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OTEX.TO - Q3 2025 Open Text Corp Earnings Call

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CORPORATE PARTICIPANTS

Greg Secord *Open Text Corp - Vice President, Global Head of Investor Relations*

Mark Barrenechea *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Chadwick Westlake *Open Text Corp - Executive Vice President, Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Raimo Lenschow *Barclays - Analyst*

Stephanie Price *CIBC Capital Markets - Analyst*

Thanos Moschopoulos *BMO Capital Markets - Analyst*

Samad Samana *Jefferies - Analyst*

Richard Tse *National Bank Financial - Analyst*

Paul Treiber *RBC Capital Markets - Analyst*

Kevin Krishnaratne *Scotiabank GBM - Analyst*

PRESENTATION

Operator

Thank you for standing by. This is the conference operator. Welcome to the OpenText Corporation's fiscal 2025 financial results conference call. (Operator Instructions)

I would now like to turn the conference over to Greg Secord, Head of Investor Relations. Please go ahead.

Greg Secord - *Open Text Corp - Vice President, Global Head of Investor Relations*

Thank you, Gaylene, and good morning, everyone. Welcome to OpenText's third-quarter fiscal 2025 earnings call. With me on the call today are OpenText's Chief Executive Officer and Chief Technology Officer, Mark Barrenechea and OpenText's Executive Vice President and Chief Financial Officer, Chadwick Westlake. Today's call is being webcast live and recorded with a replay available shortly thereafter. All of this is available on OpenText's Investor Relations website, which, as a reminder, is investors.opentext.com.

On today's webcast, we're trying something new and we'll have our prepared remarks coordinated with the slides from our Q3 financial results presentation. This presentation is available on the IR website to download. And please note that if you're logged in for the live webcast, you're already set up for the slide show.

I'll also point out that there are two presentations posted on our IR website, the Q3 fiscal '25 IR financial results sideshow, that will be used during the call and our broader Q3 fiscal '25 investor presentation, which is posted for reference throughout the quarter and used during our investor meetings. Now turning to upcoming investor events.

OpenText will be participating in the following investor conferences: on May 8, the Needham Technology Media and Consumer Virtual Conference. On May 20, the Barclays Leveraged Finance Conference in Austin, Texas, and May 22, the CIBC Technology Conference in Toronto. May 29, Jefferies Public Technology Conference in Newport Coast, California, and the BMO, Bank of Montreal Virtual Software Conference on June 9. Finally, back in Toronto on June 12 for the RBC Technology, Internet, Media and Telecommunications symposium. It will be a busy quarter, and we look forward to meeting with you.

And now for 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 could differ materially from the forward-looking statements made today. 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 last night. Each of these can be found on our IR 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, and 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 also available on our website.

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

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Thank you, Greg, and good morning, and welcome, everyone, to our Q3 earnings call. There are three key areas I plan to cover this morning. First, I want to refresh our listeners on why OpenText is so distinct, designed to perform across business cycles and is critically significant to organizations across industries and geographies. There may be external factors we cannot control that makes revenue harder to forecast, but we intend to perform in the areas we do control, like EBITDA, earnings, free cash flow and capital return.

Secondly, I'll take you through some important product customer financial updates for the quarter as well as my perspective on market volatility and how OpenText is positioned to help our customers create value through this deep uncertainty. This includes discussing the transformative expansion of our business optimization plan which is led by AI first.

Third, I'll confirm progress on our three strategic priorities, including competitive advantage, total revenue growth and operational excellence. Our differentiation is getting stronger through AI first, and this will help lead us to upper quartile returns.

Before I start, I'd like to thank Madhu for the seven years of service to OpenText and for the transition over the last few months, all the best in her continued journey. Let me formally welcome our new CFO and business partner, Chadwick Westlake. Chadwick joined us from publicly traded EQ Bank in Canada. And as you know, he is an outstanding executive and was just recognized as one of this year's best executives in Canada by the Globe and Mail. The leadership team and I look forward to working with him as we bring OpenText to its next level of performance and value potential.

Chad will speak to the highlights of the quarter here shortly. Let me jump right in.

OpenText will celebrate its 35th anniversary this summer, and our potential remains limitless. By choice and origin, we are proudly Canadian helping the world's largest organizations to deliver products and services that benefit the lives of hundreds of millions of people every day across the world from Canada.

At our core, OpenText is an information management company. We've empowered the knowledge worker over the last three decades. And now we are creating the digital knowledge worker of the future. We operate a portfolio of cloud products centered on enterprise content and process automation, securing and integrating that content across business applications and business networks, delivering exceptional services to the users of that content and doing this at scale.

We are now redefining the value of that information through our new AI platform, Aviator. Our ability is unmatched to solve global and strategic problems for our customers by universally linking information, agnostic to platform or infrastructure or language model or information format. We have always centered on building lifetime value for our customers through a *raison d'être* of we always deliver. No one else can do what we do. This is the key to our resilience.

Our capabilities are far reaching. OpenText is likely part of your daily life, and you may not even realize it. For example, where did you get your milk or breakfast? Where did you get your milk this morning to put in your coffee or your breakfast?

Did you read the morning newspaper using cellular data? How did you process family payments? Did you stop for gas? Did you see a doctor or take medicine? Or as simple as turning on your lights, turning on your TV, or watching a streaming movie or the National Hockey league.

OpenText is the platform behind the scenes for the brands that you trust every day, making all of this work. It is important for our investors to understand that we allocate capital to deliver the best value. We are both an offensive and defensive investment opportunity in Canadian technology with significant reasons to hold, buy and buy more of our stock. The team is excited about winning in F '26, with a new product cycle relevant to strategic needs of cloud security and AI.

We are an AI-led organization with a transformative business optimization plan. The external distractions of xAMC, xDXC, xRoyalty are now behind us this quarter and a clear return to capital flexibility, as you can see from our cash flow engine and our cash flow results in Q3. You can expect us to resume our traditional programmatic approach to growth through tuck-in acquisitions when they align with our strategic priorities.

We'll also carry out programmatic divestitures, when that is the best opportunity to monetize long-term returns for mature products. Our primary use of capital is approximately 50% of free cash flow to dividends and buybacks. And as free cash flow grows, so should our capital return. But also, please recall, when we introduced this, we also said we will remain flexible and allocate our capital to the highest return scenario that is in front of us. Expect us to continue to allocate capital in a flexible manner, but always to the highest return.

Bottom line, our total shareholder return proposition keeps getting stronger. Before I get into the quarter highlights, I want to speak about the market volatility. You may have heard other companies talk about two demand scenarios and thus two outlooks, and some companies are even pulling guidance. You're all very aware of what is happening, and let me add our color to recent events.

There was clearly a demand shock in the second half of fiscal Q3, driven by the sudden announcements of tariffs, which then became rolling tariffs. There was so much tariff information for our customers to understand. And some of that information quite candidly was reliable and some of it was not. We are seeing our customers move beyond these disappointments in disbelief to now take in control. They are continuing with their strategic priorities, even if in some cases, reduced near-term -- even in some cases, reducing near-term spend. I'd like to highlight an important positive trend that we are seeing where customers are looking to deploy in local clouds while reducing the dependencies on US technology.

This introduces new opportunities for OpenText, given our Canadian roots and local presence in key regions around the world. Further, customers are continuing the consolidation to the cloud, creating programs to gain more efficiency and doing this through information management AI and new digital workers. Our digital worker approach is, let AI and machines do the work.

This is a low-cost and limited workforce that will benefit all organizations in all industries. As we demonstrated at OpenText Summits in Europe a few weeks ago with our new cloud additions, AI Aviators and My Aviator, we can take human tasks that require dozens of screens and work and days of work and reduce that down to a dialogue box in minutes.

In summary, no one can predict how long the volatility will last, but we are well positioned to help organizations reposition globally, deploy locally in our private and sovereign clouds, and gain extreme efficiency through deploying a new digital workforce using our AI.

Shifting to our Q3. In a normal world, we are fully expecting to deliver to our business plan and revenue range of \$1.26 billion to \$1.3 billion. But given the large volatility, we did not meet our expectations on revenue and new bookings, we ended up 50 basis points below our target range. Once tariffs were announced, including 25% auto tariffs as well as US government spending cutbacks, customers pause to assess the impact on their businesses. Our book of business was disrupted in the range of \$40 million to \$50 million. During COVID, we saw impact on travel, transportation, retail, and it all came back. And this disruption, we are seeing impact in auto, materials, energy, government and some retail, and it too will come back.

With this said, we executed extremely well in our operations across adjusted EBITDA, adjusted EPS, free cash flow and our share repurchase program. In Q3, ex AMC and in constant currency, we delivered \$1.27 billion of total revenues, down 2.9%, down 1% when factoring in IP rights in DXC. New cloud bookings were \$151 million, down 8% due to the demand disruption. We expect to show Q4 growth in enterprise cloud bookings and for the fiscal year.

Bookings growth in Q4 is unlikely to be enough to get us to our 20% to 25% annual target. Rather, we expect the fiscal year to be in the mid-teens for growth. I will continue to encourage investors to focus on RPO and cRPO as the most effective go-forward metrics as these will have more clear benefit with year-over-year metrics as of Q4. As I noted upfront, while we may not be able to predict the headlines in the coming weeks and months, we will control well, that which we can control, including EBITDA, earnings, free cash flow and capital return.

Looking at Q3 positively within the quarter, Cloud revenues grew 3% year-over-year in constant currency, our 17th consecutive quarter of organic growth. Adjusted EBITDA was strong at \$395 million or 31.5% margin, up year-over-year, excluding AMC, adjusted EPS was \$0.83 in constant currency, up year-over-year, excluding AMC. We had record free cash flow of \$374 million, up 7% year-over-year. We scaled our repurchase program by 50% in the quarter. We repurchased and retired 4.4 million shares for \$115 million for total outstanding shares of approximately \$260 million, the lowest since September of 2016, and cash ended up at nearly \$1.3 billion.

Q3 was a strong product and customer quarter. Customer wins included ABN AMRO for application security, Froneri International for digital commerce, Japan Tobacco for application automation, the US Air Force for secure identity and Pacific Life for digital information management. These wins were led by our next-generation cloud platform Titanium X where we are winning with AI first, our business cloud suites, our new security technology for identity protection and threat detection and response. Titanium X with AI is now delivered launched last month from our European Customer Summit, and this is a game changer for us.

Combined with our business cloud suites, we can help customers make faster and more accurate decisions, deliver a step change in productivity and simplify multi-cloud complexity. We have a very ambitious multi-quarter roadmap leading with AI first, and every customer is an opportunity to upgrade and expand with Titanium X.

Let me turn to our expanded Business Optimization plan, which we announced today as outlined on Slide 13, where AI first is now the central part of our corporate DNA and culture. New hires must have AI skills. AI will be part of our performance and talent reviews. AI has now turned on in various forms for all our employees to use, and we will only hire new talent where the work cannot be done by AI. We are using AI and engineering, support, professional services, and sales, and for the general knowledge worker.

We have progressed so rapidly with AI we can now see the path to a significant reset in our cost structure through our expanded plans and other related initiatives. We expect the new annualized savings to be up to \$400 million, including an incremental net reduction of 1,600 employees. And when combined with what we have previously announced in action, this is a total annualized savings of \$490 million to \$550 million and a net reduction of 2,000 employees when fully implemented. Approximately 50% of the new savings are to be realized in fiscal '26 with the remaining benefit to be realized in fiscal '27.

This is transformative and strategically aligned to our AI-first culture and initiatives. We'll provide more clarity on this in Q4, conjunctive with our F '26 targets, including what to expect in margin improvement, reflective of the initiatives and our scaling investments in innovation and growth. Let me turn to outlook.

Let me speak to our F '25 targets. Look, the easiest thing we could do is say there is so much volatility we are pulling our guidance. But we have a job to do, and our job is to respond to whatever is thrown at us. We are not changing our adjusted EBITDA, free cash flow and capital return targets. In fact, we're going to work harder to get to the high end of our free cash flow ranges.

In a normal world, we would be holding to our previous revenue targets. However, with the volatility, it is not possible to fully predict total revenue, and we could be below the current low end of our range. So we think it's prudent to communicate an F '25 revenue target of \$5.1 billion to \$5.17 billion versus the previous range of \$5.17 billion to \$5.27 billion. If we do better, that is upside to the range. This approach reflects our ability to manage earnings across business cycles like we did in COVID.

Let me wrap up my prepared remarks by going a little deeper in our three strategic priorities and why these remain as constant priorities. First, increasing our competitive advantage through our new product cycle and leading with AI first, Business Cloud suites and new security. We can see the momentum from industry analysts, customer engagement, pipeline expansion, customer and partner wins, coupled with the market timing for consolidation, efficiency gains, local deployments, enabling a new digital workforce. This is how organizations win.

Second, our property on total revenue growth. Our narrative is AI first, no longer ex AMC. We are entering an exciting new product cycle as noted, entering new market areas such as Security, and we have completed seller excellence training across our sales force. And for the first time, and with Titanium X, partners are now allowed and enabled to sell our cloud offerings. And we have new clear capital flexibility. Our strategic partners across SAP and hyperscales keep getting stronger. Customers are gaining control in the time of disruption. We are seeing high renewal rates in our cloud and off cloud, and cloud rates were up 100 bps quarter-over-quarter.

The third on our strategic focus is operational excellence, which remains -- which means upper quartile margins, free cash flow, earnings, and capital return. With the transformative expansion of our business optimization, we're confident that we can generate more profits from higher revenues by lowering our cost curve and setting a new milestone level of free cash flow generation over the next couple of years.

With that, let me turn the call over to Chadwick.

Chadwick Westlake - *Open Text Corp - Executive Vice President, Chief Financial Officer*

Thanks, Mark, and good morning. As a very proud Canadian, I'm pleased to now be serving this proud Canadian company. Since joining the team in March, listening has been job one. I spent my first couple of weeks meeting with our shareholders, capital markets analyst and partners. I understand the opportunities, and I'm enthusiastic about the growth journey ahead.

As Mark referenced, in Q4, we will introduce fiscal 2026 targets and reframed medium-term aspirations. There should be no surprises. You will continue to see targets on what you know what's best for, including adjusted EBITDA margin, free cash flow and adjusted EPS growth, capital returns and our expectations for annual total revenue growth. We will simplify more performance metrics and look to add increasing transparency.

This includes for how more of our businesses are performing, particularly ones that are outperforming and revenue growth. For today, I'll focus on Q3 results with brief added context on enterprise cloud bookings, revenue, adjusted EBITDA margin, free cash flow and, overall earnings. As you reviewed in our material, total enterprise bookings were \$151 million, down 8.4% year-over-year. While below expectations, I would contextualize the outcome in a few ways.

We had good results in a few key segments. Importantly, in content management bookings from the financial services and technology sectors, we won more competitive business and tangible pipeline momentum. As Mark indicated, our bookings difference to target was primarily attributed to the macro disruption in the quarter, which resulted in some positives to later quarters.

And on the cloud net renewal rate, a metric we introduced in Q1. We expanded again 100 bps sequentially to 96%. You may recall, we introduced total RPO and cRPO last quarter. Once we have that year-over-year comparable in Q4, you'll have a trend, and we'll add more context.

Shifting to revenue for the quarter, where we had solid annual recurring revenue of 82%, higher year-over-year, excluding AMC. Cloud revenues were \$463 million, up nearly 2% year-over-year and represented about 37% of total Q3 revenue. That marks 17 quarters of cloud organic growth driven by AI readiness and strong demand for our Content cloud.

Non-GAAP cloud margin increased approximately 300 basis points to 62.7% year-over-year. Customer Support or Maintenance revenue was \$567 million, coming in slightly below our expectation. We are making progress here, and non-GAAP gross margin remained strong at 89.3%.

Overall, non-GAAP gross margin for Q3 was 75.7%, which excluding AMC, remained consistent year-over-year. As you see on Slide 19, important to note, we are working to expand our revenue disclosures. This is intended to add more clarity and context for our businesses where revenue is

outperforming such as Content, as you see on the left. That is compared to our businesses where we expect to perform and continuously improve on the right side. We look forward to publishing this data for you in Q4 and regularly.

Now to adjusted EBITDA margin, which was ahead of our target range at 31.5%. While revenue was lower, expense actions and improving our operations translated well. This was a good outcome for Q3 and it takes our year-to-date adjusted EBITDA margin to 34.7% compared to our annual target of 33% to 34%. As a reminder, our fiscal Q3 is a calendar Q1 and our adjusted EBITDA margin would always be lower sequentially. So the difference you see to Q2 is entirely seasonal, both in revenue bookings and expense increases, including annual reset categories such as annual merit increases, vacation and benefits that take effect January 1.

Total head count declined slightly from Q2 but you will see that come down further in Q4 as part of the announcement today. Expenses for Q3 were down year-over-year, importantly attributed to the completion of the first phase of the Business Optimization plan announced last summer. OpenText is exceptional at consistently generating strong and recurring free cash flows. As mentioned earlier, our free cash flows increased 7% year-over-year to \$374 million on a reported basis a new high-water mark in a quarter with a 30% free cash flow margin.

Q3 each year is typically the highest due to the timing of Maintenance annual renewals, but two items of note. In Q3 last year, we had the benefit of free cash flows from AMC, which is now gone. And in Q3 this year, we had a total one-time benefit of \$48 million as disclosed in our 10-Q related to the collection of a UK state aid receivable.

Mark touched on our capital allocation strategy, and I will reinforce and expand on this a little more. We expect our businesses will continue to generate strong and growing free cash flows. And in turn, we allocate that to the highest capital return scenarios, thus, reserving flexibility in our strategy.

On a primary basis, we look to deploy it by investing back into our businesses and customer innovation as well as always rewarding our investors with a steady dividend. Secondary to that, flexible to the environment and opportunity, we will deploy it to acquire tuck-in companies that align to our current strategy, and we will repurchase shares, particularly at these valuation levels. For example, based on that opportunity, we -- you saw us increase our current repurchase program by 50% up to \$450 million in March this year. It is very important we will remain strategic and flexible in this capital allocation sequence.

Moving to adjusted EPS, which was strong again in Q3 at \$0.82 diluted. Reported that is down 13% year-over-year. But excluding the AMC divestiture, it was up year-over-year. Contributing to this outcome was the benefit of repurchasing and canceling 14.3 million shares over the trailing 12 months. With purchases completed at the end of March, we had approximately \$184 million capacity remaining in our \$450 million program. We intend to continue our program.

In closing, we are focused on executing in Q4, building long-term value for our customers and shareholders. As an investor, you might want to hold OTEX stock as the best defensive name in Canadian technology with our world-class installed base, loyal customers, moats around our key businesses, and a strong earnings profile and return of capital strategy.

You should want to buy OTEX stock because of the opportunity to participate in our growth in this more than \$200 billion of total addressable market. We are a significant cash generator with scale and efficiency to reinvest in our growth products across business cycles, and you should want to buy more of the stock because of the significant discount in our valuation to key metrics as compared to our history and comparable firms. It's an exceptional time to participate in the earnings growth engine we're building.

With that, Gaylene, can you please open the line to our equity analysts for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Raimo Lenschow, Barclays.

Raimo Lenschow - Barclays - Analyst

Mark, I have two questions, one for Mark, one for Chadwick. Mark, first one, if you look at the performance this quarter, obviously, you pointed out some of the uncertainty, but we also have seen other guys in the space report numbers and kind of -- it kind of, in relative terms, slightly better than you guys. Can you talk a little bit about -- maybe there were some geographic or vertical split that is different for you than for other guys to try to understand that a little bit better. Thank you on that one.

And then Chadwick, now with you having joined, can you talk a little bit about your priorities now that you're in the seat and thinking about capital structure, portfolio, or the different products, et cetera?

Mark Barrenechea - Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer

Yes. Thanks, Raimo. Appreciate the question. Well, as we know, we ended up 50 bps below our range and actually in the low end of the range in constant currency. But for us, demand was disrupted.

And I think the tipping point for us was the auto tariffs and the rumor of them and the actualization of them around March 12. And so we have exposure in auto, materials, US government, and energy. And that Q4 impact, as I said in the call, was \$40 million to \$50 million, roughly, I'd say two-thirds of that was bookings, one-third was revenue. And in a normal world, we were on target to be right within that range.

But we acquired Covisint. We've always had a very important business in auto, auto parts, auto ecosystem, materials, US government and energy. On the government side, you just read the headlines, Nations to Health, US AID, Department of Education, and we have some business in there.

So as we've said, on the \$40 million to \$50 million, roughly two-thirds bookings to one-third revenue. With some of the relief in auto tariffs announced this week are rumored still data being worked out. Some of our auto customers are reengaging deeply now that they can manage and predict. And if you can't kind of predict your spend, you spend -- you don't know how to invest.

So like we said, if we can't control the topline in the volatile times, we will control well that which we can control. And we did an extraordinary job, the company did on its expenses, margin, earnings, record free cash flow with our operations. Yes, we had a onetime item in there, but we still performed extremely well. And the business will come back. I'm confident it will all come back just like it did during COVID.

Maybe Chadwick, over to you for the second part.

Chadwick Westlake - Open Text Corp - Executive Vice President, Chief Financial Officer

Yes, sure. Thank you, Mark. Thanks for the question. Three things I would say briefly, and again, I'm not at the two-month mark. But I'd say three things very simply.

Number one, capital allocation. Maximization and working together with Mark and our great leadership team to making sure we're picking the top choices for where our free cash flow and capital is going. And that's why you heard us speak about that even more today and more to the tradition of OpenText where our strengths are. But number one, capital allocation, number two, importantly, on the reframe guidance, and how we're simplifying and providing more clarity and more transparency going forward to help our investors and analysts understand the business,

understand where we're outperforming as we said, and understand we're going to continuously improve. And within all that, executing that guidance consistently, period.

And then three, I'd say, listening and simplifying. So I'll continue to listen, continue to work with our businesses, understand the business, but I will be listening and engaging as a top priority with our investor shareholders and teammates. So those three would be top early priorities.

Operator

Stephanie Price, CIBC.

Stephanie Price - *CIBC Capital Markets - Analyst*

Good morning. Maybe start off one with you, Chadwick. Just on the restructuring and the expanded scope. Press release noted annualized savings of about \$400 million starting in fiscal '26, just trying to understand if you expect these to be additive to current margins? Or should we think about a portion of the savings being reinvested back into the business?

And maybe just a little bit more in terms of where the restructuring will be done. It sounds like there's some technology work being done on the AI side.

Chadwick Westlake - *Open Text Corp - Executive Vice President, Chief Financial Officer*

Yes. Maybe I'll go first, but then Mark, I think should answer the second part of that question. What I would just say simply, we will provide more clarity in Q4 in terms of how that business optimization benefit will show up. You will see some of the costs that we noted incurred in Q4, all within our existing outlook, and then you'll see more of that clarity come again in Q4.

But for now, it's still a good compass on the kind of equal split between F '26 and F '27 for that benefit realization right across the board, though, right? This is -- and that headcount is a net number. So there's a gross impact, and there's a net reinvestment aspect, especially in the top products and countries of focus for centers of excellence. But I think Mark should take some of the AI first component, which is huge here.

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yes. Stephanie, thanks for the question. Thanks, Chadwick. Yeah. I mean the business optimization and our AI first strategy go hand-in-hand, Stephanie.

Our business optimization is transformative. And it's reflective of what we're building an AI operating model. So if you'll allow me, just talk a little bit about our AI-first strategy. Look, leadership is a choice, and we've decided to lead in AI.

We're building a great AI products in company. We're helping our customers transform and we're going to operate like an AI-centric company. And with -- and centering on this business optimization program.

So we've been moving very rapidly. We created the knowledge work over the last three decades with Titanium X. We've introduced 100 digital workers. With Aviator Studio coming out in the summer, we'll introduce a tool where customers can now create their own digital workers and thus now have tools built on our platform to create limitless digital workers, not just within our software, but across other software companies.

We've begun to partner with Microsoft in CoPilot, and building on their incredible success with our security offering. And we've now created an AI-first corporate operating plan with AI turned on for our employees. And as I said on the call, we're no longer to hire roles that could be done

with AI as part of our hiring skills learning and performance. And through that lens, right, we looked at expanding our business optimization plan, which is AI led, taking out up to \$400 million of new expense over the next two years.

We're focused on roles like the general knowledge worker, support, document generation, QA, entry-level program, administrative work, help desks, everything that can be accomplished through AI. And we had many wins in Q3. So the AI-first lens and building an operating model around AI first is really central to us and the expanded view of the business optimization.

Stephanie Price - *CIBC Capital Markets - Analyst*

Thanks for that. And maybe one more for me, just on the Customer Support side of the business. We calculated, I think, a 6.4% organic decline in that business in the quarter. And I know the DXC contract maybe impacted that a little bit. Could you just dig into what's going on in that Customer Support line? Thanks.

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Absolutely. So let me just start with, it is an amazing business. It remains a pillar of strength, and I'm confident that we're going to return Maintenance to growth in the future. As you were noting a bit, the Maintenance business here is primarily under pressure due to ITOM and ADM license performance, DXC, some FX and some goodness of customers transitioning to the cloud. But without DXC, our renewal rate for off-cloud would actually be moving up quarter-over-quarter, not down, if you take out DXC.

And that's going to be behind us as we enter fiscal '26. The core operating metrics, Stephanie, in the business are very positive. APA up, past due down, cancel rate down and quarter renewal rates up, the year-over-year decline in constant currency is cut in half again without DXC, cut in half in constant currency without DXC. So, in F '26, we're definitely going to improve the business, and the rate of decline is slowing. And when we get to our F '26 outlook in August, we will provide those specifics.

Operator

Thanos Moschopoulos, BMO Capital Markets.

Thanos Moschopoulos - *BMO Capital Markets - Analyst*

Good morning. Mark, could you perhaps expand on what you're doing within ITOM and ADM to work towards further stabilizing those businesses?

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yeah, absolutely. So thanks, Thanos. Let me throw Security in there first. We're on an incredible trajectory with Security. And we showed live last month from Europe our new threat detection and response platform, deeply integrated into Microsoft technology, including Copilot and we're going deeper in our integration.

So as Microsoft obviously continued to gain success in AI, just as we partner with SAP and their success, we're going to partner Microsoft and their success and bringing threat detection and response into their AI and into their installed base. So we are -- we got Security right on track where we want it to be.

In relation to ITOM, we're making really good progress. We are -- I always like to think that if you can run the platform at scale yourself, than everyone else should be -- should be able to. And we've just completed going live across discovery, observability, and service management.

So I believe we have ITOM on a very good trajectory. The product is there. Sales force expanded and trained. Titanium X in the market. The cloud offerings are there. New wins on SaaS.

We've also studied our biggest competitor extremely well, ServiceNow. And where we feel that we can differentiate and win on the service management side is in regulated industries. And that's, I don't know, \$10 billion part of the TAM. And so we're very happy to go after these very regulated industries that need content management, that need security, need process automation, and really go into our core strengths.

So I feel we have ITOM on a good trajectory, and it's going to contribute to our improved performance in fiscal '26. And ADM is going to take a couple more quarters. We have focused ADM on the top end of the market to really go after the top 1,000 software companies in the world. So every company is a software company today, but auto, financial services, insurance, biotech, the next generation of software companies as well.

So we've been -- that's going to take us another -- couple of quarters or so to get the ADM engine really performing at its best. But I love where we are in Security. We just -- we're in the right swim lane. Our stores are now in the pool with ITOM, given our deployment in Titanium X and consumers are approaching the pool on ADM to use a swimming lane analogy. So that's a quick insight into ITOM and ADM.

Thanos Moschopoulos - *BMO Capital Markets - Analyst*

I appreciate the color. And then just secondly, you have a meaningful government business. I'm just curious whether you're seeing any impact from the DOGE cuts?

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yeah. There's no doubt there's some impact from the US government expense reductions. And -- but it's not as significant as the tariffs, right? So there's in the normal world, we would just be absorbing this, but we are calling out a little bit. But it's really secondary to our message on tariffs.

And look, at the end of the day, the US government -- governments are a great partner of ours. We provide critical services and defense, intelligence and running critical citizen applications. But the effects have been de minimis, and we're still very optimistic on that business.

Operator

Samad Samana, Jefferies.

Samad Samana - *Jefferies - Analyst*

Hi, good morning. Thanks for taking my questions. And Chadwick, congrats on the new role. Maybe Mark, I'll kick off with you.

If we think about last year, we've seen deals getting longer going to maybe two to four years in terms of duration. And now you're calling out some (inaudible) what happened there. I would characterize if there had not been for tariff, would you say that the demand environment was better this year than last?

And maybe how are customers chatting before then to get a sense of what it could look like if this all goes away or if we had a pause, and then I have one follow-up.

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yeah, sounds great. Thanks, Samad. The -- look, the deal terms and ramping has stabilized.

So we're not seeing kind of a change of deals getting longer or more effects to ramping, if you will. That was sort of -- kind of a little bit of a -- it's stabilized. So there's no real changes there.

Well, customers are still spending. Clearly, I mean this is -- it was a shock when you put out 25% auto tariffs. And there were so -- and then it's a list of countries and companies paused. They had to assess the information. Some of the information was accurate. Some of it was marketing. Some of it was wrong, right?

So I know I paused on spending, right, until I could just understand the landscape. I also think there's a dynamic. As I highlighted in the script, we're a Canadian company, and we love all our markets. And in the non-US markets, if you will, customers are over their disappointment, I'm going to speak candidly, they're over their disappointment. They're over their disbelief and they are in full action mode to take control because they got businesses to run.

And I'm personally in dozens and dozens of conversations of how we can support our customers in France. (laughter) And not rely on US technology because they just don't know is coming next, right? And whether rational or irrational, based on prudent economic theory or not, they're going to take control because they got their priorities. So we're going to help our business in France, our customers in France, run and deploy France.

We're going to help our customers in Germany run and deploy in Germany. Same in the UK. Same in Canada. Same in Japan. Same in Australia. Same in South Korea. Same in Singapore. Same in India. All across the world. Well for US customers, run and deploy in the US as well.

So -- and I also think coupled with we got momentum in AI. So this is a very different scenario, if you want to make comparisons like COVID, right? This is a very different scenario for us. Customers are spending. They're going to spend differently locally.

I think this -- I hope that tariff thing rationalizes and normalize if it does, it's gained back on fully. And we're in a nice place being able to help customers deploy locally and create efficiency through the digital worker. So it feels different and positive difference actually for us.

Samad Samana - *Jefferies - Analyst*

Great. I appreciate that color. And then Chadwick, maybe just appreciate all (inaudible) days, and you're still early in executing the game plan. But if you think about the different components of capital management, what would you say are the higher RPU, (inaudible) where your folks purchase right? Is it on being more aggressive with the buyback?

Is it on some of the divestitures that you mentioned maybe tactically? How are (inaudible) where your early focus will be?

Chadwick Westlake - *Open Text Corp - Executive Vice President, Chief Financial Officer*

Thanks, Samad. I think we outlined that our flexibility is number one. And it's going to depend on the environment at the time and the opportunities at the time. So that's why it was so key in the last quarter, you saw some of the greatest opportunity for us was to continue to buy back and buy back a heavily discounted share price.

So we were doing that as smart aligned opportunities come up on the M&A front. Certainly, we're going to look at those tuck-ins going to come up. And same thing with -- as Mark indicated very clearly, more mature products or portfolios. If there's better opportunities to monetize those we'll take those as they come up.

But it's going to be that sequence. So we're going to continue to invest in the business as we are. We're going to reinvest in the business. We're going to focus on our innovation. We're going to pay that dividend, but then it's flexibly month by month, quarter-by-quarter as the opportunities are rolling for the other two. I don't know, Mark, if there's anything you want to add?

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

No, extremely well said. I mean, the -- our execution, our performance, and the addition of our transformative business authorization plan returns us back to capital flexibility. And these are the levers we've traditionally had when we've treated our highest multiples. And so we're excited to bring these levers back as we come into '26.

Operator

Richard Tse, Nashville Bank Financials.

Richard Tse - *National Bank Financial - Analyst*

Yes, thank you. So obviously, a big push here on AI. Just wondering if you may be able to provide some metrics just really to help us understand how that's being adopted by your base, like I don't know if you sort of have numbers on Aviator that you could share just kind of any growth metrics so we can kind of get a sense of that trajectory.

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yeah, thanks, Richard, and thanks for being with us, and thanks for being on the call. As I noted, leadership is a choice, and we've decided to lead in AI. And it's starting with building our AI products. It's having a 3,000-person professional service organization that everyone is trained on AI and helping transform our customers' AI. It's creating an operating model inside of OpenText that is AI-centric and a new model for us that the business optimization is kicking off.

And so I look at metrics around first adoption. Is adoption on the rise? Adoption is on the rise everywhere across what we're doing. Is our frequency of use up, right? Our frequency of use is skyrocketing internally. We only hire people that have AI skills now as part of our interviewing.

If you don't know AI skills, if you're not using them, if you don't know how to prompt, if you -- then we just disqualify you. We are training. We've turned tools on for all our employees. So frequency of use is up.

I think another measurement is reduction of expenses. And I think we couldn't be clear with our expanded Business Optimization plan that we're going to lead first, and then we're going to lead our 100,000 customers, that reduction of expense. Win rates are increasing for us of where we engage because of AI. If we look at the wins in the quarter that we have in our deck, Criteo, ABN, JTI were all AI-led in winning those.

Our partnerships are up with Microsoft. Just as we've had an amazing partnership with SAP, we have an incredible joint value proposition and product into their installed base, we're about to do the same, layering in on their incredible success in AI with our security. And then hopefully, instead of Gen Z will be Gen revenue as we lead into AI first.

So look, adoption, frequency, reduction of expense, win rates, new partnerships, that's how we're measuring right now. And as we get into '26, we can think about -- we'll keep talking about customer wins, booking rates, et cetera, Richard. But I think those are some of the metrics I've been looking at as this race goes on.

Richard Tse - *National Bank Financial - Analyst*

Okay. Great. So my second question, I don't know if this is for Chadwick or yourself. But as you make that shift, are you considering shifting the revenue model to more sort of usage or value-based pricing, similar to some of your competitors? And how should we expect if you do that, the relative impact would be to the current model?

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yeah. We're not looking at a disruptive pricing model -- excuse me, a disruptive change in how we commercially engage with our customers. We have a couple additional pieces to bring to market. Next quarter, we're bringing my Aviator to market, which is if you think on every screen you use today, you have a search button that our class.

You have what I call the hamburger those three lines, the menu called the hamburger. We're going to have a My Aviator button. It's a personal digital assistant that every user of OpenText software regardless of screen, regardless of BU, regardless of product, just like you have the hamburger, the search button -- the search glass, you'll have My Aviator. And we'll bring up a personal digital worker for you to be able to do rack style capabilities across one document across 100 documents. Complex cases, things you're working on, how do you collaborate.

We also have a very important new capability with Aviator studio where we're going to now allow our customers to create their limited digital workforce. That is a step function for us where they can create their own digital workers. And we're also going to be introducing conjunctive with that, what we call an Always on AI platform. Today, you have to go through some work to turn AI on. We will have it always on inside our SaaS and inside our private cloud.

So we're going to think through how to keep monetizing that. But I think it's too early to say, but I don't think we're going to do something radical and a move from you have to commit to just a consumptive model. But more to follow on that. It is going to really follow this very aggressive and impactful roadmap of My Aviator, Aviator Studio and Always on Aviator.

Operator

Paul Treiber, RBC Capital Markets.

Paul Treiber - *RBC Capital Markets - Analyst*

Thanks very much and good morning. Question on AI and then also the magnitude of the reductions that you're doing. So it does sound like you're seeing good usage and traction of AI internally, but how do you arrive at the magnitude of these headcount reductions? And did you contemplate a slower move and sort of dip your toe in the water as you make the transition more towards AI internally?

Mark Barrenechea - *Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer*

Yes, Paul, thanks for the question. We appreciate it. We've been at this for over a year. So -- and we're moving at just an incredible pace. So when we look across how Aviator has advanced.

Some of our partners AI tools have advanced like Microsoft, SAP and looking at totality of our usage, we've looked -- we can already see productivity gains in sales, presales, professional services, education, onboarding, general productivity and very specifically, and roles of customer support, documentation, QA, general administrative work and the general knowledge worker.

And so we've been doing a very deep analysis of what roles we can -- the work still needs to be done, it's just going to be done with a machine via AI. And this shows the totality, right? Look, I remember when ERP came into the market many years ago. As a leader in Oracle applications, really bringing ERP to market.

We took G&A expense in the ERP world from upper teens, right, to low - to mid- to high-single digit. That was a step function. This is a step function. AI is a step function and be able to reduce expense in companies over time.

And look, you can count if what percent of OpEx this is going to reduce for OpenText or other companies, but ERP was a step function of high teens to high single digit. AI is a step function of expense efficiency. So we're leading the way in doing it in our business optimization. And look, I think this if you'll allow me, Paul, I think this goes into how we're going to think about F '26 a little bit.

We're going to provide F '26 guidance in August. And maybe just a little bit, I won't go -- there's an F '26 question, I'm happy to answer it. Some of this will flow to the bottom line for sure. Some of this will be reinvested in the business. It will be reinvested back into AI, be reinvested in the sales. So let me just pause there, Paul. But I'm going to keep talking about this analogy of ERP as a step function in G&A expense. AI is the same.

Paul Treiber - RBC Capital Markets - Analyst

Second question, just for Chadwick, one of the metrics that you're considering giving guidance on is going forward is EPS. The -- which is a metric that the company hasn't guided for in the past. Can you just elaborate on the philosophy around EPS as a metric that you guide for?

Mark Barrenechea - Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer

Sure. Well, I think we are strong, very strong and distinctly strong and growing profitably. And at the end of the day, how does that translate to your earnings per share, which is very consistent no matter what company no matter what sector. And that shows also the benefits of when we're deploying our capital strategically, and also repurchase shares, right? How are we deploying every dollar capital period, EPS is a bottom-line strength period.

So I think it is valuable to show that and have some expectations. And frankly, at the level we're growing, I don't think we're getting credit for it compared to many businesses in many sectors. So it's just a good, consistent guidepost from my perspective.

Operator

Kevin Krishnaratne, Scotiabank.

Kevin Krishnaratne - Scotiabank GBM - Analyst

I do have a question on guidance. I know we're going to get more detail in August. But on one of your slides, and I think you talked about in the script, an expectation of a return to organic growth in '26. Can you just -- what gives you the sort of the confidence there? I know you've got the RPO, maybe some of the drivers to get there?

And then the second thing you point out is striving for a milestone of \$1 billion in free cash flow. So is the expectation that you'll do the \$1 billion plus in '26. I'm just trying to think about some of the puts and takes there with restructurings and just a shift in the business.

Mark Barrenechea - Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer

Thanks, Kevin. Thanks for the question. Look, as you started, we will provide our F '26 guidance in August. But with that said, F '26 is a very different year than F '25. I couldn't be happier that the phrase ex AMC is done.

And with F '26, it's about AI first. And we have some very positive levers coming into F '26. Product cycle, transformative business optimization plan, which is going to allow flexibility continued flexibility and strength and our capital model for new AI investments. The business optimization, look, somewhat dropped to the bottom line, some will be reinvested in the business, but it's going to return us to this capital flexibility, but expect some positives, right? When we talk about F '26 in August, we will have improved growth rates year-over-year. We will have improved maintenance year-over-year. We expect to have higher free cash flows. And we'll talk about all the dials that get us there when we get into '26.

As Chadwick mentioned, we'll continue to have strong capital return in our buyback and our dividend program. This flexibility is going to allow us to return to programmatic M&A. And we are, as we've noted, going to consider divestitures of more mature offerings that will create a greater return and/or increase our growth rate or both. And these are the levers we've traditionally had when we traded at our highest multiples, and we expect to have these levers back in 2016. So it's a very different year. AI first. And we want to finish out the year.

And we -- as we traditionally do when we get our August call, we'll outline what F '26 look like, but expect it to be very different.

Kevin Krishnaratne - Scotiabank GBM - Analyst

Got it. Appreciate that. One final one then. We talked about the enterprise booking softness, but about 10% of revenue basis SMB. So I'm wondering what the trends are looking like there?

That's a sensitive part of the business when there's uncertainty. So just curious what happened there.

Mark Barrenechea - Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer

Absolutely. As I said on the call, we had given the sudden shock to the system of tariffs, 25% auto tariffs and then rolling tariffs. We did have a bookings impact in Q3 as we noted. And we're unlikely to get to our aspirations of our targets of 20% plus but we are looking to be in mid-teens growth for the year, which means a strong Q4. So we actually have strong visibility into the bookings, Todd and Paul in the field are executing to the deals in front of us.

I think the news on the week of maybe lightening some auto tariffs is helpful. But it still remains a little unpredictable. And so we're still at the -- it's still volatile, but we think we're going to execute well in the volatility.

Operator

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

Mark Barrenechea - Open Text Corp - Chief Executive Officer, Vice Chairman of the Board, Chief Technology Officer

All right. Well, thank you, everyone. Chadwick, welcome, and thank you, everyone, for joining us today. We have just three things I'd end with. It's a whole new narrative for us with AI first, and everything from product initiatives through building and operating model centered on AI.

We're very excited about F '26 and all the positive levers that are in front of us. And we look forward to very strong direct in candidate engagement in the quarter. As Greg noted, we'll -- Chadwick and the team and myself will be out in the field, spending time with you, and we look forward to hearing your voice. Thanks for joining 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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