue, you know, some of the pull forward created some chaos internally. Rightfully so, you know, when you go from, you know, call it sub $1 billion in revenue to, you know, $4 billion in revenue, you know, somewhat overnight.

That puts a lot of pressure on your organization to then do things. So you saw some of that. So you go back to COVID, they were able to capture essentially the market. Again, in one way, this was great because it put them in the leadership at the front of the line in terms of video communication, but it also accelerated the motion of some of the competitors. So that's where you could say it was a gift and a curse at this moment in time.

A lot of free cash flow generated during that time, which is why today they're sitting on, know, north of, you know, $7 billion of cash and virtually zero debt. They went public just before COVID. Eric Yuan, the founder CEO, you know, he's been running this organization for quite a bit of time. I used to follow him when he was a private company. And, you know, he is somebody that is incredibly prudent with his cash. I think that's one of the grips that some of the investors have today in terms of what are you going to do with your cash? Now,

He's always said, and I've always appreciated this quote, is really around, "you raise money when you can, not when you need it." And he has done that. He had a bunch of cash on the balance sheet when he went public, took more cash on the balance sheet, because he could. There was a lot of demand for that IPO. Turning to 2021, 22, or 2021, let's say, this thing peaked out at 70 times revenue. This thing peaked out at $600, $500 a share.

Again, you mentioned it's $85 a share today. A lot of people got, the world's going to be hybrid or not hybrid, it's going to be remote forever. And extrapolating that view led to obviously a lot of exuberance around what Zoom could offer from a revenue perspective. At that point in time, we were not investors in this. We loved it. We thought it was great. We were getting questions from our investors.

around, why don't we own it? Anytime something goes high in the markets, NVIDIA's today and some others, you get those questions of why don't you own these things. And our whole thing was it's a point solution, meaning has a single product that is not necessarily defensible on a standalone basis over time. And then also you have a valuation that is just simply extreme. So you have a great leadership team and you go down the process, our process of leadership to business model to...

how the business actually operates to then the market dynamics and evaluation, a lot of checkboxes, but then valuation and also business model point solution were negatives to us. So we waited, we waited. Obviously the growth slowed from 350 % multiple quarters in a row down to like 80 % down to 50 % down to like single digits. And the online business, this is important part of the story, pre-COVID,

The online business was the minority part of the business, meaning online is the whole product-led growth story where you go on, you sign up yourself, they don't need a sales rep, and you become kind of a pretty easy sale for Zoom. Because of COVID, the demand for their product was so high. Obviously, a lot of people came directly to their website, signed up themselves. Online became roughly almost like 70 % of the business.

It doesn't have a sales rep. doesn't have a zoom face to it. beauty of that is it's very high margin at first, but at the same time, retention can get pretty weak at points in time. there was this moment in time where online business was huge relative to historicals, online turns at a higher rate, and therefore there was going to be some of this vacuum.

They're growing their enterprise business, but online churn, the fitness instructor that is no longer doing it online is now back in their gyms, are no longer using it. So this was like a churn that I think doesn't reflect, I think, the nature of the product. It wasn't somebody going from X to X. Then in 2022, you obviously had fears around the macro and recession. And that led to clear conversation around

what's going to happen for companies that have seats, user seats? And if people are firing employees, are they going to fire, basically you fire an employee, you fire a Zoom seat or you fire a Salesforce seat or any of these seat-based institutions. So that was one issue. Obviously, on top of that, had in a macro environment, people tend to try to bundle. And the question is, does Zoom have enough capabilities to bundle on versus going to the Teams and Googles and some of the other

peers out there. And, you know, that's kind of the story over the last several years. And I think we're now at a time where that online business is no longer the majority. It's now back to being in the minority. And since that time over the last two, three, four years, there's been an evolution in the product portfolio going from just Zoom meetings to a Zoom phone, which is one of the most successful voiceover cloud-based phone systems out there. It's a Zoom contact center, which is showing incredible promise here in the early

motion of the last year and a half to now the AI companion product, has, statistically is doing fairly well, not necessarily revenue generating yet, but we think can be. So point solution to product to valuation coming down, we're starting to way more boxes than we were four or five years ago.

Doug Garber (12:02)
Great. Yeah. sounds like you've been following it for a long time here and decided to be patient and wait for the sentiment to get a little negative on it. It's one of the cheapest in its enterprise software group at this point. It's just, guess, post COVID, it's not of interest. When I look at the

industry dynamic, can you talk a little bit more just about the overall communication, the UCAS ecosystem for video, for phone?

what the industry growth looks like and then kind of the market share in video for Zoom, Microsoft and there.

Sean Emory (12:40)
Yeah.

Yeah. I mean, the common thread of all that is communication. So, you know, they're really trying to be that communication platform. I actually think there's more, you know, want and desire to be beyond just simply call it voice or video communication or text communication. You know, that's a whole other story. It's not in the models. It's not in anything but productivity and collaboration, I think, are two other pillars to really round out their suite, their platform. But as it sits today, you know, if you go from

the video, know, zoom video. You know, this is just a meeting product, you know, one-on-one sales reps love it, know, internal loves it. It's usually an external product. You're competing against the likes of Microsoft Teams, Google Meet. Those are really the competitors today. You have obviously WebEx that has, you know, honestly done a really bad job. They were the leader in this category, same as Skype, obviously Skype's owned by Microsoft, but still did a really bad job. really, it was COVID that really forced

them to think about that product differently. And that's where Teams actually came from. there's Teams, there's Google. I think those are the two main competitors, really Teams to be quite frank. And this isn't our view. is our view, but it's based on different reports that we look at, whether it's app download share, where Zoom is still the clue leader in this space. A lot of that is now plateaued. Share shifts are now pretty stable.

big rise in COVID for Zoom, then some give back as teams were starting to come out. And now you're sitting here at roughly like a 50-50 market that doesn't really move much over the last couple of years. Now that's like the meetings product. And Zoom again does a really good job of that. Now I think one important data point is we look at the Okta Business Survey. So Okta...

Doug Garber (14:23)
So you can go.

Sean Emory (14:33)
is an identity platform management provider. You sign on to all your applications through Okta. They're the leader in the space that's not named Microsoft. So they see everything. They have a full purview of what's happening at the application layer within enterprises. And every year they come out with their surveys. And what you've seen actually over the last five years is Zoom take more more share inside of Microsoft 365 accounts. So they're not losing. And this is the evidence to support the fact that we hear a lot is,

know, Teams is going to eat Zoom, Google is going to eat Zoom, but it's not showing up in any of thing that we track. And I think that's the important takeaway there. So that's like the, that's the competition in Zoom phone. I mean, Zoom meetings. Then you go to phone and phone is a different ball game. You know, it's telephony. It's really your phone for your business day to day. I have Zoom phone. Obviously, you know, we're investors, so we try to play with the product as well. But you know,

I have my device, my personal device and my office device all in the same, yeah, or profile on the same device. And, you know, it's telephony. It's your work phone, you text, you can do anything on that. You can then go from a phone call to a Zoom meeting all in one swoop. And that's important, but they compete against, you know, Microsoft's in the mix. Obviously they have their phone product. Then you have like RingCentral, you have 8x8 and some others that exist in 5.9 that are also, you know, in this space.

But then you also have the legacy players that have been around for a long time that are still the phones that connect into wires that sit inside of offices. And Avaya was a big player there. They had to partner with Ring Central. that space is still like 80 % or the telephony space is still 80 % on premise. So this is very similar to what we experience in other kind of device platform shifts going from on premise to in the cloud.

And that's where Zoom's sitting here now with a number that we think is going to surpass 10 million Zoom phone seats over the next quarter or two and putting them at the forefront of growing 30%, 40 % revenue in that category and really a leader in the phone space. The contact center, these are higher value seat dollars, meaning some organizations only have a couple of support agents or

Some have a lot, just depending on the size of the organization. And it is a place where internal employees can talk to their internal departments. So if you need help with payroll, you're going to use their contact center suite to message your HR department or something like that. Same thing for the external. So if someone's your website, browsing your website or hitting your company up through WhatsApp or Instagram or something like that, you have a clean surface to communicate with them.

Zoom phone, Zoom contact center, Zoom meetings. That's the three main pillars. Spread out across that. I think they've done a really good job at adding more value. So TeamChat, we use TeamChat, which is essentially the equivalent of Slack. It comes with your Zoom meeting license. So we actually got off Slack, even though we like it, it just came for free and it has many of the bells and whistles we need. You have their whiteboard, which is similar to like a Miro.

You pay for that on the outside. It's good enough for us to use internally. You also have Zoom Scheduler, which is a small like $5 add-on. And that is the equivalent of Calendly. So, you a lot of people use Calendly. You're paying $12, $8, $9, $12 a month for that. You know, with $8, $10,

$12 a month, you're getting meetings. You're getting team chat, which is again, you're paying for Slack. You're getting Calendly or a Calendly equivalent in Zoom Scheduler.

And then what you see is people start to migrate into phone and contact center as your organization gets bigger. That's a competitive dynamics to some extent and the product portfolio at a high level.

Doug Garber (18:38)
Thanks. So Sean, I mean, sounds like you're really intimate with this product is you guys use it and you're familiar with all the other products. When you collect the data, you know, the real bear case on this is that, what your Microsoft is essentially giving this away in their bundle for free. already has it. Why are you paying more to have zoom zoom that much better than it's worth paying for when you have something that's, you know, already included that works.

Sean Emory (19:04)
Yeah, I mean, it's a good question. It's one we think about and we try to, you know, we'll have a point of view, i.e. like that, which is more opinion than it is your fact. So like when we actually look in like the Okta surveys, we're not seeing that translate. And then from there, you can create a hypothesis of like, why aren't people leaving to some extent? And, you know, one conclusion to us is, you know, not everyone wants to sit on the Microsoft suite, right? Not everyone wants to sit on the Google suite. Some organizations have both.

And therefore, if you have both, it's hard to, you what's going to be, you know, the bridge between everything. Do you really want, if you're a competitor and you're into it, who is a customer of Zoom, do you really want to sit on Microsoft servers all day? Likely not. You know, if you're a competitor to Google, you're, you know, Uber or Lyft and you compete against Waymo, do you really want to sit inside of Google Suite? So I think there's natural desire to stay off their platforms as a competitive set. There's also the fact that, you know,

any survey you look at says Zoom meetings is the most reliable and whatnot. You also know everybody on the other side. If you're a sales organization or you're the sales team inside of an organization, you know everybody on the other side has Zoom. You don't know everyone has Teams or WebEx or Google Meet. Sometimes I get a Google Meet invite and then I kind of have to like, it signs me in through my personal Gmail versus my work account. And then where does that go to?

you know, the conversation itself. So I think there's, you know, people do what they know, what works, what's reliable, what they know is going to be successful on the other side. And, know, there's something about that. So we just look at the surveys, we have our opinions, you know, I think that is a valid opinion, but the surveys and the data just doesn't support that view.

Doug Garber (20:55)
Yeah, it's interesting that you say that, know, zoom, you know, I go back a couple slides. had zoom in about 55 % market share teams at about 32, according to Statistica. So being the

incumbent that everyone uses has that advantage. I when my see my experience is, I use Google just because when I went to tech, was only in finance. moved to Mac and Google. And when I'm used to talk to my tech friends and tech colleagues, we're using Google at seamless. When I go back to the finance world and I have to use teams.

or I send them a Google, and they can't figure it out, and we have to go to Teams, that causes a problem. But no matter what, Zoom, whenever we use Zoom, it just works for everyone. So yeah, that's an interesting point there. yeah, I use all three right now. And Teams is the only one that gives me a little bit of a problem. But I'm a little biased now towards Google, since I'm a little bit in the tech world, as opposed to the finance world. And...

Sean Emory (21:47)
For sure.

Doug Garber (21:50)
It's interesting. mean, why do people even need zoom phone? They people just use their cell phones and zoom. You don't even need a phone number anymore. It's like cut it out completely, but we'll see what people do when they go back to the office now and it's required. So the next question we have is, you know, it's a business. You understand you have a good thesis. Is it available at a reasonable price today? And how do you look at that and think about it from that perspective?

Sean Emory (22:15)
Yeah, well, like the conviction really comes, we're definitely, we seek growth, right? We definitely want something that is going to grow. And more importantly, we want the asset to grow more so than requiring the business to be some sort of breakthrough growth. But again, if you go back to our point at the beginning, which is, you have a...

We're looking for these structural winners, ones that are, we think there's, the world's heading in certain direction. The world's continuing to go to more distributed work, digital work. More of our tools are digitally based. I don't remember the last time I actually wrote something down on paper. It just sits isolated as opposed to being part of something more inside of some sort of portal. So.

There's some aspect to that. On the other side, the transformation story. I think Zoom fits somewhere between both of those where directionally, the world's a tailwind for them. You could argue the cyclical nature of the last five years, meaning we had a point in time where demand was dramatic. And therefore, they had to absorb some of this and then figure out what to do next, of all in a very highly condensed window.

And that's hard to do. we're at the core of all of those, whether it's the structural winners that are growing incredibly well, 30, 40, 50%, whatever. And then the ones that are trying to reorient their business, to realign to where direction where the world's going and reignite growth. The foundation of that is some sort of margin of safety. And you look at someone like Zoom, you have seven billion dollars of cash. You take 26 billion down to 19 or 18 billion.

You're doing $1.5, $1.6 billion in free cash flow today. You're looking at a very cheap business just looking at it. Remove your views on the business. Single digit multiples if you're using like EBITDAs and low double digit teens, multiples on a free cash flow basis. Nowhere around that. Can you look at this and say it's expensive?

The question is, what gets it going? So that's kind of the framework. You have high margins. Ironically, if we were talking about competition a second ago, this company does somewhere around 35 % margins. And we all know from business case study that if it's a competitive environment, your margins get squeezed.

that hasn't shown up. that's like another data point outside of the Okta reports and stuff that suggests, is there competition? They haven't seen that. Zoom operates their own data centers. I don't think a lot of people know that. They used to be in the cloud, public cloud, now they're on the private cloud. They have their own co-location facility, so all their data is in their own environments. But that's like a big thing and that's allowed them to maintain a pretty strong gross margin. That's allowed them to, when they did...

you know, get hit with a ton of demand to maintain margins. know, Microsoft and Google are in the game of actually raising prices. Zoom's actually priced lower than those peers. So as every year when Microsoft raises prices, there's that continued gap, which part of the growth story as well is just pricing power eventually as their platform continues to emerge. So that's kind of like, you know, some of the valuation dynamics that I think matter, which is sustainability of the actual business.

The cash cushion floor, the multiples aren't expensive by any stretch. And then it just goes back to the original question, is like, how do you get, know, what's the catalyst for this thing almost?

Doug Garber (26:06)
Yeah, it was interesting that the stock has almost 30 % of its market value in cash. That's, guess, your margin of safety there. when I looked at it, did a buyback in, excuse me, they did a follow on offer in over $2 billion, or $340 a share. And now they're buying back at 60, 70, 80, they just sat on the cash and now they're buying back at lower. So pretty smart move there. When I looked at the

you know, is it available at a reasonable price? also agreed with you. It's I got to about a 7 to 8 % unlevered free cash flow on 2025 numbers. And then it's growing about 3 % on consensus. So that gets you about 10, 11%. And then I actually deduct a little bit of stock based compensation, because they are diluting you by about one to 2 % a year before the buyback. Then they use that free cash to do the buyback. And that gets you about a 9, 10 % expected return. That's about where

It says, all right, today, the price makes sense, right? You still got kind of a cash cow for, especially for a Tech stock. Your question is what happens next? What happens in the future to change that? And I think you're starting to talk about, hey, there's a lot of potential growth from this new percent you add in video, excuse me, you add in a Zoom phone, you add in contact center. Then the key is also this online video, which is about 40 % of business now that's

stabilized at as high a churn, but it's stabilized, which means it's not detracting from that revenue growth from enterprise that you've been seeing. And, you know, I think when we were talking earlier, you're like, all right, this thing trades, you know, nine, 10 times EV EBITDA, the peers are at 30 times EBITDA EBITDA because they're growing faster. So, you know, it's essentially priced as a node of low growth stock. And, um, I, I'm just trying to sum up some of thoughts that we had, guess, right before this conversation. Well, don't know if that's on that or if that sums it up nicely.

Sean Emory (27:44)
I think it's time for you to let it.

for sure.

Yeah, I mean, it sums it up. like, I think the difference is the no growth versus low growth. Like, I don't think this is going to be, you know, a 20 % grower, you know, at any stage in the near future. I do think there's, you know, if you're trying to build, you know, the roadmap of growth, it really starts with that online business staying stable, because then you can grow off that. And then that 60 % or so of the business that's more enterprise based, that's ultimately where you're attaching

more of the extra products and services to. So you get a baseline of 40 % that's pretty stagnant. Rightfully so, that'll likely be like that forever. It's a lower cost of acquisition market. People come to the website and sign up. Enterprise business, we are seeing here as we exit this quarter in the coming weeks, enterprise business that is re-accelerating somewhere around 7 % or so.

and it's a function of, you you have the meetings business. So there's going to be like on the margin, you know, net new logos, but that's at the margin. This isn't really a net new logo story. Everyone knows Zoom and most people have already engaged with them. It's really attached rates of new products. So Zoom phone is again, only like a couple of years old, three or four years old. And, you know, that's growing roughly 30%. We forecast, you know, that's somewhere around, you know, 25 to 30 % attach rates to their enterprise business.

So if you think there's value in the product and there's value in having a platform as an organization, we should assume that it becomes more than half of their users should be attached to their phone business. I would argue more than that at some point. But if that business is doing roughly like 170, 190 million a quarter, that's kind of like the forecast using kind of a bottoms up approach, surpassing near term.

10 million Zoom phone seats. You get a business that is running around anywhere from call it 10 to 20 % of the overall revenue of the company. 15 % really is kind of what it looks like it's ballparking at. They've talked over the last year around they think Zoom phone and contact center can be 25 % in the intermediate term. Is that two years, is that three years, that 18 months? It's probably closer to three years than one year.

But you have Contact Center as well, which has a list price of $79 per seat. They just signed their largest deal ever of 20,000 Contact Center seats for a European business. They signed a Fortune 10. the evidence is starting to support the idea that enterprise is winning more attach rates across their products and services.

So have a baseline of the online business. You have a good enterprise meetings business that's seeing attach rates starting to grow. They just launched Zoom. They have Zoom AI companion, which is actually a really good product. So go try it. If you like like Otter AI or anything like that, this is already embedded. It's free, comes with it, meeting summaries. It's pretty awesome. And you're not paying for it. And then they have a Zoom AI companion 2.0, which is...

really more geared for enterprises to incorporate your actual internal data to then have a more curated AI experience, which will come with some sort of expense attached to it. So that's like that aspect. have Zoom schedule, or again, the Calendly thing, but that's at the margin as well. I do believe $7 billion of cash. As of right now, they're yielding 3% to 5% on that cash. So the barrier for an investment

Prudently so is you wait until the iron's hot and strike. But I think that'll be part of the growth algorithm as well. Whether it's going after a contact center business, a phone business, or in my opinion, some sort of productivity collaboration. I've hypothesized going after a BOX. This is just me speculating and going after that $2 billion, $3 billion price tag. You pay a little bit of premium to it. Now you control enterprise.

document management. They also have box sign, which is document signing. I think that fits into a collaboration platform as well. So, teacher on, mean, that's all speculative on my part. But that's kind of how you build the growth profile. But I think it starts with a base that's stable. And then everything above that is what's the catalyst and gives you confidence. And I think in a worst case scenario where you're like, you don't really get any growth.

You kind of own what you own, you're getting buybacks plus maybe some dividends at some point. I probably don't want to be there at that point if the confidence in the growth story is no longer there. But that's kind of how you start to build the blocks. It's organic stuff with their product evolution plus inorganic that I think they're very strategic about what they're trying to do.

Doug Garber (33:15)
Got it. Yeah. It sounds like the products that they're layering onto the enterprise is the main growth engine. Now they get something from going with the acquisitions that'll that's more accreative than buybacks. That's a little lagniappe, a little something extra. And then, you know,

I wanted to just come back to the online segment where they don't have dedicated reps and stuff. That's still called 35, 40 % of the business still turns two to 3 % a month. What gives you confidence that

that business is stable, that business won't be competed away, that it won't erode the other two growth engines, right? You have kind of two growth engines with the products and the balance sheet. And then you have this other business that it's been stable for the last two years, but what gives you confidence that it's going to remain stable and not offset some of the growth from the enterprise business.

Sean Emory (34:05)
Yeah, it's so some of the numbers they provide us plus the product evolution, I think are the two different things that that kind of like the sum of those two things, I think are a constructive view. So you have on one side, you know, they provide a data point of, their online customers that have contracts that are 16 months or higher. And they chose like 16 months because after 16 months of usage, they tend to see churn like completely evaporate.

74 % or so or 75 % of their customers and that number has been increasing over time have that 16 month contract in place. So you're seeing a bigger part of their online business have longer and longer contracts that equal a certain month count that they think is a pretty good view of a number that correlates to a lower churn after that.

They've provided that number. They've been consistent in providing it. It hasn't been cherry picked quarterly. So, you know, there's some credence to that. Now, at the same time, they have the Zoom AI companion that comes with it, where it's free. You know, have TeamChat that comes with it now. You have all these, you know, baseline product solutions that I think create a much stickier user base. And that's why Zoom Online business is now at record low churn. While it's still at an elevated churn.

relative, you know, small mid-sized businesses churn at that rate anyways. That's actually like best in class churn for like SMB So that's something to think about is like best in class churn, it's continuing to shrink. They're offering more solutions. So you should assume that churn should drop even further or at least remain stable. And then, you know, the flip side of that is again, the, you know, more and more of their customers are

Doug Garber (35:36)
Yeah, that's a lot to learn,

Sean Emory (35:58)
extending out their contract lanes even at this level. So that's kind of like if you see any of that kind of giveaway, I think that's where you can maybe be concerned about the online business. But at the same time, enterprise business is growing faster than online. So as time goes on, as long as that stays stable, online will become less and less part of the business naturally without having actual decline in that business. So we look at it closely.

you thankfully we're kind of somewhat away from it being, you know, 60, 70 % of the business.

Doug Garber (36:31)
And you talked about the value proposition there being 14.99 a month for the traditional online product suite and roughly. then now you're getting essentially a Slack like product with it. So how much does that save you by not having to also have Slack?

Sean Emory (36:47)
So Slack is what, anywhere from like, I don't know the updated list price, but anywhere from like seven to eight bucks to 14, 15 bucks if you wanted to have some of the archiving capabilities and such. So at the base level, you're talking about eight bucks a month per user. mean, pretty meaningful if you're also getting, because with Slack you don't get meetings. With meetings you get Slack. So it's it's kind of these, and then you get Miro and then you can add Calendar.

They just came out with a marketing material the other day which basically showed all of their products and then all the competitive products and then the bundled savings. And it was somewhere like for a tiny business, it was like $750 a year. I think it was per user, something like that. If you're using their full product suite relative to the competitors and you're using best in class for each. Now that's the thing as well, right? Is not all their products are best in class.

I would say I use them all for the most part. Like Miro is better than their whiteboarding product, but it's a pretty lightweight whiteboarding product that serves its purpose. County is actually, their schedule is actually a really good one. I use it quite a bit and the team chat is continuing to get better and better. So I think if Slack's 100, they're a 90, 92, something like that.

It's good. We don't have any issues with it. And then you have all this AI stuff that's embedded in there. And they have an investment in Anthropic, which is one of the foundation models out there that is big. they embed that. have one thing that's important is the head of AI for 30 years at Microsoft is leading tech at Zoom. They have like four or five people that recently have left Microsoft to come to Zoom. So there's a lot of

understanding what's happening at Microsoft, but also, I think it says a lot that they've gone to Zoom. You usually wouldn't go to that if thought they were going to, if your old company was eating this company, I don't think your natural instincts are good to that company.

Doug Garber (38:59)
Yeah, yeah, for sure. And we have, we'll talk about later, we have an expert network call from AlphaSense that talks about a former Microsoft product manager coming over to Zoom. You know, I want to go back into the research process here. I know you do a lot of channel checks and you spend most of your time actually doing the research. So what is your evidence that gives you conviction that the company is going to go from, you know, this seesaw growth to, you know,

having steady, consistent, above consensus growth.

Sean Emory (39:33)
Yeah. So, you know, to echo your AlphaSense stuff, obviously great product, great stuff that they're doing there. You know, I use them quite a bit, so it's a good platform. The evidence comes in different flavors. You have like the hard data, hard data being like credit card data, know, web traffic data, app download data. All of that has pointed to a pretty strong correlation to...

the underlying business. That's more real time, right? That doesn't tell you what's going to happen in the future. So that's kind of like the here and now data that supports the notion that at the end of this quarter, it looks like they're going to accelerate growth from the street sitting at enterprise business of like 5%. It looks like enterprise business is going to come in around 7%, which leaves like a 2 % delta between total revenue versus consensus revenue, at least as of today. So that's kind of...

The hard data, the here and now. On a go-forward basis, some of the channel checks is simply talking to, we know Zoom meetings, right? And again, using the Okta reports to understand whether they're holding their own with the meetings product. That's ultimately the initial glue, that's the gravity, but then it's the new products. And then there you're talking to channel partners that are reselling not only Zoom, but like Five9 and 8x8 and

We've had multiple conversations with different channel partners suggesting that, look, Zoom is best in class. This is the best product. It's the easiest to use. The only, only, only negative I always hear, and it's gotten better over time, is the partner relationship with Zoom for a while wasn't good. That has now gotten a lot better here over the last, call it, six to 12 months. It makes a lot of sense of why.

Zoom sold itself its whole entire life. And so they did not want to give up their margin to a partner because they could sell themselves. Everyone was already penetrated with Zoom. So then how do you work the monetization with a partner of a client that already has Zoom meetings and now they're selling Zoom phone, who gets the margin? But that's all been kind of semi flushed out. So that honestly should be... It wasn't negative. No one really talks about that because you have to talk to the partners to understand that.

But that has now been alleviated and I think that those channel checks support the view that the product is best in class, number one, and that the partner program is in a much better shape than it used to be.

Doug Garber (42:09)
So you touched on something pretty important here is their sales motion and their channel. Most of their sales, are they direct or do they actually now go through partners and have to give them part of the margin at this point?

Sean Emory (42:23)
Yeah.

Yeah. So Zoom, phone and contact center, they're trying to more and more push that to partners, especially internationally. It's more asset light up front. It's margin on the back end, obviously, meaning it's not people, but they do have an internal enterprise sales force that does a good job. But their partner network continues to get better and better. they're, you know, good enterprise businesses lean on the channel and

Zoom didn't have to do that for so long that it took a little bit of, you could argue underneath all the surface was part of the issue in terms of some of the growth a year and a half, two years ago, which was really, they didn't migrate to the partner ecosystem fast enough, which also made some sense as well. It was selling itself. then how do you discern who's

Whose sale is this? If they already use meetings as an organization, and now you're just upselling them onto phone, who wins that deal? The Zoom rep or the partner? And then no one wants to give that up either. So it's like, are the partners incentivized to sell Zoom 18 months ago? No. 18 months after today? Yes. So that's kind of how it's all shifted.

Doug Garber (43:41)
It's interesting. That's probably one of the reasons they have structurally best in class margins, because they sell direct and they don't have a partner system. I mean, that's something that's structurally go back to, you know, Geico essentially that's why Berkshire loved it so much as they did their own sales. They didn't have this extra cost of an intermediary and it, you know, led to better returns over time.

The other part I wanted to just kind of dig into, at least when I was researching this over the last month, when I knew we were going to talk about it, you know, I did use AlphaSense. came up with a couple very interesting expert networks conversations. I one was a product manager that used to work at Microsoft for eight years on Teams actually. And then he went to Zoom. He was only there for about a year or two. Didn't really get into why, but it was very interesting to hear this commentary that they would just innovate faster.

because it's their main product. You would even say, you know, the CEO was in LinkedIn and reply to comments and read the customer feedback and say, Hey, we'll have that done in three to four weeks. And just, know, when it's your baby, when it's your product, you know, everyone laser focused on it. So I found that color very interesting. I don't think you really get that from the high level to say, no, Microsoft's bigger, you can't compete with them. But if you dig in, there's a lot of examples of people doing one thing better.

And then I found when you're talking about zoom, zoom phone, you know, always trying to quantify this. And I think you did a good job there quantifying that, um, what 170, 180 million of rev per quarter. There was one, one example in these expert network calls where the client was saying, Hey, we were spending 150 grand a year with zoom on just video. then when they got zoom phone, that went up to about 500,000 a year.

So I was surprised to learn that that add-on was actually, you know, two to three X the amount of revenue. Just shows you the opportunity there as you compete against Cisco and other places. any other primary research or competitor research you did that is part of your process that helps you gather the evidence that proves out your thesis on the stickiness of the product, the quality, the growth rate.

Sean Emory (45:47)
For sure.

Doug Garber (46:00)
I'm just trying to dig in so our listeners can say, maybe I should incorporate that type of channel check into my process. And also we'll try to make this, you know, a learning kind of sharing collaboration here.

Sean Emory (46:10)
Yeah, I mean, again, some of the data points I highlighted earlier, I think are the main ones for them. Every company has its own, you know, importance that, you know, if it's a physical business, know, physical visual, you know, information is probably more important for them. Again, it's, can you can you find data that, you know, shows, you know, credit card data, web traffic data, app download data that, you know, it's a digital business. And I think that's ultimately, you know, what you're looking for for them. And then, you know, some of the more

Qualitative stuff, think again, you know, there's there's the soft stuff like the Alpha Sense of the world and you're having conversations with them different Industry experts to some degree doing some of that on your own There's obviously business surveys out there like the Octa one there's G2 crowd, which is you know, the website that shows, you know Verified I guess users of these products and you can see where they fit on the quadrants

There's obviously the more mainstream research places like the Gartner's and such in the world that do a good job at at least pointing you in the right direction of stuff. And that's it. mean, again, quantitative, qualitative. I think both of those are super important to match each other. And that's kind how we look at it. So every company is different, but those are the ones I think we focus a lot for Zoom specifically.

Doug Garber (47:31)
All right, so it seems like we have a company here that has a lot of cash, has a good amount of cash generation, made all this money, seven, eight billion during COVID, didn't really deploy it yet. Now you have this view that growth is going to accelerate from this kind of 3 % where it's been the last year or so. And you're starting to see that you kind of mentioned 7 % enterprise growth. So one of the things I always try and really focus on is, so you have this view.

How is everyone else going to get this view? What are the catalysts for the street to realize the view and the research you've done? Now know you only have, you know, seven, eight, nine, 10 positions. So you're waking up thinking about how can I do more research on this name, et cetera? you know, but what are the things you're looking at for everyone else to realize that might be covered a hundred, 200 names and say, by the way, this was under, this was kind of under the current things going on and

they're going to realize and say, this is a higher growth company might be worth more. How do you outline your that path?

Sean Emory (48:37)
Yeah. So we've obviously seen that. I mean, look, we've seen this time and time again where, you know, a traditional growth company, you know, is the growth name. You know, a lot of people make a lot of money. A lot of people get burned. And it turns into a value name. You know, you've seen that time and time again from the, you know, the apples of the world, you know, trade at single digit multiples for a little bit. Then, you know, people started to get excited again and you, you shifted the paradigm from like the traditional growth investor to Warren Buffett.

And that's kind of like a natural progression. And in between that, can get a little dusty. so valuation attracts traditional value investors. In the last year, I think, I've gotten to that point where it starts to get a little bit more interesting for them. And they have to do the work to figure out, is this a decaying business or is this a stable slash cash flow generating business that will be with us for some time?

then you have that massive cohort of investors that invested at $600, $500, $400 bucks a share and down 90 % and they close their eyes and say, I'm never touching Zoom again. And it's going to take some level of growth to maybe excite them again or just time. So I think that's like the actual paradigm where we live in for most businesses.

Doug Garber (49:43)
Yeah.

Sean Emory (49:59)
At the end of the day though, I'm big believer that a company that's generating a significant amount of cash flow, that is re-accelerating growth, that has a product portfolio that is inspiring some desire to want to be a part of it, I think that ultimately is the true catalyst and the timing of that can take time. But we are entering a year where I think we're going to see growth begin to accelerate, get off the floor of 1%, 2%.

which it was over the last year, now mid single digits to potentially higher than that, assuming we're able to build on those layers of growth that I was referring to. There could be the acquisition that then ignites the idea of what is Zoom doing, and that could be a catalyst in 2025, calendar year 25, that could get people back to the story to say, well, they're growing, accelerating growth, adding on to that as well.

So I think we're at the very start of the reacceleration process. And if that continues, think ultimately people find their way to good assets eventually. You just hope that you're at the forefront of that catalyst moment. And again, I'm not sure it's going to be an instant catalyst. Everyone's going to chat GPT, therefore GPUs are getting sold catalyst-wise. But more so kind of a

an incremental catalyst throughout this year. And then you're entering 2026 calendar year, let's say, in a much higher growth level with potentially a broader suite of platforms. I also think there's the potential, if it stays too low for too long, I mean, you can imagine Zoom being a pretty interesting strategic asset for businesses. That's what I've always said. I said, this was when it was at trading at like 55, 60. go, if it stays here too long.

This is trading at single digit multiples, seven billion dollars of cash. Eric Gouwane's a great inspiring leader and this asset deserves a home if it doesn't rerate. Obviously it's rerated from there, but not rerated enough where I think it's incredibly cheap still. that's kind of like, I think that's the catalyst.

understanding the landscape, who are the potential investors that suit for this. One of them got burned or made money and got burned after and then the other ones are probably just assessing it now and they're probably watching this. the good ones, the good ones.

Doug Garber (52:40)
Yeah,

they learned something from it, right? Now, one other thing you mentioned Warren Buffett and the value and we're talking about the multiple a lot and there's a big variance here between what I would call adjusted EPS and GAAP EPS. And the big difference here is the stock based comp, mean, it's been as high as almost just under a billion dollars and that's almost half the free cash that sheds 30, 40 % off the earnings per share.

How do you view the stock based compensation expense for Zoom when you're valuing the company?

Sean Emory (53:16)
Yeah, it's a good point. That's also one of the things that I think bugged a lot of investors here in the last year and a half. Like if you were taking a look at it, stock-based comp with the macro concerns in the world was starting to become, people become more aware of it, more so than 2020, 2021, where it was almost free money and then they were funding their business through stock-based comp. So very important. Now, I think there's also an importance to understanding

where the stock base came from and why it shot up to a billion and then trickled off here. And in the foreseeable future will be actually a pretty small percentage of dilution going forward. It came to truing up their employee base. So obviously the stock went to five, 600 bucks a share. They were hiring people, a lot of people, and to retain talent, they made the decision in think early 2022 or late 21.

as the stock was crumbling to retain their talent, they had to true up their investors, basically, grant them new shares at the current price, but doing it widespread, was essentially a one-off. And since then, they've gone to essentially cash payers, but they still have these existing stock-based comp that take anywhere from three to five years to vest. So they start to flow through the P &L.

We obviously know that roughly 20 % of all employees never actually invest their stuff because they either leave or something like that. But it was a one-off event that obviously accelerated the view of stock-based comping a billion dollars. That's not obviously what they're going to do in every given year. But it was a one-off true-up in a massively declining stock that they wanted to keep their employees. And since then, again, they've migrated to a cash-based system as opposed to a

paying some of those stock-based comps that were in the past. So this will flush out in the next couple of years, 100%, and then you'll get back to one, probably 2 % maybe at most dilution impact. And that also depends on clearly the growth of the business as this thing grows, it could be even less than that.

Doug Garber (55:31)
And that's the one to 2 % dilution before the buybacks, which will make it actually the share account could decrease.

Sean Emory (55:37)
Yeah, it'll start to actually revert. If you actually look at their, exited Q3 at 315 and they think they guided to 315 in terms of shares and that was without, and they made a fine print, not fine print, they disclosed the fact that that doesn't include any buybacks. So they're basically holding share count flat in the guide without including any sort of buybacks associated with it, which obviously then

implies lower stock based comp because I'm assuming they'll buy something back but

Doug Garber (56:12)
Yeah.

they just re-upped their, they added what, 1.2 billion to their authorization after the quarter, right? Right. So just working through our checklist, you add all this up and if you had to quantify what's this worth if your bet is right and growth re-accelerates and people start having your view.

Sean Emory (56:18)
Yeah. Yeah.

Yeah. So we obviously, so at the base level, we think, you know, the multiple should be twice as much as it is today. We think that that puts it at the kind of the lower end actually of enterprise SaaS companies. You if you look at the comps, you get as high as, you know, 40 something, which I don't think, you know, they deserve that. But even at the low end, you get, you know, obviously them at the low end, but then, you know, low end outside of them, you start to get into, you know, the twenties and, know, enterprise SaaS, hard to, you know, create hard to replace.

These things stick forever. We're still talking about the IBMs of the world and Cisco still exists even though we're talking them defending WebEx and all these other things. Enterprise SaaS deserves a high multiple. Then you attach on obviously growth to that. So you're talking about if you can get back to high single digit growth at the revenue line, keeping margins fairly stable, we should assume then over the next five years, if you're underwriting the five years.

not a doubling of the business, but pretty close doubling of the business. And then therefore, you take one times one or one plus one, you're getting like a 2X from here, which is multiple expansion plus obviously growth. Those two things will probably move in tandem. So if you don't get the growth, you probably don't get the multiple. If you get the growth, decent growth. And I don't mean some double digit breakthrough. Decent growth, I think ultimately you get

pretty strong return of multiple expansion plus just the sheer growth of this business. And that gets you to instead of a $19 billion business, you're talking about somewhere closer to $50, $60 billion in business.

Doug Garber (58:15)
All right, so you're looking at a company that could go two to three X and you know, I've been really including the potential from the balance sheet to either reduce the share account or add a new business line, so creatively potentially. So that's in there as well. That's also protecting the downside. So the next question I always like to think about is what's the other side of the bet? What if you're wrong? What if you miscalculate on one of these?

Sean Emory (58:31)
Right.

Doug Garber (58:41)
parts of the business, they don't grow as fast or the bottom isn't really in, in the online segment, or there's more competition or something changes, AI, whatever. What is this worth? What's the other side of the bet? And what's the probability of that happening? I know it's never fun to talk about because we're always supposed to pitch with high conviction, but in reality, there's always a chance that something else happens or it goes wrong, right?

We live in a world of uncertainty. No one knows the future here. So I like to have somewhat of a balanced view and at least spend the time thinking through what could go wrong so I could spend some time trying to track that too.

Sean Emory (59:20)
Yeah. So the good thing is we're able to track these things pretty close to real time, meaning the credit card data and web traffic data and app download data give us a pretty good sense of what's happening in real time. So that's a good start of our risk management perspective. Now, if you do start to see, let's say you see it, you're undetermined whether it's a trend versus a silent event, and it manifests into an actual trend. You get a one-off thing where,

online starting to weaken, but is it weakening enough where you're actually nervous to make a move? At that stage, and let's say it continues to weaken further, and there's real competitive dynamics, what would that be? That would be just like natural churn. That would have to probably be price associated. They would have to be maybe macro-oriented, where you get massive layoffs in the economy, and people tend to start to turn off their product.

that have to happen soon because I think actually the protection of that is if this is three years from now, they'll be more more penetrated with more product lines, they'll be more important to an organization. So this wouldn't be the first thing you turn off of. You're not going to turn your contact center. You're not going to turn off the phones of all your employees. And therefore, your team chat, your Slack interface, which is the communication hub, you're likely not turning off either. So that's kind of like why, again,

I know this is supposed to be the negatives, but I'm trying to say, if you get to year two, from now to year two, I think you have more penetration, which in theory makes this that true enterprise software company that is deeply entrenched, that's not going anywhere, it's one of the last things you want to turn off. But the negatives is tracking in real time. You do get some sort of competitive threats, I guess, that manifest.

more rapid than today. You you're probably looking at margins decaying. You're then looking at multiple probably going even lower than they are today if you actually thought, you you're probably looking at a, you know, eight multiple, something like that for like a bad.

Doug Garber (1:01:29)
If revenue

is going down, if the online segment, the churn goes up there, and that offsets the enterprise growth where it's flattened down, that's when you get a lower multiple.

Sean Emory (1:01:42)
Yeah, like, so you'd probably get worse margins than probably worse revenue to be quite frank. mean, obviously if you got it all both and it'd be a horrible story, but going from like, know, margins that go from, you know, mid thirties, high thirties to mid twenties, you know, in that

scenario, I think, you know, you would lose 10 % margin roughly. You would get a worse multiple. you would, you know,

you would trade at maybe 30 % below where it is today. And even in that scenario, I think this would still be a prized asset for someone to step into. You'd just be selling it at a discount today, and then maybe it still gets priced in at somewhere around today, which is you're buying all this 200,000 customers from Zoom, best name in town. Who would want to buy this? I always say this. I always say this.

Doug Garber (1:02:20)
Okay.

Sean Emory (1:02:40)
If Microsoft actually had the opportunity to buy Zoom, it's a $3 trillion business. They're number one competitor in communications and collaboration, easily. What would they pay to just take them off the map? And would they pay $100 billion? Maybe. I mean, that's like a fraction of their market cap. I'm not saying like they would pay a hundred billion because that's excessive. my point is, that's actually probably would be worth just to get rid of them.

Doug Garber (1:03:10)
and then they can actually charge for teams as opposed to giving it away. So in theory, right? Because now they don't have a real competitor interest in. I mean, that's a little theory.

Sean Emory (1:03:10)
and control communication collaboration.

Right.

That wouldn't

happen, but it's a hypothetical thought of like, you know, what's the asset, what's the value of the asset to a competitor that would want to wipe it out? And their biggest competitor is obviously worth $3 trillion. So, you know, they'd pay more than, you know, 15 billion for it, that's for sure, but they wouldn't be able to buy it anyways, even if this thing was a...

Doug Garber (1:03:42)
Well, you never know now it's a we got a change into the guard here in January. maybe allowed if if you're if you haven't pissed off Elon, you might be allowed to do it. Well, let's go through the next ones here. Is management aligned with ownership? I think we talked about this in the beginning. You know, this is one these great founder led companies and I just want to go over the story or you could go over the story, I think.

Sean Emory (1:03:47)
Yeah, maybe it's allowed.

For sure.

Doug Garber (1:04:10)
I really enjoy talking about these. think it was great that, you know, one, he owned seven, 8%. So clearly he's aligned. I love that your company focuses on or part of your processes. You'd like to look for founder led companies. I know that's what a lot of people like to do. And that's why you get, you know, the CEO on LinkedIn responded. But what I loved here is he made a pitch to Cisco in 2011, to, to do a video conference and system at Cisco. said, no. So he started his own and now he's taken share from them in video and now in a zoom phone.

So it's just one of those great stories for the.

Sean Emory (1:04:42)
Yeah, he was

on one of the founding teams of WebEx. And then he went, I think it was like two, three years. They made Zoom in stealth mode and then started to do a little bit of a rollout and quickly it hit like 2 million users. And obviously after that, he didn't raise any money and yeah, didn't burn any money. He's been profitable since day one, basically.

Doug Garber (1:04:45)
Yep. So.

Sean Emory (1:05:09)
And that's why you have a company sitting here that doesn't use its cash and is sitting on best-in-class margins. With Eric Kwan now going back to the product side, during COVID, not part of the story is he went into manager mode. He had to to some degree. And then in the last year and a half, he's gone back into the products. He's actually building products, overseeing products. He's back to being a product manager.

an actual quasi-developer versus managing the organization. And I think that's a big difference. People don't realize it brings back that DNA, that ethos of what the business is about.

Doug Garber (1:05:44)
Yeah.

Yeah. Focus on what, what, what you're good at and let other people do the other things. So I always like to outline, what I call kill criteria. you know, what would make you realize, Hey, I'm wrong. need to exit this stock. always like to put that on paper beforehand because it avoids thesis drift, you know, no one's right all the time and things change. And it's always good to kind of say, well, if these things happen, I'm going to exit off for the good or bad. So I'm just curious if you've thought about things that would make you change your mind.

to exit either your price is achieved or something happens on the competitive front. Just one of those items for you.

Sean Emory (1:06:34)
Yeah, mean, again, it's going to go back to some of the harder data that's going to show the competitive dynamics being a little bit more cited to the competitors. So if you start to see a meaningful shift, whether it's on the online business or enterprise traction, significant slowing, think everything we've talked about, think the thesis requires continued success in phone contact center and the rest of the product portfolio.

Because without that, if you're only penetrating 20 % of your enterprise, there's the other 80 % that are at risk. And so it takes away from the idea that this is a best-in-class enterprise software business that is a platform that's best in class for your organization. And it still makes it more of a point solution. So look, it's well on track for that. But that is, I think, the ultimate

That's the thesis that this is going from a product which it was to a platform which it now is. It's the level of penetration that I think is required to make this thing sustainable as ever. And once you start to see that slow down, like if next year, know, phone plateaus completely and is growing like single digits, that'd be a problem unless there's some rationale behind the reason that, you know, we slowed down or this or that.

If Contact Center, which already again, they're up to 1200, they're growing 70 % year over year, they just landed a 20,000 seat customer, which is massive. We're far from that being anything that I'm concerned about, I think that's it. They need to attach these products to more customers. And if we start to see that slow down, I think that's ultimately what breaks the story, even outside of just losing

just churning, if online churns more, that doesn't break the story because it's really around this enterprise business getting more attached. Because then they can raise prices, upsell more products, raise prices again, upsell more products on the enterprise side, and then you have a full 100 % enterprise business. Probably some people would like that, I mean, to be quite honest with you, and having this kind of online business that's over here. So yeah.

Doug Garber (1:08:57)
Yeah. that,

I mean, that still brings in revenue and it's high margin revenue, right? It doesn't cost them that much to service it. What 80 % of the R &D is done. The sales isn't really heavy there. So what sounds like the key is really the phone penetration, the zoom phone, as people go back into the office and, Hey, you weren't using a phone before wanting to take a cheaper solution. Then there are other products, maybe get some revenue from AI companion, contact center, finding the right channels with partners on that and having the rest of the business kind of.

Sean Emory (1:09:04)

Yeah, exactly.

Doug Garber (1:09:25)
kind of be stable, especially the online segment. Two more things here. noticed, know, in our, I always like to look at the sell side ratings here and you kind of looks at sentiment. And when I was looking at the, sell side ratings, there were, you know, most of the people have holds on it. It's not a very loved stock. It's a 13 buys, 18 holds to sell. it's a 55 over 61%. Don't have bias. There's a lot of room for movement there.

It just shows you the stock is not exactly a sexy story with low growth. It's an easy one to say, Hey, there's competition there. Don't don't worry about it. But maybe people aren't focused on the attach rate with the phone and the contact center. know, there's the really focused management team, the focused management team that's going back to product to really execute this. One other thing is, as I always look at the short interest, I don't think there's much of a story.

Sean Emory (1:10:09)
and you know, just really focusing in.

Doug Garber (1:10:22)
Here on the short interest, it's about three and half percent of the float. It actually went up a little bit recently to 9 million shares, up from 8 million last month, but that's a small number. So I kind of bucket that in the, not really that relevant of a, you know, not that relevant. I don't know if you have any other conclusions there, but.

All right.

Sean Emory (1:10:46)
Yeah, no, no, no, else to add on that one.

Doug Garber (1:10:49)
All right, Sean. So the final thing I'd

to do is go through the variant view investment checklist, the 10 questions here on the last slide and get your opinion on how you rate and rank each one of these 10, either, you know, plus equals or negative. So, so what actions you want the PM to take? All right. I think you were clear. You want your buying.

To that end, what gave you the conviction to make this such a large position? What evidence did you see over the last year and when did you increase your conviction and size in this position and why?

Sean Emory (1:11:26)

Yeah, good question. think, look, it all goes down with that. When you said, kind like, what's the floor? The floor is here. It's right around here, in my opinion, right? So it's like, obviously you could be wrong about that. if you think there's a floor that's nearby that the fundamentals are getting better, meaning the actual business is getting better, you're seeing phone accelerate, like, perform incredibly well.

you're seeing contact center, which I could, you could probably ask nine out of 10 people, do you know what zoom contact centers? They have no idea that even exists. Uh, investors or non-investors, you know, that's kind of like the area that I think it's the special stuff that's getting more and more traction while other people aren't even paying attention to it. Um, people are waiting for the accelerating revenue growth, but have no idea where it's going to come from. So if it's coming and it looks like it's coming, then I think, uh, you know, that gives you a level of excitement. So, you know, we've been, you know,

buying as much as we can over the last year now and trying to buy this thing as the valuation bottom, I think, is incredibly attractive. that's kind of it. then I think there's something around enterprise software is very sticky when it is sticky. And you had to have the belief that how do you get to that stickiness? And some of this all goes back to the original

issue we had with it in the early days, which was this was a point solution and that therefore we're not going to invest in this thing. I'm not investing in Slack when it was a point solution. There's risk to that. That's not true enterprise. That's just a product that people use inside of their enterprise. Yeah.

Doug Garber (1:13:07)
Let me go back

just to be succinct. What was your weight in your portfolio a year ago and what's your weight now?

Sean Emory (1:13:16)
It's a question. You know, single digits for sure. And then today, you know, it's closer to 15, 16, 17 % in the portfolio. You know, it's gotten up as high as like 18 because of the run-up.

Doug Garber (1:13:25)
Got it.

Great. Great. then the next question is, do you understand the business? I think this one's definitely in your wheelhouse as, you know, focused on tech and where the world's heading and you use it, all that. Then the question is, is the stock available at a reasonable price today? Give that a thumbs up and equal or a down.

Sean Emory (1:13:49)

Yeah, for sure. mean, it's a big part of our portfolio. That's evidence that we think it's a very reasonable price.

Doug Garber (1:13:57)
Alright, and then do you understand why the stock is mispriced today?

Sean Emory (1:14:01)
Yeah, I think we have a mosaic of all the reasons why there's potential mispricing. Everything from macro to macro fears a year and a half ago to then a whole swath of investors that got hit by it, the growth investors with no growth. The value investors are probably coming up to the story today. There's the idea that this is a point solution, not understanding it's becoming more and more of a platform. And yeah, I think there's a litany of things, which I think is what makes it interesting if you think

most of those things are either cyclical in nature or not true.

Doug Garber (1:14:35)
Yeah, yeah, I get it. Not a lot of focus on people just think of it as a video COVID winner and left for dead almost. So what is your and your so then your variant view versus the street. If I had to sum it up, seems like you're just expecting higher growth than the street is that will lead to a higher multiple. And then you're also expecting the perception from point to platform to lead to a higher multiple. Is that fair?

Sean Emory (1:15:03)
Yeah,

I think that the point solution, the platform has implications beyond what we see today. So selling Zoom phone and selling contact center are revenue, but they're churn reducing as well. They provide pricing power eventually. And I think that's the story that's not here, which is we're eventually going to have a price increase algorithm attached to the story. And that's how Microsoft and all the enterprise level companies perform.

that Microsoft raises their prices every year, whether you like it or not. And I think Zoom's going to get to that point, which is you're going to have more products attached to more customers, which provides more margin, I mean, more pricing power, which again, and then if you start attaching more products, you start to get, know, a snowball effect that is positive to the name. And I think that's the long run potential that I think most people are underestimating.

People are trying to find the inflection point, some of the smarter ones that are tracking it closer, and maybe don't understand is this the inflection point or not, and we're willing to get a little bit ahead of it than not.

Doug Garber (1:16:17)

All right. And then what is your evidence? Just, I know you spend a lot of time digging into these things, but succinctly, what was your main evidence points that led you to this conclusion?

Sean Emory (1:16:28)
So there's the evidence of like the competitive stuff and whether it's the Octo reports or the conversations with partner channels to understand what was maybe some hindrance in growth over the last couple of years that's now alleviated and should propel growth in some of these newer product lines because of the channel being more incentivized to sell. They think it's best in class and these are large partners. These aren't just like small agencies.

Then you have obviously the here and now. Again, there's the here and now and then there's some of the anecdotal evidence that supports the feature. The here and now is credit card data, web traffic app downloads, correlates really strongly to revenue. We already know growth is accelerating relative to consensus into last quarter. So that is within some margin of error, pretty darn close to what it's gonna be. And...

Yeah, and then the future stuff is really around the roadmap of the product portfolio and some of the reports that we've highlighted before.

Doug Garber (1:17:28)
It also seems like you've really dug into a Zoom phone and that's not really like a line item that they report where you can just figure out that it's this much revenue and it's well, and I think you said 30, 40%, which is that accurate and how do you think about that kind of sub-segment of the enterprise that you've kind of dug out here?

Sean Emory (1:17:48)
Yeah, so they've given random disclosures over time. You if you start to try to extrapolate some of those out, you know, you get to, there's enough there where you can draw a line and, you know, be some sort of cone of confidence while all at the same time, you know, there's other credit card ways to get it, but you can kind of like get into the gist of the directionally where this thing's going. And that's what's given us the confidence is.

Disclosures plus alternative data combined giving you a decent purview of what it is, whether it's 170 or 190, somewhere around there is where it's at. And then you go from how many user seats to what people are paying to then go bottoms up to see if that's in the ballpark of possibilities. And then, yeah, so they've given us multiple disclosures in terms of size.

how many users using Zoom phone, but also revenue percentages crossing the 10 % threshold. So both of those in ours go back into that. Again, it's a ballpark, but it's pretty darn close, we think.

Doug Garber (1:18:57)
Got it. then question number eight here in this checklist, what is the stock worth if your bet is right? What's the probability of that?

Sean Emory (1:19:06)
Well, the probability, you never actually know your probabilities, but we think, again, at the base level, we think this is a 1x, and we think if you get real growth, this could be a 2x from here. And we have a high degree of confidence that the growth is reaccelerating. What people pay for it, if it's the low end of enterprise, that gets you your double.

If it's not, then I think you just get the growth and that'll hold the multiple. If you hold the multiple and you get the growth, think you can at the lower end of semi-optimistic or like base case views of the business, I think the lower end of that, you're going to get 60, 70 % upside. And that's high single digit growth for the next couple of years.

Doug Garber (1:20:01)
So when you say 1X, the stock's about 85 bucks now, 1X you're talking about, 160, and then 2X if you also get, 2X you're

Sean Emory (1:20:05)
160, 170.

multiple expansion

or growth. Those would probably come in tandem, but there's a chance no one gives you the multiple, but you get the growth. So the multiple stays constant, the growth, multiple is sentiment, right? You never know exactly what people are willing to buy a house for or willing to buy an asset for that's producing cash flow. But if you just hold the multiple constant and you get the growth, you at least grow by the growth.

Doug Garber (1:20:14)
Okay, Matt.

Yep.

Sean Emory (1:20:41)
And that could be somewhere around 8 % 8 % a year, roughly, plus some sort of cash comeback from the $7 billion. You could get to an algorithm that gets you double digit growth. Ideally, that's not what we want. We want that plus margin expansion. That's where you get the supercharge. But there's a chance where they just for some reason never get the multiple expansion that we think they deserve.

Doug Garber (1:21:07)
And when we go down to kind of your margin of safety or the other side of the bet, what's the probability of that happening? And do you take any attempt to kind of quantify that, um, or this exercise?

Sean Emory (1:21:20)
Yeah. Again, you like the margin of safety on the business side is the margin of safety is wide, right? In my opinion, when you have a high margin business that is growing, growing in real time, that's also flush with cash, right? A lot of optionality they can do there. So just the fundamentals of the business margin of safety, really wide. Good thing from a

valuation investment perspective margin of safety. You know, I also think it's fairly wide, meaning, you know, if you're in real time, seeing the data of the business improve, not weaken, that's a positive. So as we sit here today talking about it, the margin of safety there is pretty wide from a valuation perspective. The multiple people are willing to pay for things you never know.

But historically, enterprise software companies, whether they're point solutions or platforms, tend to get decent enough multiples. These don't trade like energy companies or banks or something like that that will, retail companies that'll trade as four or five times. Rarely do you see a brand of Zoom's caliber with the financial structure they're sitting in that trade sub 10 multiples.

Doug Garber (1:22:42)
Yeah,

it's the second cheapest.

Sean Emory (1:22:44)
So that's like, it would really

have to fall apart, but we would see a lot of that in real time. The question is, do we think it's a trend or an anomaly? And it'll just be the evidence of what we're seeing to make that, that's where you could get wrong in that moment in time where things are falling off, but you think you're saying it's because of the X, but it's actually because of Y and it's an actual real competitive challenge.

Doug Garber (1:23:05)
When you say real time,

you're looking at credit card data and opt-in surveys to track it kind of in real time instead of just the quarterly updates where you get the official quarterly rev.

Sean Emory (1:23:17)
Yeah, we're rarely looking at the quarterly as like the gauge of... That'll tell us margins more so than anything.

Doug Garber (1:23:21)
Got it.

Yeah.

And then is the last one is management aligned with ownership? think that's a clear yes. Right. I the guy went back to be a product guy as opposed to a CEO. So he owns a lot. So you love those stories. all right. So when I kind of down this checklist, I think all of them are pretty much, you know, positive. The other, you know, the other side of the bed and the risk, I think there's definitely, you know, it's hard to have.

margin of safety with a tech business. It's not like you can liquidate it. But in my opinion, I'd give it nine out of 10. think the other side of the bet still has a lot of cash on the balance sheet. Obviously, there's competition and innovation. I think that's one of the reasons Buffett kind of always stayed away from tech stuff because things change fast, but they're the leader and they're motivated. So it looks like I don't personally own this for fair disclosure to everyone. I don't own it at this point.

You know, after talking with Sean for an hour, hour and a half and going through everything in such depth, I'm definitely going to reevaluate and look at my model. So it's definitely more interesting getting a tech stock just keep with cash and a potential re-acceleration of revenue. That's one of the things I always look for is, you know, revenue either going from flat to upper, from low growth to high growth. That's always exciting. All right, Sean, any other?

closing comments before I let you off to Christmas Eve.

Sean Emory (1:24:53)
Hopefully we get a good gift this year and next year. Finish the year strong. had a good year and hopefully the next coming year is the same. Just stay at it. That's it. Anyone who had any questions on Zoom, just reach out, Doug or me, and try to flush out any ideas you guys have.

Doug Garber (1:25:16)
Great, well, thank you for spending your morning with us and I hope you have a great Christmas and happy holidays and we'll talk in 2025.

Sean Emory (1:25:26)
Cool. All right Doug, have a good one.

Doug Garber (1:25:28)
All right, everybody.

Sean Emory (1:25:33)
Here it is.