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Presentation

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Dolby Laboratories Conference Call discussing Q3 fiscal year 2026 financial results. [Operator Instructions]. As a reminder, this call is being recorded, Thursday, July 30, 2026. I would now like to turn the conference over to Mr. Peter Goldmacher, Vice President of Investor Relations. Peter, please go ahead.

Peter L. Goldmacher
Vice President of Investor Relations

Good afternoon. Welcome to Dolby Laboratories Third Quarter Fiscal Year 2026 Earnings Conference Call. Joining me today are Kevin Yeaman, Dolby Laboratories CEO; and Robert Park, CFO. As a reminder, today's discussion will include forward-looking statements, including our fiscal 2026 fourth quarter and full-year outlook and our assumptions underlying that outlook. These statements are subject to risks and uncertainties that may cause actual results to differ materially from the statements made today, including, among other things, the impact of macroeconomic events, supply chain issues, inflation rates, changes in consumer spending and geopolitical instability on our business.

A discussion of these and additional risks and uncertainties can be found in the earnings press release that we issued today under the section captioned Forward-Looking Statements as well as in the Risk Factors section of our most recent annual report on Form 10-Q.

Dolby assumes no obligation and does not intend to update any forward-looking statements made during this call as a result of new information or future events. During today's call, we will discuss non-GAAP financial measures. A reconciliation between GAAP and non-GAAP financial measures is available in our earnings press release and in the Interactive Analyst Center on the Investor Relations section of our website.

With that, I'd like to turn the call over to Kevin.

Kevin J. Yeaman
Consultant

Thanks, Peter, and thanks to everyone joining us on the call today. Revenue and earnings for the third quarter were within the range of guidance we provided on the last earnings call. We are narrowing the range of guidance for the full year and keeping the midpoint of revenue the same. We expect strong sequential growth in Q4, driven primarily by momentum in a number of our key growth areas. We have strong visibility into the pipeline of deals for the quarter, and many of them have closed early in Q4.

Robert will share more details on this and on the financials overall in a few minutes. Dolby has maintained its leadership position for over 60 years by innovating and raising the bar on the entertainment experience. We do this by working with creatives, content distributors, and device makers, giving us a unique perspective on the collective needs, challenges and opportunities of the entertainment ecosystem, which enables us to deliver experiences that come to life in the highest possible quality.

This quarter, I would like to start with our focus on expanding our total addressable market beyond device licensing. We are working with a growing number of content partners that are looking to differentiate on experience and drive deeper engagement with their audiences. And we are making good progress on our target for 10% of revenue from these partners by the end of FY '28. Let's start with the video distribution program, the patent pool that licenses imaging patents to content streamers.

Meta, one of the world's largest streamers of video content, became a licensee of the program covering its Facebook, Instagram, and WhatsApp platforms. Also, Alibaba became a licensee this quarter to cover its video operations, including e-commerce, entertainment, and digital media platforms. We are encouraged by the early traction and the quality of the participants joining the pool. In less than 1 year since inception, 45 licensors have already attracted some of the biggest names in streaming as licensees to the pool, including ByteDance, Kuaishou, Meta, Roku, Tencent, and Alibaba.

We remain excited by the early momentum from this pool, and we expect it to continue. Moving on to Dolby OptiView. We closed a number of key deals in the quarter, including a multiyear agreement with Roberts Communication Network, the largest provider of horse racing content in the U.S. for ultra-low latency video streaming. Also in the quarter, Google announced that Dolby OptiView Ads, our ad insertion engine was the first product certified through their Ad Manager technology partner program.

This certification recognizes the performance and monetization improvements that Dolby OptiView ads delivers when integrated with Google Ad Manager. While this partnership is early days, we are looking forward to working with Google to win new customers.

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Last quarter, I talked about how at the NAB show in Las Vegas, we showed new solutions for fan engagement and live sports. These solutions use AI to predict viewer behavior and to generate compelling stories for individual fans based on the action and their interests.

Fan engagement is a top focus for the sports industry, and we have seen strong interest in these new solutions, which we will be shipping in the coming months. We believe that the Dolby OptiView platform, which brings together these capabilities with ad monetization, low-latency streaming, and cross-platform playback is a unique system that will lead the future of the live sports experience. We are excited by the progress we are making in expanding our addressable market to include content platforms where we earn revenue based on usage.

Moving on, Dolby Vision and Dolby Atmos continue to bring the most immersive experiences to life. Starting with the World Cup, viewers in all 3 World Cup host countries were able to enjoy the World Cup in Dolby through partners, including Peacock and Comcast in the U.S., Bell in Canada and TV Azteca in Mexico. Fans in some of the most passionate football countries like Brazil, Colombia, Germany, and Spain were also able to enjoy the World Cup in Dolby.

On TVs, Dolby Vision 2 is now in market with some Hisense TVs. And by the end of this calendar year, TCL and Philips will also be shipping televisions with Dolby Vision 2. Moving on to auto. We have announced agreements with over 40 auto OEMs since the program started. A few of our new OEM wins this quarter include Volkswagen in China, launching its first Dolby Atmos vehicle and Buick announcing pre-sales for the Electra E7, a plug-in hybrid SUV with Dolby Atmos, also in China.

Also this quarter, Google announced support for Dolby Atmos through Android Auto with launch partners, including BMW, Genesis, Mahindra, Mercedes, Renault, and Skoda. With Dolby Atmos supported across Apple CarPlay and now Android, it has never been easier for users to stream Dolby Atmos to their car. It also makes it easier for dealers to demo and sell the Dolby Atmos experience in the car. We're excited about the continued momentum in in-car entertainment, which continues to be a top focus for the industry.

Moving on to user-generated content and social media. High-quality user-generated content is an important factor in driving engagement, and we have strong adoption of Dolby Vision on many of the world's largest social media platforms, like Instagram, Facebook, and Douyin. In addition to driving demand for Dolby on mobile phones, we are starting to make our way into new device categories like smart glasses and video cameras. RayNeo, the leading provider of augmented reality glasses, launched the RayNeo GT Max, the world's first AR smart glasses equipped with Dolby Vision. And Insta360, the market share leader in action and panoramic cameras, launched the Luna Ultra, which supports Dolby Vision capture.

We are pleased by the momentum behind user-generated content in Dolby and expect it to continue to grow as a priority for device OEMs. Wrapping up, we remain confident in our opportunity to drive growth beyond device licensing with progress on both the video distribution program and Dolby OptiView. And we continue to bring more Dolby experiences to more people around the world with the growing adoption of Dolby Atmos and Dolby Vision across a wide range of devices and use cases. All of this gives us confidence in our ability to drive long-term growth.

With that, I'd like to turn the call over to Robert to cover the financials.

Robert J. Park
Senior VP & CFO

Thank you, Kevin, and thanks to everyone joining us on the call today. Revenue for the quarter came in at $305 million, which was within the guidance we shared last quarter. We saw better-than-expected revenue in Dolby Atmos, Dolby Vision and imaging patents, offset by deal timing and foundational audio revenue. Non-GAAP earnings per share was $0.69, just above the middle of the range of guidance as lower-than-expected operating expenses offset lower-than-expected revenue and higher taxes.

Licensing revenue was $282 million and products and services revenue was $23 million. We generated approximately $167 million in operating cash flow and repurchased 1.2 million shares or $65 million of common stock. We recently received Board approval to increase the existing share repurchase authorization by $350 million, bringing our total authorization to about $427 million. We declared a $0.36 dividend, up 9% from our dividend a year ago and ended the quarter with cash and investments of $756 million.

Q3 GAAP operating expenses include a $4 million restructuring charge for organizational changes made as we align our resources to focus on the most impactful areas. Detailed licensing performance by end market can be found on our IR website. As a reminder, end market growth rates are typically smoother on an annual basis as the timing of recoveries, minimum volume commitments and true-ups can drive quarterly volatility.

End market performance for the quarter came in mostly as expected with no significant outsized moves.

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Turning to guidance. For Q4 fiscal '26, we expect revenue to be between $362 million and $392 million. Within that, we expect licensing revenue to be between $335 million and $365 million. Gross margin should be approximately 90% on a non-GAAP basis, and we expect non-GAAP operating expenses to be between $195 million and $205 million. Non-GAAP earnings per share is expected to be between $1.13 to $1.28.

Let me provide more context on Q4. Our Q4 revenue guidance at the midpoint represents a 23% year-over-year increase in revenue. This reflects momentum we are seeing in key growth areas we have been prioritizing, namely the video distribution patent program, including a large deal with Meta that signed early in Q4, higher units from Dolby Atmos in the car and revenue from new device categories like wearables. In addition, Q4 is also benefiting from timing of deals like minimum volume commitments.

For fiscal year '26, we expect total revenue to range from $1.41 billion to $1.44 billion. Within that, licensing revenue is expected to be between $1.31 billion and $1.34 billion. We are targeting non-GAAP operating expenses to be between $785 million and $795 million. We expect non-GAAP earnings per share to be between $4.25 and $4.40, this reflects the higher tax expense from discrete items in Q3.

We are expecting an annual operating margin improvement of approximately 100 basis points for the year on a non-GAAP basis, up from the range between 50 basis points and 100 basis points we guided to last quarter. For the full year, we are expecting other revenue to be up high teens driven by auto and VDP, broadcast to be up mid-single digits due to higher recoveries and imaging patents. Mobile, which includes wearables, is expected to be up mid-single digits, driven by adoption of Dolby Atmos and Dolby Vision.

And CE should come in flattish with lower unit volumes offset by higher recoveries and Dolby Atmos adoption. PC is down low single digits, primarily due to lower unit shipments and lower recoveries. We expect foundational Audio revenue to be down slightly for the year and Dolby Atmos, Dolby Vision and imaging patents revenue to be up roughly 15% year-over-year.

In summary, the team has executed well, and our performance reflects the operational focus on our key growth areas despite an environment that has remained dynamic all year. As we have demonstrated over multiple economic cycles, our approach is to control what we can control. We remain focused on our growth strategy, driving innovation and allocating resources to the areas that will have the greatest impact. Our financials remain solid with organic revenue growth, high gross margins, expanding operating margins, healthy cash flows and a strong balance sheet.
With that, I'll turn it over to the operator to open the line for any questions. Operator?

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Question and Answer

Operator

[Operator Instructions]. Your first question comes from the line of Ralph Schackart with William Blair.

Ralph Edward Schackart
William Blair & Company L.L.C., Research Division

Robert, I want to circle back on your Q4 commentary with the extra color. I think you talked about 23% year-over-year growth. And you called out some momentum, I think, in video distribution program. I think it was signed early in the quarter, Dolby in a car and wearables. Historically, this business has been difficult for -- at least for analysts to forecast on a quarterly basis, but that growth rate is sort of a standout.

And I know you could have revenue sort of move in and move out of quarters, a little bit long-winded to basically ask, can you talk about maybe the sustainability or durability of this growth rate? And how much of this could also be impacted by maybe some quarterly revenue shifting out of Q3 into Q4?

Robert J. Park
Senior VP & CFO

Yes. Ralph, those are the areas driving the growth and the momentum we're seeing, both the VDP, including the large deal was signed at the beginning of this quarter. Higher units from Dolby Atmos in the car and new device categories like wearables. But also mentioned that there are -- Q4 also benefits from timing of things like minimum volume commitments, particularly in mobile that tend to be a little bit more back-end loaded than they were last year. Last year's Q4 was a little softer if you look at the quarterization and just happens to be timing of certain things that come in.

Ralph Edward Schackart
William Blair & Company L.L.C., Research Division

Great. And then you had some large licensees on the VDP part, Meta, and I think you talked about Alibaba. Maybe talk about after signing these sort of larger companies, what that does in terms of encouraging participation from future licensees. They seem like pretty standout announcements this quarter.

Kevin J. Yeaman
Consultant

Yes. Thanks, Ralph. It is one of the things that's giving us confidence in the program and our long-term growth. It's about a year into the program, and we've seen a lot of these programs come together. And this one is coming together really well, both in terms of the pace of it and the breadth of it. We're at 45 licensors. We've got a number of high-profile licensees. You mentioned Meta and Alibaba signing this quarter.

And the impact that has is, yes, it does tend to make it easier to get the next deals. In any given point in time in a program like this, there's a group of customers that are looking for a solution to the problem of operating in a fragmented IP environment for which patent pools are a very helpful solution. There's a group of companies that are doing their homework. They want to know is the pool comprehensive enough? Is it the right pool? Is it the right price?

More people coming along starts to get them to move faster along their process. And then, of course, in any given program, there's always going to be some holdouts and you keep working each of those phases of the pipeline. But clearly, for 1 year, this program is coming along very nicely and great to see some really nice wins this quarter.

Operator

Your next question comes from the line of Steven Frankel with Rosenblatt Securities.

Steven Bruce Frankel
Rosenblatt Securities Inc., Research Division

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Kevin, when you first introduced the concept of VDP, you talked about targeting some of the large domestic streaming networks. And Meta is a great win, and hopefully, we'll get more like that. But what's the level of discussion with these targets in the streaming space today? And do you still feel like that's a realistic potential win on the horizon?

Kevin J. Yeaman
Consultant

Yes. Thanks, Steve. Well, first of all, yes, I mean, Meta is one of the largest streamers of video content on the planet. And the pipeline is strong, and it includes streamers of all types of video content. And I'm not going to go into the details of the pool's discussion with any one customer. But again, I think for 1 year, we feel really good about how this program has come along. And every time you get another licensee on board, it makes it that much easier to get the next licensee. So we are -- I mean, relative to a year ago, given the way that, that the execution has gone, I would say we're feeling increasingly confident in that program.

Steven Bruce Frankel
Rosenblatt Securities Inc., Research Division

Great. And given the strength in other, auto seems to be continuing its ramp and you're announcing new customers and now you've expanded to Android Auto. Are we getting closer to a point where the auto business might get broken out?

Kevin J. Yeaman
Consultant

Yes, we're getting closer. And as you know, we've typically done that when it's 10% of licensing. And I think certainly, as we go into the next year, that's something we're going to have a close look at because it is the highest growing end market for us, and it's the largest within other.

Steven Bruce Frankel
Rosenblatt Securities Inc., Research Division

Great. And Robert, a couple of questions on the numbers. What were true-ups? And were any of the buckets affected by large catch-up payments?

Robert J. Park
Senior VP & CFO

Yes. The true-up was really negligible this quarter, Steve. It's less than $1 million positive. So really, really small. The second question regarding any true-ups, we have got recoveries every quarter.

Steven Bruce Frankel
Rosenblatt Securities Inc., Research Division

Recoveries? Okay.

Robert J. Park
Senior VP & CFO

No. As I noted on the call, nothing notable this quarter in terms of outsized movements.

Steven Bruce Frankel
Rosenblatt Securities Inc., Research Division

Okay. Great. And then from a macro perspective, there's been a lot of fear that the rising memory cost was going to impact how CE customers thought about new product introductions. What can you tell us as you look to what's coming down the pipeline using your technology? Do you feel like the plans they talked about at CES are still going forward? Or have they been impacted in any way?

Kevin J. Yeaman
Consultant

So I think at CES, we were largely focusing on the big focus areas for us at CES were automotive, where, as you noted, we continue to see really strong adoption, strong pipeline, things continue at pace. We also were highlighting Dolby Vision 2, where we saw -- there are now Hisense customers that are -- that have Dolby Vision 2 on their TVs, and we are on track for them to have more and then Philips and TCL by the end of this year. I think backing up because memory is obviously a hot topic, Steve.

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I think as it relates to our end markets, mobile is by far the market that is impacted the most by memory prices. Our largest device market is TV. That's one of the lesser impacted markets in terms of a percentage of BOM. Second most impacted market would be PC in terms of the memory impact on them. So for this year, all that's factored into our guidance. As I've said before, as it relates to mobile, because of the prevalence of minimum volume commitments that has a kind of a mitigating or I guess, you might even say sort of a delaying effect.

And so all that's factored into our guidance, it kind of falls into the category. We've got some ups and we've got some downs. As we look into next year, the longer this goes on, the longer it starts to -- the more it starts to flow through. Now we do expect to grow with strength in video distribution program, automotive, the new categories like wearables. We've got some exciting new products coming in Dolby OptiView. But how much that is in part offset by memory chip is something we're watching closely.

So again, TV is not affected as much mobile and PC the most. There's no uniform answer as to how that impacts Dolby. Each customer approaches this quite differently. So on the one hand, you might get customers that have room to absorb this into their gross margins, and that may not have any impact on unit volumes and so minimal impact to Dolby. Others are raising prices. Some are doing a combination and we're raising prices, then it really is a matter of how much pricing power do they have and what's the price sensitivity, but it's not necessarily a one-for-one impact on Dolby.

And then in other cases, particularly in mobile, where at the low end, memory cost has gone from -- my understanding is it's gone from plus or minus 15%, to even over 50% of BOM. It's really significant. We're seeing some customers that are just eliminating one of their lower lines because they just can't solve that equation. Then what they're doing is trying to get people to move up a level, and they're also investing in trying to maintain those higher-end lines.

And so again, that does, in fact, of course, that lowers device shipments. But on the other hand, for Dolby, it's not proportionate in the sense that we have a higher attach and we have higher technology content, the further you go up those lines. So there's very dynamic. We're watching it really closely. And again, we expect to grow with the strength we have in our focus areas, but we're definitely watching memory prices and how much of an offset that might be.

Operator

Your next question comes from the line of Patrick Sholl with Barrington Research.

Patrick William Sholl
Barrington Research Associates, Inc., Research Division

Within Dolby Vision 2, I was wondering if there was any sort of differentiation in terms of the pace of adoption between the various tiers on that new technology?

Kevin J. Yeaman
Consultant

I would say there's no change in pace from what we've talked about. We've got those 3 customers that -- Hisense has some of its in-market TVs updated. We expect TCL and Philips to be shipping by end of the year. We're kind of at that point in the year where I think that CES will become the focal point for most of our customers that will be adopting it going forward. And on the content side, Canal Plus and Peacock are both on track to -- they're integrating now and getting ready to be able to provide content in Dolby Vision 2.

Patrick William Sholl
Barrington Research Associates, Inc., Research Division

Okay. And then on the VDP, is there a content-type focus within that like -- and how you expect like the pace of getting licensees to be a part of that program? Or is it kind of -- as you said, more -- I certainly understand it's more broad, but is how you're seeking to generate growth on that focusing on a specific type of content initially first?

Kevin J. Yeaman
Consultant

Well, really at the center of it is companies that are at scale, taking advantage of the best in video codec technologies in order to achieve their business objectives. And that is a broad range of content. You can tell from some of our first licensees from Meta to Roku, ByteDance to Alibaba's covering -- has coverage, including e-commerce. So it really is a function of anybody who is relying on the IP covered by this patent pool, which is growing with more licensors joining with the success it had over the last year to deliver video at scale.

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Operator

Your next question comes from the line of John Rigatti with Baird.

John Francis Rigatti
Robert W. Baird & Co. Incorporated, Research Division

This is John on for Vik Kesavabhotla. A couple for me. I wanted to start with auto. I'd be interested to hear if you could unpack what's driven -- what you think has driven some of the faster adoption with your technology in some of the international autos? And then what needs to change in the U.S. market for you to be able to unlock more of that segment there? And I have a couple of follow-ups.

Kevin J. Yeaman
Consultant

Yes. I think, I mean I think if I go back to the beginning of the program, a lot of our initial momentum was in China, where they were becoming the leading innovators in EVs, and they were putting a really high focus on the in-car entertainment experience. And China is -- also happens to be the largest vehicle market in the world. And so that got the attention of auto manufacturers around the world to be able to compete in China, at which point then it makes it -- you just to step away from then shipping those cars throughout the world.

And so that's what -- and so in Europe, we've got Mercedes and BMW. In India, we now have Mahindra and Tata. The U.S., we do have Cadillac. So I think -- well, I mean, we're pleased with how the pace and how it's grown. Like I said, 40 OEMs in -- since the program began. And I think the next big milestone for us is looking to get further penetration into mainstream. And we've got -- we've talked about some cars in the past, like the Hyundai in China and some of the cars in India, but just -- but people always start with the high end, and now it's a matter of really focusing on getting that into the mainstream higher volume models. And that will benefit us in the U.S. and around the world.

John Francis Rigatti
Robert W. Baird & Co. Incorporated, Research Division

Yes. Great. And then maybe on OptiView, if you could talk a little bit more just about the vision there. And obviously, it's still very early days, but just some of the -- a couple of examples on maybe what's resonating most as you've taken that out to partners.

Kevin J. Yeaman
Consultant

Yes. Thank you. So look, at the highest level, the vision is this, which is that we're no longer in a world of one-to-many where we all have to experience the exact same sports experience at the exact same time. We're in a world of streaming where we ought to be able to understand what engages you and be able to personalize that experience and to do that in real time in a way where you can interact with your friends around the experience.

So the vision for Dolby OptiView is to provide a solution that allows these sports organizations and streamers to be able to do that. And so we started, of course, with the ability to stream in ultra-low latency. That's important so that you're not seeing the touchdown 15 seconds before I am, which is no fun for either of us. Maybe it's fun for you. It's not fun for me. We've got the player that's integrated with that. And we have some -- now you're beginning to see some new -- some additions to the portfolio, which get closer to that more personalized experience.

So one of the things I talked about today was OptiView Ads, which is something we mentioned a couple of quarters ago, but we've now been in market with the first couple of customers. They're in the process of testing the third generation of the product. And once that testing is complete, we're planning to really begin to scale this to our customer base in the fall.

And the big difference there from the customer perspective is the revenue generation potential. One of our customers is seeing increases of 75%. And that's because we have a server-guided technology, which requires far less lead time than competing solutions to kind of pick the ad and deliver the ad, which means that by filling that ad slot just before it's needed, we can do a better job of targeting that ad to the viewer. It's more likely that the viewer is still there and ultimately, it just increases the fill rate.

So -- and then the solution is also integrated with the player and that prevents the ads from being blocked. So we're pretty excited about that. And as I said, it became one of the -- well, the first -- at the time was the first technology to be certified by Google Ad Manager as a partner technology, and that's because it's designed to slot right into their workflows, work seamlessly with Google Ad Manager. So as we get to the fall and are looking to scale this as well, we're also looking forward to working with them to highlight the benefits to their customers.

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And then I talked about last quarter about how at NAB, we were previewing our sports intelligence platform. And so we continue to get really good engagement from customers on what we're doing with that. We look forward to having some specific solutions in market next year. And this is really focused on now moving toward really being able to understand how engaged a fan is or when their interest is waning.

But importantly, being able to do something about that with the audiovisual experience that keeps them engaged. So again, the vision is simply to provide our customers with the ability to better engage their fans and audiences with real-time personalized experiences. And we are really excited about how the portfolio of solutions is coming together to make that happen.

John Francis Rigatti
Robert W. Baird & Co. Incorporated, Research Division

Yes, that's great. I guess the last one for me is just -- you touched a little bit on the Dolby Vision 2 and some of the -- that's obviously in market now, some of the demand you're seeing there. I'd be interested if you could talk a little bit as well about the impact that the Dolby Vision 2 being in the market is having on adoption of Dolby Vision 1 and possibly kind of the segmentation or the tiering that OEMs are able to do across both of those?

And then also maybe just for Robert on capital allocation. If I look at kind of the repurchase activity on a quarterly basis, it looks like so far in '26, you're going at about twice the rate of 2025. Just any kind of color you could give on how you're thinking about capital allocation for the balance of this year and then going forward would be great.

Kevin J. Yeaman
Consultant

Yes. I think -- so as it relates to Dolby Vision 2, I would say it's early days. I mean, again, we're focused on getting these first 3 customers in market, and these are all examples where they're moving from Dolby Vision to Dolby Vision 2, as you would expect, starting with some of their higher end. We do have strong engagement. And like I said, I think CES is probably about the time we'd expect for our customers to say more about their go-forward plans with Dolby Vision 2. And Robert...

Robert J. Park
Senior VP & CFO

John, yes, thanks for noticing that we have increased the velocity and volume of our buyback activity, and we'll continue to do -- execute on our policy of at least offsetting dilution of stock-based comp. But we do look at this quarterly, make our decisions quarterly based on facts and circumstances and needs of the business. But yes, we have been stepping up year-to-date every quarter.

Operator
There are no further questions at this time. This concludes today's call. Thank you for attending. You may now disconnect.

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