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EDITED TRANSCRIPT

OTEX.TO - Q1 2025 Open Text Corp Earnings Call

EVENT DATE/TIME: OCTOBER 31, 2024 / 1:00PM GMT

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PRESENTATION

Operator

Thank you for standing by. This is the conference operator. Welcome to the OpenText Corporation first-quarter fiscal 2025 financial results conference call. (Operator Instructions) And the conference is being recorded. (Operator Instructions) I would now like to turn the conference over to Greg Secord, Vice President, Investor Relations. Please go ahead.

Greg Secord - *Open Text Corp - VP, Global Head of IR*

Good morning, everyone, and welcome to OpenText's First Quarter Fiscal 2025 Earnings Call. With me on the call today are OpenText's Chief Executive Officer and Chief Technology Officer, Mark J. Barrenechea; and OpenText's President and Chief Financial Officer, Madhu Ranganathan. Today's call will be webcast live and recorded with a replay available shortly thereafter on the OpenText Investor Relations website at investors.opentext.com.

Before today's call, we posted a press release and investor presentations online. These materials will supplement our prepared remarks and can also be accessed on the OpenText Investor Relations website. I'd like to take the opportunity to invite institutional investors and financial analysts to join our OpenText World, 2024 Investor Track. It's on Tuesday, November 19, in Las Vegas.

The OpenText World conference is a great opportunity for investors and financial analysts to learn about the latest product innovations with full conference access, allowing open dialogue with leadership, customers and partners on site. The investor track will be available to investors attending in person, and virtually by webcast or live streaming in replay. You can contact myself or the Investor Relations team for more details and to register.

In addition, please to inform you that OpenText will be participating in the following upcoming investor conferences including the TD Technology Conference on Monday, November 25 in Toronto with Mark. Wells Fargo's Technology, Media and Telecommunications Summit on December 4 in Rancho Palos Verdes and Barclays Global Technology Conference on Thursday, December 12 in San Francisco with Madhu.

And now on to the reading of our safe harbor statement. During this call, we'll be making forward-looking statements relating to the future performance of OpenText. These statements are based on current expectations, assumptions and other material factors that are subject to risks and uncertainties, and actual results may differ materially from the forward-looking statements made today.

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Additional information about the material factors that could cause actual results to differ materially from such forward-looking statements as well as risk factors that may impact future performance results of OpenText are contained in OpenText's recent Forms 10-K and 10-Q as well as in our press release that was distributed earlier this morning, 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. Reconciliation of any non-GAAP financial measures to their most directly comparable GAAP measures may be found within our public filings and the other materials, which are available on our website. And with that, I'll hand the call over to Mark.

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Thank you, Greg, and welcome, everyone, to today's call. Let me start with in Q1, we delivered to our revenue quarterly factors as well as exceeded expectations in adjusted EBITDA and adjusted EPS. We grew our adjusted EBITDA percent year-over-year to 35%, and this growth comes from sustained efficiency gains even after the divestiture of the ultra-high-margin AMC business. Over the last two quarters, we purchased and canceled 7.72 million shares at an average price of $30.43, expect us to continue purchasing our shares. And in Q2, I'm deeply excited about our momentum.

We are strengthening our competitive advantage with Titanium X, our next-generation autonomous information management platform powered by AI and security, coupled with strong investments we are making in our enterprise and SMB go-to-market, strategic partners and customer success organizations, all of which leads us to a stronger second half of the fiscal year. Further, we are reaffirming our fiscal '25 targets and our outer year aspirations.

On to Q1. Our Q1 results include delivering $1.27 billion in revenues well within our quarterly factor range of $1.25 billion to $1.3 billion. Q1 is a seasonally lower quarter, yet it was the largest Q1 of enterprise cloud bookings in our history, up 10% year-over-year and up 53% over three years.

As it relates to our cloud business, Q1 marked our 15th consecutive quarter of organic growth of $457 million or revenues up 1.2%, of 1.3%, and we expect this to ramp throughout the year. We also had strong customer wins at Raytheon, FedEx, Virgin Mobile, Alaska Airlines, Nippon Gas, the European Medicines Agency and Dick's Sporting Goods across content, business network, digital operations and security.

Financial services, technology, public sector, health care and biotech and consumer packaged goods were top industries for our book of business. Revenue by GEO, Americas, 57% with the majority in the United States; EMEA, 33% and APAC and Japan, 10%. We had 38 deals over $1 million, the majority being cloud-based deals. We had 20 wins related to our GenAI Aviator offering. We keep building strength and progress every 90 days, more aviators, more agents, easier to use and less expense to operate.

We see AI as a long-term opportunity and a key priority for the company. Net cloud renewal rate of 94% and of course, adjusted EBITDA of 35%, which is year-over-year percent growth inclusive of the AMC business. This is incredible progress and reflects our deep focus on capturing the large margin opportunity ahead of us and adjusted EPS of $0.93, well above expectations.

Looking ahead into Q2, we expect total revenues of $1.29 billion to $1.34 billion, supported by a strong pipeline and customer engagement, continued adjusted EBITDA strength of 34% to 35%, continued enterprise booking strength ramping towards our annual target of 25% growth, and Madhu will expand on our outlook here in a few moments.

Q2 is a tougher year-over-year compare, given the large AMC contribution and the license revenue from grants of certain IP rights in Q2 of last year. The business is executing well. And as I kicked off the call saying we are reaffirming today our fiscal '25 targets of total revenues of $5.3 billion to $5.4 billion, that's $100 million spread ex-AMC, this is constant to 1% growth.

Annual adjusted EBITDA of 33% to 34%, free cash flow of $575 million to $625 million, and we're on track to return approximately $570 million of capital via our dividend and share buyback programs. It will be a record year of capital return for OpenText.

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Further, as you can see from our comments today, we are expecting a stronger second half to our fiscal year, driven by four factors: expect demand for Titanium X, our next-generation autonomous information management platform led by our business cloud, business AI and security. Second factor, realizing our new go-to-market investments led by Todd in the sales organization; third factor, expanding partner contribution led by Sandy Ono and our fourth factor, realizing our new customer service investments led by Paul in the renewals, professional services and customer success teams.

Let me expand on these drivers more and how they point to a stronger second half. First, our competitive advantage clearly gets stronger with Titanium X or Cloud Editions 25.2 and we are on track for the final delivery in the second half of this fiscal year. Information is the heartbeat of every organization.

It flows through every process, every workflow, every innovation, every experience. It touches all roles. It enables the modern organization. Titanium X will elevate our customers' capabilities in significant ways. OpenText World 2024 November will bring this all to life, and we hope to see you there.

As a preview, customers and partners will see key differentiation and compelling reasons to adopt the new Titanium X. First, a modern SaaS platform for our core information solutions. So as I'd like to say, everything downstream of SaaS is goodness. It's faster time to revenue, it's easier to expand capabilities and it's higher margin. Second key piece, a private cloud that is global, secure, trusted and autonomous.

And we've obviously made significant progress here over the last few years. And once in our private cloud, we keep customers current on the latest version, latest security and the latest AI. So customers are free to run their business and elevate their -- and evaluate our new innovations we provide every 90 days.

Third is our compelling new capabilities in each of our business clouds. For example, in the content world and content cloud, it's all about SaaS, AI and integrated security and deep integration into business applications. In our business network, it's about being global, global supply chain, global e-invoicing, a global supply chain control tower that can see across all your suppliers, the new traceability applications from being able to determine cobalt field in Africa to finished electric vehicles in Germany as an example.

Security. We are delivering a full stack of protection from users, applications, e-mail, network and cloud. We call it XDR as a Service. Titanium X is a major step forward for enterprise and SMB security a composable approach in the cloud to identify, detect and respond against active threats. We will demonstrate our next-generation as a service at OpenText World. Security trust compliance is a major investment area for OpenText.

Other compelling areas, ITOM, discovery and observability at our new corporate help desk expanding to include HR IT and all internal CXO organizations into one unified corporate health desk, all focused on elevating the employee experience.

ADM, we're introducing, dev sec ops for large-scale software organizations. And at SMB, we are already live on our next-generation secure cloud platform for the partner community to easily transact as you may have seen some of our social media last week and going live in Secure Cloud.

And then lastly, Wave 2 GenAI aviators, built for every industry and embedded everywhere in OpenText software. Titanium X will have 15 aviators and over 100 agents. As we like to say, never bring a human to do the work of a machine. We'll be announcing support for Microsoft CoPilot in addition to Google Vertex and BYOM, Bring Your Own Language models into our private cloud.

So you'll see all of this at OpenText World 2024. It's a packed agenda of innovation and the value that comes at the right time for our customers in OpenText -- for OpenText to bring this all together for them in a powerful way. I hope to see you there at OpenText World.

Next, let me expand on our new go-to-market investments led by Todd Cione in the sales organization. As mentioned in our last earnings call, we're making investments in our go-to-market across three priority areas: people, customers and innovation. On people, we continue to find much success attracting new sales talent.

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We are right on our AE and SE capacity targets. In addition, our new unified global sales organization structure has allowed us to launch unified programs to the entire organization on a global basis, all within this dynamic marketplace of cloud AI and security. And the first program we've launched is cross-selling security across all of our AI, and particularly important with our new XDR as a service coming out.

OpenText always puts customers first and we are finding very strong momentum and engagement. Our cloud AI pipeline is the largest it's ever been and up 20% year-over-year. On sales innovation, we have deployed internally OpenText AI. We're now live. We call it Ollie.ai to act as a sales Aviator for the sales force.

I'll be demoing live, our new Ollie.ai tool at OpenText World and how we are using Aviators internally to generate proposals, accelerate sales velocity and win more. We are seeing very favorable impact in our sellers' ability to build effective account plans, articulate value propositions and build compelling business cases now live on OpenText AI.

Third, in support of a strong second half -- stronger second half as moving on to expanding partner contribution. The demand signals for information management are strong. Our customers see the growing availability of business AI for many places and including the importance of effective information management solutions. You need strong data management to have strong AI. I've talked about how we help companies operate in the world of the Internet of disconnected clouds.

You'll hear at OpenText, our next big steps in this area on how OpenText makes multi-cloud work. You see all enterprise customers have many cloud providers. This is the new normal. I can't meet a customer; I can't find a customer only has one cloud provider. Our customers have many cloud providers, and no customer standardizes just on one cloud provider. So further, customers will have multiple AI suppliers as well. It is a multi-cloud world.

We see a growing role for OpenText, where we make multi-cloud work for one source of truth for data, user authentication across all these systems, workflow across all the clouds, search across all the clouds, governance across all these clouds. We make multi-cloud work.

In achieving this, our strategic partnerships are more important than ever, and at all layers of the enterprise stack from the app layer to infrastructure, to security and to the supply chain. For example, on SAP, we continue to work closely to remain day one current across all their amazing cloud solutions.

On Google, we've expanded our support to improve their full AI stack and services. On Microsoft, we've expanded our partnership to now include Copilot for security. We continue to work with Salesforce that our business clouds work in tandem with their business clouds.

Titanium X has integrations across content security and ITOM for Salesforce. We recently added Content Cloud for Guidewire to expand our presence in the insurance industry and for Amazon, our business network better integrates and leverages their commerce platform. We'll continue to foster our strategic partnerships to ensure OpenText solutions are at the center of the multi-cloud world. We make multi-cloud work.

And then finally, in support of a stronger second half, while we will increasingly see returns on our customer success investments. On our last call, we told you, we informed, that we would be building a new digital renewal center and going live July 1, and we went live, July 1. We'll continue to take humans out of the renewal process.

And in doing so, our business scales with lower friction, lower cost, and our best people can help our customers expand consumption. This team had an incredible first quarter and exceeded our expectations. So a lot more to follow in this particular area.

I'd like to conclude with two items. First, join us at OpenText World and see the momentum we see and engage with our customers, partners, leadership and product teams directly. My Tuesday keynote will center on demonstrating Titanium X with AI embedded everywhere as well as our new security and multi-cloud capabilities.

We have over 150 sessions and speakers describing how they are using our business clouds, business AI and business technologies, including security. See how customers are redefining their relationship with their data, staying secure in the age of increasing cyber attacks and what's needed

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to leverage the next generation of cloud in the AI. We also have a special investor analyst track that Greg can sign you up for, so feel free to reach out to Greg or the IR team.

Second comment in conclusion is we have a strong belief in our four-point strategy to create shareholder value. Strengthening our competitive advantage, accelerating cloud growth, capturing the large margin opportunity in front of us and strong capital returns via cash flow expansion, dividends and share buybacks. Of course, these three factor -- these four factors assume stable externalities and positive economic drivers. We continue to monitor the economies in Europe, North America, APAC and Japan and we're prepared to adjust our approach if we need to.

The team is focused on delivering to our F25 targets, building a strong, longer-term business and creating value for all our stakeholders. Our fundamentals remain strong. Demand is there, and we have the innovation our customers need. This is a winning strategy, and we see our path very clearly today.

With that, I'd like to thank you for joining us today, and may the one that brings peace, bring peace for all. I'd like to turn the call over to Madhu.

Madhu Ranganathan - *Open Text Corp - President, CFO and Corporate Development*

Thank you, Mark, and thank you all for joining us today. Please refer to the IR materials posted on our website. During Q1, we executed very well on our operational efficiencies and exceeded our plan to bring operating leverage to the P&L. We are committed to delivering on operational efficiencies. And in Q1, we led with higher adjusted EBITDA performance and delivering 35% adjusted EBITDA in Q1, excluding the impact of ultra-high-margin AMC business is a significant achievement.

Now turning to the numbers. I will share where relevant year-over-year comparison, excluding the impact of AMC divestiture. Our Q1 results reflect typical seasonality we experienced in the September quarter. Q1 total revenue of $1.269 billion was down 11% or down 1.8% when adjusted for AMC divestiture. Q1 cloud revenue was $457 million, up 1.3%.

Our cloud business continues to exhibit strong performance with bookings of $133.5 million, up 10.3%. ARR of $1.0525 billion was down 8.4% and down 1.1% when adjusted for the AMC divestiture. ARR percentage of total revenues was approximately 82.9%. Customer support was down 3% when adjusted for the AMC divestiture.

And moving to other financial metrics. GAAP net income was $84.4 million or $0.32 diluted EPS, up 6.7% year-over-year. GAAP gross margin of 71.7% was up from 71.4% year-over-year. Non-GAAP gross margin of 75.8% compared to 77.3%. It reflects the AMC divestiture and continued investment in AI, global security and in our global cloud infrastructure. Adjusted EBITDA of $443.8 million or 35%, as mentioned earlier, it reflects our extreme operational focus during the quarter.

Non-GAAP diluted EPS was $0.93, down 7.9%, also due to the impact of AMC divestiture. Our overall working capital performance remained strong with our DSOs at 42 days, a decrease of 1 day from 43 days in the last quarter. We reported negative $77.8 million in operating cash flows and negative $117.1 million free cash flows in the quarter, and these reflect the one-time tax payment on the gain relating to the AMC divestiture included in our Form 10-Q is the total cash payments during the quarter at $240 million.

Our GAAP tax rate in the quarter was 2%, and that reflects expiry of certain -- of certain uncertain tax positions due to statute limitations, some onetime acquisition charges and accruals, such factors are unique to Q1. We expect our annual GAAP tax rate to be in the mid-teens of fiscal 2025.

As we communicated during our last earnings call, today, you will see in our filings that we defined and standardized on net renewal rate, or NRR, which is a better reflection of our cloud -- of our business as it now includes the expansion and impact driven by customers who renew and migrate to the cloud.

Now moving to outlook. First, let me draw your attention to our Q2 quarterly factors included in slide 9 of our financial results and target presentations, and I will add to Mark's comments. We expect $1.29 billion to $1.34 billion of total revenue and ARR of $1.025 billion to $1.055 billion.

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And let me reemphasize that this Q2 has a difficult year-over-year compare as the prior year had both AMC revenue and higher license revenue from the grant of certain IP rights in fiscal '24, neither is expected to occur in Q2 fiscal '25. We maintain an incredible focus on cost to continue capturing our large margin opportunity. We're targeting adjusted EBITDA margin of 34% to 35% during Q2.

In today's call, our second half of the year commentaries are very important for all of you to note. We expect stronger momentum in revenues and cloud bookings during the second half of this fiscal year and a seasonally strong Q4 for all the reasons outlined by Mark earlier.

And with respect to expenses, we will continue to invest in our people as we experienced record retention and low attrition rates. As you all have seen in the past, our second half expenses will be higher than the first half. Starting in Q3, specifically in January, we expect higher cost due to annual employee merit increases, typical calendar year benefit cost uplifts and vacation accruals.

I will recall Mark's earlier comments, we are making investments in our go-to-market across three priority areas: people, customers and innovation. We have much success in attracting new sales talent, and we expect to maintain our capacity targets in sales, account executives and solution consultants.

So with all of that, we have factored strong second half business momentum in revenues and cloud bookings as well as the additional spend and investments into our fiscal '25 targets, which I will summarize shortly and also included in slides 10 and 11 of our investor presentation.

So cloud revenue of $1.85 billion to $1.9 billion, annual recurring revenue of $4.25 billion to $4.30 billion. Total revenues between $5.3 billion and $5.4 billion, which is constant to 1% growth, excluding AMC. Adjusted EBITDA margin range at 33% to 34%. As a reminder, in August, we raised our adjusted EBITDA outlook for fiscal '25, up 100 basis points to the 33% to 34% range. We are well positioned to meet our adjusted EBITDA targets.

As a reminder, our 2025 adjusted tax rate is expected to be in the mid-20s. Free cash flows of $575 million to $625 million. And let me now summarize our path to grow adjusted EBITDA and free cash flow during fiscal '25 on an annual basis. We are experts in driving meticulous expense management on a global scale, and that is what we're focused on.

And regarding cloud revenue growth, future margin expansion will be driven by higher revenues, including more SaaS. We will deliver in the cloud with lower cloud cost and more cloud automation. For the full year fiscal '25, we expect non-GAAP cloud gross margins in the low 60s.

We are beginning to leverage AI internally. Our business optimization plan we announced earlier to locate great talent in the right places is going well. Higher EBITDA will directly support free cash flow growth given the strides we've made on working capital and efficient capital expenditures, driving what we expect to be the highest return of capital to shareholders in OpenText's history during fiscal '25.

As we have communicated our four-point strategy to create shareholder value, capturing the large margin opportunity and cash flow expansion, they remain front and center. Our strong efforts during the last 2 fiscal years is paying off. Our efforts continued in Q1, posting 35% adjusted EBITDA in Q1, which is better than the last year, even after the divestiture of high-margin AMC business.

The decisions we make today, alongside programs and projects to deploy will set us up well beyond fiscal '25 into fiscal '26 and '27. We remain on target for fiscal '25, have momentum towards meeting our long-term aspirations, and we intend to update you annually on fiscal '26 and '27.

On behalf of OpenText, I would like to thank our shareholders, our loyal customers and partners for your continued support and always big thanks to Team OpenText. We look forward to seeing you in person at OpenText World in November. I will now request the operator to open the call for your questions.

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QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Steven Enders, Citi.

Steven Enders - *Citigroup Inc - Analyst*

Okay, great. Thanks for taking the questions here. I guess I just want to start a little bit on kind of maybe the demand environment and the macro and what you're seeing out there. I guess, was there maybe any shift in deals? Are you seeing anything kind of get pushed off and maybe gives a little bit more confidence in that -- in the second half that maybe is impacting things in the first half would be great to get a little bit more detail on what it is that's maybe going on out there in the deal environment?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. Very good. And good morning, Steven, thanks for joining the call. We're here in California as well. So early start to the day. Thanks for joining. The demand environment is stable. Even though I called out, we're going to continue to monitor the volatility in the world. We see demand as stable. The drivers for us are all point towards a stronger second half.

We have the largest release of our software and cloud in the history of the company coming up, Titanium X, or Cloud Editions 25.2. We've been out kind of well chronicling and well demoing, all the steady capabilities we've been adding. So directly to your question, we see the demand environment stable, so we're monitoring it as everyone else is. We have a very large innovation push that's going to drive demand for us in the second half.

We've just gone live on our new SMB platform that I highlighted we used was Project El Dorado, which is now live on Secure Cloud, which went live last week. And we got a big product upgrade in security, XDR as a Service. We have significant step-ups in ITOM from our Micro Focus acquisition, and we have a very large SaaS push coming with Titanium X. And everything downstream of SaaS is just goodness. It's faster time to revenue, higher margin and easier to expand for us.

And as we noted, we have a tougher compare in Q2. It's a high quarter for AMC, and we have our one-time royalty from certain IP grants from a year ago. So demand is stable. We're executing well, and we're looking for a stronger second half.

Steven Enders - *Citigroup Inc - Analyst*

Okay. That's helpful context there. I guess just a quick clarification. Just the -- can you remind us what the IP right impact is for 2Q that would be embedded in that comp? And then I guess secondarily, just think about the second half and the execution that needs to go into that, I guess, are there certain things that you're seeing on either the deal environment or go-to-market investments that you are making that gives you that confidence in the line of sight to the pipeline, the ability to kind of close on that for the second half?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. I mean, I'll take the second part first, which is the two things, the things that give us confidence are as we highlighted in the script, we're on track for delivery at Titanium X. On our people side on the sales force, we're at capacity. As I noted in the script, it's just an incredible thing.

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We're doing incredibly well on talent attraction and retention at record rates of retention in the company. I also noted that our pipeline is up 20% for the second half year-over-year, which is very tangible. So we're at capacity. Our pipeline is up. We have a product release. And we're also now live on AI internally.

We're going to demo at OpenText World, so Ollie.ai, where we're enabling our new hires and our experts in the sales force to what could take a couple of weeks to build proposals, we can now generate out of content management. So we think that's going to increase our response velocity in our win rates. So those are some very tangible things, Steve.

In relation to the grant of certain IP rights, [is as we chronicled] last year, we didn't talk about the quantum because we're always in the business of IP. And secondly, the nature of this particular item, there were a confidential -- confidentiality aspects. So we have no new disclosure from last year, and we didn't disclose the quantum last year.

Steven Enders - *Citigroup Inc - Analyst*

Thanks. All right. Well, I appreciate the context there and thanks again for taking the questions this morning.

Operator

Samad Samana, Jefferies.

Billy Fitzsimmons - *Jefferies Group LLC - Analyst*

Hey, everyone. This is Billy Fitzsimmons, on for Samad. Maybe first for you, Mark. You may have talked about it in the prepared remarks, I may have missed it, but it's been a couple of quarters now since Project [Athena] was announced, would be curious if you have any updates on progress thus far? And maybe going a step further, is there any anecdotes around early efficiency gains or early internal feedback from employees as you can implement these changes?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. Very good. Thanks, Billy. Thanks for your question. We had kicked off a handful of initiatives. One what I just talked about, right, which is Ollie.ai. I can't wait to show you at OpenText World. It's going to be main stage. We're going to have our sales force on stage, showing how we are using 10 years of data to enable our sales force to auto-generate proposals. Imagine an AE who's doing a FedRAMP proposal who's new to the company, and it were all my FedRAMP solutions, what's the best presentations.

Here are three questions, produce me a stellar generated response to give to my client. We're live on that now. And it's just going to keep getting better and better as we tune it. So the early feedback is very positive on that. Project Athena, which is for developers.

So Ollie.ai is for our sales force and support and Athena is for our developers. So we expect with 25.2 to generate our first applications. And those apps will be generated on top of all our API services. So we call our API layer -- our strategy is to build apps and to deliver APIs.

On the APIs, we're going to generate software on top of those APIs. And that's what Athena is going to do. And we'll have our first production apps by 25.2 for April of next year. We're just four, five months away. And the early feedback is fantastic. What APIs, how do I use them?

What are kind of the templates to generate simple things. They had to upload a file. How do I build a screen? How do I do security? So Athena, in its first generation of software is focused on basic apps, is focused on language translation. We deliver our product now put into the 40, localize it across 40 countries and generate the documentation.

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So we'll start to see the impacts with Titanium X 25.2, early feedback great. And it's working right in the areas where we thought we could, which is app generation, localization and documentation. And that's a wave 1 for us for developer experience productivity.

Billy Fitzsimmons - *Jefferies Group LLC - Analyst*

And then -- that's super helpful, Mark. And then if I could sneak in another. I know a couple of quarters back, (multiple speakers) that's from two -- sorry, three to four years. Is that continuing to roughly track at four years now, one quarter into 2025? And then just help us think about kind of the pace of on-prem decline conversions you're seeing in your business in 2025 relative to what you saw in late fiscal 2024?

Madhu Ranganathan - *Open Text Corp - President, CFO and Corporate Development*

And Billy, Madhu here. The very first part of your question didn't come through, if you don't mind repeating it.

Billy Fitzsimmons - *Jefferies Group LLC - Analyst*

Yeah. The first part was just -- I know a couple of quarters ago, cloud contract duration stretched from three years to four years. Is that continuing to track at roughly four years?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yes. Fair enough. I got it. Thanks, Billy. Look, I'd note on SAP's earnings call, they talked about their average contract length going out to about 4.5 years. And we're we tow right along with SAP on our SAP business, which is an important part of our business. So they've talked about extending out to 4.5 years.

We're about 4 years right now. We -- I think we have a little better control over that ramping. We did note -- as you noted -- we noted a couple of quarters ago that we began to see this increasing ramp in agreements. So it has stabilized. And we're getting a little -- and we're also getting better control of our partners, right?

So of saying, okay, this is sort of the high watermark. So it's not continuing to ramp. I would say that it's hit a high water mark. We're starting maybe to dial it back a little bit. But we're seeing just around 4 years. SAP was very -- had their disclosure around 4.5 years.

And then on the on-prem to cloud, which I think was another part of your question, it's all about the second half drivers for us. When I look at Titanium X and one of the design principles of Titanium X, the first principle was to have the Titanium X is designed and built for staff. And that's why we're calling it out.

So that's where our major piece is core content, service management, digital operations, developer experience, and XDR as a service is only a SaaS offering. And so I think we'll continue to see in a very controlled way. Customers continue to move from on-premise, and we've done great to the private cloud, and Titanium X will give us now the next growth swim lane, which is to move on-prem into SaaS and continue to do this in a very controlled way.

Operator

Raimo Lenschow, Barclays.

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Raimo Lenschow - *Barclays plc - Analyst*

Okay. Thank you. Mark, since we are in this new AI world, like how do you think about adoption patterns between like your Aviator offerings, et cetera, and kind of the more kind of initial steps with the Microsoft Copilot, et cetera, like how do you think that will play out in terms of (inaudible) and then when you're talking to customers in terms of like adoption -- cycle adoption patterns?

Is that like first, you kind of do the standard kind of Microsoft type Copilot stuff, then you come to you? Is it going straight to you because the value add is so high. Can you speak to that of what you're seeing there in the market, please?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. I mean, I'll speak first. Thanks, Raimo. I'll speak first to us, which is we are seeing steady progress. We've been -- this is our third, fourth quarter of having Aviators in the market by Titanium X. We're going to have 15 Aviators and 100-plus agents, and it is commonplace. So like having a search button on a screen right? We have an Aviator button on screens now, and over 100 agents permeated through all of Titanium X. And so it's easier to use. It's easier to deploy, and it's getting less expensive.

Still a little expensive. When you look at the platform providers, you sort of buy by the drink, right? Or you make multiyear commitments. Interestingly for us, we see customers working on big problem sets. And so there's -- so and we're like -- we're very close to like breakthrough moments on very big problem sets.

So it's steady as we go. It's in every conversation. We're so delighted with Titanium X in the world we see it live here in a couple of weeks, where it's almost like a search button on every screen. We had 20 wins directly related to GenAI Aviators in the quarter. And we're just going to keep making steady progress.

And it's all going to support our bookings aspirations up to 25% bookings growth, is going to support our cloud growth -- revenue growth of 2% to 5%. But I think it's just steady, steady, steady, and then there's a step-up at some outer point. But we're making really good progress on making it easy to use, deeply embedded, radically focused on driving down the cost and making it a button, an agent button on all our major processes.

Raimo Lenschow - *Barclays plc - Analyst*

Okay. Perfect. Thank you. And then one for Madhu, like if I look at the margin performance this quarter was very strong, guidance is really healthy here. Is there anything that we should be aware of in terms of timing that some of the costs got pushed out in the second half? Or is this just all kind of you're doing your job and controlling what you can control? Thank you.

Madhu Ranganathan - *Open Text Corp - President, CFO and Corporate Development*

Yeah. Thanks, Raimo. We are doing the job and beyond our job. And I'll explain that in the last couple of years since the close of Micro Focus transaction, we have taken a lot of cost out, and we've been reporting that to you systematically, right? We also announced a business optimization plan in early July, the implementation of it was also very early to provide us the benefit throughout the year.

What's really happening in the second half is very consistent for OpenText, our annual merit increases on January 1. And as I said, we are seeing -- that could employ your retention as well as sales capacity we mentioned. So that's really what you're seeing in the second half of the year. But having a great start on adjusted EBITDA in Q1 is what's really supporting us and the confidence to maintain the 33% to 34% for the year.

Raimo Lenschow - *Barclays plc - Analyst*

Okay. Perfect. Thank.

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Operator

Paul Treiber, RBC Capital Markets. Mr. Treiber, your line is open.

Perhaps we should move on.

Erin Kyle, CIBC.

Erin Kyle - *CIBC Capital Markets - Analyst*

Hi, good morning. It's Erin Kyle on for Stephanie Price. I wanted to ask a question just on the revenue growth, excluding AMC, which was negative 1.8% this quarter. So assuming this is all organic now. How do you think about organic growth at Micro Focus post the AMC divestiture? And what are the key lines of business that you expect that will drive you towards achieving organic growth?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yes. Sounds great, Erin. Thanks for being on the call this morning. Let me start with that we're maintaining our outlook for the year, which is constant to 1% growth. And we -- we look at our business by market area today. So in particular, for what we acquired from Micro Focus, deconstruct that into security, into digital operations and into the developer, if you will. We are deeply excited on the security side.

As noted, our XDR as a service is taking what we acquired from Micro Focus plus components from other parts of the business like forensics, like Bricata on the network side, plus our e-mail security from Zix. And we're bringing it all together in a unified composable offering called XDR as a Service, and we're quite excited about it. So we see security being a growth driver for us.

Second piece is what was historically called ITOM what we now call digital operations. And I'm just really excited about the product offering around discovery, which feeds into security, by the way. What are you securing [indiscernible] discover the assets.

Observability into the infrastructure, observability across multi-cloud, financial ops management, sustainability and green computing, which has been our priority. So the product has just made incredible strides, if you will. We've got a little more work to do on the developer side. It's more of a complex area.

So we stabilized historical Micro Focus last year, as we talked about. We are now in a platform where we're looking to grow Micro Focus, particularly in security and digital operations. We got a little more work to do on ADM, and we factor that all into our constant to 1% organic growth this year.

Erin Kyle - *CIBC Capital Markets - Analyst*

Okay. Thank you. That's helpful. Quick color there. And maybe if I could just ask one more question just on capital allocation. So you did $85 million in buybacks this quarter. And I noticed targets are unchanged for the year. So I just wanted to clarify the strategy is still to focus primarily on that organic growth and return of capital to shareholders and whether M&A fits into the picture at all?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. So a couple of things there. We're excited about delivering a record amount of capital this year to shareholders. So we are -- we've announced plans around approximately $570 million of return of capital will be the highest in the company's history. And delivering that amount by the end of this year, we will have delivered $3 billion over a decade, and we're on target to have the highest capital return in the history of the company this year.

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We're also looking at M&A. And so with the stabilization of Micro Focus, the divestiture behind us, of Titanium X coming into the market. Yes, you can expect us to continue to look at M&A, small- to medium-sized cloud companies, profitable, generating ARR for us, that fit into our current strategic thesis.

Erin Kyle - *CIBC Capital Markets - Analyst*

Okay. Thank you very much.

Operator

Richard Tse, National Bank Financial.

Mike Stevens - *National Bank Financial - Analyst*

Hi, good morning. This is Mike Stevens on for Rich. Just more broadly, you touched on M&A there. But are there any further opportunities to streamline the company for growth, a la the AMC divestiture?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. I mean our whole script and our whole narrative is on driving organic growth, right? So -- and having some M&A what was the question. So yes, I mean, it's all about the second half and what we've talked about. It's bringing Titanium X to market, which is across all our business clouds.

It's driving growth in our new AI offering, business AI and business technology in particular, security. And as we noted, we're at a high watermark for sales capacity. Our pipeline is up 20% year-over-year for cloud and AI. And the main thrust of the company is all focused on organic growth.

Mike Stevens - *National Bank Financial - Analyst*

Okay. That's helpful. Additionally, with the Aviator, you mentioned the number of wins in the quarter. How much approximately would that represent of bookings? And where do you see that kind of going forward?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yeah. No, we didn't break out of the 10% bookings growth. How much of that was related to Aviators, if you will. But clearly, it was in the large deals and in the bookings growth that we had within Q1. So it's the main part of how we sell today, right?

So we go to market today and our strategy. Again, we start with our business clouds, from content all the way through the developer. We go to market around, supported right underneath there, a multi-cloud offering and then coupled with security and AI.

So it is now a coordinated part of how we go to market. And I expect steady, steady, steady progress every single quarter. Q1, 20 direct wins related to AI. We'll have direct wins in Q2. It will add to our targets of going from 10% up to our mid-20s, 25% cloud bookings growth for the year. So it is contributing to the bookings growth for sure.

Mike Stevens - *National Bank Financial - Analyst*

Okay. I appreciate the insights, and I'll pass the line. Thank you.

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Operator

Thanos Moschopoulos, BMO Capital Markets.

Thanos Moschopoulos - *BMO Capital Markets - Analyst*

Hi, good morning. The cloud revenue growth was subdued this quarter. And I understand you're looking for that to accelerate for all the reasons cited. But just in terms of the quarter in particular, -- is that a function of the delayed deal ramp dynamic that you called out? Is there any just in SMB? Or what are some contributing factors?

Madhu Ranganathan - *Open Text Corp - President, CFO and Corporate Development*

Yeah, Thanos, it's Madhu here. I'll pick up the question and Mark can chime in, of course. So think of cloud revenue as it is recurring. But certainly, in our third and fourth quarters, we do see a lot more of the volume and sort of the variable side of the cloud revenue picking up. So we had over 3% growth in Q4 of last year, and that's typical of our sort of end of fiscal year strength.

And Q1, the growth is right where we expect it to be on revenue. As Mark outlined earlier, no further sort of expansion of where the cloud contracts are, they're still around the 4-year mark for what we do and slightly longer when we look at SAP. So nothing has changed there. And I would look at Q1 cloud revenue as more of Q1 light seasonality.

Thanos Moschopoulos - *BMO Capital Markets - Analyst*

Great. And then Mark, can you comment on SMB. So another business implies there if you go back a few months. How has that been looking? And you alluded to a new platform you're launching for SMB, you can stand on that?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yes. Thanks, Thanos. And yes, I mean, as Madhu noted, we had our quarterly factors for Q1, and we delivered right to what we said we're going to do on revenue. And that's inclusive of cloud seasonally lower quarter for us and inclusive of SMB, right, in all those numbers. Now we're excited.

It's a different year for us in SMB than it was last year. And we now have our partner platform live in the market, what we call secure cloud. So we've gone from project El Dorado to the actual service offering called Secure Cloud or live.

And the platform allows us -- allows partners to be able to buy from us, allows partners now we can easily add new products like our Pillr acquisition, which is on Secure Cloud, and allows partners to then go sell to their customers and then to be able to monitor their installed base and usage. So it's sort of a PRM, is a partner relationship management platform that allows us to sell, partners to sell and partners to manage. And it's now all built by OpenText, flexible, customizable and we're just delighted with it. So that's an enabler for us.

Second is we've gotten closer with our biggest partner in this area, Microsoft. And Microsoft is one of their biggest investment areas for the year. And then thirdly, the demand is starting to pick back up. So we think those three factors, we have gone from a headwind, if you will, to just steady as you go. And I think we'll pick up some tailwinds throughout the year.

So we're quite excited about it.

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Thanos Moschopoulos - *BMO Capital Markets - Analyst*

Great. I'll pass the line. Thanks.

Operator

Adhir Kadve, Eight Capital.

Kiran Sritharan - *Eight Capital - Analyst*

Good morning, all. This is (Kiran Sritharan) on for Adhir. My first, I just want to touch on the cloud growth range again between 2% to 5%, following this quarter, what factors you'd call out that contribute to the bottom and the top end of that range?

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

I would say three factors. First is SaaS. Customers adopting our SaaS capabilities in Titanium X; two, seeing Aviator and our AI contribute revenue. And then some product-specific pieces, in particular, I'd call out security, XDR as a Service. Those are three things that are going to drive us to the top end of the range.

Kiran Sritharan - *Eight Capital - Analyst*

Thanks, Mark. And then on -- I'd like to zoom in on the investment in the sales and go-to-market. Where are you in the hiring cycle of these days? And maybe you can also comment on the experience levels and the pace at which this cohort would contribute just given the refresh your go-to-market strategy? Thanks and I'll leave it there.

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Yes. Thanks for the question. Yes, as noted, we're having great success in going to market, attracting and in hiring very qualified account executives and solution consultants. And we are at sort of our capacity, if you will, -- and that's driven by a few things. So first of all, the schedule, we attract skilled professionals.

We don't tend to look for kind of the fresh grad to come into enterprise selling. We do hire those straight out of college, maybe into inside sales and then to grow in the organization or account development executive. So it's a great place to enter OpenText and then to grow, But what I was talking about was the qualified sales executives that have been in the market 7 to 15 years joining OpenText.

So we're just having great success in doing that. We're at capacity. We're also -- our employee engagement is incredibly strong with our highest retention rates for employees. So our employee value proposition is very strong. strong for the new hire kind of entering OpenText as inside sales or account development and then to grow your career, get your first job out [of school] and grow with us.

And then the skilled professional 7 to 15 years out of enterprise software companies that has brought us to the top of our capacity. And it will help them both with AI, both cohorts with AI and Ollie.ai.

Madhu Ranganathan - *Open Text Corp - President, CFO and Corporate Development*

And if I could just add here, when Mark mentioned we're at capacity in Q1, early part of the year, I mean, that was a very important conscious step we undertook in order to have a strong second half, given all the product innovation that are coming through. And then when I spoke about the

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second half at expense continuing to invest, keep in mind that that's also needed for our fiscal '26 and beyond. So there are really two parts to the sales investment.

Kiran Sritharan - *Eight Capital - Analyst*

Thanks for the color, guys.

Operator

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

Mark Barrenechea - *Open Text Corp - CEO, CTO and Vice Chair*

Okay. Very good. Thank you, everyone, for joining us today, and we'll welcome your feedback, if you like, the early morning calls or the afternoon call. So -- but we'll welcome your feedback on that. We hope you'll join us. We hope you'll join us at OpenText World, November 19. And I'll be live and in person at the TD Conference, November 25, and as well as all the other conferences that Greg and Madhu highlighted. So thanks for joining us today, and we look forward to seeing you in person soon. That ends today's call.

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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