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OTEX.TO - Q1 2024 Open Text Corp Earnings Call

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PRESENTATION

Operator

Thank you for standing by. This is the conference operator. Welcome to the OpenText Corporation First Quarter Fiscal 2024 Financial Results Conference Call. (Operator Instructions) The conference is being recorded. (Operator Instructions)

I would like to turn the conference over to Harry Blount, Senior Vice President, Investor Relations. Please go ahead.

Harry Edward Blount - *Open Text Corporation - Senior VP & Global Head of IR*

Thank you, operator. Good afternoon, everyone, and welcome to OpenText first quarter fiscal 2024 earnings call. With me on the call today are OpenText Chief Executive Officer and Chief Technology Officer, Mark J. Barrenechea; our Executive Vice President and Chief Financial Officer, Madhu Ranganathan; and also joining us is Paul Duggan, Executive Vice President and Chief Customer Officer.

Today's call is being webcast live and recorded, with a replay available shortly thereafter on the OpenText Investor Relations website. Earlier today, we posted our press release and investor presentation online. These materials will supplement our prepared remarks and can be accessed on the OpenText Investor Relations website, investors.opentext.com. I'm pleased to inform you that OpenText management will be participating at the following upcoming conferences: RBC Capital Markets Global Technology, Internet, Media, and Telecom Conference on November 14 in New York; Needham's Virtual SaaS Conference on November 16; TD Securities Technology Conference on November 21 in Toronto; Bank of America Securities Leveraged Finance Conference on November 28 in Boca Raton; Wells Fargo Technology, Media, and Telecom Summit on November 29 in Rancho Palos Verdes; UBS Global Technology Conference on November 30 in Scottsdale; Scotiabank's Global Tech Conference on December 5 in San Francisco, Nasdaq's Investor Conference on December 5 in London; and Barclays Global Technology, Media, and Telecom conference on December 7 in San Francisco.

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And now onto our Safe Harbor. Please note that during the course of this conference call, we may make statements relating to the future performance of OpenText that contain forward-looking information. While these forward-looking statements represent our current judgment, actual results could differ materially from a conclusion, forecast, or projection in the forward-looking statements made today. Certain material factors and assumptions were applied in drawing any such statement. Additional information about these material factors that could cause actual results to differ materially from a conclusion, forecast, or projection in the forward-looking information, as well as risk factors that may project future performance results of OpenText are contained in OpenText's recent Forms 10-K and 10-Q, as well as in our press release that was distributed earlier this afternoon, which may be found on our website. We undertake no obligation to update these forward-looking statements unless required to do so by law.

In addition, our conference call may include discussions of certain non-GAAP financial measures. Reconciliations of any non-GAAP financial measures to their most directly comparable GAAP measures may be found within our public filings and other materials which are available on our website.

And with that, it's my pleasure to hand the call over to Mark.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Harry, thank you. Thank you for joining us today. It's an exciting start to our new fiscal year 2024. We had record Q1 revenues of $1.43 billion, double-digit cloud revenue growth, and adjusted EBITDA of 34.7%. It was another quarter of cloud organic growth, ARR organic growth, and strong renewal rates in the mid-90s. Customers showed tremendous trust and confidence in OpenText during the quarter. Bombardier chose OpenText for their legal tech AI platform. CNP chose OpenText for large contract AI analysis. And Infosys chose OpenText for developer testing, automation, and generation. Great information management is a prerequisite for great AI, and we intend to compete in and win both information management automation and AI.

The OpenText business is best analyzed and measured on annual performance. We manage the business to longer cycles than 90 days. Thus, our quarters do vary. Based on our strong Q1, our strong product cycle, and forward visibility, we have confidence in our F '24 constant currency targets: $5.85 billion to $5.95 billion in revenues; 36% to 38% adjusted EBITDA; $800 million to $900 million in free cash flows, including total revenue organic growth, 15% plus enterprise cloud bookings growth; and returning Micro Focus to organic growth. We are shifting from growth primarily driven by M&A to growth driven by product innovation and go-to-market execution. You can see our new Total Growth model with our F '26 aspirations on Slide 21 of our Investor Relations deck. It includes 15% plus enterprise cloud bookings growth, 7% to 9% cloud revenue growth, 2% to 4% ARR growth, plus any future M&A and margin expansion, plus dividends and buybacks. And when all combined, yields return to shareholders. We are focused on the fundamentals that drive shareholder value.

Slide 13 of our Investor Deck highlights our new shareholder value approach and how we intend to create value through 6 fundamentals: first, expand our competitive differentiation in information management; expand customer consumption; unlock new value areas such as SaaS and AI; expand our go-to-market; realize higher profits and cash flows from those higher revenues and continue to return capital to shareholders via our dividend programs and future share buybacks. Let me walk you through each one of the value drivers. Competitive advantage is everything. We offer the most comprehensive information management platform in the market affording customers many paths to value and paving the way for new value as the world embraces AI. And to accelerate these outcomes, we expect to invest up to 16% of revenues in R&D, and we expect these investments to support our F '26 growth aspirations of 7% to 9% organic cloud growth.

Second, expanding our customer consumption is a threefold strategy: first, by being the market leader in each of our business clouds and driving more consumption within each, content, experience, business networks, applications, automation, IT operations, and security; second, by embedding security and content across all of our business clouds; and third, by providing customers choice and continuing to provide them choice, off cloud, private cloud, public cloud, API cloud. We provide the flexibility to pair the right workload with the right consumption approach so our customers can focus on the right model for their business.

Third, value driver. We have new value areas to unlock, very focused in SaaS and AI. While we are executing well overall, and we have many programs to enhance value, we are very focused on unlocking new value from SaaS and AI. Titanium was SaaS driven. Titanium X is both AI and Micro Focus cloud driven. Expect us to spend disproportional time in these areas. And for Q2, we expect to see 20% year-over-year growth in enterprise cloud

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bookings, another positive sign of unlocking new value. We will expand our go-to-market. We have one of the largest enterprise sales forces in software, and we enter F '24 with clear market lanes and resources across strategic accounts, enterprise accounts, corporate and business accounts, as well as the home. We are making it easier for customers to connect with our products to consume more.

Over 500 partners attended OpenText World as we relaunched our partner network focused on cloud and AI. And you can already see our progress within strategic accounts such as Microsoft in SMB, SAP in enterprise business applications, Google with cloud infrastructure and AI, and AWS with mainframe modernization, a remarkable level of interest in our long-term strategy. We also intend to realize higher profits and higher free cash flows from higher revenues. With our expanded mission in information management and greater operational scale, this provides us greater opportunities to automate and to use AI to drive even greater operational synergies. Higher revenues and higher EBITDA translates to increased cash flows, which is reflected in our F '26 aspirations of adjusted EBITDA of 38% to 40% and $1.5 billion plus in free cash flows. And we anticipate the operating leverage in future years to only get stronger.

As well, and finally, capital allocation as a strategic value driver. Our capital allocation principle is to return approximately 20% of trailing 12-month free cash flows via dividends. Since fiscal '13 we have returned $2.2 billion via dividends and share buybacks. And we expect that as our free cash flows grows, so do our dividends. And as our net leverage decreases below 3x, we would expect to return to our share buyback program. This is our new growth model and our new value creation approach as we shift from growth primarily driven by M&A to growth driven by product innovation and go-to-market execution.

Let me close on a few points. OpenText is in a great position to help our customers build the next generation of work, the next generation of experience, the next generation of service management, business fabrics, and supply chains. And to do this with the highest levels of trust and security. I'm excited about our growth agenda helping customers modernize their businesses and their information platforms, helping them consolidate customer data into our information cloud, providing cyber tools to create trust and security, consuming more SaaS applications, helping developers be more productive and at the highest levels of quality, and building AI platforms for humans. The promise of AI starts with great information management. Our Aviator AI software is built into our business clouds, Aviator Platform embedded into our automation with pluggable language models, Aviator Thrust building smarter applications, Aviator Search interacting with information in whole new ways, Aviator IoT embracing the next generation of device-generated information, and our individual Aviator Business Clouds.

We are already working with customers to create exciting new AI personas via Aviator, such as the next-generation tech support assistant, a mortgage advisor, a claims adjuster, an HR business partner, as well we're working with customers to simply get more efficient via AI. You can start to see us unlocking AI value with our expected Q2 20% year-over-year growth in enterprise cloud bookings. Our shift to a new Total Growth model driven by innovation, with emphasis on high-quality growth, will enable us to deliver strong metrics for profitability and cash flows at scale. Our 6 fundamentals of new shareholder value will uniquely position us as a choice investment in the technology sector. My deepest appreciation to our 24,000 colleagues at OpenText who live our mission every day to make our customers wildly successful.

Our hearts pray for the hostages and innocent everywhere, and we join the global community in the hope of a peaceful and prosperous future for the Middle East region. May the one that brings peace bring peace for all. Let me turn the call over to Paul Duggan, our Chief Customer Officer, who will speak to our renewal business, which grew organically in Q1; then Paul will hand the call over to Madhu, our CFO, who will speak to our financials and outlook. Over to Paul.

Paul Michael Duggan - *Open Text Corporation - Executive VP & Chief Customer Officer*

Great. Thank you, Mark. It's a privilege to be with all of you today to talk about our renewals business and the work we're doing to unlock value for our customers and shareholders. Before I do, let me tell you about my team, the Customer Success organization. We're responsible for renewals of cloud and off-cloud subscriptions, professional services and cloud delivery, and technical support. We brought these functions together following the Micro Focus acquisition and took on an enhanced mission called OpenText L.O.V.E., Land together, Operate, Value, Expand. OpenText L.O.V.E. means focusing on customer outcomes. It's all about turning promises made into promises delivered. When it comes to renewals, we believe if you deliver on those promises, customers succeed. And when they succeed, they stay with you, and those relationships will grow over time.

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Today, I'll speak to 3 areas: the strength of our renewals; an update on Micro Focus; and a few of the goals ahead for our team. First, OpenText has a strong record of maintaining exceptional and predictable renewal performance. Despite historic and disruptive world events, economic uncertainties, and unprecedented tragedies of the last decade, our renewal rates are unwavering. Q1 was no exception, finishing at 94% for cloud and off-cloud, excluding Micro Focus. Of course, renewal rates directly correlate to the value of products and services to our customers, but it's also a measure of operational excellence. From our renewal systems, processes and controls, to pricing and programs, to the automation simplifying the transactional elements, collectively, these also create a lifting force on renewal rates and help us protect and grow ARR over time. It's not just renewal rates either. All of our primary indicators are trending positively on time renewals, past due contracts, cancellations, pricing at the point of sale, and our annual price adjustment at renewal. These trends are the hallmarks of customer confidence and a tightly run world-class renewal function.

Second, as we've shared before, raising the renewal rate on Micro Focus is a critical value unlocker. We started on day 1 of the acquisition, immediately bringing the business onto our internal standards. We also implemented a risk identification and mitigation playbook, growth programs like an extended support offering, and deep engagement with our sales and engineering leadership to shape overall consumption and expansion strategies. By the end of Q2, we'll have touched roughly 75% of the Micro Focus cloud and off-cloud subscriptions. We expect to touch 90% by Feb 1. As a result, we'll increasingly see the positive impacts of running the business in all the ways I described.

And I'll give you 2 proof points on that impact. One, back in February, we took on a business operating in the low-80s on renewal rate. Q1 ended in the mid-80s, and it gives us now 2 consecutive quarters of improvement. We remain confident we'll end in the high 80s this year and expect to operate in the 90s in fiscal '25. Two, we did it for Documentum taking renewals from the low-80s to the mid-90s, where we are today. And now we are doing it for Micro Focus.

And finally, looking to the future, it's all about growth. We already have a successful cloud renewal expansion motion in Business Network and SMB. We're adding new offerings like a premium support upsell on our OpenText install base, taking a very successful offering within the Micro Focus business, understanding the profile of customers that consume it, and extending that to similar OpenText customers. We also announced a new customer renewal portal last month. More than 90% of our cloud renewal business is auto renewed, and with this new portal, we'll bring an automated and self-service option to our off-cloud customers as well. As we do that, we plan to shift more renewal professionals to customer management versus renewal management and drive expansion across the entire customer base. Our overarching goal is to position renewals and the entire Customer Success organization to play a more prominent role in consumption, AI adoption, and public cloud expansion.

Let me close by saying thank you to our customers. Success is a team sport, and the fantastic results we saw in Q1 ultimately represent your trust in OpenText. That trust is earned, not given. And we're committed to delivering on the promises we make to you every day. And with that, I'll hand the call over to Madhu.

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Thank you, Mark. And thank you, Paul. We appreciate all of you joining us today. So let me summarize the key points for today. Regarding Micro Focus, we expect to return Micro Focus to organic growth this fiscal year driven by successful integration. And in particular today you all received an excellent overview on renewals from Paul. In addition, we are delighted to share that we expect Micro Focus to be on our target operating model of 36% to 38% adjusted EBITDA this fiscal year as well.

In Q1, OpenText executed extremely well in a volatile world with record Q1 revenues and year-over-year growth. Turning to our outlook. Our outlook fully reflects the performance we expect, bringing together 2 businesses with different seasonality trends and sales cycles. With Q1 actuals and Q2 quarterly factors, we remain on target for our internal plan. We expect a stronger second half and a seasonally strong Q4 as we end our fiscal year, including a return to organic growth for Micro Focus. These are important factors for our quarterization, and we encourage the analysts to better balance your quarterly models. We remain fully on track to meet our fiscal '24 targets and fiscal '26 aspirations. You are hearing today that we're shifting from growth primarily driven by M&A to growth driven by product innovation and go-to-market execution. This is our new Total Growth model with our fiscal '26 aspirations led by cloud and ARR.

My final summary point. We remain highly committed to shareholder value, and today we're sharing with you our new shareholder value approach through 6 fundamentals that Mark outlined earlier. So, moving to our Q1 results, please refer to the investor presentation as posted on our IR

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website. Starting on Page 24 of the presentation for the slide titled Q1 Fiscal '24 and Trailing 12-month Financial Highlights. All references I will be making are in millions of USD and compared to the same period in the prior fiscal year and are on a reported basis, unless stated otherwise. On a year-over-year basis, enterprise cloud bookings of $121 million, up 8% year over year. We had record Q1 cloud revenue of $451 million, up 11.5% and 10.9% in constant currency. Q1 ARR revenue of $1.15 billion, up 59.1% and 57.5% in constant currency, and this represents over 81% of total revenue. This is 11th consecutive quarter of organic growth in constant currency for both cloud and ARR. Its record Q1 total revenue of $1.43 billion, up 67.3% and 65.4% in constant currency, with Micro Focus contributing $563 million in the quarter.

And moving to other financial metrics. GAAP net income was $80.9 million, and this reflects increased operating expenses, amortization, special charges, and interest expenses related to the acquisition of Micro Focus driving GAAP EPS of $0.30. GAAP gross margin of 71.4%, up from 69.7%, and this reflects increased relative revenue contribution from customer support and license. Non-GAAP gross margin of 77.3%, up from 75.2%, also reflecting increased relative revenue contribution from license and customer support. Adjusted EBITDA of $495 million, an increase of 62.8% year over year and 58.2% in constant currency. Our adjusted EBITDA margin was 34.7%. We expect Micro Focus onto our adjusted EBITDA model by the end of this fiscal year. Adjusted EPS of $1.01 continues to reflect his progress.

Turning to DSOs. Our DSOs were 43 days, down slightly by 2 days compared to Q4, given Q1 seasonal factors. Micro Focus continues to perform well and our overall working capital performance remains strong. As stated in our last call, we expected Q1 free cash flows to be neutral to slightly negative as a result of interest, special charges, and integration costs, as well as seasonally lower working capital at the start of the fiscal year. We generated $47 million in operating cash flows and $10 million positive free cash flows in the quarter. Starting from Q2, we expect free cash flows to grow on a year-over-year basis in each subsequent quarter. We remain on track to realize our fiscal '24 FCF targets of $800 million to $900 million and achieve our fiscal '26 aspirations.

Now, turning to the balance sheet, please refer to Page 26 of the investor presentation. We finished Q1 with $920 million in cash and $8.9 billion of total long-term debt. Our net leverage ratio was 3.6x for the quarter. In Q3, and in our last call, we mentioned our net leverage ratio would fluctuate slightly over the next few quarters, while we remain on the path to a net leverage ratio of less than 3x by the end of fiscal 2025 or sooner. We have completed approximately $560 million of debt repayments since the close of Micro Focus transaction. Our revolver is now fully paid, and we have begun to make discretionary principal payments on the term loans.

Turning to our dividend program. On November 1, our Board of Directors approved a quarterly cash dividend of $0.25 per common share. The record date for the next quarterly dividend is December 1, 2023, and the payment date December 20, 2023. And let's turn to our targets and aspirations. As Mark highlighted, for Q2, we expect enterprise cloud bookings to grow 20% year over year.

And let me comment on the SMB market. The SMB market has been the most impacted by the current macroenvironment. This trend has an impact on our cloud revenues, not on enterprise cloud bookings. During Q2, we expect to have a $10 million to $15 million revenue headwind from SMB. Our enterprise cloud business remains strong and expected to grow revenues organically in Q2 and the rest of the fiscal year. As the SMB market gains more strength, we are well positioned to capture share and accelerate cloud revenue growth.

Starting with our Q2 fiscal '24 quarterly factors of our investor presentation. On a year-over-year basis, we expect revenue of $1.45 billion to $1.50 billion, ARR of $1.1 billion to $1.13 billion, FX revenue tailwind of approximately $10 million to $15 million, adjusted EBITDA year over year the margin between 36% and 37% and reflects Micro Focus integration costs, FX adjusted EBITDA tailwind of approximately $5 million to $10 million.

Our fiscal '24 targets in constant currency are provided on Page 30 of the Investor Relations presentation. Mark spoke on fiscal '24 targets in his comments and let me provide a full summary. Total revenues of $5.85 billion to $5.95 billion, enterprise cloud bookings growth of 15% plus, cloud revenues up 6% to 8%, customer support revenues up 40% to 42%, ARR up 24% to 26%, total revenue growth of 30% plus with organic growth in the range of 1% to 2%, non-GAAP gross margin in the range of 77% to 79%, total operating expenses of 42% to 44% of revenues, adjusted EBITDA margin of 36% to 38%.

Two changes to our fiscal '24 targets. At current exchange rate, we expect FX to be neutral. We're also reducing our net interest expense for the year to be $550 million to $570 million, and this reflects a 75 basis point reduction in the interest on our acquisition term loan. Our free cash flows are on track to achieve $800 million to $900 million, which is our fiscal '24 target range. Our fiscal '26 aspirations remain unchanged. These are

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included in Page 32 of our investor presentation materials. We are reaffirming fiscal '26 FCF aspirations of $1.5 billion plus. We expect to realize higher adjusted EBITDA margins and free cash flows from higher revenues. And let me put these in numbers for you, and relative to fiscal '23, our fiscal '26 aspirations show revenues to be 40% higher, adjusted EBITDA to be 67% higher, and free cash flow to be 129% higher.

Our fiscal '26 aspirations show a highly predictable and growing business at scale led by cloud and ARR. Acquisitions will remain additive to our future growth as we delever and capital flexibility returns. Lastly, please refer to our Financial Integration Framework slide on Page 31. We have updated to reflect timing on system integration and global entity simplification.

So in summary, our Micro Focus integration is ahead of plan, and we expect to achieve important milestones in fiscal '24. It's a return to organic growth and renewal rates in the high-80s, and Micro Focus business to be on the OpenText operating model of adjusted EBITDA of 36% to 38%. Also, as Mark mentioned, our shift to a new Total Growth model driven by innovation, with emphasis on high-quality growth will enable us to deliver strong metrics for profitability and cash flows at scale. Our 6 fundamentals of new shareholder value approach will uniquely position us as a choice investment in the technology sector. Our OpenText team members have proudly delivered a solid Q1 kicking off our fiscal 2024. On behalf of OpenText, I would like to thank our shareholders, our loyal customers, and partners.

I will now request the operator to open the call for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from Richard Tse with National Bank Financial.

Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Can I ask Paul a question here?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Richard, go right ahead.

Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Okay. Paul, so from your vantage point, you've obviously been in the role and been successful at it. What do you think have been the biggest, I guess, most meaningful driver to increasing Micro Focus's renewal rate here?

Paul Michael Duggan - *Open Text Corporation - Executive VP & Chief Customer Officer*

Richard, look, I think it comes down to 3 things. First, we moved fast to get Micro Focus on our OpenText practices for renewals, as I discussed in my prepared remarks. Second, that also meant moving quickly to integrate the teams doing the work, getting renewals doing renewals and sales doing sales. And we believe that when those lines are not clear, renewal rates tend to underperform. And I'd say, third, as I speak to customers, I think that they also see our product roadmap and the other things we've unveiled in terms of our AI path, and they recognize that information management is becoming really a gating factor to fully embracing those step functions. So I think all of those play a significant role in the decision to renew. And we can already empirically see that in the rental rates in the improvement we made since February.

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Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Okay, great. So, Mark, your recent OpenText World was a great event. Certainly a ton of excitement around Aviator. What's been the follow through since the event last month and maybe give us a sense of the momentum from a product perspective?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. As I said in my notes, the product cycle, customer engagement, clarity of our ability to provide practical value, all fed into our comments today on the call of increasing our bookings outlook for the quarter of 20% year-over-year growth. So we're definitely getting to the next phase of engagement to specific use cases. Product delivery in October, it's just November 2 or 3rd, so it's still very early November. We have the next wave of product delivery in January. We've engaged with customers. Got fantastic feedback from OpenText World, including 500 partners who were with us in Vegas, and we're in engagements now and we're going to win our first business, and you're going to see it reflected first in bookings and thus our 20% year-over-year growth expectations for the quarter.

Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Okay. And then just a last one for me. Certainly appreciate the shift here to an organic growth focus. But I imagine you still have a fairly robust M&A team evaluating transactions. And so I'm just curious, given the backdrop today, what's your sense of the acquisition landscape, perhaps from an evaluation standpoint? And if you came across a great opportunity, would you be in a position you think to move on something within the next 12 to 18 months?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. I have the organization focused on a singular powerful concept, information management. It's a $200 billion market. We are transitioning from M&A driven growth to organic growth. And that starts with a rich product pipeline, unlocking value in the cloud, new value areas of SaaS and AI, and that is an enhanced motion for us, with expectations of 20% year-over-year growth in our enterprise bookings. So that's -- we're focused on a singular powerful concept. And we're going to remain focused on a singular powerful concept. For sure, if we find an opportunity, like we did recently with KineMatik, that can enhance a specific aspect of our product in the context of our strategy. We won't be bashful at all. But we're focused on this singular powerful concept in our expanded mission in information management and being driven primarily by organic growth.

Operator

The next question comes from Thanos Moschopoulos from BMO Capital Markets.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Technology Analyst*

Also a question for Paul. Just to be clear, what remains on maximizing the renewals at Micro Focus. Is it primarily a question of going through the annual renewal cycle with all the customers or are there still some key steps that need to be done internally to really drive that organization to its potential?

Paul Michael Duggan - *Open Text Corporation - Executive VP & Chief Customer Officer*

Yes, great question. It's a number of things. So you nailed the first one right. We actually got to get to each of the renewals. And like I had said in my remarks, we'll be mostly there by February. And look, I think the step functions for us from there are really going to be value driven, the product roadmap, the conversations we're having around that. I think those are the things that really go into decision points on renewal. The things that we see today are really, in large part, decisions that were made 12 months ago. So you got to go, rewind the clock back, and look at the product roadmap at that time, and look at what was out in front of the customers at that point.

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So there's going to be some runup here, I think, of you're going to get these initial improvements and benefits from all the systems and all the processes and those sorts of things. And then the longer end of this is going to be all about the intrinsic value of our offering. And you saw it with Documentum. Like I'd mentioned, we started in a very similar place, low 80s. The Documentum business is running ahead of our average renewal rate. So we're in the mid-90s, and we've been there for some time. So there's confidence in our playbook. We've done it before. There's a scale with this, but it comes down to these fundamentals.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Technology Analyst*

Great. And then, Mark, just in terms of integrating the go-to-market, it sounds like you've done the heavy lifting for integrating your internal teams. But as far as integrating the Micro Focus and OpenText channels, where does that stand, how much opportunity remains on that front, and when do you expect to start capitalizing on some of that?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. Certainly, our direct sales forces are fully integrated and fully aligned as we kicked off the fiscal year. We have in the investor deck, I think, it's Slide 18 where we talked about that segmentation, really important. We've really matured as we've scaled up to our current revenue levels, and looking well beyond the full coverage out into the Global 10,000. We now have very formal segmentation, and it's very well aligned to how Oracle thinks of the world, SAP, Microsoft, we're now in that category. Strategic accounts, enterprise accounts, corporate accounts, business accounts, and home accounts, very well-defined stratification, very well-defined go-to-market. We are one sales organization pursuing those market areas.

Where we have more work to do is on the partner network that we launched in July. Partner networks, by definition, they're networks, so they got a lot of tentacles that go out over many, many years. We announced our landing zone for all our partners, including Micro Focus partners, of deal registration. We announced where they can engage on selling cloud. We began the AI discussion with them and where we want to be kicking off July 1 next year, takes systems, takes contracts, takes execution. But we announced where we want to land come July 1. So there's a little work to do there between here in November and June of next year. But on the direct enterprise side, we're fully aligned, we're united, we're one organization. We have one organization on the new partner network, and we defined our landing zone of where we want to be July 1, announced it to partners, we're working on all the details behind it. So that's the remaining work, Thanos.

Operator

The next question comes from Paul Treiber with RBC Capital Markets.

Paul Michael Treiber - *RBC Capital Markets, Research Division - Director of Canadian Technology & Analyst*

Your outlook to achieve 20% cloud bookings growth this quarter is great, and it seems like an inflection from Q1, which is only 8%. Is that the right way to characterize it? Is that new AI products are likely to drive an inflection and growth for OpenText? Or is that reading too much into it and there's maybe just quarterly dynamics between Q1 and Q2?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Paul, thanks for your first question to me, so I appreciate that. Just kidding. So, no, our 20% bookings growth, we're going to see our first AI bookings in that number. So AI is going to contribute. As we talked about 2 quarters ago, we announced our direction. We have a strong history over a decade of innovation in AI. We presented for customers how to get practical value. We announced our roadmap. Now we've delivered wave 1. We're delivering wave 2. And it's being very well understood where we can start to unlock value across our Platform being built in, our Thrust services, Search, IoT and each of the Aviator Business Clouds.

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And it's interesting kind of a new language we're hearing from customers, and we're helping them get there, is that through our business clouds, we're helping them build these AI personas. So they have contract administrators today, but now they're going to build the AI persona of the contract administrator or mortgage advisor or technical support assistant. So now that 20% expected bookings growth year over year has AI contribution to it. And look, our Q1 is always seasonally light. And it's our Q1, I know it's the world's Q3, but it's our Q1. And so our customers are trained that way. But no, that number reflects our next set of wins in AI, and I can't wait to present them to you.

Paul Michael Treiber - *RBC Capital Markets, Research Division - Director of Canadian Technology & Analyst*

And you've had product releases and product cycles in the past. You sound quite enthusiastic about AI. Could you give us some context around how customer interest and the sales pipeline for your new AI products compare versus previous product releases?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Well, sure. I think, I'll say 2 things. The first is I don't have to spend a dollar of marketing on AI. The whole world's talking about it. So that's an interesting new dynamic, right? So customers are proactively engaging. The world is very focused on generative AI. We, of course, think the landing zone is general AI because there's a lot more to it than just the generative aspect. So, Paul, dynamic #1 that's different is the world's talking about it and it's got a big awareness aspect built in.

Second is we have very relevant product sitting on top of very large datasets that we've helped to build for our customers over the last year. And we believe this is the inflection point, the singular powerful concept that unlocks information management to its next level in the enterprise. There was inflection points for ERP and CRM of integrated e-business suites. This is an inflection point for information management to unlock the value of those datasets. So you've got natural demand being driven by market and breakthroughs in technology, [the baby speaks]. And #2, we have very relevant and very timely technology on top of our platform. And as I said at OpenText World, it is okay to speak this way. We were late in SaaS. We are not late in AI, and we're going to capture the opportunity here for the company.

Operator

The next question comes from Kevin Krishnaratne with Scotiabank.

Kevin Krishnaratne - *Scotiabank Global Banking and Markets, Research Division - Analyst*

Just a couple of clarifications. You said Micro Focus contributed $563 million in the quarter. Is that correct? And if so, was that within your expectations or is it going better? And do we have a margin for Micro Focus in the quarter?

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Yes, Kevin, it's Madhu here. So, yes, $563 million in revenue. And as we mentioned, the integration is going very well. We are ahead of our internal plan. And from a margin perspective, I would point you to the fact that being ahead of the plan, we are able to project that Micro Focus will be on our 36% to 38% this fiscal year, which is really the first full fiscal year since the transaction closed.

Kevin Krishnaratne - *Scotiabank Global Banking and Markets, Research Division - Analyst*

Okay. And then a second clarification here, just on the SMB dynamic. I think you'd mentioned a $10 million to $15 million year-over-year revenue headwind, is that correct? And just curious if you can dig into that a bit more and then remind us, if you can, on how big SMB is in your base.

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Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Yes, I'll comment and I'm sure Mark will chime in as well. So, $10 million to $15 million revenue headwind is what we see in Q2. We pay attention to a couple of cycles, obviously the PC cycles, and of course, all things associated with Microsoft as it intersects with our SMB business. Now, having said that, I think Paul also mentioned in his notes, that we do have some products and innovation and new items to bring to market, and we factored those into account for the second half of the fiscal year. And overall, we remain on target for our fiscal '24 revenues, including the cloud revenue. Mark, anything to add?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes, sure. This is not an OpenText challenge. This is a market challenge. And we all read the same headlines about the challenges in SMB. And SMB is less than 10% of our business. It's a new area for us. We've only been in this area 2 to 3 years. We're never going to realize our full potential in information management if we can't get to that midmarket. And we're much more interested in the midmarket than the S, the small part of the market. So, as Microsoft has recently said, it's the most important sector for them. And as they do well, we will do well. As PC shipments rebound, we will do better. We're also bringing new product into this area, like our service management, midmarket business network capabilities. So it's really not our challenge, it's the market's challenge right now. And we're so well positioned that as the market picks up, we're going to be a beneficiary of it, but we wanted to call it out just to be clear on our cloud momentum and help you model the business.

Operator

The next question comes from Stephanie Price with CIBC.

Stephanie Doris Price - *CIBC Capital Markets, Research Division - Executive Director of Equity Markets Research*

I just want to circle back on the focus on achieving organic growth at Micro Focus in fiscal '24. Just curious if you can share what organic growth at Micro Focus was this quarter and how you expect to trend over the fiscal year. As you work towards organic growth at Micro, obviously, maintenance is going to be the key driver. But also curious if there's anything else we should be thinking about there as we think about organic growth in business by the end of fiscal '24.

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Yes, Stephanie, it's Madhu here. So I'll take the first thought, how to think about Micro Focus organic growth in the quarter. It's going to be a hard year-over-year compare. As we said in the last couple calls, our starting point is $2.3 billion of revenue. You take IFRS to GAAP, you take the Digital Safe divestiture, and we did decide to shed some contracts and not carry them forward. And $2.3 billion is really our baseline. And at $563 million, we've done well. It is our first quarter of this fiscal year, and we do expect to grow organically in the entire year. And everything you heard so far on the Micro Focus integration, the customers, the partners, all of that is going to play a role for us to exceed the $2.3 billion number.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. And Stephanie, let me jump in as well. We're doing exactly what we said we would do, and we're going to show you Micro Focus every quarter for this fiscal year, though we don't have to through disclosure, but we're going to. You take $2.3 billion divided by 4, that's $575 million. Our first quarter, seasonally a light quarter for us in Q1, we delivered $563 million, and you'll see that momentum build, and it's really that simple. We are very confident we're returning Micro Focus to organic growth. We're off to a great start. And as Paul talked about the renewals, our strong product cycle with private cloud, new SaaS offerings, and SMAX, Fortify on-demand, NetIQ, UCMDB, SaaS, a first set of AI on top of Micro Focus, which they would've never been able to get to if not part of OpenText. So we're doing exactly what we said we'd do. We're going to show you every quarter along the way. And we're off to a great start at $563 million.

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Operator

The next question comes from Raimo Lenschow with Barclays.

Jeremy Asher Horowitz - *Barclays Bank PLC, Research Division - Research Analyst*

This is Jeremy on for Raimo. Just wanted to follow up on the SMB headwind that you called out. So is it having maybe an outsized impact on any of the business lines, like with security having Zix and Carbonite, which is more SMB focused, is it showing up more there? Or really anything you can call out there would be helpful.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Jeremy, I would call it a headwind, maybe a light breeze. And we provided the additional color to help you model. Really simple, right? So there's no product to point to across the portfolio. Again, it's not us, it's the segment. PC shipments are clearly down, so there's less to sell into. Microsoft had delayed certain programs. They've now recently declared this is the most important segment, so it's going to build momentum. So, no, nothing specific to point to. I would not call it a headwind, maybe a light breeze. And it's the segment, it's not us, it's not something specific. And we're excited about being a beneficiary as PC shipments go up, as Microsoft builds their amazing machine here.

Operator

The next question comes from Adhir Kadve with Eight Capital.

Adhir Kadve - *Eight Capital, Research Division - Principal*

Maybe outside of the AI showing up in bookings and driving that 20% growth, is there any other particular areas across the 6 markets that you've defined, Mark, that are really driving that confidence in the 20%?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

SaaS. So SaaS and AI. Titanium was focused on many things, but top of the stack was SaaS applications, having core content, core signature, core capture, core archive, starting to get into the machine, SaaS-based service management, which we call SMAX, SaaS-based security through NetIQ, SaaS-based asset management with the Universal Configuration Management Database or UCMDB, so getting additional products in there as well, midmarket SaaS and business network. So here I'd say it's 2 things: it's Titanium, deliver the product, start to get in the market, build demand, win business, and it's the second value unlocker of AI starting to get its first win.

Adhir Kadve - *Eight Capital, Research Division - Principal*

And then just on AI, you guys introduced a fairly robust product roadmap as well as products that are in market right now. Mark, any of those that are really driving excitement or really driving undue excitement from your clients that you could speak to?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Oh, I have to pick a child which one I like. No, I think it's going to follow where the datasets are and the value that we can unlock. I'll start right in our heritage in content management and building these Aviator personas next to the human persona for the claims manager, the claims adjuster, the contract author. So content certainly is up there. I'd also say in ITOM. We have a very large install base around service management and the

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ability to create that AI Aviator persona around the technical support assistant. So content, ITOM, I would probably shout out are going to lead the way early. Now with that said, the general applicability of Search, very interesting for us and a lot of workloads out there for machine-generated and device-generated content via IoT. But I'd look to content and ITOM here in the early days.

Operator

(Operator Instructions) The next question comes from Steve Enders with Citi.

George Michael Kurosawa - *Citigroup Inc., Research Division - Research Analyst*

This is George on for Steve. I want to talk about the AI products at the Aviator set of products. You guys were fairly quick out to market with them, which I think is a testament to that 90-day release cycle. But maybe you could just talk about the decision to monetize these when maybe some of your customers are in an experimental phase and I guess how are we thinking about the timeline to revenue contributions?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

As I said last quarter, until we have revenue signals, we're not going to change our outlooks, if you will, until today. And I look at Q2 and we've gone through this whole cycle of the [baby speaks] through generative AI in the consumer world, the rise of algorithms, the ability to do that in the consumer world, we've worked with our partners, Google and others, to ensure they can be private environments. We have our own technology that we've advanced to do certain aspects of the AI preparatory work for customers, embeddings, vectorization. We've worked through a lot of the technology hurdles to have pluggable language models because they're going to get very specific. And we've now with 23.4 have wave 1 of very practical capabilities. 24.1 brings the rest of the business clouds to very practical capabilities. And we're demonstrating how within content management, business network, in the ITOM space, in the developer space, where you can apply these Aviator personas to sit next to the human to add significant value. So this is the next step, and we're seeing the first demand signals and thus calling it out that we expect to see 20% bookings growth year over year.

George Michael Kurosawa - *Citigroup Inc., Research Division - Research Analyst*

Got it. Yes. That's a really encouraging number. Maybe just to double click on that 20%, loud and clear that AI and SaaS are the top 2 drivers. Is there any contribution from Micro Focus adoption of private cloud in there, or is that maybe a little farther down that line?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

There'll be some in there, sure.

Operator

The next question comes from Daniel Chan with TD Cowen.

Daniel Chan - *TD Securities Equity Research - Research Analyst*

Hey, Mark, earlier you were mentioning that your customers were trained on your fiscal year end. Micro Focus's fiscal year end is in October. I know you've been trying to move some of those customers onto your timeline, but should we still expect a large number of their customers to still be on the Micro Focus fiscal year end?

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Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Look, Dan, I think it's going to take a year or 2 to get the full quarterization from the Micro Focus install base. And thus Madhu's comments on paying attention to the quarterization. And we spent a lot of time -- Madhu and team spent a lot of time on the quarterly factors for Q2 and just a clear shout out to balanced models in the second half of the year. So, look, we're making progress. We're going to always default to the customer and what the customer wants to do. But we're going to get to the OpenText cycles. It'll take a year or 2, but we'll get there.

Daniel Chan - *TD Securities Equity Research - Research Analyst*

And then appreciate the color on the SMB impact from the macro. Just wondering if there's any update on the enterprise side of things. Last quarter you said things were still looking good. Just wonder if there are any updates on the enterprise customers.

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Yes, from the enterprise customers, Dan, thank you again for the question, and I assume you're referring to the cloud side. Things are looking strong, and certainly that's why we called out SMB. Going back to all that Mark said, in addition to the AI, the core solutions that we continue to build upon and innovate, there continues to be strong demand for those, all business clouds included, right? So on the enterprise side, cloud, non-SMB continues to be strong.

Operator

I will now hand the call back over to Mr. Barrenechea for closing remarks.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Very good. Madhu, Paul, thank you. And thank you, everyone, for joining today. Look, we're very excited to engage with you and tell you more of our story and on our new model for growth. And we're going to be participating at many upcoming conferences, as Harry noted: the RBC Conference, November 14, New York City; the Needham SaaS Conference virtually on November 16; TD Securities Conference, November 21 in Toronto, which I'll personally be at; the Wells Fargo Technology Summit, the 29th in Rancho Palos Verdes; the UBS Global Tech Conference, November 30, Scottsdale; Scotia, December 5 in San Francisco; Madhu is going to host the Nasdaq Investor Conference in London on December 5; and we'll be at the Barclays Global Tech Conference December 7 in San Francisco. Look forward to connecting with you, telling you our story. And may the one that brings peace, bring peace for all. That ends the call today, operator.

Operator

This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.

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