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EDITED TRANSCRIPT

OTC.TO - Q2 2015 OpenText Corp Earnings Call

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OVERVIEW:

Co. reported 2Q15 total revenue of \$467.8m, GAAP net income attributable to Co. of \$74.3m or \$0.60 per diluted share.



CORPORATE PARTICIPANTS

Greg Secord *OpenText Corporation - VP IR*

John Doolittle *OpenText Corp - CFO*

Mark Barrenechea *OpenText Corp - President & CEO*

CONFERENCE CALL PARTICIPANTS

Kris Thompson *National Bank Financial - Analyst*

Richard Tse *Cormark Securities - Analyst*

Thanos Moschopoulos *BMO Capital Markets - Analyst*

Scott Penner *TD Securities - Analyst*

Phillip Huang *Barclays Capital - Analyst*

Paul Steep *Scotiabank - Analyst*

Kyle Chen *Credit Suisse - Analyst*

Paul Treiber *RBC Capital Markets - Analyst*

Stephanie Price *CIBC World Markets - Analyst*

PRESENTATION

Operator

Welcome to the Open Text Corporations second quarter 2015 financial results conference call.

(Operator Instructions)

The conference is being recorded.

(Operator Instructions)

At this time, I would like to turn the conference over to Greg Secord, Vice President Investor Relations. Please go ahead.

Greg Secord - *OpenText Corporation - VP IR*

Thank you, operator, and good afternoon, everybody. I'd like to start the call with the reading of our Safe Harbor statement.

Please note that during the course of this conference call, we may make statements relating to the future performance of OpenText that contain forward-looking information. While these forward-looking statements represent our current judgment, actual results could differ materially from a conclusions forecast or projection in the forward-looking information and statements made today. Certain material factors and assumptions were applied in drawing any such conclusion while making a forecast or projection as reflected in the forward-looking information.



Additional information about the material factors that could cause actual results to differ materially from a conclusion forecast or projection in the forward-looking information. And the material factors or assumptions that were applied in drawing a conclusion while making a forecast or projection as reflected in the forward-looking information. As well as the risk factors that may project the future performance results of OpenText, are contained in OpenText's forms 10-K and 10-Q as well as in our press release which was distributed earlier this afternoon. Each of 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 will include a discussion of certain non-GAAP financial measures. Reconciliations of all non-GAAP financial measures to their most directly comparable GAAP measures have been included in today's press release, which will be found on our website. And with that, I'd like to welcome everybody to the call. With me today is OpenText's President and CEO, Mark J. Barrenechea, as well as our Chief Financial Officer, John Doolittle. As with our previous calls, we'll read prepared remarks followed by a question-and-answer session and the call will last approximately one hour. With a replay available shortly thereafter.

I'd also like to direct investors to the Investor Relations section of our website where we've posted an updated PowerPoint that will be referred to during this call, as well as a summary table which highlights OpenText's historicals trend and financial metrics. And with that, I'll hand the call over to John.

John Doolittle - OpenText Corp - CFO

Greg, thank you very much. First of all, I want to welcome everybody to the call. Thank you very much for joining. This is my second OpenText earnings call, and I'm now nearing five exciting months with the Company.

Turning to the financial results for the second quarter. As a headline, I'm pleased with our focus on cash flow generation, expense management and bottom-line performance in the quarter in spite of the headwinds in the currency markets. Total revenue for the quarter was \$467.8 million, and was up 29% compared to \$363.5 million for the same period last year.

And recurring revenue, which we define as cloud services, customer support and professional services for the quarter, was \$392 million, up 39% year-over-year compared to \$282.3 million for the same period last year. Regionally, the Americas contributed 54%, EMEA 36%, and Asia Pac 10%.

Foreign exchange volatility had an impact on our revenues this quarter in our overall results compared to rates from the second quarter of FY14. Our revenues were negatively impacted by \$15 million, primarily due to the weakness in the euro. Cloud services revenue for the quarter was \$151.3 million, up 259% compared to \$42.1 million in the same period last year. The increase is primarily due to the inclusion of GXS.

Cloud services gross margins remained stable at approximately 62% compared to the same period last year. Customer support revenue for the quarter was \$179.5 million, up 2.9% compared to \$174.4 million in the same period last year. Customers, or gross margins, remained relatively stable at approximately 87% compared to the same period last year.

Professional service revenue for the quarter was \$61.3 million, and was down 6.8% in the quarter. Compared to \$65.8 million in the same period last year, a significant component of the revenue decline is due to the foreign exchange volatility. The professional services gross margin was 24% in the current quarter versus 22% in the same period last year, and the improved margins were primarily due to lower labor related expenses and a reduction in the use of subcontractors.



On the license revenue for the quarter was \$75.8 million, it was down 7% compared to \$81.2 million reported for the same period last year. The decrease in license revenue is primarily due to the negative impact of foreign exchange, and slower than expected growth from developing markets.

License revenue broken down by industry sector is as follows. 20% from services, 20% from financial services, 14% from technology, 11% from public sector, 8% from basic materials and conglomerates, 8% from healthcare, 7% from consumer goods, 7% from utilities and 5% from industrial goods.

Our gross margin for the quarter before amortization of acquired technology and stock compensation was 72.2%, compared to 74% in the same period last year. The change in gross margin is primarily due to a shift in the revenue mix.

Our pretax adjusted operating income before interest expense and stock compensation was \$153.3 million or 32.8% this quarter. Up 36% compared to \$112.3 million in the second quarter of last year.

Our adjusted net income increased 26% to \$118.8 million this quarter, up from \$94 million in the second quarter of last year. Adjusted earnings-per-share was \$0.97 on a diluted basis, compared to \$0.79 for the same period last year up 23%.

The year-over-year effect of foreign currency movement on our adjusted earnings-per-share for the second quarter was negative \$0.03 and negative \$0.04. Versus rates that were in effect at the beginning of the fiscal year. There is a reason to expect this trend to continue or worsen based upon the ongoing strength of the US dollar.

The adjusted tax rate for the quarter and the year remains at 18%, up 4% year-over-year. And on a GAAP basis, income from operations before interest and taxes for the second quarter was \$110.6 million, up 49.6% from \$73.9 million in the second quarter of last year. Our GAAP income before taxes was \$92.8 million in the current quarter, versus \$70.2 million in the same period last year.

Net income attributable to OpenText for the second quarter in accordance with GAAP was \$74.3 million or \$0.60 a share on a diluted basis. Compared to \$53.5 million or \$0.45 a share on a diluted basis last year.

Our operating cash flow for the quarter was approximately \$109 million, an increase of 80% compared to \$60.9 million in the same period last year. Excluding the impact of special charges, operating cash flow for the quarter was approximately \$115 million, compared to \$69 million in the same period last year.

A few comments on our capital structure. There were approximately 123 million shares outstanding on a fully diluted basis for the second quarter FY15. On January 15, 2015, we issued \$800 million of bonds with a 5.625% coupon, and an 8-year maturity. And concurrent with that transaction, we used the proceeds from the bonds to repay in full our term loan A balance of \$492 million. This was the first high-yield bond offering from OpenText, and it provides us a stronger more flexible balance sheet as well as a better mix of fixed and floating debt exposure. It was a very strong debut for us in the high yield markets.

In return for all the positives that I mentioned, our cash interest expense will increase by approximately \$8 million per quarter pre-tax compared to current floating rates. Additionally, we increased the limit on our revolver from \$100 million to \$300 million, and we extended the tenor to 5 years.

On the balance sheet, customer support deferred revenues were \$310.2 million compared to \$349.9 million at June 30, and \$259.8 million at December 31. The decrease in deferred revenues this quarter compared to our last fiscal year end is due to the normal cyclicity of our business. As typically our deferred maintenance revenues are at the lowest point at the end of any calendar year.



Our accounts receivable, \$258.2 million at December 31, compared to \$292 million at June 30, and \$173 million at December 31. Our days sales were 50 at December 31, 2014 compared to 53 in June, and 43 last December.

At the end of December, we had 8,000 employees. That's consistent with the prior quarter: 1,900 in R&D, 2,000 in cloud services, 700 in customer support, 1,000 in professional services, 1,400 in sales marketing, and 1,000 in G&A. Our target operating model remains unchanged, and is posted in the updated Investor PowerPoint deck, which can be found in the Investor Relations section of our website.

And finally on January 26, the Board declared a cash dividend of \$0.1725 per share for shareholders of record on February 26, 2015. Payable on March 19, 2015.

With that, I'd like to turn it over to Mark. Sir, over to you.

Mark Barrenechea - *OpenText Corp - President & CEO*

Very good, thank you, John. And welcome, everyone, to our FY15 Q2 earnings call.

It's been a very fast start to the calendar year for OpenText, with the closing of two acquisitions, Informative Graphics and Actuate. Our inaugural bond offering, which strengthens the balance sheet, as John noted, as well as the introductions of many key product and service initiatives announced at Enterprise World in November. Most notably, those related to the OpenText Cloud.

The closing of Actuate is a significant milestone for the Company, for it allows us to bring analytics everywhere within the OpenText ecosystem. To our on-premise install base, our OpenText cloud customers, and to the broader developer community.

We are entering the age of digital, and digital processes, digital content, and a mindset of digital. Digitalization is key for all industries to deliver the next level of competitiveness and efficiencies. 15 years ago, you could be Amazoned, today you could be Ubered, which is a reflection of digitalization.

OpenText is well positioned, as our vision is a digital first world. And our key platforms allow customers to begin digitalization other enterprise processes today, such as the customer journey, supply chains, risk and governance, innovation and employee functions. EIM, our business network, the OpenText cloud, and now analytics are key technology enablers to help enterprises transform into digital enterprises, and if you will, raise their digital quotient.

I'm very excited about what 2015 will bring to our customers and to OpenText. Let me transition and spend a moment on our Q2 results, and start at the highest of levels.

On a year-over-year basis, total revenues were \$468 million, up 29%. Our quarterly recurring revenues were \$392 million or 84% of total revenues, and up 39%. Cloud services revenues were \$151 million, up 259%, including sequential growth. The majority of the growth is driven by our GXS acquisition.

Licenses were \$76 million, down 7%. Adjusted net income up 26%. Operating cash flow up 80%. Our adjusted operating margin was 32.8%, and our adjusted EPS was up 23%.

I am pleased with our top line results, up 29%. Our relentless focus on growing our cash flows, up 80%. And a business that is getting more efficient and delivered 32.8% adjusted operating margin.



Year-to-date, in constant currency, we are tracking to our business plan. Customer support was 39% of our business, Cloud services was 32%, license 16% and professional services 13%. As for total revenues by geography, the Americas was 54%, EMEA was 36%, and APJ 10%.

As for licenses our ECM, CEM and BPM businesses performed well. We had lower than planned performance in our developing markets, such as [fifth] and central Europe, Middle East, Africa Latin America, China and India.

Last quarter, I commented on some global macro issues that were creating a change in customer buying behaviors. Our license business was most affected by currency, and our emerging market's performance. Within the quarter, we closed 15 deals over \$1 million, nine on premises, and six in the cloud.

Financials, services and technology sectors saw double-digit demand. Cloud customers in the quarter included Schneider Electric, Coca-Cola, Lincoln Financials, Mars, and Nestle. On premises customers in the quarter included DB Shenker, IAG, Singapore Power, IGATE and Fox Entertainment.

OpenText Core is now GA and available, and I invite you to go to core.opentext.com where you can sign up and try it on your own. Core is our enterprise-based SaaS offering for ECM that complements our EIM offerings.

Our focus is on enterprise workloads. In the first two weeks, we added 10,000 new registrants and had 50,000 files uploaded. Enterprise customers can now enjoy consumer like benefits, but purpose built for the enterprise.

I need to spend a little more time on the OpenText Cloud. Over the last three fiscal years, we have transitioned our business from zero cloud services revenues to a hybrid model. Where in FY15, our target model cloud services is 28% to 33% of revenues.

Over this three year period of time, we have made this transition while expanding our adjusted operating margin from roughly 27% in FY12, to 33.5% FY15 year to date. We've also near doubled our cash flows over the same transition period.

Let me highlight some of the core OpenText Cloud facts. A third of our revenues are now from the cloud. We have a marquee customer list that includes many of the top Fortune 5000 customers, and the world's leading supply chain companies.

We are approaching 20 billion annual transactions in our cloud. We run 25 core data centers worldwide, with approximately 1,500 production racks and 150,000 square feet of raised floor space. 900 managed service customers, 60,000 cloud customers, 600,000 trading grid partners, and near 2,000 dedicated staff.

This is a very serious cloud effort, and we are operating one of the world's largest cloud infrastructures. We have been at the license business for 20 years, and have optimized the mechanics of that business as reflected by our gross margin for example on license.

We have been at the cloud business for three years. And we are delivering gross margins already in the low 60%s, and we already operate a very profitable cloud. Just as we have optimized the mechanics of license, we expect to optimize mechanics of the cloud.

As I talked about at Enterprise World, we want to be better aligned to help customers consume software and services in today's market. And that hybrid means choice and flexibility. That stronger alignment is about offering a choice between purchasing a license, a subscription, managed services, or even shared SaaS.

As we kick off calendar 2015, the organization has launched cloud subscription, managed cloud services for all major products and OpenText Core. And we now turn our attention to driving adoption.



Our sales reps are now paid equally on a license, as they are on what we call MCV, or Minimum Contract Value. MCV is a guaranteed multi-year agreement for subscription or managed services. Our sales force is now equally incented and motivated to sell a license or MCV.

Customer consumption may move between revenue lines, and that is fine with us. We are focused on winning the lifetime value of that customer, on growing recurring revenue, and on expanding margin and cash flows. And we have a successful demonstrated history of doing this over the last few years in our cloud transition.

Let me briefly touch base on OTIGS. I look at the OpenText intelligent growth system as a methodology that leads with and produces value. Over the last seven years, we have achieved a 15.4% revenue CAGR through a combination of yearly organic and acquired growth, and in most years acquired growth being a larger revenue contributor than organic growth.

We continue with this model of a combination of organic and acquired growth. In any given year, our performance can of course vary based on the economy, availability of assets at the right price, and of course our own execution. But in the long term, should balance appropriately to a reasonable CAGR. We make investments in organic growth prudently, and we look for value in our acquisitions.

Let me turn to our other big topic for the call and that is analytics. OpenText acquired Actuate, a leader in embedded analytics, to complement its existing information management and B2B integration offerings. OpenText customers using virtually any OpenText product will be able to add analytics to their existing deployments, and OpenText will leverage Actuate IP to offer a new breed of analytics that will provide insight across entire information flows.

The acquisition of Actuate strengthens OpenText's leadership in enterprise information management by adding powerful data analytics for structured, semi-structured and unstructured data. The capability to analyze the data, together with a compelling visualization experience will allow enterprises to gain deeper insight, greater brand experience and better efficiencies.

We closed Actuate on January 16, just 11 days ago. The enterprise value upon closing was approximately \$272 million, or roughly 2.5 times trailing 12 month revenues, or roughly 4 times trailing 12 month maintenance revenues. We expect the transaction to be slightly accretive to adjusted earnings in this fiscal year, and then fully on our operating model by the end of FY16.

Actuate is headquartered in San Mateo, California, and we plan on consolidating all our Silicon Valley operations into the San Mateo facility. Upon closing, Actuate had approximately 500 employees, with roughly 72% of the revenues in North America and 28% rest of world.

Actuate revenues were declining at the time of acquisition, given their business model shift from licensed to the cloud. Consistent with previous acquisitions, we could see revenues decline 10% to 20%. We look to stabilize this decline, and then grow the business over time.

Further, we have also immediately aligned Actuate to the OpenText business model of allowing a customer to consume the way they want to via a license or subscription or managed services.

Actuate's goal is to be the leader in delivering personalized analytics and insights by increasing the richness, attractivity and effectiveness of enterprise information. Actuate is focused on big data analytics for powerful easy-to-use predictive businesses. They're also focused on embedded analytics, delivering built-in analytic capabilities for data-driven applications.

Some of Actuate's more key customers include the Royal Air Force, NAFCO, HSBC, Scotia Bank, Johnson Controls, CGI, Lufthansa and Shell. Some of Actuate's more key embedded Partners include NetApp, Cisco, NCR, [T] Systems, Dell and GE Healthcare.



There's a solid opportunity in driving further adoption of embedded analytics, as our customers asked for easy-to-use and easy to understand analytics. Organizations require intelligence from their data.

Finally, the value of the brick developer community cannot be overlooked. There are 3.5 million BIRT developers globally, and this will help us expand our overall focus on the development community.

Actuate has been focused on analytics for 20 years. They are a leader in the force to wave. I see three large technology platforms: data store, statistics, and visualization. Actuate comes with all three. Back data store, easy-to-use statistical algorithms, visual data mining GUI, high-speed columnar database, business friendly interface and a large statistical library.

Let me summarize the OpenText opportunity with Actuate. Greater EMEA and APJ distribution. With only 28% of their business outside of North America, we have an opportunity to increase their non-North American distribution.

Continue with embedded analytics and attract more partners. Integrate Actuate with our EIM suites, and offer analytics to the EIM install base. We have always been a source for big data, we can now deliver predictive intelligence.

Integrate Actuate in our information exchange business network, and offer analytics across our business network and the trading grid. And lastly, access to 3.5 million BIRT developers globally. The opportunity is far and wide with Actuate, and I'm delighted to welcome the company, customers and employees to OpenText.

In addition to Actuate, we also closed Informative Graphics on July 5. Informative Graphics has been a longtime Partner of OpenText. Delivering three products: Brava, Redact-It and Blazin'. Brava allows customers to view, annotate, redact, and publish renditions of any file.

Redact-It allows customers to find and redact proprietary and sensitive content from a document. And Blazin' automates the document transformation process to create renditions according to predefined business rules.

The Informative Graphics products are pre-integrated for EIM suites. To from a financial perspective, we look at the acquisition more as a technology purchase to reduce our cost of sale. Some of Information Graphics' key customers include the US EPA, [Byer], Genentech, McKesson, Samsung, CSC, Xerox and Chevron.

In summary, it's been a fast start to calendar year 2015 for OpenText with the closing of two acquisitions, Informative Graphics and Actuate. Our inaugural bond offering, as we strengthen the balance sheet, as well as many key product and service initiatives coming out of Enterprise World. Most notably, those in the OpenText cloud.

The closing of Actuate is significant for us. For it allows us to bring analytics everywhere within the OpenText install base, cloud, and the developer community. OpenText could not be better positioned, as our vision is a digital first world.

And our key platforms allow customers to begin digitalization of their enterprise processes today. Such as the customer journey supply chains, risk and governance, innovation, and employee function. PIM, our business network, the OpenText Cloud, and now analytics are key technology enablers to help enterprises transform into a digital enterprise, and if you will, raise their digital quotient.

We have demonstrated we can expand margins and cash flows, as we onboard more Cloud services revenues and are occurring revenue is now over 80%. I'm pleased with our Q2 performance and year-to-date, in constant currency, we're on track to our business plan.

With that, I'd like to open the call to your questions.



QUESTION AND ANSWER

Operator

Thank you.

(Operator Instructions)

Kris Thompson, National Bank Financial.

Kris Thompson - National Bank Financial - Analyst

Great, thanks. Mark, I'd just like to talk about the Actuate deal for a couple of minutes here. I believe they're discontinuing their perpetual offering, and I think I heard you say you're going to reintroduce that?

Mark Barrenechea - OpenText Corp - President & CEO

That is correct. So, we've already, if you will, aligned them to the OpenText model where we'll allow customers to consume via a license, a subscription, or via our managed services.

Kris Thompson - National Bank Financial - Analyst

Okay. And can you give us a little bit of color on how you plan on integrating their sales team with your guys?

Mark Barrenechea - OpenText Corp - President & CEO

We're going to keep them as a standalone organization as we come out of the gate. We see them as a strong shared services team to both deliver on, if you will, their own business plan as well as adoption across our EIM suites. So we're going to keep them as a unified sales force reporting up into John Hunter, and let them have at it.

Kris Thompson - National Bank Financial - Analyst

Okay. And what about channel conflict? Do you think there's any conflict there with some of your key Partners, SAP and Microsoft, for instance?

Mark Barrenechea - OpenText Corp - President & CEO

No, not at all. We've heard no conflicts at all. So it's been a relatively good reaction, so we haven't heard any conflicts.

Kris Thompson - National Bank Financial - Analyst

Okay. Just last one, maybe John or Mark, you said that you expect it to be accretive, slightly accretive in 2015. Is that before or after the higher interest expenses associated with the new debt?



John Doolittle - OpenText Corp - CFO

No, Mark was talking specifically about Actuate when he made that comment, Kris.

Kris Thompson - National Bank Financial - Analyst

Okay. So you're not attaching that to this deal.

John Doolittle - OpenText Corp - CFO

No, not at all. No.

Kris Thompson - National Bank Financial - Analyst

Got it. Okay. Thanks, guys. Appreciate it.

Mark Barrenechea - OpenText Corp - President & CEO

Yes, thanks, Kris.

Operator

Richard Tse, Cormark Securities.

Richard Tse - Cormark Securities - Analyst

Yes, thanks. Mark, could you I guess give us a gauge on the size of the potential opportunity for Actuate in your install base? I'm sure you guys have done some kind of rough math on that. Just to give us an impression of what that could be?

Mark Barrenechea - OpenText Corp - President & CEO

Richard, without associating a number with it, let me just speak conceptually about it. We've come a long way as a business, without providing a modern analytics package to our customers. We haven't had a reseller agreement with other packages in the market.

RKT was sort of a reporting package to work in a specifically inside certain compartments of ECM. And that's why I'm excited about the opportunity, because we haven't gone to market with a formal analytics package.

We like what Actuate does on its own for embedded analytics, as well as their developer community. But driving adoption, integration into our suites, and then adoption for ECM, CEM, BPM we think is powerful.



As you know in our acquisitions, we tend not to bake in revenue synergies. There are unexpected upsides for us. But we've never gone to market with an analytics package, and that's why I'm pretty excited about Actuate.

Richard Tse - Cormark Securities - Analyst

Okay. And then just switching gears a little bit, you guys are offering quite a spectrum of pricing models right now. Can you give us an impression of which model you found the most popular among your existing and prospective customers?

Mark Barrenechea - OpenText Corp - President & CEO

Well consumption models, I'll call them consumption models. Look, we're just coming out of the gate. We announced at Enterprise World that we would be basically taking the GXS managed services, and offering that globally within our core EIM suites.

Now, we kicked that off in early January. We talked about subscription at Enterprise World. We'll kick that off early January. And we talked about OpenText Core, and that's now gone GA here over the last couple of weeks. So we're really just kicking off the calendar year by offering that full spectrum of consumption models.

Now I'll provide a little bit of color, we had a couple customers who went to this model early for us last quarter, City of Madrid, New Zealand Ministry of the Environment. Where historically, they may have been a licensed customer, they decided to consume via a subscription because it matched up best with their budgets and how best they wanted to consume. But I think it's a little early to tell.

Richard Tse - Cormark Securities - Analyst

Okay, fair enough. And this is an odd question, but I haven't seen any data out there on this patent infringement case against Box. I think that they overturned one of 400 or 500 cases you guys had within that broad case. What's the status of that right now?

Mark Barrenechea - OpenText Corp - President & CEO

We go to trial next week.

Richard Tse - Cormark Securities - Analyst

Okay. All right. Looking forward to hearing the outcome of that. Thanks, guys.

Mark Barrenechea - OpenText Corp - President & CEO

Yes. Thanks, Richard.

Operator



Thanos Moschopoulos, BMO Capital Markets.

Thanos Moschopoulos - BMO Capital Markets - Analyst

Mark, just going back to the licenses. Should our takeaway be that the more developed markets performed more or less in line with your expectations, or was there any weakness there?

Mark Barrenechea - OpenText Corp - President & CEO

No, Thanos, our license business was really primarily affected by currency and our developing markets. If we go back and look at all throughout the data point here, if we go back you look at our trailing 12 month organic license rate now, it's dropped to 6%. My last quarter it was 11% to 12%.

Now all in, it would be 8%. But the in quarter performance is the two things that affected it the most was currency and our emerging market performance. And our organic growth rate now over the trailing 12 months is 6%, and all in 8%.

Thanos Moschopoulos - BMO Capital Markets - Analyst

And just to be clear, those are currency, constant currency numbers, or no?

Mark Barrenechea - OpenText Corp - President & CEO

No. Those are just straight up numbers. And in concert currency, they would be higher.

Thanos Moschopoulos - BMO Capital Markets - Analyst

Okay. And should we think about that developing market weakness persisting into the current quarter, or is it too early to tell at this stage?

Mark Barrenechea - OpenText Corp - President & CEO

I think it's too early to tell. We took a position a couple quarters ago on the economy, where we felt it was prudent to be cautious on investments. And maybe unfortunately, we were right in what we were seeing.

If anything, it's turned a little more volatile with outside of the US. The US is strong, the US currency is strong. But outside of the US with FX, volatility, price of oil volatility, deflation worries in EMEA, I think we were wise to take our cautious position. And that cautious position remains.

Thanos Moschopoulos - BMO Capital Markets - Analyst



Okay. And then just one last one for John, are maintenance renewals still tracking in the low 90% range, or has there been any change there?

John Doolittle - *OpenText Corp - CFO*

No change, low 90%*s*. Same as the last quarter.

Thanos Moschopoulos - *BMO Capital Markets - Analyst*

Great. Thanks a lot, guys. I'll pass the line.

Mark Barrenechea - *OpenText Corp - President & CEO*

Thanks, Thanos.

Operator

Scott Penner, TD Securities.

Scott Penner - *TD Securities - Analyst*

Thanks. Just first of all, Mark, what has been the feedback on the Core products since you guys unveiled at Enterprise World? And do you think the use case sets up the product against Box or Dropbox?

Mark Barrenechea - *OpenText Corp - President & CEO*

Well, I wouldn't say against Dropbox. But look, the first two weeks of unabated uncontrolled access, if you will, you can -- core.opentext.com. The world can go sign up and use it, has been very favorable.

This is asset we built from the ground up. We took all our ECM and enterprise experiences and created a new platform. We're going to add more applications to it over time, and the first two weeks have been positive.

Scott Penner - *TD Securities - Analyst*

And with the upcoming release of SP1, I think given your geographical comments, the answer to this is no. But did you see that having any real impact on license revenue or customer renewals?

Mark Barrenechea - *OpenText Corp - President & CEO*

No.



Scott Penner - TD Securities - Analyst

Okay. Richard asked a good question about the -- and you made a good answer about a couple customers that went early to subscription instead of licensed revenue. Were those sizable deals?

Mark Barrenechea - OpenText Corp - President & CEO

One of them was greater than \$1 million.

Scott Penner - TD Securities - Analyst

Okay. One last question for John, and just what is -- what's going on if you could flush out the special charges? It looked like there was a reversal this quarter. And then following on that, have you guys formulated the plan for charters related to Actuate?

John Doolittle - OpenText Corp - CFO

So the answer to the second part of the question is, no, we haven't. We're working on that, Scott. So nothing to announce there as yet.

There was a reversal of a sales tax liability that was set up on a previous acquisition, and we had some favorable news in a couple of jurisdictions in the US. And so there was a reversal of an accrual that had been previously set up, and that came through special charges. So that's why you're seeing the credit.

Scott Penner - TD Securities - Analyst

Excluding Actuate, should we expect any additional charges for the next couple of quarters?

John Doolittle - OpenText Corp - CFO

I think we've got about \$5 million-ish dollars left on GXS. So we're expecting to finish up our GXS integration over the next couple of quarters, so you may see a bit come through on GXS.

Scott Penner - TD Securities - Analyst

Okay. Appreciate it. Thank you.

John Doolittle - OpenText Corp - CFO

Yes.



Operator

Phillip Huang, Barclays Capital.

Phillip Huang - Barclays Capital - Analyst

Thanks. Good afternoon. Question on the installed base's upgrade to red oxygen. I was wondering what improvements have you seen on cross-selling?

Deal size seems like it's continuing to grow. I think it's up 5% year over year this quarter. I was wondering if you can see that growth accelerate from here with SP1 and launch?

Mark Barrenechea - OpenText Corp - President & CEO

Yes, Phillip, thanks for the question. Yes, year-over-year, the deal size up I think [\$272 million] to [\$289 million]. So that's a good indicator.

We don't have any additional metrics we're going to put out today. We're looking towards SP1 to be that next wave for us before blue carbon. So we're happy with the average deal size increasing year-over-year, and we'll get more data out there when we bring SP1 fully to market.

Phillip Huang - Barclays Capital - Analyst

Got it. And how quickly will your customers be able to see added functionality from Actuate on the new integrated platform?

Mark Barrenechea - OpenText Corp - President & CEO

We've already released -- we were working in parallel with some of the open source versions of bricked. And conjunctive with the close, we've offered some integration packs day one.

Phillip Huang - Barclays Capital - Analyst

I see. Got it. And then switching gears to the more like the macro environment for a second. Can you maybe talk a little bit about the sales cycles under the current environment?

Are you seeing any improved visibility since the last quarter, or has it remained relatively lower than normal? And if so, how's the sales team matching through this phase of lower visibility?

Mark Barrenechea - OpenText Corp - President & CEO

I wouldn't say we have any lower visibility. In fact, I'd say our visibility is reasonably good actually as we come into the year. Our new CMO, Adam, is pipeline oriented and very focused on driving pipeline globally. I



talked a little earlier about -- we thought it was prudent to take the conservative financial position given FX deflation worries, price of oil.

I see a strong a sense of commitment and morale around having our sales reps being equally incented, whether it's a license or it's MCV. And that's been a strong motivator for the sales force.

We require a multi-year agreement. These are guaranteed agreements. GXS has operated this way for almost near a decade. We learned -- we took some of the best things from GXS and EasyLink and some of the things from industry, and put our own program in place.

But the motivator -- and I think if the economy remains cautious just like we saw in [United Barcelona] Madrid rather, as well as the New Zealand Ministry. Subscription can be an easier path to come on board as a new customer, maybe perhaps as a license.

Phillip Huang - Barclays Capital - Analyst

Got it. And then final one for me, if my calculation is correct, you're roughly 1/9 through your acquisition target of \$3 billion in the five years. Can you maybe give us an update on how much liquidity you currently have to pull in acquisitions, and also your view on the current environment for accretive opportunities? And whether you see good opportunities for tuck-ins or more maybe platform size deals? Thanks.

John Doolittle - OpenText Corp - CFO

So, Philip, really a two-part question there. One is liquidity, which I'll take, and then Mark will take the pipeline. So we finished the quarter with \$543 million of cash.

As we said, we went to market on the bond deal, we were very successful with that. We upsized our revolver from \$100 million to \$300 million. So overall, our liquidity -- and combined with that, we generate cash every month, every quarter. So our liquidity position has never been stronger. Mark, do you want to talk about the pipeline?

Mark Barrenechea - OpenText Corp - President & CEO

Yes, sure thing. So look, Informative Graphics and Actuate, in my prepared remarks I talked in the script. But we continue to be active in working our pipeline within corporate development. So we'll continue to work our pipeline and the Corp Dev is 100% at work.

Phillip Huang - Barclays Capital - Analyst

Got it. And then just to clarify, a question for John. So, based on that calculation, is it roughly like just over \$1 billion dollars in terms of liquidity for deploy -- available for acquisitions currently?

John Doolittle - OpenText Corp - CFO



Well, that's a point in time reflection, Philip. So I'm looking at it -- how much cash do we have on the balance sheet at the moment? So we finished the year at \$542 million. Of course we paid for Actuate, then we had another \$300 million come on from the bond deal.

So we're about flat there. We've got an incremental \$200 million liquidity from the revolver, and then we're generating cash every month and every quarter. So looking out over the next several years, we believe we can keep our capital structure intact, have a very conservative debt load, and at the same time still finance these acquisitions.

Phillip Huang - Barclays Capital - Analyst

Great. Thank you very much, guys.

Mark Barrenechea - OpenText Corp - President & CEO

Thanks, Phil.

Operator

Paul Steep, Scotia Capital.

Paul Steep - Scotiabank - Analyst

Great, thanks. Mark, maybe you could talk just about cloud deals in general, and more at the OpenText Core which I know has just launched. What targets does the sales team or do they have any targets in terms of selling cloud or license? It sounds like they're agnostic, but are you pushing the team to try to gain more experience around selling on the cloud side in the traditional business?

Mark Barrenechea - OpenText Corp - President & CEO

Paul, thanks for the question. No, we're not -- we want customers to consume that's best for them. And I've never believed that you get the corporate result you want by really manipulating the way -- encouraging a rep to sell the way corporate wants to sell, versus the way a consumer or customer wants to consume.

So we're agnostic. We're agnostic as to whether it's a license, or MCV, as I said in my script. We -- I don't want to sound professorial here.

But if we look at over the last three years, we are very pleased with our growth in recurring revenues. Our demonstrated performance of improving adjusted operating margins as we've transitioned to a third of our revenues in the cloud, that stands in contrast to the other companies, we're profitable. In a lot of ways, four years ago, with license in the high 20% as a mix of our business, to where year to date it's 14% to 15%, we've de-risked that revenue line significantly.

So that's why we want to go faster in offering the full choices for customers of how they want to come on board. So we're agnostic to the revenue line. We're not agnostic, in fact we have a very strong point of view that we



want to win the maximum customer lifetime value, whether it's a license, subscription, managed services, combination of all three.

Paul Steep - Scotiabank - Analyst

Great. Just on the cloud as well, since presumably the majority in this quarter and you indicated one likely was correlated of those six the \$1 million-plus deals. Of those though, what are we seeing in terms of the core GXS business? Are these new clients, old clients, are they upsizing or renewals? I think some context around GXS given where we're at would be I think useful and helpful. Thanks.

Mark Barrenechea - OpenText Corp - President & CEO

Yes, I would say -- I guess I didn't call this out in my script. But for our managed services business, we brought on board roughly 40 new customers in managed services business last quarter.

Paul Steep - Scotiabank - Analyst

Great. And that was up -- I think you were tracking at 80 or something before, so it's a significant lift there if I'm not mistaken. But I'll go back and check that. The last part would be, what's been the move to version 10 in the core basis as a final point? Thanks.

Mark Barrenechea - OpenText Corp - President & CEO

Fair enough. I would highlight Coca-Cola and Lincoln as two new customers. Clearly very marquee names.

Those are new customers to OpenText, and both of them specifically into managed services. I'm going to -- when we get SP1 out, we'll come back with some more metrics I think would be more meaningful of the discussion on install base.

Paul Steep - Scotiabank - Analyst

Sounds great. Thanks.

Mark Barrenechea - OpenText Corp - President & CEO

Thank you.

Operator

Michael Nemeroff, Credit Suisse.

Kyle Chen - Credit Suisse - Analyst



Hello. This is Kyle Chen in for Michael. Thanks for taking the question. Just a couple of housekeeping questions for me.

John, can you quantify what the revenue contribution was from GXS this quarter? Was there any benefit to license? And also given the significant FX impact to the total revenue, can you quantify the individual impact to license cloud support service lines?

John Doolittle - *OpenText Corp - CFO*

So, we don't break out the license coming from GXS, but it was immaterial this quarter as it was the last quarter. The second question was FX by line item, is that what you asked?

Kyle Chen - *Credit Suisse - Analyst*

Correct.

John Doolittle - *OpenText Corp - CFO*

Yes, I can give you that. So if I look at -- I'll give you second quarter versus rates at the beginning of the year. So the impact overall was \$16 million, license \$3.5 million, Cloud was about \$3.5 million, customer support was just over \$6 million, and services was around \$3 million.

Kyle Chen - *Credit Suisse - Analyst*

Great, thanks. And relative to your revenue expectations for Actuate, you had mentioned a 10% to 20% decline year over year. But how does that look like from a revenue mix perspective considering their revenue -- ongoing revenue transition?

Mark Barrenechea - *OpenText Corp - President & CEO*

Yes, no comment on where we think it's going to fall. If we sell a license, it will go on the license line, if it's a subscription, it will go on the cloud services line. So as we get a little more experience with Actuate, we'll talk more about it.

Kyle Chen - *Credit Suisse - Analyst*

All right. Thanks very much.

Operator

Paul Treiber, RBC Capital Markets.



Paul Treiber - RBC Capital Markets - Analyst

Thanks very much. I just wanted to speak about the efficiencies that you're seeing in the business over the last year or so. In particular, and just in regards to sales and marketing, it looks like it dropped from about 22% a year ago down to 19% currently. Is that coming from GXS, or is it related also to efficiencies in the traditional in enterprise software or core OpenText business?

John Doolittle - OpenText Corp - CFO

Yes, I think it's a combination. The marketing expense is up overall, but down as a percentage of revenue. You're right. And that really is the inclusion of the additional revenue from GXS.

Overall, the business, we've contained headcount. We're at 8,000 people overall in total. It's the same this quarter as it was last quarter, and the quarter before. So we're really managing the overall expenses of the businesses Mark talked about, and sales and marketing is a product of the GXS inclusion of revenue.

Paul Treiber - RBC Capital Markets - Analyst

And then could you just delve into further on the prudent cost actions that you took? Just how are you implementing those so that you don't overly constrain the spending, particularly when you have some new product launches on the roadmap?

Mark Barrenechea - OpenText Corp - President & CEO

Paul, I'd say we've been leveraging our Manila and India facilities over the last year very well. We are also looking at a stronger force ranking system of where we put programs and initiatives that we think will drive pipe and revenue. And are accelerating just through good visibility and an executive review, some of our consolidation programs of facilities, data centers, network, and operations.

Paul Treiber - RBC Capital Markets - Analyst

Great. Good to hear. Just lastly, just on the emerging markets license business. Did you see the lower than expected performance, do you attribute that more towards external factors, or is it related to execution in the quarter? And then what changes do you think are necessary or would you make to improve performance going forward?

Mark Barrenechea - OpenText Corp - President & CEO

I'm not one to hesitate to say it's on us with execution, but in this particular case at least over the last quarter, I'd say is more macro factors. And in a lot of ways, we just have to -- we remain very committed to these markets. We're not going to add additional markets right now, we're doing deeper reviews in each of the markets. But I would say it's more oriented towards macro versus execution.

Paul Treiber - RBC Capital Markets - Analyst



Okay, great. Thank you. I'll pass the line.

Operator

Stephanie Price, CIBC.

Stephanie Price - CIBC World Markets - Analyst

Good evening.

Mark Barrenechea - OpenText Corp - President & CEO

Hello, Stephanie.

Stephanie Price - CIBC World Markets - Analyst

Hello. Just a bit of a follow on to the last question there. Can you talk a bit about the channel and partner strategy? I think that's the way you're mainly entering these emerging markets. Please lay the VARs and the SIs, and maybe the mix between those and your traditional Partners, such as SAP.

Mark Barrenechea - OpenText Corp - President & CEO

So our SAP relationship remains strong. We had a good ECM quarter, which includes our SAP application business. I was pleased with the performance.

Channel influence was roughly a third of our business, I think 36%, maybe a little higher than a third of our business. Relatively consistent performance year-over-year.

And we're making progress with some of the larger SIs, especially as we think about digitalization and analytics. SIs such as Deloitte, Accenture, Cap Gemini, McKinsey as well. We're making steady progress with some of the larger SIs.

Stephanie Price - CIBC World Markets - Analyst

Okay. And then in terms of your sales force, that's been pretty stable over the last couple quarters as well. Can you comment if there's any changes you're looking at there, or if you're happy with the organization as it is?

Mark Barrenechea - OpenText Corp - President & CEO

I'm happy with the organization. The only change we've made is to incent and motivate every quota carrying rep, whether it be a license or MCV.



Stephanie Price - CIBC World Markets - Analyst

Great. And then final question for me just around the competitive situation. Has there been any changes in the quarter that you saw?

Mark Barrenechea - OpenText Corp - President & CEO

Pretty consistent to my comments at Enterprise World. We're paying attention closely to the HP breakup, as well as the Symantec breakup, and as well as ReSoft and a few other secular competitors.

Stephanie Price - CIBC World Markets - Analyst

Okay, thanks.

Operator

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

Mark Barrenechea - OpenText Corp - President & CEO

Very good. Thank you, everyone, for joining. As we enter calendar year 2015, we enter the year with a very strong lineup around digitalization, cloud and analytics. A third of our revenues are now delivered in the cloud, and over 80% of our revenues are recurring.

Total revenues were up 28.7%, operating cash flow is up 80%. Adjusted operating margins 32.8%, and adjusted EPS up 22.8%. We're pleased with our top and bottom line performance in Q2. Thank you for joining the call, and that concludes today's remarks.

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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