

Q4 & FY 2017 Earnings Call

February 12, 2018

Important Information

- This presentation contains forward-looking statements that involve risks, uncertainties and assumptions, including guidance, projections, and estimates of future financial condition and results of operations. If the risks or uncertainties materialize or the assumptions prove incorrect, our results may differ materially from those expressed or implied by such forward-looking statements. Typically, these statements contain words such as “if,” “believe,” “may,” “will,” “estimate,” “continue,” “anticipate,” “intend,” “expect,” and similar expressions.
- The forward-looking statements in this presentation are based on estimates and information available to us at the time of this presentation. These statements are subject to risks and uncertainties that could cause actual results and events to differ materially and are not guarantees of future performance. Except as required by law, we undertake no obligation to update the forward-looking statements to reflect subsequent events or circumstances. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included in our Report on Form 10-K for the 2016 fiscal year end and our other periodic reports filed with the Securities and Exchange Commission, which can be accessed at <http://www.sec.gov>.
- This presentation refers to certain non-GAAP financial metrics. See the GAAP to non-GAAP reconciliation tables contained in this presentation and our earnings press release posted on the Investor Relations portion of the ServiceSource website for a reconciliation of the non-GAAP metrics to the closest GAAP financial measures.

Q4'17 Non-GAAP Operating Expenses

Non-GAAP

In \$ millions except EPS

	Q4 2017	Q4 2016
Cost of Revenue*	38.4	39.8
<i>% of Revenue</i>	58.2%	58.0%
Sales & Marketing*	7.1	10.3
<i>% of revenue</i>	11%	15%
Research & Development*	1.1	2.0
<i>% of revenue</i>	2%	3%
General & Administration*	10.9	12.6
<i>% of revenue</i>	17%	18%
Total Expenses*	57.6	64.8
<i>% of revenue</i>	87%	94%
Adjusted EBITDA*	\$ 10.3	\$ 5.7
<i>% of revenue</i>	16%	8%
Non-GAAP Net Income*	5.1	1.7
Non-GAAP EPS*	0.06	0.02
Shares used in calculating basic net Income (in the millions)	89.0	87.5

Please Refer to Appendix for GAAP
to Non GAAP Reconciliations

* Financials are Non-GAAP and exclude, where appropriate, stock-based compensation expense, amortization of internally developed software and purchased intangibles, restructuring and other costs, and non-cash expenses relating to the convertible note.

Q1'18 Guidance – Key Metrics*

Q1'18 Guidance

Please Refer to Appendix for GAAP to Non GAAP Reconciliations

In \$ millions except EPS	Q1 Low	Q1 High
Revenue Range*	\$ 53.5	\$ 55.5
<i>y/y growth</i>	-5.7%	-2.1%
Adjusted EBITDA*	\$ (1.5)	\$ 0.5
Non-GAAP Net Income*	\$ (3.00)	\$ (1.00)
Non-GAAP EPS	\$ (0.03)	\$ (0.01)

* Financials are Non-GAAP and exclude, where appropriate, stock-based compensation expense, amortization of internally developed software and purchased intangibles, restructuring and other costs, amortization of certain sales commissions that will be capitalized under Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU No. 2014-09") and non-cash expenses relating to the convertible note. Excludes restructuring and other costs.

FY'18 Guidance – Key Metrics*

FY'18 Guidance

In \$ millions except EPS

	FY Low	FY High
Revenue Range*	\$ 243.0	\$ 246.0
<i>y/y growth</i>	1.6%	2.9%
Gross Margin*	36.5%	37.5%
Operating Expense (% of revenue)	32.0%	32.5%
Adjusted EBITDA*	\$ 19.0	\$ 22.0
Non-GAAP Net Income*	\$ 8.0	\$ 10.0
Non-GAAP EPS	\$ 0.09	\$ 0.11
Free Cash Flow **	\$ 0.0	\$ 3.0

Please Refer to Appendix for GAAP to Non GAAP Reconciliations

* Financials are Non-GAAP and exclude, where appropriate, stock-based compensation expense, amortization of internally developed software and purchased intangibles, restructuring and other costs, amortization of certain sales commissions that will be capitalized under Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU No. 2014-09") and non-cash expenses relating to the convertible note

** Excludes restructuring and other costs

Appendix

Q4'17 GAAP to Non GAAP Operating Expense

GAAP to Non-GAAP Reconciliation

(In thousands)

(Unaudited)

		Three Months Ended December 31, 2017
GAAP operating expenses		\$ 23,513
Non-GAAP adjustments:		
Stock-based compensation	(A)	(2,921)
Amortization of internally-developed software	(B)	(216)
Amortization of purchased intangible assets	(C)	(131)
Restructuring and other costs	(F)	(1,049)
Non-GAAP operating expense		\$ 19,196

Q1'18 Guidance GAAP to non-GAAP Reconciliation Tables

Q1'18 Guidance GAAP to Non GAAP–Net Loss & EPS

GAAP to Non-GAAP Reconciliation

(In thousands, except per share data)

(Unaudited)

	Three Months Ended March 31, 2018		Three Months Ended March 31, 2018
GAAP net loss	(\$13,800) - (\$11,800)	GAAP basic net loss per share	(\$0.15) - (\$0.13)
Non-GAAP adjustments:		Non-GAAP adjustments:	
Stock-based compensation (A)	3,300	Stock-based compensation (A)	0.04
Amortization of internally-developed software (B)	3,000	Amortization of internally-developed software (B)	0.03
Amortization of purchased intangible assets (C)	100	Amortization of purchased intangible assets (C)	0.00
Non-cash interest expense (D)	2,400	Non-cash interest expense (D)	0.03
Income tax effect on non-GAAP adjustments and impact of normalizing the effective income tax rate (E)	1,500	Income tax effect on non-GAAP adjustments and impact of normalizing the effective income tax rate (E)	0.02
Amortization of costs capitalized upon adoption of ASC 606 and contract acquisition costs (I)	500	Amortization of costs capitalized upon adoption of ASC 606 and contract acquisition costs (I)	0.01
Non-GAAP net income	(\$3,000) - (\$1,000)	Non-GAAP basic net income per share (G)	<u>(\$0.03) - (\$0.01)</u>
		<i>Certain totals may not add due to rounding</i>	
		Shares used in calculating basic net loss per share on a non-GAAP basis	<u>90,386</u>

Q1'18 Guidance Net Loss to EBITDA

Reconciliation of Net Loss to Adjusted EBITDA

(In thousands)

(Unaudited)

	Three Months Ended March 31, 2018
Net loss range	(\$13,800) - (\$11,800)
Income tax (benefit) provision	100
Interest & other expense, net	3,000
Depreciation & Amortization	5,400
Amortization of costs capitalized upon adoption of ASC 606 and contract acquisition costs	(1) 500
EBITDA range	(\$4,800) - (\$2,800)
Stock-based compensation	(A) 3,300
Adjusted EBITDA range	(\$1,500) - \$500

FY'18 Guidance GAAP to non-GAAP Reconciliation Tables

FY'18 Guidance GAAP to Non GAAP – Gross Margin

GROSS MARGIN - GAAP TO NON-GAAP RECONCILIATION

(In thousands)

(Unaudited)

		Twelve Months Ended December 31, 2018
GAAP Gross Profit		\$81,900 - \$85,500
Non-GAAP adjustments:		
Stock-based compensation	(A)	1,300
Amortization of internally-developed software	(B)	5,400
Amortization of purchased intangible assets	(C)	100
Non-GAAP Gross Profit		<u>\$88,700 - \$92,300</u>
GAAP Gross Margin		<u>34% - 35%</u>
Non-GAAP adjustments:		
Stock-based compensation	(A)	1%
Amortization of internally-developed software	(B)	2%
Amortization of purchased intangible assets	(C)	0%
Non-GAAP Gross Margin		<u>36.5% - 37.5%</u>
<i>Certain totals may not add due to rounding</i>		

FY'18 Guidance GAAP to Non GAAP–Net Loss & EPS

GAAP to Non-GAAP Reconciliation

(In thousands, except per share data)

(Unaudited)

	Twelve Months Ended December 31, 2018		Twelve Months Ended December 31, 2018
GAAP net loss	(\$21,800) - (\$18,800)	GAAP basic net loss per share	(\$0.24) - (\$0.20)
Non-GAAP adjustments:		Non-GAAP adjustments:	
Stock-based compensation (A)	13,700	Stock-based compensation (A)	0.15
Amortization of internally-developed software (B)	8,600	Amortization of internally-developed software (B)	0.09
Amortization of purchased intangible assets (C)	100	Amortization of purchased intangible assets (C)	0.00
Non-cash interest expense (D)	5,800	Non-cash interest expense (D)	0.06
Income tax effect on non-GAAP adjustments and impact of normalizing the effective income tax rate (E)	(\$400) - (\$1,400)	Income tax effect on non-GAAP adjustments and impact of normalizing the effective income tax rate (E)	(0.0) - (0.02)
Amortization of costs capitalized upon adoption of ASC 606 and contract acquisition costs (I)	2,000	Amortization of costs capitalized upon adoption of ASC 606 and contract acquisition costs (I)	0.02
Non-GAAP net income	\$8,000 - \$10,000	Non-GAAP basic net income per share (G)	<u>\$0.09 - \$0.11</u>
		<i>Certain totals may not add due to rounding</i>	
		Shares used in calculating basic net loss per share on a non-GAAP basis	<u>91,852</u>

FY'18 Guidance Net Loss to EBITDA

Reconciliation of Net Loss to Adjusted EBITDA

(In thousands)

(Unaudited)

	Twelve Months Ended December 31, <u>2018</u>
Net loss range	(\$21,800) - (\$18,800)
Income tax (benefit) provision	500
Interest & other expense, net	7,100
Depreciation & Amortization	17,500
Amortization of costs capitalized upon adoption of ASC 606 and contract acquisition costs (I)	<u>2,000</u>
EBITDA range	\$5,300 - \$8,300
Stock-based compensation (A)	13,700
Restructuring and other costs	-
Adjusted EBITDA range	\$19,000 - \$22,000

FY'18 Guidance Cash Flow from Operations to Free Cash Flow

Supplemental Cash Flow Information Free cash flow analysis, a non-GAAP measure

	Twelve Months Ended December 31, <u>2018</u>
(In thousands) (Unaudited)	
Net cash provided by operating activities	\$14,000 - \$20,000
Less:	
Capital expenditures	\$14,000 - \$17,000
FX adjustment	-
Free cash flow	<u>\$0 - \$3,000</u>

Footnotes

- (A) **Stock-based compensation.** Included in our GAAP presentation of cost of revenue and operating expenses, stock-based compensation consists of expenses for stock options and awards and purchase rights under our stock purchase plan. We exclude stock-based compensation expense from our non-GAAP measures because some investors may view it as not reflective of our core operating performance as it is a non-cash expense.
- (B) **Amortization of internally-developed software.** Included in our GAAP presentation of cost of revenue and operating expenses, amortization of internally-developed software reflects non-cash expense for certain software purchases and software developed or obtained for internal use. We exclude these expenses from our non-GAAP measures because we believe they are not indicative of our core operating performance.
- (C) **Amortization of Purchased Intangibles.** Included in our GAAP presentation of gross margin and operating expenses is amortization of purchased intangible assets. We believe amortization of acquisition-related intangible assets, such as the amortization of the cost associated with an acquired company's research and development efforts, trade names and customer relationships, are items arising from pre-acquisition activities and therefore are properly determined at the time of an acquisition. Although these intangible assets are continually evaluated for impairment, amortization of the cost of purchased intangibles is a static expense, one that is not typically affected by operations during any particular period.

Footnotes (cont.)

- (D) **Non-cash interest expense.** Under GAAP, we are required to separately account for liability (debt) and equity (conversion option) components of the \$150 million convertible senior notes that were issued in August 2013. Accordingly, for GAAP purposes we are required to recognize effective interest expense on our convertible senior notes which includes interest cost related to the amortization of debt issuance costs and the contractual 1.5% interest rate of the note. The difference between the effective interest expense and the contractual interest expense is excluded from our assessment of our operating performance because we believe that this non-cash expense is not indicative of ongoing operating performance. We believe that the exclusion of the non-cash interest expense provides investors a view of our core operating performance.
- (E) **Income tax effect on non-GAAP adjustments as well as the impact of normalizing the effective income tax rate.** This adjusts (i) the provision for income taxes to reflect the effect of the non-GAAP items A, B, C, D, and F on our non-GAAP net loss; (ii) the income tax rate to a normalized effective tax rate of 40%; and (iii) non-GAAP earnings per share based on a fully-diluted share count.
- (F) **Restructuring and other costs.** Included in our GAAP presentation are expenses associated with our announced restructuring effort, commencing in Q2 2017. Restructuring and other costs consist of: employee severance and other benefits, costs of write-off of leasehold improvements, other property, equipment, and other lease exit costs. These are one-time in nature costs that are not indicative of our core operating performance.
- (G) **Non-GAAP basic net income per share** For this per share reconciliation, basic share count was used.
- (I) **Adoption of ASC 606.** Financials are Non-GAAP and exclude, where appropriate, stock-based compensation expense, amortization of internally developed software and purchased intangibles, restructuring and other costs, amortization of certain sales commissions that will be capitalized under Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU No. 2014-09") and non-cash expenses relating to the convertible note.