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OTEX.TO - Q1 2021 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 2021 Conference Call. (Operator Instructions) And the conference is being recorded. (Operator Instructions) I would like to turn the conference over to Mr. Harry Blount, Senior Vice President, Investor Relations. Please go ahead, sir.

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

Thank you, operator, and good afternoon, everyone. On the call today is OpenText's Chief Executive Officer and Chief Technology Officer, Mark J. Barrenechea; and our Executive Vice President and Chief Financial Officer, Madhu Ranganathan. We have some prepared remarks, which will be followed by a question-and-answer session. This call will last approximately 60 minutes with a replay available shortly thereafter.

I would like to take a moment and direct investors to the Investor Relations section of our website, investors.opentext.com, where we have posted our consolidated investor presentation that will supplement our prepared remarks today.

The presentation includes information and financials specific to our quarterly results, notably our updated quarterly factors on Page 9 as well as strategic overview. Please also note the following update on our Investor Day. We are moving our previously announced Investor Day from next week to early next year. We just provided a tremendous amount of new information at OpenText World, and we have our earnings call today, and Enfuse is just around the corner. We will also be attending several investor conferences in the coming weeks. I'm pleased to announce that OpenText management will be participating at the following upcoming virtual conferences: TD's Canadian Technology Conference on November 16; RBC's Global Technology, Internet, Media and Telecom Conference on November 17, Needham's Data Analytics and Infrastructure Software Conference on November 18; NASDAQ's Investor Conference on December 1; Credit Suisse's Technology Conference on December 3; Raymond James' Technology Conference on December 8 and Barclays' Global Technology, Media and Telecom Conference on December 10. We look forward to virtually meeting with investors in the coming days and weeks.

And now I will proceed with the reading of our safe harbor statement. Please note that during the course of this conference call, we may make statements relating to our 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 the material factors that could cause actual results to differ materially from a conclusion, forecast or projection in the forward-looking information as well as

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risk factors, including relation to the current global pandemic that may project future performance results to 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 direct comparable GAAP measures may be found within our public filings and other materials, which are available on our website.

And with that, I'm pleased to hand the call over to Mark.

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

Thank you, Harry. Good afternoon to everyone, and thank you for joining today's call. I want to continue the conversation we started at OpenText World where we gathered over 7,500 information management professionals focused on the future of business and work. COVID-19 has changed everything from the way we work, to the way we live to the way we conduct business. There will be many structural and long-lasting changes due to the change in human behaviors, including work from anywhere, direct-to-consumer commerce, contactless experiences and payments, to extreme customer experience expectations in new supply chains.

Before the pandemic, Industry 4.0 was just getting started, and now it's in full acceleration. I call this the new equilibrium and it's driving the fastest, deepest, most consequential technology disruption in the history of the world and thus creating tremendous opportunity. Businesses are accelerating their digital capabilities and are placing greater emphasis on time to value, all things cloud, customer experience and edge computing. And they are all looking to proven, trusted global partners, such as OpenText, to help them navigate these seminal times. This new equilibrium has also changed OpenText as I chronicled at OpenText World. You can clearly see how we become even more digital and extended our lead in the cloud. Since the beginning of the pandemic in the calendar year, we've conducted over 10 million team meetings in Chat, processed over 320 million e-mails through support and as a company. We are managing 250 million secure endpoints, an estimated 100 million end users, 11 million cloud subscribers, 75,000 enterprise customers and over 2,000 private cloud customers.

It has been our vision at OpenText to build organically and through M&A, the most comprehensive information management cloud platform for the future. And with the introduction of our new architecture, Cloud Editions, running in the OpenText Cloud and other clouds, we have never been better positioned to deliver for our customers in the new equilibrium.

We're delivering massive new capabilities every 90 days. We already have over 1,000 customers on Cloud Editions. And by Cloud Editions 21.4 just 1 year away, our customers will never have to upgrade again. I know I've said this in the past, but let me repeat it as it is so important. 10 years ago, license was 26% of our business. In Q1, it was 9%. We have derisked the business over time. 10 years ago, we had 0 cloud revenues. Now it's our largest revenue line, $341 million in Q1 or 42% of our revenue, and it is now the first revenue line on our income statement. Madhu will speak more about this in a couple of moments.

Our customer support business continues to expand, and customers leverage our updates and new security features, both in the cloud and off-cloud. We had a 94% renewal rate in Q1 for our customer support business.

Our annual recurring revenues were 83% in the quarter, and we became a cloud company while expanding adjusted EBITDA to an upper quartile, 42.6% within the quarter. I said many years ago, we were not born cloud, but we are reborn cloud, and we would create the new OpenText at higher margins and sustained efficiencies and we did. And soon, again, with Cloud Editions 21.4 customers will never have to upgrade again.

Our Cloud Editions are well aligned to the digital needs of our customers. The OpenText Content Cloud is benefiting from businesses that need cloud-based information platform to seamlessly and securely support content management, process management, collaboration, applications and new capabilities like e-signature.

The OpenText Experience Cloud business is benefiting from the trends to all things contactless, the direct-to-consumer explosion and all the associated technologies that enable omni-channel and social commerce. The OpenText Security and Protection Cloud, our Cyber Resilience business

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is benefiting from the work from anywhere and the integration of corporate and home networks. The need to protect devices, everywhere and anywhere, is growing in importance and will only become more profound as 5G bandwidth becomes ubiquitous and the connections to human and machine-based devices explode.

The OpenText business network cloud, our business network is benefiting from the acceleration to digital as companies become more mobile and regionalize. If a country can't get raw materials to build a product, they're going to move their supply chains. And our new OpenText developer cloud, API-driven, driving the API economy. Embedding OpenText information management into the next generation of customer and SaaS applications is a key long-term strategy for us.

OpenText has already seen the benefit of the new equilibrium as businesses accelerate owning their digital capabilities. Information management's time has come. And we aren't just ready rather we are leading in the cloud, and our domain leadership positions us -- our domain leadership positions have never been stronger, and our Q1 results reflect that. It was the best Q1 and strongest start to a fiscal year in the history of our company and another record high for our key businesses of cloud and customer support and a record high for our annual recurring revenues.

For the quarter and on a year-over-year basis, total revenue of $804 million, up 15%; Cloud revenue of $341 million, up 44%, customer support of $329 million, up 5%, ARR of $670 million, up 22% and at 83% of total revenue, the highest in dollars and percent in our history, demonstrating the predictability of our business.

Adjusted EBITDA of $342 million or 42.6% adjusted EBITDA margin, also the highest in our history. The company has never been this productive and efficient, and we've gained efficiencies over the last few quarters and free cash flows of $219 million, up 84% and 24% of revenue, that's Q1 in our history.

By the end of the quarter, our business network volumes had returned to pre-COVID-19 levels, except for those industries still affected like hotels, hospitality, airlines and a few others. We had many notable customer wins in Q1 that included Sephora, the global retail provider of personal care and beauty products, WM Morrison, one of the largest supermarket chains in the U.K., Pacific Gas & Electric; one of the largest electric utilities in the United States; Southern California Edison, one of the largest electric utilities in the United states; Hydro-Québec, one of the largest electric utilities in Canada, ON Semiconductor; FreshDirect, Heritage LAB Express, the California Department of Managed Health Care, the U.K. Department of Works and Pensions; and Texas A&M, a public research university in College Station, Texas. I'm so proud of my colleagues for their focus and commitment to our customers.

At the beginning of COVID-19, we took several preemptive actions given the historic nature of volatility the world was about to face. Six months later, our business is operating stronger and more efficient than before the start of the pandemic due to our business leaders, great execution and accelerated digital automation. You can see in our improved operations and results, the predictability that ARR brings to our business model, the strength of our margins and cash flow and our forward confidence in continuous improvement.

Given our new operating efficiency and confidence in the road ahead, we are announcing a variety of key actions today. We repaid the $600 million drawn on our revolver and there are no outstanding balances. We are restoring all salaries and benefits. We have opened over 400 new positions in innovation and sales. We are investing in products and sales, and we look to strategically hire the best global talent.

Two years ago, our R&D investment was approximately $300 million per year. This fiscal year, R&D investment will exceed $400 million a year. We're also announcing today that we're increasing our quarterly dividend by 15% to $0.2008 per share from $0.1746 per share for holders of record December 4, 2020, with a payment date of December 22, 2020, as approved by our Board of Directors. We continue to target 20% of trailing 12-month free cash flow for our dividend program. And we have increased our dividend rate 15% every year since its inception as we have increased cash flows.

With this quarterly dividend, we will have returned over $1 billion in cash to our shareholders since 2013. We're also returning to our standard cadence of reviewing our dividend rate at the end of each fiscal year. And today, we announced a new share repurchase plan of up to $350 million over the next 12 months. The announced repurchase plan is additive to our returns-based capital allocation strategy intended to complement from time to time, our ongoing M&A activity and dividend program.

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I want to spend some time today on our unique total growth strategy of retain, grow and acquire. On retain, We had another great quarter with our customer support renewal rates at 94% and margins of 91%. Our enterprise cloud renewal rates remained strong in the mid-90s. With our Digital Zone and new cloud platforms, we see opportunity to improve the quality of our customer experience even more by automating portions of the renewal process, enabling our CF personnel to spend more time with customers on cross-sell and upsell.

Again, with CE 21.4 all new updates, features and facets will be automatically immediately available to all customers.

On growth. Over the last few quarters, we've made significant investments in our go-to-market. Let me highlight some key aspects of this. Having 5 domain clouds versus many point products simplifies our customer messaging and our go-to-market friction. We can accelerate customer time to value through our managed services. We are accelerating our ongoing shift towards vertically-focused applications and solution-oriented selling such as public security, legal, cyber and the health care industry.

We remain on track to double our enterprise sales coverage of the Global 10,000 within 3 years. We continue to make great progress on cross-sell and upsell initiatives, specifically, our SMB&C channel has begun to successfully sell Carbonite, Webroot and Hightail products. On the enterprise side, we're seeing success cross-selling Carbonite, Webroot security offerings and Carbonite Migrate and High Availability products.

Finally, we are excited about the growing opportunities with partners. On the enterprise side, we have expanded relationships with Google, Microsoft, AWS, Salesforce, AT&T, SAP and others. On the SMB side of our business, we expect to grow our partners through increased sales focus, additional product offerings and the completion of the integration of the Carbonite and Webroot channels.

With our adjusted EBITDA above 40%, we are accelerating our investments in products and sales as we said we would, by expanding R&D investment dollars and accelerating our sales coverage and capacity, all for the Global 10,000 and SMBs.

On acquire. As it relates to M&A, we remain patient, disciplined, value-based buyers with ROIC and cash flow as key criteria, and we continue to build strong and actionable pipelines. I'm pleased to say that our Carbonite integration is ahead of schedule, and we achieved our financial integration goals in 10 months. We acquired Carbonite just last December, and we increased our cloud revenue, increased our ARR, increased our cloud gross margins and improved our cash conversion cycle. Carbonite continues to grow in its core market, and starting this fiscal year, we expect to begin seeing meaningful revenue synergies from cross-selling Carbonite products into our install base of enterprise customers and selected OpenText products through Carbonite SMB&C channel. Carbonite is a great example of our M&A strategy, a growth asset gave us strong entry and presence in cyber resilience in the SMB channel and met our disciplined value-based criteria while offering significant opportunity to create revenue synergies. Our balance sheet is strong at 1.8x leverage. Cash and cash flows are strong. We have capital to deploy, and we will deploy capital, as and when the right opportunity arises in our disciplined manner. Our total growth strategy of retain, grow and acquire is unique, massively scalable and delivering returns.

On our financial outlook, Madhu will cover the details of our financial outlook for Q2 and fiscal 2021 and our 3-year aspirations. But let me highlight what you will hear; an improved demand outlook and confidence in our operating model and future cash flows.

Let me summarize. OpenText is firing on all cylinders. Our ARR target model for fiscal '21 is 81% to 83%. Growth in strategic areas such as cloud and customer support and ARR, upper quartile margins of 42.6% adjusted EBITDA, already incorporating increased R&D and sales investments, new efficiencies and a high conversion ratio from EBITDA to cash flow, a healthy balance sheet at 1.8x leverage; on M&A, accelerated time to return for Carbonite on the OpenText model sooner than expected. Most top companies take 2 to 3 years to get these type of benefits. We've accelerated it down to 10 months, and the company is ready for the next set of opportunities.

We have a return-based capital allocation approach with increasing our dividend by 15% and initiating a share repurchase program up to $350 million over the next 12 months. And lastly, a new product platform, Cloud Edition that is aligned to the needs of our customers. We are not waiting to return to normal. I learned that in my personal cancer journey. This is the new normal, and we are going on the offense. We are stronger today than we were a year ago.

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On behalf of OpenText, I'd like to thank our shareholders, loyal customers, partners and 14,000-plus dedicated employees for all contributing to our success, and I am so proud of the resilience and durability that continues to be demonstrated. Finally, a big thank you to all the nurses, doctors, frontline responders, health care workers, those in the food industry, those in the delivery industry, those working in data centers and the power grid and distribution. Thank you for all that you do in keeping the world running.

It's my pleasure to turn the call over to Madhu Ranganathan, OpenText's Chief Financial Officer. Madhu?

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

Thank you, Mark, and thank you all for joining us today. We had a strong first quarter of fiscal '21. Our performance during the global pandemic reflects the underlying resilience and agility of our operating framework. I will speak to Q1, Q2, our quarterly factors, our fiscal '21 target model and our long-term aspirations as outlined in our Q1 investor presentation that is posted on our IR website today. I would also like to highlight that we have changed the order of revenue line. Cloud is now first, customer support second, and license third followed by professional services. We see this as a permanent shift to our revenue disclosures, reflecting the strength of annual recurring revenue growth led by cloud and customer support. All references will be in millions of USD and compared to the same period in the prior fiscal year. So let me start with revenues and earnings. Total revenues for the quarter were $804 million, up 15.4% or up 14.5% on a constant currency basis, including a strong contribution from Carbonite. There was a favorable FX impact to revenue of $6 million. The geographical split of revenues of total revenues in the quarter was Americas 63%, EMEA at 28% and Asia Pacific, 9%. Annual recurring revenues for the quarter was $670.4 million, up 22% or up 21.4% on a constant currency basis. As a percent of total revenue, ARR was 83% for the quarter, up from 79% in the first quarter of fiscal '20. Here, I would like to note that ARR was positive organic growth during the quarter on a reported basis. Cloud revenues are particularly strong at $341.0 million, up 43.7% or up 43.4% on a constant currency basis. This growth was driven by a strong contribution from Carbonite and exiting our fourth quarter a return to pre-COVID transaction volumes in our business network.

Our cloud -- our enterprise cloud renewal rate in the quarter remained in the mid 90s. Customer support revenues of $329.4 million, up 5.5% or up 4.8% on a constant currency basis. Our customer support renewal rate for Q1 was 94%, reflecting continued strong efforts of our team to drive renewals and support our rich install base. Our license revenues were $68.5 million, down 12% or down 13.8% on a constant currency basis. Our Professional Services revenue was $65.1 million, down 6.2% or down 8.5% on a constant currency basis. GAAP net income was $103.4 million, up 38.9%, primarily driven by higher revenue achievement and the savings of the preemptive measures introduced in the third quarter of fiscal '20.

Our adjusted net income was $241.9 million, up 39.4% or up 36.2% on a constant currency basis. GAAP earnings per share diluted were $0.38, up from $0.27. Our non-GAAP earnings per share diluted was $0.89, up $0.25 from $0.64 and up $0.23 on a constant currency basis.

And now turning to margins. GAAP gross margin for the quarter was 69%, up 180 basis points. Adjusted gross margin was 76.5%, up 340 basis points. Also, on an adjusted basis, cloud margin was 67.2%, up from 57.1% driven by continued improvement in our cloud service delivery and a strong contribution from Carbonite. Our customer support margin was 91.3%, up from 90.7% reflecting continued strong renewal performance. The license margin was 96.4%, down from 97%, primarily due to lower license revenue. Our Professional Services margin was 29.2%, up from 22.1% and reflects the benefits we see from lower travel while effectively delivering our solutions on a digital and remote basis. Adjusted EBITDA was $342.3 million this quarter, up 34.7% or up 32.1% on a constant currency basis. This represents a record 42.6% margin, up from 36.5% in the same quarter last year and higher than our fiscal '21 target model range of 37% to 38%.

Now turning to cash flow. It was excellent performance, with operating cash flows of $233.9 million for the quarter, up 70.2% and free cash flows of $218.6 million, up 84%. DSO was 44 days compared to 54 days in Q1 fiscal '20. The year-over-year reduction of 10 days is a real testament to our digital business services organization formed about a year ago that includes receivables, collections and other key financial operations as well as strong contribution in the quarter from the integration of Carbonite.

From a balance sheet perspective, we ended the quarter with approximately $1.8 billion in cash, given our strong cash flow performance. Our consolidated net leverage ratio is 1.82x an improvement from 2.04x last quarter. And subsequently in October, we repaid the $600 million that was previously drawn on the revolver, and we now have fully available $750 million revolver line of credit.

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As Mark noted, our strong balance sheet provides us the flexibility to navigate changing macro scenarios and provides ample opportunity to generate substantial long-term value for our shareholders through growth, dividends, and now as well as what Mark noted, potentially, share buybacks from time to time through our announced repurchase plan as a complement to our capital allocation strategy.

On Carbonite. Carbonite delivered another strong quarter of results with strong ARR, cloud margins, adjusted EBITDA and working capital. Carbonite's operations are already tracking to the OpenText operating model as of September 30, 2020. We achieved our financial integration sooner than planned. What we have looking ahead relates to systems and applications integration.

While we will continue to talk about the business, this will be the final integration update on the acquisition itself, a big shout out to the Carbonite integration piece.

So let's turn to total growth, target models and quarterly factors, all available on our investor website. First and foremost, we view our business as annual and quarters will vary. Long-term value is created from sustained annual performance and 90-day cycles are too short to measure. We are in a volatile macro environment due to health, financial and social crisis related to the resurgence of global COVID cases and the U.S. election. We continue to see deferring impact industry by industry and geography by geography. While we remain watchful of the macro environment, we continue to perform well on our business model, growth in cloud, growth in products and innovation and our strong cash flow enable us to continue to invest in go-to-market products and digital projects.

So now let me turn to our full year fiscal '21 total growth strategy. Compared to a quarter ago, our outlook for fiscal '21 has improved. We now expect mid-double-digit growth on cloud revenue compared to our previous target of low double digits. Low single-digit growth on customer support revenue compared to constant. High single-digit growth of annual recurring revenue compared to mid-single digits. No change in our license and professional service revenue targets, which we see declining and consistent with the broader industry trends and also as cloud adoption accelerates.

So with that, total revenue moved from constant to constant-to-low single-digit growth in fiscal '21. New M&A opportunities remain additive to our model. Our assumptions do not include an FX impact in the second half of fiscal '21.

On our fiscal '21 target model, we are pleased to share the following revenue target changes from a quarter ago. Annual recurring revenue gains moved up from 80% to 82% of total revenue to 81% to 83%. Our license moved down from 10% to 13% of revenues to 9% to 12% of revenue. On gross margins, cloud is maintained at 63% to 65% and customer support at 89% to 91%; our license at 96% 98%; and professional service margin is expected to move up to 20% to 22% from 18% to 20% as we continue to see benefits of remote deliveries and less travel. Gross margins overall remains at 74% to 76%, and our full year adjusted EBITDA expectations remain at 37% to 38% as we continue to invest in the business.

Our fiscal '21 target model fully reflects the savings from previously announced restructuring, the compensation restorations, Mark referred to in his commentary, and our fiscal '21 hiring plan.

So coming to our immediate quarter Q2, I would like to highlight the following quarterly factors here. We expect Q2 total revenue to be constant versus Q1 with a favorable FX impact up to $3 million. Our FX is based on current exchange rates, but note that currency volatility appears higher than normal. Annual recurring revenue is expected to remain constant in Q2 compared to Q1. Our adjusted EBITDA dollars are expected to decline low single digits in Q2 compared to Q1. As shared previously, we remain an annually focused business while our quarters will vary. On long-term aspirations, our long-term aspirations remain unchanged, following adjusted EBITDA aspirations of 38% to 40% and free cash flow of $900 million to $1 billion for fiscal '23 with a plan to reinvest any margin gains above 40% into additional growth initiatives.

For our tax update, the IRS matter is still in the appeals phase, and our resolve remains strong as we continue to vigorously defend our position.

So in summary, a special thank you to the entire OpenText community for their incredible efforts. Their contributions demonstrated continued resilience, leading the way in digital working, high productivity and a laser focus on results. And thank you to our shareholders, whose trust and confidence we greatly value, and wishing you all continued safety and good health.

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I would now like to open the call to your questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We will now begin the question-and-answer session. (Operator Instructions) The first question comes from Raimo Lenschow from Barclays. these.

Frank Joseph Surace - *Barclays Bank PLC, Research Division - Research Analyst*

This is Frank on for Raimo. Congrats on another great quarter. So Cloud was clearly very strong again. Would you be able to dig a little bit more deeper, provide a little bit more color on how some of those recent partnerships with some of the big cloud players like Google from this year, you're feeding into the cloud side of the business and how we could expect those relationships going forward?

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

Yes, Mark here. Thanks for the question. The strength of our cloud quarter, certainly driven by some of the return of our business volumes and the accelerated needs of our customers of time -- accelerated time to value. And the greatest time to value is to deploy our capabilities in our cloud or a partner's cloud. And as we look over the coming quarters and next few years, we expect the partnerships to really contribute to that cloud momentum. We've taken the approach with Cloud Editions that our solutions will operate across the hyperscalers: Google, AWS as well as Azure. And we continue to stay committed to customer choice where customers would like to place the workload.

We saw some wins, for sure, together with our cloud partners. And -- but the strength of the cloud was primarily driven both by Carbonite return-to-business volumes and an accelerated time to value from our enterprise customers.

Operator

The next question comes from Stephanie Price from CIBC.

Stephanie Doris Price - *CIBC Capital Markets, Research Division - Director of Institutional Equity Research and Software & Business Services Research Analyst*

Just on the cloud. Wondering if you can share a little bit more about Carbonite and maybe what the Carbonite contribution was in the quarter.

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

Madhu, are we speaking to the precise Carbonite contribution in the quarter?

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

No, we're not, Mark.

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

Yes. So Stephanie, there's no doubt that Carbonite had a significant and important contribution. The business is operating very well, both in the -- we first go to RMMs who then sell to SMBs. We have a bit of our business direct to SMBs, and we have our prosumer and consumer business that really came back from the early part of the start of the pandemic. We are also well underway of integrating the Carbonite and Webroot channels, which were not integrated when we acquired the business. And we've brought into the Carbonite channel new OpenText solutions to sell as well; and work-from-home is it's permanently changed, right, the hybrid work model. So it certainly contributed on the revenue side in the quarter.

If you look at our adjusted EBITDA at 42.6%, our relentless focus on fast, rapid integration, taking the cost out where we think we should, integration of the cloud teams, integration of engineering teams, Carbonite contributed as well to such stellar adjusted EBITDA. And in fact, so greatly, we're already on the financial model.

Stephanie Doris Price - *CIBC Capital Markets, Research Division - Director of Institutional Equity Research and Software & Business Services Research Analyst*

Great. And then on capital allocation, you mentioned a new NCIB here. Just wondering how you kind of think about capital allocation, share repurchases, maybe versus capital here?

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

Yes. Very good. Well, I'll just start with the large narrative on we -- companies talk about they're going to exit the pandemic stronger than they came into it. We're at a new operating efficiency within the business. And it's reflected in the efficiency, our processes, the new digital automation we're running internally, and it translated it into a higher level of adjusted EBITDA, and our conversion ratio from EBITDA to free cash flow is enormously high, given our effective tax structures and low CapEx deployment. So we have great confidence in the efficiency of the business and future cash flows.

With that in mind, that led us to getting back to our valuation of our dividend program. I know we -- 90 days ago, we didn't raise the dividend sort of on our annual cadence. So at this point, with that confidence, we paid back our revolver. We increased our dividend rate back to where we were, if you will.

And then looking at that strength in the cash flows, we thought we'd add an additional program, which was -- which is the NCIB, as you know. So we see that as an additional tool for us going forward.

Operator

The next question comes from Paul Steep from Scotia Capital.

Paul Steep - *Scotiabank Global Banking and Markets, Research Division - Analyst*

Mark, maybe talk a little bit just with the shift to the cloud happening fairly hard in this quarter. As we think about M&A in the future for OpenText, how -- has your willingness to maybe take on legacy assets that previously would have migrated, has that appetite maybe changed? Or is there maybe greater confidence? And then I've got one quick clarification.

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

Yes, sure thing. Our M&A strategy remains unchanged. We -- it is the great -- one of the greatest levers we have to adding value in the business conjunctive with organic growth, but our philosophy of M&A remains the same. And within M&A, it's really recurring revenues that we focus on.

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So we'll look for businesses that have high recurring revenues and recurring revenues are both cloud and support businesses or as I like to call them, update businesses.

So it's not exclusively cloud. It's much wider than that. It's really recurring revenues. That's our focus. Paul, you have a clarification question?

Paul Steep - *Scotiabank Global Banking and Markets, Research Division - Analyst*

Yes. That's great. So then just the other question, I think you've alluded to it. Should we be thinking -- and I don't know if you've set -- I don't remember a policy, but around net leverage ratio, should we be thinking that you're going to force that deployment of all the cash flow? Obviously, you look to the dividend as you just enumerated, but more importantly, about the return of capital through the share repurchase, should people think that, that level of the floor is maybe 1.5 or no, there isn't the floor and you're going to leave yourself flexible?

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

Well, let me jump in and then I'll hand the mic to Madhu as well. We're going to remain flexible. I'll talk about the ceiling first, then maybe the floor. On the ceiling side, nothing's changed our view that we like to operate around 3x leverage. We -- as I've said many times and chronicled through the years, I think it's very simply, if the market turns really bad for liquidity, which it hasn't, I'd like to be able to pay back our debt in 3 years. Therefore, the 3x ratio. We're not bashful about going over it in the short term, as we have done twice given our commitment and disciplined operations to bring it well under.

Again, the buyback is an additive tool. It doesn't change our M&A strategy. In fact, our pipeline and the due diligence activities are up, we see it as an additive tool given the strength of our cash flows. We've always targeted 20% of trailing -- used to be OCF but now FCF, but we target trailing 12 months, 20% of free cash flows to return that dividend and give us all the strategic opportunities we need. We now have the extra toll and stand a program on buyback. And M&A remains the top ROIC generator for us in deploying capital. And we expect to get deals done this year -- this fiscal year. Madhu, anything you'd like to add to that?

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

Yes. Sure, Mark. So Paul, when you think about apples-to-apples, right, when you asked about the floor, during our fiscal '20, we were about 1.48 net leverage when all the way slightly above 2 with Carbonite. And given the strength of the cash flow, we were able to bring it back down to 1.82. So I would really think about it that way going above with the feeling Mark has described. And again, the cash flow is going to allow us to have that band in the mid-1s to slightly above 2 if need be.

Operator

The next question comes from Richard Tse from National Bank Financial.

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

Mark, I think you said you had 1,000 customers today on Cloud Edition? Would you say, the average number of products taken up by those customers to be more than those that are not on Cloud Edition?

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

Yes. Richard, interesting question. I think that it's slightly above the off-cloud average. And part of our opportunity is really getting to a next-generation cross-sell and upsell and really focusing that in the cloud. Because with more integration and our efficiencies and as we march towards 21.4 where

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customers will never have to update again, we can turn on more solutions for customers at very, minimal expense running in the cloud and thus expose customers to more features and more modules and thus reduce friction.

So I'd say we're slightly up on kind of the average module usage in-cloud versus off-cloud. And this is a strength we're going to sell right into and leverage for cross-selling in the coming years, sort of pre-installing, pre-turning on additional modules for customer access.

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

Yes, especially with 21.4, it seems like there is probably a big opportunity for you to accelerate organic growth as the friction is reduced here. Is it fair to say that, that's something that we should think about here in terms of modeling going forward in terms of looking at organic growth and what that can mean to it?

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

I don't mean to do this but I'm going to hand modeling question to Madhu.

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

Yes. So, thanks for the question. As Mark said, directionally, absolutely, from a modeling perspective, we have shared all our perspective. So I would really use the boundaries and parameters we've shared from a margin perspective. But certainly, opportunities in the future it's really exciting.

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

Okay. And then maybe I sort of misheard, but I think the way you talk about your sales cycle, even though this health backdrop that gave us sort of a kind of gone back to the normal with the exception of some of those verticals you pointed out. That seems different from some of the things that we've heard from other sort of enterprise companies that we cover. But I just want to make sure that I sort of characterize what you said correctly?

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

Yes, Richard. So just gave a recap. And it's -- in our investor presentation as well, and let me just see if I can quickly get to the page number, which is Page 7, fiscal year '21 OpenText total growth strategy where we have our revenue lines and what the expected growth rates are for the year. We have certainly seen our business network volumes return to pre-COVID levels, except for some of the well highlighted industries that still haven't recovered: hotels, hospitality, airlines and a few others. So we're not back to full revenues. We're back to pre-COVID levels except for those industries. We are increasing our outlook for the year on cloud as we do highlight it from low double digit to mid-double digit, customer support from constant to low single-digit, ARR from mid-single digit to high single digit, but we're also still looking at [license] (corrected by the company after the call) and PS at the same levels we talked about last quarter, which is -- we're not changing the outlook on license and PS, which we expect to decline this year. So the transactional side of the business hasn't returned to pre-COVID levels. But the vast majority of our business network has, and that's translated into an updated and increased outlook for the year, among other things. Is that helpful?

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

Yes.

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Operator

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

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

I want to drill deeper into the cloud guidance. So if I take your Q1 cloud revenues and just flatline them for the rest of the year, that would give me high teens cloud growth on a full year basis, though you're guiding for mid-teens cloud growth. So that would imply some erosion. And I appreciate you like to be conservative with your guidance, but can you comment on whether there are some dynamics or some risk we should be aware of that could cause that erosion. I mean, is it maybe just the transaction businesses in the verticals you called out where there could be a risk of some further weakness? Or how do we think about that?

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

Yes, let me speak a little bit to the business and have Madhu maybe speak a little bit to the model. The -- I'm very pleased with how the volumes have returned to pre-COVID levels. And some industries are still very heavily affected, and we don't know the timing or the consolidation that may happen in those markets as well. So that's a bit of an unknown. That's informing us to talk about cloud at mid-double digit. And there's also remained volatility in the world, as we all well know. And with the next wave in Europe and how far behind is North America. What I'm certainly seeing is that it's a very different business reaction in this wave versus the first wave, where there's a very focused view on keeping business running in a healthy way and safe way through the second wave. But it's a long way to say it still remains a bit of a volatile market.

What we do know and -- is that we're going to -- we're increasing our outlook for the year from low double digit to mid-double digits. And you said it well that there's still some affected industries in our business network. And we're still going to remain a little cautious just given the volatility in the world. I think it's a fine place to be.

So Madhu, anything you'd like to add?

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

No, Mark, you covered all of the pieces. And Thanos, I would point you all of Mark's comments, which we have factored into our Q2 quarterly factors as well as the annual outlook.

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

Great. And you take down the revolver, should we take that as a negative indicator with respect to the size of your near-term M&A pipeline? Or is it less about that and more about your confidence regarding the stability of financial markets relative to what the world looked like when you initially drew that down?

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

Yes. Pretty straightforward for us. It was uncertain if there would be a liquidity crisis early in the market, early during the pandemic. That didn't turn out to be so. But we're no wiser than the next person, so we took a preemptive action. I'd do it the same way all over again. I hope I don't have to, of course. We also have reached a new level of efficiency. So we decided to pay back.

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

So again, nothing in particular to read into as far as what that means for pipeline, having a new pipeline?

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

No, not at all. The revolver remains -- they are active. It's a fully available facility of $750 million. It was the volatility and uncertainty around the liquidity in the markets. And many companies pre-drew the revolver. We weren't alone doing that. And now that it's much clearer on the liquidity in the markets, we decided to just reduce our expense and pay back the revolver.

Operator

Next question comes from Paul Treiber from RBC Capital Markets.

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

I just wanted to kind of have a high-level question, and it ties into your comments at Enterprise World, but we're seeing massive change in the industry with work from home and collaboration apps moving to the cloud and other options the cloud and new digital transformation. And it seems like the importance of enterprise information management would also go with it and become more important.

And are you seeing that from your customer base or in your pipeline, the increasing importance put around enterprise information management?

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

Paul, absolutely. I very prescriptively use the phrase in my script that I believe that information management, its time has come. And look, we were going into the fourth industrial revolution before the pandemic. And for many, that was still kind of academic, but the pandemic has turned the academic into the acute. And companies need to operate, right? They need to operate and share information. They need to go through financial closes, regulatory submissions. They need to manage -- I hate to say look how the Canadian government is being challenged with not having network access and full utilization of tools.

So it's gone from academic to quite acute in the ability to simply run on an information platform, share, collaboration, project management, workflow, form, e-signatures. And it's a brilliant basics in being able to do that globally and at scale that is benefiting us.

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

And then it seems like most companies are taking a -- or have taken a piecemeal approach to the cloud or particularly information management in the past. And you mentioned that the 1,000 customers, enterprise customers that deployed CE, I think you have a total number of 75,000 enterprise customers.

Do you anticipate or is it reasonable to anticipate that eventually all or the majority of those customers would need a cloud EIM strategy?

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

Short answer is yes. Short answer is yes. Maybe it's 5%, 10% that doesn't in some very unique security requirements, but we'd offer a private cloud in those cases. But to get that accelerated time to value, the fastest path is to deploy in one of our domain clouds unequivocally. And we have a long way to go. It's the greatest opportunity we have is to continue to upgrade, transform, new deployments into the OpenText platform. One of the reasons we announced that in OpenText World, 7 days to the cloud. And we have more standard products, we're preinstalling instances, the ability for enterprise customers to stand up new workloads, it could take months and months and months. We can get it done down to a week now for standard deployment.

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

And last question for me and maybe the hardest one, but in terms of time frame of -- is this like a 5-year cycle? Is it a 20-year cycle? I mean, how do you think -- how quickly will companies prioritize this transition?

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

Well, we're unique. I will highlight our -- the journey that we've been on in using chess terms, is it the early game mid game or late in the game. For us, we've gone to where license is 8% of our business in the quarter. So we're in that last -- we've sort of completed the last mile here. And I'm going to point to Cloud Edition to 21.4. As I said at OpenText World and again here today, we are very focused on these 90-day cycles. And it's not only that it's faster, we're actually bringing more features to market in these shorter cycles. And by Cloud Editions 21.4, which is just actually a little less than a year from now, 11 months, we'll be at a point of where customers never have to upgrade again. All features, all capabilities, all facets will be automatically available, and customers will have a clear path to never upgrading again, running in our cloud.

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. Well, I'd like to thank everyone for joining us today. We wish everyone much happiness, health and well-being in these very volatile and seminal times. And we look forward to seeing you -- I hope you can join us at Enfuse over the coming weeks, and we look forward to our discussions, engagement, one-on-ones as well as our upcoming conferences. Thank you for joining us today.

Operator

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

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