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EDITED TRANSCRIPT

OTEX.TO - Q2 2022 Open Text Corp Earnings Call

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PRESENTATION

Operator

Thank you for standing by. This is the conference operator. Welcome to the Open Text Corporation Second Quarter Fiscal 2022 Earnings Conference Call. As a reminder, all participants are in listen-only mode, and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. (Operator Instructions).

I would now 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's second quarter fiscal '22 earnings call. With me on the call today are OpenText's Chief Executive Officer and Chief Technology Officer, Mark J. Barrenechea; and our Executive Vice President and Chief Financial Officer, Madhu Ranganathan. Please note that we have shortened our prepared remarks this quarter to allow more time for the question-and-answer session. Today's call is being webcast live and recorded with replay available shortly thereafter on the OpenText Investor Relations website.

Earlier today, we posted our inaugural quarterly shareholder letter, along with our press release and investor presentation. These materials will supplement our prepared remarks and can be accessed on the OpenText Investor Relations website, investors.opentext.com.

Before I proceed with the reading of our Safe Harbor statement, I would like to inform investors that OpenText 2022 Investor Day will take place virtually on March 1st. Registration for the event will be available in the coming days on our Investor Relations website. In addition, OpenText's management will be participating at the Scotiabank TMT Conference on March 8th and the Morgan Stanley TMT Conference on March 9th.

And now for our Safe Harbor statement. 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.

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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 risk factors, including in relation to the current global pandemic 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 today -- 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 a great pleasure to hand the call over to Mark.

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

Thank you, Harry. Well, good afternoon to everyone, and thank you for joining today's call. Today, we are introducing our new call format. Earlier today, we published our inaugural quarterly shareholder letter in addition to our press release and investor presentation, all available on investors.opentext.com. The 3 documents are intended to provide more insight into our strategy, aspirations, growth programs and results over short, medium and long-term horizons. Going forward, you can expect the quarterly shareholder letter and shorter prepared remarks from Madhu and myself, leaving more time for Q&A. Today, we'll spend a bit more time in our remarks to ensure a smooth transition to our new format. We welcome your continued feedback on how to improve our communication.

On to Q2 accomplishments, we had an amazing quarter financially and strategically. We provided demonstrable progress towards our longer-term fiscal '24 aspirations of up to 4% organic growth, 38% to 40% adjusted EBITDA margin and free cash flows of $1.2 billion plus. Today, we increased our fiscal '22 targets to include total growth of up to 4% and cloud revenue growth of up to 10%. This reinforces our aspiration to generate over $6 billion in cumulative cash flows over the next 5 years.

Please recall, our plan to return 33% of free cash flow to investors in the form of dividends and buybacks, while investing the majority of our cash in organic growth and corporate purposes, primarily M&A. Our capital return strategy has 2 fundamental pillars: one, returning 20% to trailing 12-month free cash flow via dividends; and two, keeping our share count constant via our buyback program. We believe our cash generation prospects and capital allocation strategy puts us in a stellar position to create sustained long-term value.

I listed our quarterly accomplishments in the shareholder letter, but let me call out just a few. We bettered our best and delivered the strongest Q2 revenue quarter in the history of the Company at $876.8 million, up 2.5% year-over-year, cloud up 4.1% year-over-year, with bright line organic growth. It was a very strong cloud bookings quarter with double-digit year-over-year growth, adjusted EBITDA of 39.2%. We're expecting strong year-over-year annual growth in our free cash flows. We view our business as annual. We make decisions -- many decisions based on that, while driving upper quartile adjusted EBITDA and free cash flow on an annual basis. I'm very proud of the recent talent recognitions our teammates received, including Canada's Most Admired Cultures, Canada's Top Employer for Young People and being named one of Forbes' Best Employers. The pandemic strengthened our culture and results.

We announced the OpenText Zero Initiative with bold ESG objectives. We plan to lead here. To our core, we believe the future of growth at OpenText is both inclusive and sustainable. By 2030, we are setting out to achieve 0 barriers, 0 waste and 0 net emissions. These are our 3 pillars to the OpenText Zero Initiative. Specifically on 0 barriers, we are actively striving to become a majority diverse company and to expand our leadership to a total of 40% female leadership, as defined as manager and up.

I'll comment on mid-market and Zix and enterprise growth programs and partners in a moment, simply said, Zix significantly improved our mix. It was an exceptional quarter across the board. We entered Q3 with increased visibility, both near term and over the longer horizon, and OpenText best days are ahead. Let me tell you why? Businesses of all sizes are transforming, and they are transforming into the cloud and by digitizing processes, but more importantly, they are transforming through information or as I like to call it, information-led transformations. This includes the way their employees work and how we're all mastering modern work. This includes the way they manage their supply chains and digitizing

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supply chains. It includes the way we sell and go to market and how we power modern experiences and the way we secure our digital infrastructures and strengthen cyber resilience.

We are the information management market leader, and our Cloud Edition offerings are optimized to help our customers regardless of their size or where they are in their transformation journey. We are going to take market share through organic growth and acquisitions on our path to doubling the Company over the next 5 years to 7 years.

We had amazing wins in the quarter, and you can read the detail in our investor presentation. Some of those wins include Volkswagen, Kimberly Clark, the U.S. Army Corps of Engineers. Raytheon Space and Intelligence and Amazon's new PillPack and many more.

Let me turn to Zix, our enterprise growth programs and partners - each strategic points of emphasis within my prepared remarks. On Zix, we see an amazing opportunity to expand our information management leadership in the enterprise and the SMB market. Nearly 50% of U.S. GDP is generated by small and medium-sized businesses and most need a secure and scalable digital presence. We just started our third year as a scaled provider of information management in SMB. And with the acquisition of Zix, we have market-leading platforms for data protection, data and e-mail security as well as being a top Microsoft cloud solution provider for mid-market solutions.

By bringing together Carbonite, Webroot, Zix and CloudAlly, plus our strategic relationship with the most important endpoint company on the planet, Microsoft, we are able to offer the industry's most complete total protection and security platform to RMMs and to 23,000 MSPs direct from OpenText. We intend to lead, grow and win information management by addressing the high compliance and cyber resilience needs for small and medium businesses and you can expect us to continue to acquire in the SMB market.

On to the enterprise, in the enterprise and for larger businesses, we have a fantastic direct sales force and high-impact strategies to drive profitable growth. First, one of our most important recent investments is to cover our top 100 customers direct for global account managers. This program is now in place. Second, one of our important recent investments is to cover direct the top 20 supply chain companies. This program is now in place. And as the large get larger and more global, we have a clear opportunity to grow the top of the market, and we are investing to do just that via our top 100 customer GAM program and our top 50 supply chain program.

On partners, third, I want to speak about partners here as we are building a remarkable business model with enterprise partners. We are fully committed to this model and partners are a force multiplier over the long term. Google, we announced today a greatly enhanced partnership to bring our joint content and experience solutions to enterprise customers. Microsoft, we have massively expanded our SMB and security relationship. Amazon and AWS is the core data platform for our protection cloud. SAP, we are leading -- we are a leading cloud partner with SAP with near 3 million cloud users already and strong product and selling momentum heading into the new calendar year. ServiceNow is a new opportunity for us to bring extended ECM to their large and expanding install base.

Here's an even greater macro point. Via our API Cloud, our Developer Cloud, we have the opportunity to win the next-generation set of cloud app vendors for their information management needs through content services, metadata, workflow, capture, supply chain, threat intelligence and more via our developer and API Cloud. I'm delighted with our Q2 results and our strategic progress with Cloud Editions, SMB and Zix and our enterprise growth programs and partners. We believe our outlook heading into calendar '22 is vastly more positive than the previous 2 years.

OpenText is on the offensive, as it relates to inflation because the best answer to inflation is to remove labor, where you can, reduce your friction costs and create new just-in-time supply chain through the digitalization of global processes and to do this smartly through information-led transformation. We intend to help our customers be on the offensive, as it relates to inflation.

Let me conclude by saying, I'm humbled by the resilience, courage and unstoppable nature of my colleagues through this pandemic. We used the last 2 years to transform into a cloud company with 80% annual recurring revenue, and today, we are raising our cloud growth target to up to 10%. The leadership team is excited to present at our March 1 Investor Day, and they plan to detail our next generation of cloud capabilities and our business journey to achieve increased market share, customer success and financial aspirations. Let me leave you with 2 things: targeting up to 10% cloud growth and Zix improves our mix.

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Now, let me turn the call to Madhu to provide the financial commentary on the quarter, Zix and our outlook. Madhu?

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

Thank you, Mark, and thank you all for joining us today. This is our new call format and we will focus on selected financial highlights rather than a line-by-line review. On the Investor Relations section of our website at opentext.com, please find under Q2, the latest quarterly results, you'll see the PDF of our earnings, the PDF of our shareholder letter, as well as the quarterly investor presentation. All references 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.

Q2 fiscal '22 results. We are very pleased with our record Q2 revenue, record annual recurring revenue and record cloud revenue. Growth, annual recurring revenue, ARR and cloud bookings, we grew total revenues low single-digit organically. We posted another quarter of double-digit enterprise cloud bookings. Cloud revenue saw its fourth consecutive quarter of low single-digit organic growth with positive organic growth in all of our cloud market domains, strong renewal rates in cloud and off cloud. And Q2 annual recurring revenue at 80% of our total revenues. On a first half year basis, ARR was 81% of total revenues. On the bookings front, enterprise cloud bookings were strong across many products and geographies, and our large deal trend was up.

GAAP-based net income was $88.3 million during the quarter, higher than Q2 of fiscal '21 loss of $65.5 million, primarily due to the tax settlement recorded in the prior year. Adjusted EBITDA for Q2 was $343.5 million or 39.2%, down slightly from Q2 fiscal 2021 of $360.8 million, primarily due to investments in talent across the board, including restoration of compensation, sales coverage and growth initiatives.

Turning to operating and free cash flows. We generated $216.6 million in operating cash flows in the quarter, down 23.3% and $756.1 million in the trailing 12 months, down 32%. We generated $206 million in free cash flows in the quarter, down 25% and $688 million in the trailing 12 months, down 35.6%.

During the quarter and compared to the prior year, there are 3 items I want to share with you with respect to OCF and FCF. First, integration costs relating to the Zix acquisitions in the current quarter; second, timing of tax refunds in the prior year, including CARES Act benefits that are not recurring in this quarter and 2 months of salaries forbearance in the prior year now restored and augmented with competitive salary increases as well.

And I'll just spend a few minutes on our working capital framework. Our working capital metrics are strong. Working capital ratio increased from 1.4x to 1.6x on a year-over-year basis. DSOs improved from 47 to 44 days, while our cash conversion cycle improved by 3 days. Our operating cash flows and free cash flows on a trailing 12-month basis, the reasons are similar in terms of CARES Act benefits last year, salary forbearance plus the onetime IRS settlement in the current year. Our next quarter Q3 is expected to remain our strongest free cash flow quarter. Also, free cash flow comparisons will continue to improve on a year-over-year basis, as we anniversary the IRS settlement payment last year and COVID-related comparisons also become easier.

Turning to balance sheet and liquidity, we ended the quarter with $2.3 billion of cash and available liquidity and a very strong net leverage ratio of 2x. And before I speak to our outlook and aspirations, let me share details regarding our Zix acquisition. We closed the Zix acquisition on December 23rd, 2021. And relative to Zix's reporting prior to our acquisition, please note the following. OpenText will record revenues on a net revenue basis. It will be 100% part of cloud with gross margins in the low 80s. During integration, we are factoring year 1 customer partner disruption in our overall models. We expect to share with you at the end of this fiscal year, as we complete the June quarter, the combined growth prospects for our SMB powerhouse offering that Mark referenced in his commentary.

And now let me turn to our updated targets and aspirations. For the third quarter of fiscal '22 and on a year-over-year basis, we look for total revenue to grow mid to high single-digits, ARR, annual recurring revenue to grow mid-single digits year-over-year, and FX headwind of $20 million to $25 million. We expect adjusted EBITDA margin percentage to be down 450 basis points to 500 basis points due to higher investments in talent and continued support of our growth ambitions, Zix acquisition and typical calendar year reset of higher benefits expense.

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For full year fiscal 2022, we're increasing our cloud revenue growth outlook from 1% to 2% to a range of 3% to 4%, and our cloud revenue growth from 3% to 4% to a range of 8% to 10%. A higher revenue outlook is predicated on our cloud bookings, contributions from Zix and confidence from strong Q2 and first half results.

And let me expand on the cloud revenue line. Our fiscal 2022 cloud growth at 8% to 10% includes the Zix's acquisition. We expect to grow cloud organically, both in reported and constant currency in fiscal '22 despite the Q3 FX headwind. And where we sit today, we expect FX headwinds in Q4 as well.

Setting FX aside, as I said earlier, we saw the strongest booking growth in our enterprise cloud bookings during the first half, and along with our expanding hyperscaler relationships, Carbonite and Zix acquisition, we expect cloud to continue to drive our future organic growth aspiration.

Moving to adjusted EBITDA margin. We now expect our fiscal '22 adjusted EBITDA margin to be in the range of 35.5% to 36.5%, reflecting the integration of Zix and internal investments to support growth initiatives. We have made demonstrable progress towards a solid fiscal '22 finish and continued momentum into fiscal '23.

Our fiscal '24 aspirations remain unchanged at up to 4% organic growth, 85% annual recurring revenue, 38% to 40% adjusted EBITDA margin and $1.2 billion plus of free cash flows. We plan to continue to invest anything higher than 40% back into sales, marketing and product initiatives driving organic growth.

We're seeing growth in all the right places. Our investment in talent, sales coverage and innovation are paying off in organic growth. Our strong bookings also give us long-term visibility, while the predictability of our business remains high. All of this is made possible by the amazing OpenText team and your contributions are invaluable. On behalf of OpenText, I would like to thank our shareholders, loyal customers, partners and employees across the globe.

I would now like to turn the call over to your questions, and over to you, operator.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions) Our first question comes from Raimo Lenschow of Barclays.

Raimo Lenschow - *Barclays Bank PLC, Research Division - MD & Analyst*

Congrats from me on these solid numbers. Mark, the more bigger picture question, the one thing that gets discussed a lot with software investors here at the moment is the demand situation in terms of spending with customers. Digital transformation was a big theme in the last couple of years, the pandemic kind of really sharpened people's mind here. And is this kind of notion that we kind of overspend a little bit over the last year, and now we're coming back to kind of more normal levels. What are you seeing in terms of how this is playing out for you? And I had one follow-up for Madhu, please.

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

Yes. Thanks, Raimo, and good to hear from you. Like I said in my prepared remarks, I mean coming into '22, it's a vastly -- calendar '22, it's a vastly more positive year for us. And I mean, look at our customer wins, Novartis, in new machine learning and capture, Volkswagen building a new platform for electric cars and rough math, 10 million cars times 1,000 documents, 10 billion documents a year across purchasing, delivery, assembly, service warranty and more. U.S. Army Corps of Engineers, big new projects going on in the U.S., 600 dams, 2,000 levies, and they're all on Cloud Editions. So we see increased demand, not shortening demand as we come into '22, calendar '22. And we're very focused on also upgrading and

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migrating our install base into our Cloud Editions. So at least OpenText's position is more positivity coming into '22 than we had over the last 2 years.

Raimo Lenschow - *Barclays Bank PLC, Research Division - MD & Analyst*

Okay. Perfect. That's good to hear. And then so Madhu, like, if you -- if I think about your EBITDA guidance, if I do the math, it came down a little bit. Can you talk a little bit about the drivers in terms of -- if I look at the absolute level, if I look at the drivers here in terms of between FX, kind of investment to business, higher employee costs, et cetera, just could you break down a little bit. Thank you, and congrats from me.

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

Yes. Thank you, Raimo, for the comments. So I'll take FX first. And certainly, on the top line on revenue, FX does play a big role. We're calling it out in our quarterly factors. And the 2 lines that FX impacts the most is the cloud services line as well as customer support. And we're definitely seeing that in Q3. And where we sit today, I would say expect a similar FX impact in Q4, again, where we sit today. But the underlying business, as I said, is absolutely growing and growing from an organic basis.

As far as adjusted EBITDA growth, I put the #1 Zix acquisition, and this is not uncommon for us. If you go back to the Carbonite acquisition, we did the quarter immediately following, yes, we did take a downward tick on adjusted EBITDA, and then, we saw how we came back up. So the #1 reason is going to be Zix and we're targeting to get fixed to our operating model in our usual time frame of a year plus.

And number two, as you outlined, yes, we did have some salary forbearance and commensuration, but more importantly, we did pass through two merit increases, and we're investing in talent overall. In addition to investing in talent from an expansion perspective, as we've shared sales coverage, marketing, R&D, products and innovation. So in terms of the order of the reasons that go, any time we do a large acquisition, Zix in #1 and in -- and in number two, people investment and more go-to-market and products as well.

Operator

Our next question comes from Paul Steep of Scotia Capital.

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

Just 2 quick ones. Mark, maybe you could just update us on the road map for 22.2 and maybe other key releases that should be on our radar screen. And then Madhu, just can you -- when we get to it, can you go back because it doesn't look like the transcript caught your third comment after gross margins, low 80s in terms of maybe the impact on customer that at least broke up on my side as well? And then just one last one on gross versus net at Zix? Thanks.

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

Yes, Paul, thank you for the question and good to hear from you. And we're going to have a large and important product update at Investor Day. So I'm going to save some of the gun powder for March 1. But in advance of that, for 22.2 and 22.3 first, we remain on our 90-day cadence, which is our battle cry. And the reason I highlight that -- have highlighted that, it is so important. How do you -- how do we help a developer go faster? And how can we go faster? And how can we go from thought to code to quality to pre-prod production capabilities in customers' hands faster and faster. We're now releasing 20,000 facets, features and tools a quarter across our cloud.

And I go back to the days when Silicon Valley was part of this model, we moved talent to India. And it wasn't just labor arbitrage, we're able to work 24 hours a day and that differentiated very large companies from their process. So this is the next big process improvement is to go faster every

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90 days. So with that or what we can look forward to over the next 90 days is on our content cloud, all support for partners and embedding extended ECM on the content side, which is really enabling Salesforce, ServiceNow, SAP, Google, Microsoft, so this notion of extended ECM.

On the business network cloud, and we actually have a supply chain summit coming up in a couple of weeks. We have a new global invoicing capability, supporting about 60 countries that are going to enable what we call just in case supply chains, not just in time, but just in case. And we're bringing to market our new mid-market offering directly targeted at SPS Commerce in the mid-market with a product line called Freeway.

On the experience cloud, we have a new CPaaS platform in the marketplace and enhanced over the next 90 days. We're going to be integrating Zix very rapidly for e-mail protection and encryption within the security and protection cloud. And more advanced APIs, Magellan Risk Guard, you guys send us content, we'll send you back content score. Does it have a SIM number? Does it have a social security number? Is it in violation of GDPR.

We just won a real nice win at Paladin cyber for threat API and over a dozen SAP customers for machine learning and capture. So it will be more machine learning capabilities. So that's a bit of a flavor across our 5 clouds and 22.2, but please expect a very important significant product road map update at Investor Day in March.

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

Okay. Yes. Thank you, Mark. And Paul, let me address the Zix speed as well. Again, keeping in mind, Zix was a public company before we acquired and there's certainly data and information out there about Zix. We want to take the opportunity to clarify how we are approaching Zix. So as I mentioned, we closed the acquisition on December 23rd. We will record revenues on a net revenue basis. We've done our complete and thorough diligence, and that's the appropriate way in our view.

And by the way, keep in mind that our sales channel, the partner channel, they are all bringing in business from a gross perspective, and that's what they are supposed to do, right? So this doesn't sort of discount the totality of the efforts that goes into the business, I did want to emphasize that. Financial reporting, we will be recording on a net revenue basis. All of Zix's revenue goes in as part of cloud and gross margin is in the low 80s.

During integration, we generally do this for every acquisition. We do factor a year 1 customer partner disruption in our overall revenue models. We certainly strive to meet the higher end of it, but it is prudent in our view to factor some discount to the normal run rate, just given the year 1 customer partner disruption. And that was my point #2.

And the third point was, we'll share with you at the end of the fiscal year, the combined growth prospects of SMB powerhouse that Mark talked about in his commentary.

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

Great. The last line was what we've missed. So on the integration, should we think to the traditional, I believe we were used to be 18% to 20% sort of step down? Is that what sort of embedded into the thought process at this point?

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

Paul, yes, I would agree. Yes.

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

Sorry, last clarification, I promise. Can you give us a sense Madhu of how -- what that sort of translation obviously from gross to net is on their revenues since certain folks are going to be looking at the Zix numbers and trying to read across understandable, and you stated already the deal that you were going to recast it in your IFRS standard?

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

Right. Totality of growth to the totality of net, again, I would think somewhere in the range of -- look, they have 2 different types of businesses, right? And the resale business is where we are taking the position that we will go from a net -- go to a net revenue basis. And without getting into the hairy components here, on the resale side, it really translates into somewhere in the 30% to 35% of a dollar of resale revenue.

Operator

Our next question comes from Thanos Moschopoulos of BMO Capital Markets.

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

Maybe just to follow up on Zix and accounting. When we look at their deferred revenue balance, would that have been some resale revenue in there that needs to be marked down to a net basis? Or with the stuff they had in deferred as a public company would that all pertain to the stuff that you're recognizing that anyway?

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

Yes. Again, it's a great question. Zix had adopted a gross revenue accounting for their entire business, right? So that applies to the deferred revenue as well.

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

Okay. So even the resale revenue had some deferred element in it that would be in the deferred revenue balance.

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

Deferred element. Yes.

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

Okay. Also, given that it's going to be a higher gross margin profile, does that mean that once integrated it might actually be above your target operating model?

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

Yes. In fact, the convergence to our target operating model is actually the goal, as we come out of integration. The mention of the gross margin is important because you would expect that from sort of a SaaS cloud-based business in the low 80s, and that's why we wanted to make it a point, very akin to Carbonite.

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

Okay. Then finally, Mark, just touching on M&A. You obviously announced a new Head of Corporate Development and we're seeing valuations come down in the public markets. I'm not sure you're seeing that yet at this point in terms of assets you may be exploring, but any color or update on that front, would be good? Thanks.

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

Yes, very happy to, and thank you Thanos and good to hear from you. So first is I'm pleased to give my first live voice to the promotion of Doug leading corp dev and reporting to me and somewhat expansion of the team. We have a fantastic in-house corporate development organization, and Doug is just a fantastic leader and delighted to have him reporting to me.

And let me just use this also opportunity to add my voice to Gordon's retirement. He's been a great partner over the last decade, and we wish him all the best in his continued journey in his retirement. So Doug's promoted, working for me, expanded team in corp dev. And Thanos, we are seeing more assets today than we were a year ago. We're seeing better valuations as well. So there's more optionality that we see. You should expect us to complete more deals here in calendar '22.

And I'd also note that if you look at our cash flows and the strength of our cash flows, we can be bold here, but we can fund double-digit acquired growth straight from our cash flows. And we may choose to use other instruments, but our cash flows are strong enough that we can now fund double-digit growth -- acquired growth straight from our cash flows. So those are things I would note for M&A. Doug reporting to me, expanded team, seeing more assets, improvement in valuation, we're expecting to get more deals done in calendar '22, and the strength of our cash flows directly implies strong acquired growth straight from cash flows.

Operator

Our next question comes from Richard Tse of National Bank Financial.

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

I kind of been following your website here, and you've got a lot of material there on IBM, and it seems like you guys are still making some pretty big gains against them. Has that sort of changed in any way in terms of those share gains that you've had over the past few quarters?

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

Yes. Richard, thanks for the -- thanks for the question and good to hear from you. We launched at the beginning of January a campaign called Bye Bye Blue. And the campaign, which is very asset rich, very program rich is communicating to FileNet and Sterling Commerce customers, the challenge they have when Kyndryl got carved out of IBM that you now have 2 different companies, 2 different road maps, 2 different contracts, 2 different SLAs and the increased complexity of running your supply chains or information management platform.

We think it's a great time to call every FileNet and Sterling Commerce customer and provide an alternative because they're not investing. We're in the upper right for Gartner, they're not. We have a private cloud, they don't. We have a SaaS alternative, they don't. So this is going to yield wins. It's going to yield wins probably over the next 1 years to 3 years. And so we just love the campaign. We have won customers. We're building tools to make the automation of the IBM platform even more rapid.

Let me just also note on the competitor front that in the mid-market, we're very focused on bringing our business network into the mid-market. I spent a lot of time on a product line, which we call Freeway, and it's now an alternative to SPS Commerce in the marketplace. And we're very focused on winning Microsoft's transition, helping customers support the Microsoft transition. So as Microsoft moves to their NCE program, we want to be

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right there to help Microsoft and any competitor in our way is also going to be an important watch dog for us because we're here to help Microsoft establish their NCE program. So that would be my comments on competitors.

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

Okay. And then, I guess, kind of a related question on acquisitions, if they are not investing and they view that sort of information management business as non-core. If they were to sort of think about spinning that out, is that an asset that you would consider looking at?

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

Well, the short answer, of course, is yes, we'd look at it. And it has to be at the right value. But of course, we would look at it. And -- but I'm very happy with our competitive position. But of course, we'd look at it. It's been in the market way to -- it's been established for way too long, and of course, we would look at it. Having said that, I really like how we're competing against them. And we're going to keep competing, and we've got a great campaign in the market.

Operator

(Operator Instructions) Our next question comes from Paul Treiber of RBC Capital Markets.

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

In the prepared remarks, you called out double-digit cloud bookings growth. And I was wondering how important was content cloud 21.4 the release this quarter to growth of bookings? And then more generally speaking, how do you think about product cycles in the future? I mean do you expect the ebbs and flows in cloud bookings around more significant product releases? Or is that less a factor?

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

Yes. Paul, thank you for the question and good to hear from you. There's no doubt that our content cloud is a call out right now. And if we look at some of our customer wins, Novartis, great content cloud customer, bringing machine learning, capturing machine learning capabilities into many of their information rich processes from regulated documents to clinical trials. Volkswagen, and I had mentioned a little earlier, 10 million cars times 100,000 documents equals 10 million documents a year from everywhere from purchasing to warranty. That's a single platform of content.

U.S. Army Corps of Engineers, I'm very proud of this win and very proud to partner with one of the most prestigious engineering firms in the world from everything, from civilian to military construction and everything from dams, locks, hydroelectric facilities, levies, water supply to over 100 cities in the U.S., one information platform, content, services, all on cloud editions. So yes, our 90-day cycle is really important. 22.1 really brought up big capabilities. 22.2, as I highlighted earlier. And Investor Day, I'm real eager to get to March 1 to have some significant announcements for the road map ahead. So if you allow me, Paul, I'm going to hold on to some of our gun powder for our Investor Day and the big pieces on the road map ahead, but they're significant. But yes, 21.4, 22.1 really contributed to some of these very impressive cloud edition wins.

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

My second question, and maybe it relates to road map, but I'll try to speak about it more generally. Just on SMB and the opportunity there, the products that you mentioned have been acquired to build out or further build out your SMB product portfolio. Should we expect the more sort of traditional enterprise grade software that OpenText has to be repositioned down into SMB? Or do you think that, that is a distinct market and it would require distinct products?

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

It's a bit of both. It is a distinct product. And going back to kind of our vision and our strategy for information management, it's both in the cloud and at the edge. And we think both are really important right? No edge, no cloud, no cloud, no edge. So they're both really important. And at the edge, it's data protection, it's information security, it's e-mail security, EDR, MDR and forensics, and it's helping customers constantly move information off the edge into more cloud-based solutions. But we do -- we spend our lives on the edge and we innovate at the edge. So they're all unique technologies for the edge. And the edge is both SMB and its enterprise.

I'll take some Zix technology. We think the e-mail encryption integrates really well into our experience cloud for secured information in health care. We think the secure edge, e-mail security is going to be really helpful in the business network for our Covisint platform. And those technologies scale up, but they didn't have a sales force to bring there. We think our guidance software goes into SMB very well for law enforcement, but we didn't have a big channel to do that. So it's multilayered, right? It's edge and cloud, it's SMB and enterprise. There are unique technologies for both, but that intersecting circle is large enough that we can bring technologies both ways.

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

And last one for me. I was on your developer website today, and I went through all the APIs that are available and there is quite a number of them. The -- what I was thinking through though is, what's the marketing strategy for developer cloud? I mean it seems quite different of a channel than enterprise sales. So how do you -- what's the plan to raise awareness for OpenText's APIs for developers?

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

It's a great -- well, Paul, I'm delighted you're on developer at opentext.com, so thanks are being there. So look, I think it's one of the gems we have inside the Company, and we haven't cracked the scale code yet. It is roughly a $100 million business today inside of OpenText, and it's a Twilio locked inside our Company. So part of the strategy to unlock it was bringing in Sandy Ono on board, our new Chief Marketing Officer. We've set up a new internal group to go to market. We think being able to come in and attach an API sale to a platform sale is a good strategy.

For example, Becton Dickinson, we brought some APIs into that -- into that sale on our business network. We won over a dozen SAP customers for machine learning and capture. We've introduced some new APIs, the Magellan Risk Guard and enhanced our threat intelligence. But it's going to be a combination of things. We've got a new Chief Marketing Officer, who understands the market. We've set up a new selling team reporting to Ted Harrison. We are going to attach it to platform sales. Christina and our customer success group is going to set up a PS organization to build applications on top of it. It's going to be that comprehensive learning from Twilio and making this a future growth driver for us. But we have the technology, we have the know-how, now we're going to crack the scale code. You can hear the passion in my voice on this one because it's something very unique we have.

Operator

Our next question comes from Stephanie Price of CIBC.

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

And you talked a bit about the potential from the Google partnership that you announced this afternoon. How are you thinking about that partnership evolving?

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

Yes. Very good, and thanks for joining us, Stephanie, and good to hear from you. Yes. I purposely focused my prepared remarks on our enterprise partners. And we've just come a long way in developing out our technology and our strategy with partners. So in relation to Google, which we also announced today, we announced we put new MOU in place and a greatly enhanced partnership in the enterprise. One is, we're going to jointly innovate together. We are at OpenText going to consume more of their platform for our customers and our use. And we're going to bring our content and experience platforms to their customers via their workspace platform.

And we will build out joint selling teams like what we've done at SAP and other places to engage with enterprise customers. So it's a very evolved and complete strategy to move kind of the next level of engagement around joint innovation, more mutual consumption and bringing our content cloud and experience cloud to the enterprise via their Google Workspace, and then layering around that, a joint selling organization to create demand, close deals and make customers very successful and happy. So that's a bit more on the Google announcement today.

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

And then switching to the SMB market, I'm curious about the ability to cross-sell other SMB solutions through Zix's partner channel and what the time line looks like for starting that?

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

Sure thing. I would highlight a couple of things today. The first opportunity is to bring Zix products to Carbonite and Webroot customers, opportunity #1. Two is to bring Zix e-mail security, which is a cloud service. They're processing 100 million e-mails a day like Proofpoint and bring that scaled service into our CPaaS platform and experience to strengthen health care, auto and some other of our big EDI traffic, if you will. We think there's a good relation, good opportunity -- an immediate opportunity there.

We also think on the Microsoft reseller side is we've identified close to 5,000 MSPs in the Carbonite, Webroot world that doesn't have a relationship with Microsoft NCE, and we're going to -- we're actively reaching out to them to bring the cloud service platform for Microsoft to those new 5,000 MSPs. And that's immediate active real time that we're doing that. So those are -- Stephanie, those are some of the immediate programs that we're going to cross-sell and cross-pollinate.

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

That's helpful. And finally for Madhu, customer support came down as a percentage of total overall revenue in the target model. Just curious about the puts and takes here?

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

Yes. So Stephanie, it's -- I would say 2 things. One, it's more of an adjustment at the cloud revenue, you see going up the target model slightly. That's the main driver. Customer support continues to have very strong renewal rates, as you see in our commentaries. And maybe the last comment, I will share is, I spoke about FX and FX impacts, the headwinds do impact customer support and the cloud lines as well.

Operator

Our next question comes from Howard Leung of Veritas Investment Research.

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Howard Leung - *Veritas Investment Research Corporation - Investment Analyst*

Thanks for taking my questions. It doesn't sound like, I guess, the -- from the Zix acquisition, a lot of the focus on the call, the remarks are about the cross-sell, which makes sense. And it sounds like, I guess, for the resale part of their business, even with the larger size that OpenText and Zix combined are, it doesn't look like, you'll try to renegotiate those margins or try to get a little bit of a lift there.

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

Howard, welcome, and thanks for your question, and good to hear from you. No, there's multiple vectors here of opportunity. First, obviously, is our -- are the Zix secure cloud products. And -- and I noted kind of the better integration with data protection, information security and e-mail security. And ultimately, our strategy is to have an integrated endpoint edge platform. And this is another strong component for us to do that across data protection, information and e-mail security plus our forensic offerings and then eventually EDR and MDR. That's the arc of our strategy to an integrated platform.

Second is our ability to cross-sell across those companies as noted, bringing Zix into Webroot and Carbonite customers, bring Carbonite and Webroot into Zix customers. And then the resale opportunity, there's just enormous opportunity -- resale equals relation -- the relationship is the power ultimately and the force multiplier for us. So the ability to go further with our great Microsoft relationship, bringing that relationship into the Carbonite and Webroot MSPs is very important and then expanding larger than 23,000 MSPs as well.

And then on top of that, there's no reason we can't bring even other third-party resales into that singular platform. And I won't go into others -- we're working with on top of Microsoft, Microsoft complementary to bring in there for even a little more resale. So Howard, it's a very comprehensive approach to create, as we do call the SMB powerhouse for us from everything from an integrated platform at the edge, through the power of the relationship with Microsoft and Microsoft complementary vendors.

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

Howard, it's Madhu here. Yes. I was just going to say, thank you for the question as well.

Howard Leung - *Veritas Investment Research Corporation - Investment Analyst*

Yes. No problem, no problem. And then actually, just a follow-up on the MSPs. Can you talk about your process of how to onboard the -- or how you guys, I guess, introduced the new MSPs to your products and maybe talk through that a bit?

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

Absolutely. And this is a very important question because it's all driven by software, and we're going to speak a bit about it at Investor Day. But effectively, our digital zone is software running the cloud as a platform. The goal is to have a single pane of glass or one application that MSPs come to self-service. And after our selling and after our engagement and their tries and buys, with a single platform in the cloud, where they can transact and they can provision and they can support and they can renew. And so part of our strategic approach to invest in that platform, writing software to remove the friction from try and buy, remove the friction from selling, buying, renewing, monitoring, and we today call that our Digital Zone.

Howard Leung - *Veritas Investment Research Corporation - Investment Analyst*

Thanks for explaining the process. And then just maybe one final one for me on the renewal rates. I know on the cloud side, I think it's slipped a bit from 96, 93. Is there anything you want to call out there? Should we expect it to go back up? Or it's -- I guess the growth trajectory is more about new deals and maybe less about the mid-90s retention.

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

Madhu, you maybe on mute.

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

And my apologies. So Howard, I was saying, we announced, I believe a quarter ago, Paul Duggan, he is an Oracle veteran, was running a $5 billion renewal business. He's been heading up our renewals, where a lot of new and implementation ideas are coming along. So I would say stay tuned.

And the second piece is that would also lead to a continuous improvement in the cloud renewal rate right? There were earlier questions about products and innovations and value and expect this organization to keep introducing that to our customers. There is churn, but I would say the value is going to be higher than the churn, as we look ahead.

Howard Leung - *Veritas Investment Research Corporation - Investment Analyst*

Thanks for the comments, and I'll turn it back.

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

Yes. Thanks, Howard. Thanks. Good morning. Yes. Any given quarter -- any given quarter will vary on a cloud renewal rate, but the trajectory is definitely into the mid to high 90s.

Operator

This concludes the question-and-answer session. I'll now hand the call back over to Mr. Barrenechea for any closing remarks.

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

All right. Very, very good, and thank you for joining today, and we welcome your feedback on our new format with our quarterly shareholder letter. Madhu and I are going to be very disciplined to keep our remarks majoring in the majors and narrowing our prepared remarks to provide more time in Q&A, which we think is the most important point of this call. I hope you'll join us on March 1st for our Investor Day. The executive team will be altogether out here in Silicon Valley Live, and you are most welcome to join us in-person or virtually for our Investor Day on March 1st and look forward to seeing you then. Thank you.

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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