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Nutanix, Inc. (NTNX)

Q2 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and thank you for standing by. Welcome to the Nutanix Second Quarter 2024 Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your first speaker today, Rich Valera, Vice President of Investor Relations. Please go ahead.

Richard Valera

Vice President-Investor Relations, Nutanix, Inc.

Good afternoon and welcome to today's conference call to discuss second quarter fiscal year 2024 financial results. Joining me today are Rajiv Ramaswami, Nutanix's President and CEO; and Rukmini Sivaraman, Nutanix's CFO. After the market closed today, Nutanix issued a press release announcing the second quarter fiscal year 2024 financial results. If you like to read the release, please visit the Press Releases section of our IR website.

During today's call, management will make forward-looking statements, including financial guidance. These forward-looking statements involve risks and uncertainties, some of which are beyond our control, which could cause actual results to differ materially and adversely from those anticipated by these statements. For more detailed description of these and other risks and uncertainties, please refer to our SEC filings, including our annual report on Form 10-K for fiscal year ended July 31, 2023 and our subsequent quarterly reports on Form 10-Q as well as our earnings press release issued today. These forward-looking statements apply as of today and we undertake no obligation to revise these statements after this call. As a result, you should not rely on them as representing our views in the future.

Please note, unless otherwise specifically referenced, all financial measures we use on today's call except for revenue are expressed on a non-GAAP basis and have been adjusted to exclude certain charges. We have provided, to the extent available, reconciliations of these non-GAAP financial measures to GAAP financial measures on our IR website and in our earnings press release.

Nutanix will be participating in the Morgan Stanley TMT Conference in San Francisco on March 6. We hope to see some of you there. Finally, our third quarter fiscal 2024 quiet period will begin on Tuesday, April 16.

And with that, I'll turn the call over to Rajiv. Rajiv?

Rajiv Ramaswami

President, Chief Executive Officer & Director, Nutanix, Inc.

Thank you, Rich, and good afternoon, everyone. We delivered a solid second quarter with results that came in ahead of our guidance. The macro backdrop in our second quarter remained uncertain, but stable, relative to the prior quarter. We continue to see steady demand for our solutions driven by businesses prioritizing their digital transformation and infrastructure modernization initiatives and looking to optimize their total cost of ownership, or TCO.

Taking a closer look at the second quarter, we were happy to have exceeded all of our guided metrics. We delivered record quarterly revenue of $565 million and grew our ARR 26% year-over-year to $1.74 billion. We also had another quarter of strong free cash flow generation. Finally, we achieved quarterly GAAP operating profitability for the first time in Q2, demonstrating the progress we continue to make on driving operating leverage in our subscription model. Overall, our second quarter financial performance reflected continued discipline execution.

Our largest wins in the quarter demonstrated the appeal of the Nutanix Cloud Platform to organizations that are looking to adopt hybrid multi-cloud operating models, optimize the performance of their workloads and improve their TCO, all while managing through some of the disruption from recent industry M&A.

A good example is a seven-figure win with a global EMEA-based provider of automotive technology solutions. This new customer had an existing three-tier footprint in need of a refresh, but was frustrated by the recent price increases of their incumbent vendor, and was also looking to have the flexibility to potentially move some of their footprint to the public cloud in future.

They chose our Nutanix Cloud Platform, including our AHV hypervisor, as well as Nutanix Cloud Management, based on its superior TCO, built-in automation for Infrastructure as a Service, and its ability to seamlessly transition workloads to public cloud via our NC2 solution. We see this win as a good example of the value customers see in our cloud platform for both modernization and providing a seamless pathway to the public cloud.

A second good example is a win with a large North American-based hedge fund that was looking to mitigate the growing cost of its public cloud-hosted virtual desktop infrastructure, or VDI, and for a more responsive solution to meet the performance demands of its traders. They chose to repatriate their VDI onto the Nutanix Cloud Platform on GPU-based servers, resulting in a meaningful improvement in performance and an estimated 60%-plus TCO savings. We believe this win demonstrates the ability of the Nutanix Cloud Platform to seamlessly run and manage workloads wherever the optimal performance and TCO can be achieved, whether on-premise, at the edge, or in the public cloud.

A final example is one of our largest new customer wins in the quarter with a global airline based in the EMEA region that was looking to modernize their three-tier infrastructure while enabling a hybrid multi-cloud environment. This customer chose the Nutanix Cloud Platform, including Nutanix Cloud Management, to run their business-critical applications, leveraging its simplicity and built-in automation for Infrastructure as a Service. They also adopted Nutanix Database Service for managing and deploying their databases throughout their organization, and Nutanix Unified Storage to service their unstructured data needs. We see this win as evidence of the value companies see in adopting our full-stack solution.

Moving on, adopting and benefiting from generative AI is top of mind for many of our customers. As such, interest remains high in our GPT-in-a-Box offering, which enables our customers to accelerate the use of generative AI across their enterprises, while keeping their data secure. Last quarter, we saw our first win for GPT-in-a-Box with a large federal agency. And this quarter, we saw multiple additional wins for our genAI-ready infrastructure offering. While it's still early days and the numbers remain small, I'm excited about the longer-term potential for GPT-in-a-Box.

Finally, on the partner front, I'm happy with the early progress we're seeing with our Cisco partnership. We continue to see good customer interest in our joint offering, and saw additional wins for it in the second quarter. While it's still early in this partnership, I'm encouraged by what we've seen so far.

In closing, we are encouraged that the compelling value proposition of our cloud platform and the strength of our business model enable us to increase our top and bottom line outlook for fiscal 2024. We remain focused on delighting our customers, while continuing to drive sustainable, profitable growth.

And with that, I'll hand it over to Rukmini Sivaraman. Rukmini?

Rukmini Sivaraman

Chief Financial Officer, Nutanix, Inc.

Thank you, Rajiv. I will first review our Q2 fiscal 2024 results, followed by guidance for Q3 fiscal 2024, and finally provide an updated view of our full year fiscal year 2024 guidance. Results in Q2 2024 came in higher than the high end of our range across all guided metrics. ACV billings in Q2 were $329 million, above the guided range of $295 million to $305 million, representing year-over-year growth of 23%. The outperformance was driven by better-than-expected renewals performance due to a combination of good discipline around renewals economics, improved on-time renewal performance, as well as some early and co-term renewals.

Revenue in Q2 was $565 million, higher than the guided range of $545 million to $555 million, and a year-over-year growth rate of 16%. ARR at the end of Q2 was $1.737 billion, representing year-over-year growth of 26%. In Q2, we continued to see modestly elongated average sales cycles compared to historical levels. Average contract duration in Q2 was 2.8 years, slightly lower than Q1, and more or less in line with our expectations.

Non-GAAP gross margin in Q2 was 87.3%, higher than our guided range of 85% to 86%. Non-GAAP operating margin was 21.9%, higher than our guided range of 14% to 16%, largely due to higher revenue and lower operating expenses as a result of timing of hiring.

Non-GAAP net income was $136 million, or fully diluted EPS of $0.46 per share, based on fully diluted weighted average shares outstanding of approximately 299 million shares. Q2 marked our first-ever quarter of positive GAAP operating income of $37 million and of positive GAAP net income of $33 million, with fully diluted GAAP EPS of $0.12 per share. Given expected variability in quarterly revenue and timing of expenses, we would not expect to be consistently profitable at the GAAP operating profit level over the near term.

DSOs based on revenue and ending accounts receivable were 31 days in Q2. Free cash flow in Q2 was $163 million, representing a free cash flow margin of 29%, higher than our expectations due to higher billings and lower expenses in the quarter. We ended Q2 with cash, cash equivalents, and short-term investments of $1.644 billion, up from $1.571 billion at the end of Q1.

We continued repurchasing shares in Q2 under the share repurchase program previously authorized by our Board of Directors. Our sustainable generation of free cash flow enabled us to transition our net share settlement to pay for employees' tax liability on RSU vesting in Q2 and going forward from our previous method of sell to cover. This, along with our share repurchase program, will help us continue to manage dilution.

Moving to Q3 2024, our guidance for Q3 is as follows: ACV billings of $265 million to $275 million, revenue of $510 million to $520 million, non-GAAP gross margin of approximately 85%, non-GAAP operating margin of 7.5% to 8.5%, and fully diluted shares outstanding of approximately 301 million shares.

The updated guidance for full year – fiscal year 2024, which is higher than our previously provided fiscal year 2024 guidance across all metrics, is as follows: ACV billings of $1.09 billion to $1.11 billion, representing a year-over-year growth of 15% at the midpoint of the range; revenue of $2.12 billion to $2.15 billion, representing a year-over-year growth of 15% at the midpoint; non-GAAP gross margin of 85% to 86%; non-GAAP operating margin of 12.5% to 13.5%; free cash flow of $420 million to $440 million, representing a free cash flow margin of 20% at the midpoint.

I will now provide some commentary regarding our updated fiscal year 2024 guidance. First, we are seeing continued new and expansion opportunities for our solutions, despite the uncertain macro environment. However, as we mentioned previously, we have continued to see a modest elongation of average sales cycles relative to historical levels. Our fiscal year 2024 new and expansion ACV performance outlook assumes some impact from these macro dynamics. We are also seeing a higher mix of larger deals in our pipeline, which is driving greater variability in the timing of our new and expansion business.

Second, the guidance assumes that our renewals business will continue to perform well. Third, the full year guidance continues to assume that average contract duration would be flat to slightly lower compared to fiscal year 2023, as renewals continue to grow as a percent of our total billing. Fourth, a reminder that the full year ACV billing is not the straight sum of the ACV billing of the four quarters due to contracts with duration less than one year. We expect full year ACV billing to be about 5% to 6% lower than the sum of the four quarters ACV billing.

In closing, we are pleased that our Q2 results exceeded guidance and to raise our top-line and bottom-line guidance for the full fiscal year. We remain focused on driving growth to capture the significant opportunity ahead of us and on investing prudently for that growth, consistent with our stated philosophy of sustainable, profitable growth.

With that, operator, please open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. At this time, we will conduct a question-and-answer session. [Operator Instructions] Our first question will come from Jim Fish from Piper Sandler. Your line is open.

James E. Fish
Analyst, Piper Sandler & Co.

Q

Hey, guys. Thanks for the questions. Awesome quarter here. Look, I'm going to ask the obvious that's on top of everybody's mind, and I'm sure you're totally prepared for. On the VMware opportunity – and Rukmini, you even just mentioned you're seeing a higher mix of larger deals in the pipeline. So, my question to you is, what sort of pipeline or bookings build have you seen relative to this stage last year between either direct customers kind of coming to you or partners coming over to you as well in terms of signups?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. Why don't I start, Jim, and Rukmini can give you color on the pipeline. So, first of all, I think, as you said, I mean, there are significant concerns from VMware customers regarding the Broadcom acquisition. And we think that this is a significant multi-year opportunity for us to win new customers and to gain share. Now, getting to your question a bit here, the timing and magnitude of these deals is a bit unpredictable. Our pipeline is quite substantial and growing.

Now, for a number of reasons, we expect contribution from the opportunity to build gradually, right? And here are the reasons. The first one, Jim, is that many customers signed multi-year ELAs, enterprise agreements, with VMware prior to the deal closing, three to five years. So, it buys them some time to make decisions.

The second, converting from VMware three-tier accounts or legacy storage accounts, which is a good chunk of VMware footprint, in many cases, requires a refresh of their storage and/or servers, right, one of the two, which could also impact the timing of the potential software purchases that they would make with us, okay? And the last piece is, like with all these accounts, we typically have a land-and-expand motion. So, the first deal could be smaller, and then there's a lot of potential for expansion further than that. And then, Rukmini, you want to take this further?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.
A

Sure. Yeah, I'll add one thing, Jim, to your question, is that – I mentioned my prepared remarks about this, higher mix of larger deals that we're seeing in our pipeline, and that is driving the greater variability, we believe, in the timing of our new and expansion business, as well as potentially contributing to the longer average sales cycles, because larger deals do tend to take longer to close. And we believe that this higher mix of larger deals in the pipeline is driven by, one, our segmentation upmarket, as we've talked about before, and improved product readiness for those larger customers. And secondly, some of the dynamics that Rajiv talked about already, regarding concerns from larger customers, regarding the impacts from Broadcom's acquisition of VMware. And so, we have continued and continue to factor all of the impact of some of these dynamics into our updated fiscal year 2024 outlook.

James E. Fish
Analyst, Piper Sandler & Co.
Q

Makes sense. And just to follow up here, there's a bit of confusion out there from what I can tell in the conversations with investors between what VMware can do that Nutanix can't do. And so, Rajiv, what differences actually exist, if any, or features or function exist – what differences kind of exist, if any, between vSphere, for example, and Acropolis, or the VMware platform versus Nutanix platform, or features, functions you plan to add in order to make it an apples-to-apples compare? Or is it simply just a legacy market perception thing that you guys can't address really what most of VMware could do? And really, why wouldn't we start to see that Acropolis attach rate get closer to 100% on every deal that you sign from here on forward? Thanks, guys.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.
A

Yeah. So, Jim, I think, first of all, if you compare the full stack that Broadcom is offering with VMware Cloud Foundation, that – and our Nutanix Cloud Platform pretty much goes head-to-head against that, right? We've got all the capabilities. So, that's a full stack that includes the hypervisor, software-defined storage, networking, and management. So, we compare very well, right, with that full stack, and we're able to go do a very comparable offering. And indeed, as you can see, right, our AHV penetration, our hypervisor penetration, our install base is about 70%. And we are seeing new customers who adopt our full stack start with our own hypervisor, okay? That part is correct.

Now, when it comes to the lower-tier offering, right, VMware does have a vSphere, and now it's called, I believe, VMware Virtual Foundation, VVF, that includes vSphere some operations management capabilities, et cetera. Now, what I mentioned earlier in response to the other question was that there is some amount of VMware, in fact a big chunk of VMware, where it's only the hypervisor that's connected to legacy storage, right, three-tier storage areas. Now, the way we go after the market is not to just simply replace the hypervisor with our hypervisor, right? Because our hypervisor also is part of our complete solution, right, which includes our storage.

So, customers are actually making a shift from a legacy architecture that's a hypervisor plus external storage to a modern HCI architecture that includes our hypervisor, but also the rest of our stack. So there, it's not just a simple like-for-like, but it's a conversion and modernization of the infrastructure as well. So, I feel pretty good about what we can do. We can handle all the workloads. We have a hybrid cloud solution. We have a modern apps platform that customers can run Kubernetes applications on. We have partnerships with Red Hat for OpenShift. We have partnerships with our cloud partners like Azure and AWS. So from a capability of the portfolio perspective, we are very much there.

Operator: Thank you. One moment for our next question. Our next question comes from line of Jason Ader from William Blair. Your line is open.

Jason Ader
Analyst, William Blair & Co. LLC

Q

Thank you. Hi, Rajiv. Hi, Rukmini. I just wanted to ask on that kind of the – follow-up thread from the last question just on the three-tier architectures out there, and most of those running VMware today. Does it feel like this change with the Broadcom acquisition actually could accelerate the transition away from three-tier architectures as customers maybe get a little bit disenfranchised and are looking for alternatives? And then it's like, well, we never really looked at HCI that closely, but now maybe we should. Are those kinds of conversations happening?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Oh, very much so, I would say, Jason. So, in fact, you're right, right? There's a lot of VMware with what we call three-tier. And one of the things that Broadcom itself has done, by the way, is that with their VMware Cloud Foundation, that includes HCI, and that's their default offering to a lot of the bigger customers. So, effectively now, it's not just us doing HCI, but they're also putting HCI, which puts a little bit of pressure on the three-tier storage piece of it. And so, we are clearly focused on that opportunity, right? And we've been doing that all day long, right, since we started migrating legacy three-tier over to HCI, and potentially that – this might help.

Now, the other thing we should also keep in mind, just so that we don't lose track of it, is there are even easier insertion opportunities now, because there is a substantial base of vSphere plus vSAN HCI out there. And so, that's almost a like-for-like, right? Those customers have already made the HCI decision, and they might be looking. If they're looking to migrate away from VMware, we pretty much have a like-for-like solution that we can migrate over to. And we are doing – we're not sitting idle here, right? We are doing a bunch of things to capitalize on the opportunity.

I'd say three things that we're doing. First is that we have been targeting some more advertising dollars to maximize the awareness of Nutanix as the simplest, easiest viable alternative for these customers. Number two, we've also put in place incentives for our partners, who are helping customers get to our platforms, for new customers, as partners bring new customers to us, we give them more incentives.

Number three is, we're also helping end customers with migration. When they have a VMware environment, they're looking to bring our environment on, there's a period of time where they might have dual operating costs, and we try to help them out on that front. So, we're also taking some very specific steps to go after the opportunity.

Jason Ader
Analyst, William Blair & Co. LLC

Q

Great. And then, one quick follow-up just on your comments on Cisco, that you're happy with the early progress. When do you think, Rajiv, that could start to really be a material contributor to the business?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. We factored in a modest contribution this year, Jason, from Cisco. I do expect that the contribution is going to be more significant in FY 2025, and we'll cover that when we get to – when we're ready to talk about that FY 2025 guide. But clearly, it takes time to build this up. We focused on enabling the full solution, training their sellers, and we're happy with the progress we're making. We are getting new customers through that route now, and they are motivated. So, I think over time, it'll build.

Operator: Thank you. One moment for our next question. And our next question will come from line of Wamsi Mohan from Bank of America. Your line is open.

Wamsi Mohan
Analyst, BofA Securities, Inc.

Q

Yes. Thank you so much. You drove very strong operating leverage in the quarter. Can you talk about if there were any one-time things in there? I think, Rukmini, you mentioned something around hiring, I didn't fully catch. But was there any one-time things in there? And why is that reverting lower next fiscal quarter? And I have a follow-up.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Yes. Hi, Wamsi. Thanks for the question. So, the reference I made in terms of our operating margin performance in Q2, which came in strong at 22% and higher than our expectation, was, one, revenue was higher than we expected and expenses were a bit lower because of timing of hiring and just overall good expense management. And we do expect that expenses will go up in the second half. So, if you look at half-over-half operating expenses implied in the guide, that does go up in the second half, Wamsi, and, of course, Q3 compared to Q2, seasonally the revenue is lower in Q3 than it is in Q2.

So, those are some of the things that are factoring into the outlook. But overall, I'd say we have continued to be focused on investing and investing thoughtfully on this growth opportunity that's ahead of us. And so, that's the approach we've taken. And overall, we've been pleased to take up our full year outlook on both top and bottom line.

Wamsi Mohan
Analyst, BofA Securities, Inc.

Q

Okay. Thanks a lot, Rukmini. That makes a lot of sense. And then, Rajiv, I mean, you made some comments already, but can you perhaps maybe quantitatively talk about the wins that are coming your way because of this M&A and sort of how many points of growth potentially we should be thinking about or how many points of share that you think you could see shift over to Nutanix given this disruption? Or even maybe if you can talk about it in qualitative terms around rate and pace of pipeline build just quarter-over-quarter over the last few quarters, that would be helpful. Thank you.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. Wamsi, first of all, I think it's going to be hard for me to give you some very specific quantitative numbers at this point. But what I'll say is, for sure, right, if you look at our last Investor Day, we talked about our TAM and the SAM as part of that, right, the $60 billion, $70 billion TAM and SAM. And what we really expect is – I mean, we've always been [ph] going (00:29:42) and continuing to grow market share and eat into that SAM. And what this event creates is an opportunity to speed that up, right? So it's the same – the TAM and SAM haven't really changed. It's still the same, but now we're able to get after more of it quicker.

Now, the challenge with quantifying it is that it's very hard to predict, right? I mean, it's, yes, we've got that. How much of this is going to come how quickly? And this is what – it's a little early for us to say something there, right? So, like I said, we've got customers who want to do something different, but they've got these three, five-year ELAs. They're not in a rush. There's some time it takes to convert customers and they have to depreciate the hardware that they've got, for example. And then, you bring us in for a small portion and expand.

So, all these things create some unpredictability in terms of timing and how quickly can we capture it. But I certainly think that this provides us an opportunity for us to capture more of that market quicker. And we're trying to move as quickly as we can. I don't know, Rukmini, if you want to provide any color on the pipeline.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Yeah. I may add one thing to that, Rajiv, which is that, I think, Wamsi, your question is specifically around what we can tell about this opportunity as a result of VMware's acquisition by Broadcom. And I'd say, I think the other nuance here is we've always competed against VMware, right? And so, in some cases, it's quite clear to tell, well, this door wasn't open to us before, and now it is, because of what they may be seeing from our competitor. But in other cases, and we talked about an example on the last earnings call, where existing customers of ours are maybe choosing to invest more in us or go single source with us are partly influenced by this, right?

So, there's this idea of, in some cases it's clear, in other cases it's more of a factor, an important factor, but one factor. And so, in those situations, it's harder for us to attribute specifically dollars and pipeline and things like that to this particular disruption in the competitive market. So, all those factors combined are what makes us feel good that this is a multi-year opportunity, as Rajiv has mentioned, but difficult to get precise in terms of magnitude and timing.

Operator: Thank you. One moment for our next question. Our next question comes from the line of Pinjalim Bora from JPMorgan. Your line is open.

Pinjalim Bora
Analyst, JPMorgan Securities LLC

Q

Great. Thanks for taking the question. Congrats on the quarter. Rajiv, one of your partners compared the Nutanix-Cisco relationship and the buzz around it to the formative years of VCE and noted how VCE was kind of a game-changer for VMware at the time. Do you think the Cisco partnership could be that pivotal for Nutanix? And secondly, do you think there are any learnings from the rise and fall of VCE that you can apply, I guess, to this relationship?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah, I was actually there at Cisco at that time when the VCE partnership and clearly very successful initially. Now, it's hard for me to compare VCE, back then converged infrastructure, with this. But I'll tell you the – I'll give you the sort of the puts and takes, right? So, clearly, Cisco has huge market leverage and market position, right, in terms of their sellers and their access to big accounts and their presence in all these accounts.

Now, if you look at this particular space in the market, their server position is not that – they're a small, relatively small market share player when it comes to servers, right, compared to some of their other competitors. So, they're not as strong in this segment of the market. However, I mean, they certainly have a big overall market cloud.

So, now, what could the two of us do together, really, to go into the market? And that's really, I think, where I do see significant potential here over time. Again, it has to take time to build up. And Cisco also has a complex selling motion. They have generalists, they have specialists. And right now, we are more focused on the data center specialists that they have, and working together with them.

So, to answer your question, I mean, it's a little early days for us to predict how big this could be for us. And I would say, I am optimistic, and I think this opportunity is also going to build up over time. And certainly, continuing to – and in fact, there's a lot of cooperation happening between our sellers and Cisco sellers in the field. So, all good, good omens at this point in time, but still very early.

Pinjalim Bora
Analyst, JPMorgan Securities LLC

Q

Understood. I guess we'll stay tuned. One question for you, Rukmini. The ACV billings guidance for fiscal Q3 seems like it calls for maybe a little bit higher sequential drawdown. I want to ask you, the sales cycle elongation comment that you made, was that versus Q1, the elongation Q2 that you saw, was that sequential? And are you assuming kind of a similar sequential higher elongation in the Q3 guide as well?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Hi, Pinjalim. Thank you for that question. So, I think the first part of the question was on seasonality between Q2 and Q3. And so, on that front if you look back to sort of our initial guidance that we gave for Q3 last year, this time, Pinjalim, it was actually quite similar in terms of what we guided for Q3 versus Q2, but we were able to beat Q3. And so, the actual, I think, is what you're referring to was smaller than what we guided to. But the decrease, I would say, is more or less in line with what we'd expect for seasonality and what we expected at this time last year as well.

And then to your point on the average sales cycle and the modest elongation we're seeing there, it moved around a bit quarter to quarter, Pinjalim. But what I was referring to is that when we look back to historical levels, it remains somewhat elevated. And so, that's what I was referring to.

Operator: Thank you. One moment for our next question. Our next question comes from the line of George Wang from Barclays. Your line is open.

George Wang
Analyst, Barclays Capital, Inc.

Q

Oh, hey, guys. Congrats on the quarter and the guidance. I have two quick ones. Firstly, you briefly touched on the potential – the discounts and promotions to promote VMware customers. And I just want to kind of see if you can elaborate on the approach for the Cisco partnership, the HyperFlex customers. Maybe you can give some color just on the incentives you guys are providing to kind of further drive the adoption from the older HyperFlex customers.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah, we have – I think I would say that's Cisco, right? With Cisco, clearly, we have a – they've end of life HyperFlex, first of all, and there's a limited time where they're – so they're no longer selling the product and there's a limited support window for it. So that by itself, by the way, creates an incentive for HyperFlex customers to migrate. And we, through Cisco, of course, has a whole – Cisco has a set of programs for migration and they're good at driving those types of migration initiatives. And we are supporting them as they do that. So, this is being done largely through Cisco and through the Cisco route to market.

George Wang
Analyst, Barclays Capital, Inc.

Q

Also, Rajiv, quickly, you talked about the repatriation in the prepared remarks. I'm just curious, are you seeing a more visible inflection point in terms of the repatriation to the private cloud or is there a continuation of a prior trend? Just besides, lower TCO kind of versus [ph] extensive (00:37:47) public cloud, can you talk about other factors that may contribute to continued repatriation to the private cloud?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah, I'll give you a two-part answer to that, George. So, I don't know if I can call it a point of inflection, but certainly we are seeing more examples of people repatriating, but those are examples. It's hard for me to say that there's a whole trend here, right, yet. But some are certainly repatriating, like the example I talked about. But also, I think the other thing that we should keep in mind is that the bulk of enterprise workloads are still not in the public cloud. They're still sitting in data centers. I'm talking about enterprise workloads, because what has gone to the public cloud largely have been net new applications.

So for these workloads that are still sitting in the enterprise environment, I think CIOs are being a lot more careful about how much of that do they take to the public cloud. So there's – yes, there's some repatriation happening from the public cloud back on-prem, but there's also a lot more scrutiny and forethought being applied to what should I take going forward into the public cloud from where I'm at.

Operator: Thank you. One moment for next question. Our next question will come from the line of Mike Cikos from Needham. Your line is open.

Mike Cikos
Analyst, Needham & Co. LLC

Q

Hey. Thank you, guys. And I wanted to echo my comments as well, in addition to the others, as far as the great quarter and the results here. I think a bit of a two-parter here, but the first, I know coming back to the financials specifically, Rukmini, can you help us think about the benefit to the quarter from the co-terming that occurred?

And if – I guess, to what degree anything was pulled forward that was expected to land later this year when we think about the magnitude of the beat and raise for guidance?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.
A

Sure. Hi, Mike. So, yeah, I talked about renewals outperformance in Q2, and there were three factors that I highlighted as a reason for that outperformance. One was better renewals economics. And by that, I mean just our team is able to get better sort of pricing at the time of renewal, which is good. Secondly, we talked about better on-time renewal performance, which was strong in the quarter as well. And then the third piece, I think, is what you're referring to, Mike, which is around – I said that we did do a little better on early and co-term renewals.

And those, as we've said before, we go out to our customers well in advance of a renewal being due and start that conversation early, and that's what they prefer as well. And often, we will be able to transact those renewals earlier than when they are due – in an earlier quarter than when they are due. And co-term, similarly. Co-terms are beneficial both for us and for the customer, because it then brings a lot of their licenses that may have been purchased at different times to all be aligned to the same end date. And so those, we generally welcome as long as they are coming at good economics for us. It's good for the customer. They give us cash up front. And so, those are all generally things that we welcome.

Now, in terms of the dynamic of the pull forward, which I think was another sort of aspect of your question, Mike, I'd say there is normal variation, right, between quarters, and we would expect that to continue going forward. And I would say I think we had also talked about this dynamic between fiscal year 2024 and fiscal year 2025, and I'm not sure if that's where you were going, Mike, but at this point, we still do see that the renewal available to renew for next year, the growth in that is accelerating compared to what we saw for fiscal year 2024 because that was partly earlier than co-terms, but it was also just a bigger renewal cohort that is coming up in 2025, which is leading to that accelerated renewals ATR in 2025 compared to 2024.

So, overall, again, I would say a pretty strong quarter from a renewal perspective. And generally, these are all the outperformances driven by things that we like to see. So, nothing that I would sort of characterize as better than expected, certainly, but allows us to sort of certainly manage the business on a more predictable basis, going forward.

Mike Cikos
Analyst, Needham & Co. LLC
Q

Got it. And it's funny you're ending that response on predictability. I think one of the things that I've been going through on my side this earnings season is certain companies have cited seeing larger deals in their pipeline and greater variability based on when those deals close. So, I wanted to get a sense, if possible, but can you help us think about the magnitude when you're citing these larger deals, like are they coming with an X percent increase in size from a dollar perspective versus what you're historically seeing? Just to help us get a better sense of that.

And then, the second piece tied to that is, how do you get confidence in driving those deals? Again, just because they are obviously more strategic, there's less certainty around the timing of when those close. Just anything there as far as how you do gain confidence on that front. It's a high quality problem to have, I'll start with that, but I just want to make sure that you guys are thinking about this and wanted to see how you'd respond to that on our side.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Yeah, it's a good question, Mike. And you're right, these larger deals are inherently more unpredictable, which is why I think my point on your previous question, right, was renewals generally more predictable, although, of course, as with everything, there is some variability there, but definitely more predictable than the new and expansion portion. And so, I won't give you a specific number, Mike. I know you were looking for some percentage or size or something like that.

What I will say is when we look at our pipeline of opportunities, and we look at the mix of that, meaning how much is coming from deals of a certain size versus a larger size, and if you think, as you may have buckets of deal sizes, what we're seeing in the data is that a larger proportion is coming from those higher – larger deal size buckets than we've seen previously, right? And that's in addition to the pipeline growing, or [ph] just saying (00:43:59) that the mix of it is also changing to be weighted more towards larger deals. So, that's sort of the first part of the answer to your question.

Now, in terms of just how do we get comfortable, we look at what's in the pipeline, we're looking at, a lot of other things in terms of conversion rates and things like that, and related to the pipeline. And we put a probability on how many of those we think we can convert, right, during a period of time. And so, that's sort of a little more color into the methodology of how we're approaching this. And all of that is factored into the guidance that we provided, right? But Rajiv, did you want to add anything to that?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. Just a couple of things. First of all, I think one of the reasons we're seeing these large deals is because we – of course, for a while, we've been working on a portfolio that – product portfolio, which we think is ready for large-scale enterprise deployments. And so, we have segmented our focus a bit further up the market in terms of our own sales force segmentation. And then on top of that, we've got this industry disruption with VMware, where many large customers, of course, who were not necessarily engaged with us before are now engaging with us. So, that's the reason for why we're seeing more of these large deals in our pipeline.

Now, I think with respect to prosecuting these deals, I would say we keep getting better at going after these deals. I mean, we have a whole 360 approach towards going after this. We have executive sponsors on the big accounts where we have large deals. We have a full team assembled to go pursue these deals. And having said that, so it's still going to be – timing is going to be a bit unpredictable and the size of these things also tend to vary over time. So, it doesn't completely replace the unpredictability.

But it does – it's a [ph] sea of (00:45:44) engagement, right, when you have these types of deals between both companies, we are investing resources, customer is investing a lot of resources as well, because there's a lot of testing, certifications, going through contract negotiations, security audits, a whole bunch of things that get through this process. And so, I would say we as a company are getting better and better at going after these types of opportunities.

Operator: Thank you. One moment for our next question. Our next question will come from the line of Meta Marshall from Morgan Stanley. Your line is open.

Meta A. Marshall
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks. A couple of questions for me. Maybe just on – you noted clearly some macro headwinds still. Just wanted to get a sense of any of the shape of that, is it still things that are just elongating lead times? Are you seeing it on larger deals, smaller deals, certain verticals, certain types of projects? Kind of just any change in color from the past couple of quarters, if there are any.

And then maybe on the second question, I would imagine you guys are getting a number of resumes in your inbox right now, just kind of given the disruption. Just any notable hires or how you're finding kind of the pool of talent to add in terms of some of your OpEx adds? Thanks.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. Rukmini, why don't you take number one, I'll take the number two question?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Yeah. Sure, Rajiv. So on macro, Meta, which I think was your first question, it's more or less remained stable relative to what we've seen in the last few quarters. So, fairly consistent, okay, with what we've seen in the last few quarters. And we characterize that as somewhat uncertain, but stable. And that's sort of what we continue to see. So, no significant change from that, which, again, as we talked about, did show up in the continued modest elongation of sales cycles compared to our historical levels.

Now, some of that could also be driven by this larger mix of larger deal sizes in our pipeline. So, that's sort of showing up now. But again, that is also a factor of just the fact that we've gone upmarket. It's not necessarily a macro-related point. So, on macro, nothing else I would call out in terms of specific verticals seeing strength or weakness that we're noticing at this point. Somewhat uncertain, but stable is how we'd characterize it.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

And, Meta, on the talent question, there's no doubt this is – two years ago, it was a difficult market for talent, right? Everybody was hiring and it was a tough market as we tend to hire at the top of the pyramid in terms of software developers. Now, that has changed quite significantly for us, right? In this market today, we're able to attract the best talent from every place, not just VMware or other places you might think of, but also from hyperscalers, for example. And so, we see a good talent environment.

We have been using that, of course – we have been hiring carefully, but selectively in both R&D and sales. And we are seeing really good talent come in the door. And overall, it's helping up-level the talent that we have in the company. And I'm very happy about that. And that's happening at the individual contributor levels, but also at the management levels as well. So, across the board.

Meta A. Marshall
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks.

Operator: Thank you. One moment for our next question. Our next question comes from the line of Erik Suppiger from JMP. Your line is open. Erik, your line is open. We'll go ahead...

Erik Suppiger
Analyst, JMP Securities LLC
Q

Sorry there. Sorry.

Operator: One moment. Let me go ahead and bring him back up. Okay. Erik, your line is open again.

Erik Suppiger
Analyst, JMP Securities LLC
Q

All right. Sorry about that. I want to just touch on the subject of larger deals and elongated sales cycles. As previously noted, there have been other vendors that have seen similar trends, and there was some discussions around consolidation, customers that are getting more focused on consolidating on to a single – or a few vendors as opposed to a lot of tools out there. Is that one of the things that could be contributing to the elongated sales cycle, or is it more of an economic and uncertainty issue?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.
A

I'm not sure as much, Erik, whether it's because people are consolidating, whether they're – in our case, for example, certainly there's a lot of like, okay, I've got an incumbent vendor that I need to rethink my strategy and bring on an alternative vendor. And that's certainly playing very much for us, right, very much in play. So, they were happy with the vendor prior, and now they're no longer so happy, so they've got to look at an alternative, and we are a very solid infrastructure alternative. That's one factor that's clearly playing.

The second factor, as I mentioned a little earlier, is that we ourselves, as a company, have gotten to a point where we have a portfolio that can address pretty much across the enterprise all the applications that customers are running. So, all applications, from small scale to very large scale, and that makes us a bigger player in our customers' minds. It's not that they're thinking about us as a vendor for just one use case anymore. They're thinking about us as a platform vendor for them that can run all their applications. And so, that typically leads to a larger strategic engagement with the customer, which also takes longer, right? So that, I think, is what's playing for us – playing out for us now.

Erik Suppiger
Analyst, JMP Securities LLC
Q

Okay. Very good. And then just on the ChatGPT-in-a-Box (sic) [GPT-in-a-Box], just curious if you have seen particular groups or segments of your customer base that are adopting that. Who is doing AI in a private cloud these days?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.
A

Yeah. First of all, I'd say it's early days for us, Erik, on that, for sure. But we are seeing traction across all kinds of verticals, yeah, financial services, defense, federal – in fact, one of our first wins was with a federal agency – manufacturing, pharma, or medical devices, so there's just many different verticals, but the use cases tend to be somewhat similar. Document summarization, search analytics, co-piloting, customer service, enhanced fraud detection, these are some of the same – sort of same use cases, but across a range of verticals.

Operator: Thank you. One moment for our next question. Our next question comes from the line of Ben Bollin from Cleveland Research Company. Your line is open.

Benjamin J Bollin
Analyst, Cleveland Research Co. LLC

Q

Thank you. Good afternoon, everyone. Thanks for taking the question. Rukmini, you made a comment about investing carefully for the growth in front of you and there's been a few questions on hiring. I'm curious about how your hiring plans have evolved since the start of the year. When you look at what you see out there and, in particular, how you're managing the amount of inbound activity that you are seeing from partners and customers? And then I had a follow up.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

So, maybe I'll take that, Ben. So, I think there's a couple of points. One is related to hiring. The other is inbound activity from partners, customers, et cetera. So, slightly different question there. So, I think on the hiring, if you look at our history here, we've been very, very tight on OpEx the past few years for the right reasons, as we consolidated our portfolio, got some more focus into the company and got our execution going. And now, this is the year where we are investing. Our OpEx is going up based on what we've talked about. But we are investing judiciously, continuing to drive both growth and leverage to our bottom line.

But we're certainly investing. We're investing in terms of building out our portfolio from an R&D perspective. We're investing in terms of our go-to-market so that we can be more effective in terms of getting – handling the demand that we're starting to see. And to your point, over the last, I would say, year or two years, we've seen more incoming from customers, partners, and managed service providers. And we now have focused efforts in terms of addressing all of those, right?

Whether it be a larger set of customer engagements, whether it be more focused in terms of the partners, which was one of the priorities that I said very early on when we started here three years ago. So, more focus on the channel, enabling them, recruiting partners, giving them incentives, making them more autonomous, and extending that to our managed service provider partners where we continue to add more of them to our partner network over time.

Benjamin J Bollin
Analyst, Cleveland Research Co. LLC

Q

Okay. That's great. Rajiv, one other question for you is, you commented earlier about some CIO scrutiny as it relates to the data center investments and public cloud investments. I'm curious if you're seeing any change in how customers are thinking about their longer-term infrastructure planning from an investment perspective, notably because of what's happened with Broadcom and VMware? And that's it for me. Thank you.

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Oh, I mean, certainly, Ben. So, the Broadcom-VM, I think, absolutely it is, right, I mean, again, VMware was a great technology vendor with a lot of innovation and customers and with a large footprint of customers. And now, they have to rethink whether that's the right long-term strategy for them. And so, that says, okay, well, we've got to either look at alternative providers, of which we are an easy alternative, or they could say, well, I could go more to the public cloud, okay, which is not as easy a thing for existing workloads, to just take everything and move it to the public cloud, that's not easy to do. And then they factor into the fact – cost, regulatory aspects of it, and so forth.

So, clearly, I think, for us as a vendor, there's certainly – we see customers continue to invest in infrastructure modernization in terms of digitization, in terms of running modern applications, not just in the public cloud, but also on-prem. And like some of these new cycles that are happening now, like AI, for example, will also find its path down the same route, right, which is starting out with a lot of training happening in the public cloud, but it's moving towards, okay, I'm going to run my AI. I'm going to fine-tune the training on my own data sets, which are proprietary that I want to keep carefully, and I'm going to have to potentially look at slightly different solutions for inferencing, which are going to be running closer to my edge locations. So, these things are driving what we call hybrid multi-cloud, and I think that's very much, I think, the world that many of our customers are here for the next several years.

Operator: Thank you. One moment for our next question. Our next question comes from the line of Dan Bergstrom from RBC Capital Markets. Your line is open.

Daniel Bergstrom
Analyst, RBC Capital Markets LLC

Q

Hey, it's Dan Bergstrom for Matt Hedberg. Appreciate you taking our question here. To build off a recent answer that mentioned a 360 approach around VMware deals, could you go into some of the mechanics and processes involved in migration over from VMware? I guess, specifically what tools are in place to facilitate migrations? And then how long does a typical migration take?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. And the answer to that varies, but I'll go through the process, Dan. So, there's clearly an assessment of what the workloads are or applications are that are running on that infrastructure. That's one part of it, and making sure that we can run all those workloads with good performance, which by and large is the case these days. The second is what elements of the stack have they deployed. And the more of the elements that they have deployed, the stickier or the more complex the migration becomes.

So, for example, for a customer that just only deployed a hypervisor, it's a largely automated move away from the hypervisor to our hypervisor. We have automated tools. In fact, our tool is called Move. We've done a lot of these VM migrations all day long. And so, that's a relatively simple migration that can be done automated.

Now, at the other end of the spectrum, if they've invested a lot of custom automation work, custom security work on top of the stack, then some of those will have to be converted over. And that requires a professional services engagement, which also is part of our offering to help convert over some of those onto our platform or onto more open types of platforms. For example, automation people are looking at Terraform, as an example. So in those cases, it's a more complex migration.

I'll give you some examples, though. In a lot of cases, actually, what happens is that the migration planning takes some time. The actual execution of the migration is very quick. There was a case study that we published recently of a healthcare system that we've been engaged with for the past three years or so. The name was Pediatrix, it's public at this point. And they planned this migration for a few years. But when they actually came around to doing the migration, they were done within 90 days.

So, that's a typical example. There's a cycle of selling and engagement and everything and then getting everything ready. And then once it's ready, they were able to migrate in 90 days. And I would call them as a medium complexity environment. They're not at the high end of the complexity, but they're not necessarily the lower – the simplest type.

Daniel Bergstrom
Analyst, RBC Capital Markets LLC

Q

That's very helpful. Thank you.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Thank you.

Operator: Thank you. One moment for our next question. And our next question comes from the line of Simon Leopold from Raymond James. Your line is open.

Victor Chiu
Analyst, Raymond James & Associates, Inc.

Q

Hi, guys. This is Victor Chiu in for Simon Leopold. Just really quickly, can you help us understand what's baked into your full year outlook? Specifically, does the current guidance reflect gains from VMware at a similar rate or are you expecting this accelerates from here?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Thank you, Victor, for the question. So, the full year guide assumes some benefit from the VMware being acquired by Broadcom, as we said at the beginning of the year. And no, it does not expect any acceleration at this point. It just assumes it has some benefit in there. It also assumes a small benefit, as we've talked about before, towards the end of the year from the Cisco partnership as well. But that, again, as Rajiv said, we expect that to grow over time and certainly into fiscal year 2025, but there's a small benefit from that baked in as well, in addition to sort of all the other dynamics we've talked about on this call, right, including modest elongation of average sales cycles, unpredictability with regard to large deals in the pipeline, et cetera.

Victor Chiu
Analyst, Raymond James & Associates, Inc.

Q

Okay, great. That's helpful. And just lastly, I wanted to follow up on the macro question. We've been hearing through the channel that the sentiment on the HCI market overall has turned slightly more cautious. Can you help us understand what you're thinking for HCI growth overall this year and how Nutanix performs relative to that?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.

A

Yeah. Maybe I'll take that. I don't think we haven't seen a slowdown or caution around HCI adoption. I think it's been the same kind of dynamic that we've seen in the past. There is a legacy infrastructure out there. The HCI capabilities have continuously gotten better over time, where HCI today can run pretty much all enterprise workloads on the platform and, in many cases, can do so with better performance even than legacy architectures. So, better performance, better TCO, much simpler to operate.

But I think what we've always had to overcome is inertia. Right? We've got a set way of doing things that customers have been doing for a long time. And here is a shift to a more modern, software-defined architecture.

And that shift we have to do. And we have to overcome that with all the – but that's been what we've been doing for the entire existence of the company. So, I wouldn't see that there's been a bunch of change in how our customers are thinking about it, certainly not in the last year or so that I've seen.

Victor Chiu
Analyst, Raymond James & Associates, Inc.
Q

Great. And how the growth – what you're thinking for growth and kind of how Nutanix is growing relative to that?

Rajiv Ramaswami
President, Chief Executive Officer & Director, Nutanix, Inc.
A

Yeah, I think we – I don't have much to add beyond what we covered at Investor Day just last September, where we provided both TAM and SAM opportunities and our growth outlook in terms of 20% ARR growth in terms of what we could drive through FY 2027 is what we said there.

Operator: Thank you. And with that, this will conclude our question-and-answer session today. Thank you for your participation in today's conference. This does conclude the program. You may now disconnect. Everyone, have a great day.