



1 **Pandora (P) Web IV Update Conference Call December 16, 2015**

2 **Scripts for: Brian McAndrews, Chairman, CEO, & President**

3 **Mike Herring, Chief Financial Officer, Pandora**

4 **Dominic Paschel, Vice President, Pandora**

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6 **Version Final – December 16, 2015**

7 **Dominic Paschel**

8 Good afternoon and welcome to Pandora's update call following the US Copy
9 Right Royalty Board's recent Web IV rate decision. Some of our discussions will
10 contain forward-looking statements which may include projected financial results
11 or operating metrics, business strategies, anticipated future products or services,
12 anticipated market demand or opportunities and other forward-looking topics.

13
14 These statements are subject to risks, uncertainties, and assumptions.
15 Accordingly, actual results could differ materially. For a discussion of the risks that
16 could cause our results to differ from today's discussion, please refer to the
17 documents we file with the Securities and Exchange Commission.

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19 Today's call is available via webcast and a replay will be available for two weeks
20 following the conclusion of the call. To access the press release, supplemental
21 financial information, or the webcast replay, please consult the Investor Relations
22 section of Pandora.com. With that, let me turn the call over to Brian McAndrews,
23 Pandora's Chairman and CEO.

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24 **Brian McAndrews**

25 Thanks Dom.

26

27 Today the Copyright Royalty Board—the CRB—released its decision in the
28 “Webcasting IV” rate-setting proceeding, establishing the sound recording
29 performance royalty rates paid to performing artists and record labels by Internet
30 radio services from 2016-2020.

31

32 In a moment, Mike will walk you through the details including the slides available
33 on our website regarding the financial impact compared to our 2015 “pure play”
34 rate.

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36 But first let me share my own high-level perspective about the new rate structure

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38 First and foremost, we’re pleased to finally have much-needed certainty on the
39 rate structure for our core Internet radio business. While next year’s CRB rate will
40 be 15% higher than we currently pay, it is still well within our range of expected
41 outcomes. This is a rate we can work with and grow from. Importantly, the new
42 structure is set at a level that allows us to aggressively invest in a vibrant and
43 growing music ecosystem and pursue our strategic plan to build the world’s most
44 powerful music discovery platform as well as a strong business.

45

46 We have a strong vision for the next chapter of our growth, and remain 100%
47 focused on advancing that plan. We’ve recently announced a series of initiatives,

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48 acquisitions and direct partnerships that form the foundation of an aggressive
49 strategy to grow Pandora into the definitive music destination globally, unifying
50 the full music experience under one roof, spanning radio, on demand, and live
51 music. We intend to provide music **where** you want it, **how** you want it, and for
52 **everyone who** wants it. Today's decision does nothing to change that.

53

54 As I mentioned on our last call, our strategy is built on core beliefs, one of which is
55 to **establish productive and collaborative partnerships with music makers to put**
56 **Pandora in the strongest possible position to deliver on our long-term vision.**

57 Over the past 2 years, we've worked hard to do just that, investing aggressively
58 and collaborating directly with industry partners to demonstrate the power of
59 Pandora. At the highest level that means helping connect artists with their
60 audience. And I'm proud to say definitively these investments have helped us
61 become increasingly more effective at breaking artists, selling tickets and
62 increasing music sales.

63

64 Pandora is creating the world's definitive music discovery platform, bringing
65 together music fans, music makers and advertisers in a marketplace that benefits
66 everyone, with Pandora at the center. The increased participation of artists, the
67 expansion of listening options and the access to, and discovery of, live music will
68 in turn drive additional fan engagement. And then, this expansion of fan
69 engagement across the entire music experience will attract additional advertising
70 and sponsorship dollars. By taking a marketplace approach, we have expanded
71 the total monetization opportunity available to Pandora from the \$40-plus billion

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72 dollar US radio and digital advertising opportunity to something that is multiple
73 times larger.

74

75 That was true before today's CRB decision, and our pace of investment in music
76 will only accelerate as we move ahead.

77

78 As we noted last month, the CRB rates are likely to play a far less central role in
79 Pandora's business as we move toward the future. To fully unlock the global and
80 functional potential of our business, we're aggressively pursuing direct licensing
81 agreements and making fast progress, including recent publishing agreements
82 with Sony/ATV, SONGS and Warner/Chappell Music. With the CRB process behind
83 us, I'm confident our discussions with labels will accelerate, although it will take
84 some time for this part of our strategy to fully materialize.

85

86 So while the CRB decision is obviously an important moment, it is one of many
87 aspects of our business. We've been aggressively building a business capable of
88 long-term growth, diversifying and adding ballast to our business, and positioning
89 ourselves for long-term leadership regardless of CRB outcome. And now with the
90 CRB rate set for our core business, we can move full steam ahead on pursuing our
91 long-term strategy.

92

93 To close the prepared portion of my remarks, I'll simply reiterate that we're going
94 to come to work each day just as focused and invigorated by our ambitious plan

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95 to build the world's most powerful music discovery platform. We have a solid plan
96 and are executing with a sense of urgency.

97 I'm excited about the future of music, and what's ahead for Pandora.

98 With that, let me turn the call over to Mike.

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99 **Mike Herring**

100 Thanks Brian. As Brian just discussed, today the CRB released its decision in the
101 “Webcasting IV” rate-setting proceeding, establishing the sound recording
102 performance royalty rates paid to performing artists and record labels by Internet
103 radio services for the period of 2016 to 2020.

104

105 The decision creates certainty for our business and will help us more definitively
106 plan and act on our vision and goals Brian just laid out. To help you understand
107 the impact that the rates will have on our business, we’ve created a few slides
108 posted to our website that I would like to walk you through.

109

110 On slide 1 we have recalculated the royalty costs for the first nine months of 2015
111 as if the costs were calculated using the rates set by the Web IV ruling that are
112 effective for the calendar year 2016 – these are represented by the second bar in
113 the table. The first bar is the actual costs incurred by Pandora for the first nine
114 months of 2015, so you can see that the impact of the 2016 rates would have
115 been to increase total costs by \$50.4 million, or an increase of 10.6%.

116

117 Slide 2 shows the royalty rates for five years - 2016 through 2020 - in the table at
118 the top of the slide. The rates for 2016 are set at \$0.0017 per performance for
119 non-subscription services and \$0.0022 per performance for subscription services
120 and then adjusted for 2017 through 2020 based on the Consumer Price Index
121 each year. For the purposes of this illustration we are assuming a CPI adjustment
122 of a 2% increase per year. To put these rates in context for Pandora in relation to

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123 the most important metric we use to measure our revenue performance and
124 potential for driving profit leverage in our business – RPM or revenue per
125 thousand hours – the bottom half of the slide shows the relative gross profit
126 margins we will expect under these rates within a range of RPMs from \$50 to \$80.
127 As a reminder we had an overall RPM of \$60.52 in Q3 2015, and our most
128 developed markets are operating at RPMs of \$80, \$90 and \$100. These gross
129 margins are net of all royalties Pandora expects to pay.

130
131 On our Q4 call in February we will outline the steps we will be taking to manage
132 costs under these new rates and optimize RPM to ensure we can drive the right
133 gross profitability while continuing to support future growth initiatives. As you
134 can see, with the right management of our cost structure and continued
135 execution on our monetization strategies Pandora will be able to maintain gross
136 profit levels of 40% to 60%+ under the new royalty rates.

137
138 While the new higher rates will have a near-term impact on the profitability of
139 our core business, with the certainty of royalty rates established and our clear
140 vision for growth across several vectors, we believe the impact is manageable and
141 that we can operate effectively in 2016 and beyond.

142
143 Earlier this month, we added nearly \$300 million dollars to our balance sheet
144 through the sale of convertible notes and will close the year with a total cash
145 balance of approximately \$450 million at the end of 2015 which will enable
146 Pandora to continue to execute on our business plans and invest in new initiatives

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147 into 2016. The fourth quarter of 2015 has been progressing as expected and we
148 look forward to entering the year with a solid user base and on strong footing
149 financially. We will be giving a full update on the fourth quarter and giving full
150 guidance for 2016 at our earnings call in February We have a well-developed
151 strategy that has progressed over the last 18 months, and I'm very excited about
152 the future of Pandora, and the future of music, as we execute on our vision **to be**
153 **the definitive source for music enjoyment and discovery globally.**

154

155 Now I'll open the call for your questions. Operator?