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Nutanix, Inc. (NTNX)

Q4 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and thank you for standing by. And welcome to the Nutanix Q4 2023 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 like to introduce your host for today's call, Richard Valera, VP of Investor Relations. You may begin.

Richard Valera
Vice President-Investor Relations, Nutanix, Inc.

Good afternoon and welcome to today's conference call to discuss the fourth quarter and fiscal year 2023 financial results. Joining me today are Rajiv Ramaswami, Nutanix's President and CEO; and Rukmini Sivaraman, Nutanix's CFO.

After the market close today, Nutanix issued a press release announcing fourth quarter and fiscal year 2023 financial results. If you'd like to read the release, please visit the Press Releases section of our IR website.

During the call today, management will make forward-looking statements, including statements regarding our business plans, strategies, initiatives, vision, objectives, and outlook; including our financial guidance as well as our ability to execute on them successfully and in a timely manner; and their benefits and impact on our business, operations, and financial results; our financial performance and targets, expectations regarding and the factors driving our growth and profitability, our competitive position and market opportunity, customer demand, the impact of our business model transition and macroeconomic, geopolitical, industry customer and other trends.

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 the fiscal year ended July 31, 2022, and 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.

Lastly, I'd like to remind you again that Nutanix will be holding its 2023 Investor Day in New York City on September 26. Please go to the Events section of the Nutanix Investor Relations website if you'd like to register.

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 good fourth quarter with results that came in ahead of our guidance, capping off a strong fiscal 2023. The uncertain macro backdrop that we saw in our fourth quarter was largely unchanged compared with the prior quarter. And we continue to see steady demand for our solutions in Q4. This was driven by businesses prioritizing their digital transformation and infrastructure modernization initiatives and looking to optimize their total cost of ownership.

Taking a closer look at the fourth quarter, we were happy to have exceeded all of our guided metrics. We delivered strong ACV billings growth and record quarterly revenue of $494 million, a nearly $2 billion annualized run rate. We also had another quarter of good free cash flow generation, despite some expected one-time payments. Overall, our fourth quarter financial performance was a strong finish to our fiscal year.

Our full year fiscal 2023 results demonstrate the progress we've made with our subscription model. Specifically, we delivered healthy year-over-year ACV billings growth of 27%, led by outperformance of our renewals business. We also delivered our first year of non-GAAP profitability in the company's history with a non-GAAP operating margin of 9%.

Finally, despite the impact of several one-time payments, we generated free cash flow in excess of $200 million, a roughly tenfold increase compared to our prior fiscal year. Beyond the financials, we made significant progress across all aspects of our business in fiscal 2023. On the product front, we delivered general availability of NC2 on Microsoft Azure, announced meaningful new products in areas such as Kubernetes, data services and cloud management, and defined our data services vision with Project Beacon to enable companies to build portable applications. We also enhanced our corporate governance profile through amendments to our bylaws and certificate of incorporation.

Finally, on the go-to-market front, we closed multiple large deals with major enterprise and government customers. These wins demonstrate the strategic relevance of our platform to our customers key transformation initiatives and the success of our focus on landing these larger, more strategic transactions.

Overall, for fiscal 2023, we demonstrated consistent execution, solid top line growth, strong renewals performance, sharp improvement in profitability and free cash flow, and continued progress on our longer term strategic priorities.

Moving on, gaining sales leverage via partners has been a priority since I joined as CEO. We said we would focus on deepening our partnerships to provide more impact in how we go to market, as well as provide more opportunities within larger accounts. This week, we made a milestone announcement on this front with a global strategic partnership with Cisco. This partnership is about combining the best of breed between our two companies.

Cisco will combine the Nutanix Cloud Platform along with their UCS compute and cloud management, deeply integrated with their networking and security. It's a fully integrated solution with joint engineering and interoperability and expanded support that will be sold by Cisco. We're excited about working with Cisco on this partnership and having them sell our leading hybrid multi-cloud software, leveraging their extensive go-to-market reach.

Now, I'd like to talk about our customer wins this quarter, which demonstrate the success we've been having in landing large multi-million dollar ACV deals. A good example is a significant expansion we won in Q4 with the UK's Department for Work and Pensions, or DWP, the UK's biggest public service department. This win demonstrated the value customers are seeing in the broader capabilities of our platform. The DWP has already adopted our cloud platform, including Nutanix Cloud Management and Nutanix Unified Storage, to run its business critical workloads and was looking for a way to extend its footprint into the public cloud.

In Q4, DWP chose NC2 to enable the shift of workloads from their private cloud to the public cloud. In their words, "Nutanix NC2 allows DWP to seamlessly extend our on-premise footprint into public cloud while avoiding the costs traditionally associated with lift-and-shift migrations. Furthermore, NC2's cost effectiveness and ease of use enable us to maintain a layer of abstraction for our most critical workloads that avoids both platform and vendor lock in." We couldn't have said this better ourselves and are grateful for the opportunity to partner with DWP on their cloud journey.

Another notable win in the quarter was the service provider partner in the EMEA region that was implementing a nationwide electronic health record, or EHR, system for a government health ministry. This partner chose Nutanix Cloud Platform, including Nutanix Cloud Management and our AHV Hypervisor to host critical EHR applications across 20 strategically located sites. They also chose Nutanix Unified Storage for managing the data on GPU-based image servers associated with the project. We see this win as a testament to the value our customers see in adopting our full stack offering and the growing contribution we are seeing from our service provider partners.

Now, I'd like to talk about AI and what it means to Nutanix now and in the future. Today, we already have customers using our platform to deploy AI, often for inferencing [ph] on video or (00:11:15) sensor data, who are seeing the same agility, performance and TCO benefits from our platform as customers running other workloads. They're deploying us for use cases ranging from faster checkout in retail applications, ensuring compliance with safety protocols at construction sites, to quality assurance [ph] in (00:11:40) manufacturing applications. However, we see an emerging opportunity in the surging demand for Generative AI.

To-date, there's been a lot of investment in large language models, or LLMs, running in the public cloud. However, as AI models become more compact and organizations become concerned with issues such as intellectual property leakage, compliance and privacy, we expect there will be more demand to fine tune and run models on premises and at the edge. We believe there's an opportunity to provide a turnkey solution for those looking to jumpstart these AI initiatives.

That's why we recently launched GPT-in-a-Box. This is a full stack software-defined AI-ready platform, along with services to help our customers size and configure hardware and software to deploy a curated set of LLMs using the leading open source AI frameworks on our platform. It allows customers to easily deploy AI-ready infrastructure to fine tune and run generative pre-trained transformers, or GPTs while maintaining control of the data and applications. While it's still early, we are pleased with the initial interest we've seen to-date in GPT-in-a-Box.

Moving on, I'd like to highlight the recent addition of Mark Templeton to our board of directors. Mark's previous tenure as a public company CEO, combined with the strong domain knowledge of both cloud and data center infrastructure software makes them an excellent fit for Nutanix. I look forward to working with him closely as we execute on our hybrid multi-cloud vision.

Finally, on the back of our strong free cash flow performance in FY 2023 and in conjunction with our earnings release, we announced that our board of directors has approved a $350 million share repurchase authorization. We see this repurchase program as a reflection of confidence in the company's long-term market opportunity and financial outlook, and an important milestone in our subscription journey.

In closing, we are encouraged by the compelling value proposition of our cloud platform and the strength of our business model, enable us to provide an initial outlook for fiscal 2024 that calls for continued solid top line growth, improving profitability and solid free cash flow growth from a strong fiscal 2023 level. We look forward to providing an update on our strategic priorities and longer term financial outlook at our Investor Day in September, and we remain focused on delighting our customer 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 provide commentary on our Q4 2023 results and fiscal year 2023 results, followed by our outlook for Q1 2024 and fiscal year 2024. Q4 2023 was a good quarter in which we exceeded all guided metrics. ACV billings in Q4 was $279 million, higher than our guidance of $240 million to $250 million. Revenue in Q4 was $494 million, higher than our guidance of $470 million to $480 million.

ARR at the end of Q4 was $1.562 billion, a year-over-year growth of 30%. Similar to last quarter, we saw a modest elongation of sales cycles likely due to increased deal inspection. New logo additions were about 500 in Q4. Average contract duration in Q4 was three years, flat quarter-over-quarter as expected. Non-GAAP gross margin in Q4 was 85.8%, higher than our expectations because of higher revenue than expected, certain non-recurring savings and timing of hiring.

Non-GAAP operating expenses in Q4 were $361 million. Non-GAAP operating margin in Q4 was 13%, higher than our guidance of 9% to 10%. Non-GAAP net income was $68 million or EPS of $0.24 per share based on fully diluted weighted average shares outstanding of approximately 286 million shares. Billings linearity was good and DSOs were 29 days in Q4.

Free cash flow in Q4 was $46 million, implying free cash flow margin of 9%, higher than our expectations, largely due to better than expected billings and collections. We ended Q4 with cash, cash equivalents and short-term investments of $1.437 billion, up from $1.358 billion in Q3 2023.

Looking at our full year financial results, we exceeded all guided metrics for fiscal year 2023 as well. ACV billings in fiscal year 2023 were $957 million, higher than our guidance of $915 million to $925 million and representing a year-over-year growth of 27%. A reminder that the annual ACV billings is slightly lower than the sum of the ACV billings from the four quarters due to adjustments for deals with duration of less than a year.

Revenue in fiscal year 2023 was $1.863 billion, higher than our guidance of $1.84 billion to $1.85 billion and representing a year-over-year growth of 18%. A reminder that revenue in fiscal year 2023 benefited from the normalization of orders with future start dates resulting from our partners supply chain challenges. Largely because of this dynamic, fiscal year 2023 revenue included the benefit of approximately $23 million in deferred license revenue that would have been recognized in late fiscal year 2022 instead.

We ended fiscal year 2023 with an ARR of $1.562 billion, as mentioned earlier, a year-over-year growth of 30%. GRR or gross retention rate at the end of fiscal year 2023 was 90-plus percent, and NRR or net retention rate was 123%. Our fiscal year new and expansion ACV performance was impacted by some of the macro uncertainty we have previously discussed and performed slightly below our expectations entering the year and below what we believe its longer term potential is. The renewals business continues to perform well, and it tends to be at a lower aggregate average contract duration compared to our new and expansion business.

Our relative economics on renewals have also continued to improve over time as the renewals team has improved their execution. Average contract duration in fiscal year 2023 was three years, lower than the 3.2 years in fiscal year 2022 as expected. Non-GAAP gross margin in fiscal year 2023 was 84.6%. Non-GAAP operating expenses in fiscal year 2023 were $1.414 billion, an increase of 1% year-over-year.

Non-GAAP operating margin in fiscal year 2023 was 9%, representing our first year of non-GAAP operating profit. Non-GAAP net income was $169 million or EPS of $0.60 per share based on fully diluted weighted average shares outstanding of approximately 282 million shares.

Free cash flow in fiscal year 2023 was $207 million, implying free cash flow margin of 11%, representing a free cash flow margin expansion of 10 percentage points year-over-year. Overall, fiscal year 2023 was a significant year, marking our first year with a positive non-GAAP operating margin at 9%, significant free cash flow generation of over $200 million, while growing ARR at 30% and growing revenue at 18% year-over-year, all in an uncertain macroeconomic environment.

Moving on to Q1, the outlook for Q1 2024 is as follows. ACV billings of $260 million to $270 million, revenue of $495 million to $505 million, non-GAAP gross margin of approximately 84%, non-GAAP operating margin of 9% to 11%. The guidance for full year fiscal year 2024 is as follows. ACV billings of $1.075 billion to $1.095 billion, exceeding the $1 billion threshold and representing year-over-year growth of 13% at the midpoint. Revenue of $2.085 billion to $2.115 billion, representing year-over-year growth of 13% at the midpoint of the range. Non-GAAP gross margin of approximately 84%, non-GAAP operating margin of 11% to 12%, and free cash flow of $280 million to $300 million.

I will now provide some commentary regarding our 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 sales cycles. Our fiscal year 2024 new and expansion ACV performance outlook assumes some impact from these macro dynamics.

Second, the guidance assumes that our renewables business will continue to perform well and while our available to renew, or ATR, pool continues to grow year-over-year, it is growing at a slower pace in fiscal year 2024 but is expected to reaccelerate in fiscal year 2025 based on our current view. Third, the full year guidance assumes that the average contract duration would decrease slightly compared to fiscal year 2023 as renewals continue to grow as a percentage of our billings.

And regarding our bottom line guidance, we will continue to make targeted and prudent investments into our go-to-market and innovation engine to continue to invest in growth while improving our profitability and free cash flow margin year-over-year. Overall, we remain confident, in our view, around a large and growing market for our solutions, combined with a growing mix of renewals as a significant driver of both billings growth and margin expansion over a multi-year period.

We also announced today that our board of directors has authorized a share repurchase program of up to $350 million. We remain focused on investing in our business to support profitable growth and on delivering strong returns for our shareholders. This share repurchase program is consistent with these objectives and a reflection of the confidence we have in our long-term market opportunity and financial outlook.

In closing, we are pleased that our fiscal year 2023 results reflect our continued execution towards our stated objective of sustainable, profitable growth and we expect to continue that focus.

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

QUESTION AND ANSWER SECTION

Operator: And thank you. [Operator Instructions] And one moment for our first question. One moment, please. And our first question comes from Pinjalim Bora from JPMorgan. Your line is now open.

Pinjalim Bora
Analyst, JPMorgan Securities LLC
Q

Oh, great. Hey, congrats on the quarter. Thanks for taking the questions. Rajiv, I wanted to talk about AI, the GPT-in-a-Box, help us understand is that largely kind of an integrated offering, kind of with a bundled pricing, or is there any new functionality that you have developed? And seems like it's spanned across hardware, software and services, how are you kind of thinking of going to market with it?

Operator: One moment, please.

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

Can you folks hear me now?

Operator: Yes. You can be heard.

Pinjalim Bora
Analyst, JPMorgan Securities LLC

Q

I can hear you.

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

A

Okay. Sorry. So – yeah. So, first of all, in terms of the platform, it's the same Nutanix Cloud Platform integrated with standard server platforms with NVIDIA GPUs as part of the solution. Okay. And on top of that, what we add is a curated set of MLOps software and LLMs largely open source models, and we put that all together with the services offering that helps customers deploy this out of the box.

Now what do they use it for? So what we see with Generative AI is there's been a lot of focus about training these large LLM models in the public cloud. But when it comes to the actual usage of these, what you're going to see is companies need to run these AI models where their data is. And in a lot of applications, enterprise applications, sensitive data is stored on-prem or perhaps at edge locations where they're actually gathering the data in the first place.

So with GPT-in-a-Box, they can run their AI applications – Generative AI applications by fine tuning these large LLM models that have been trained in the public cloud using what we call foundational models and public data, they can fine tune this, make them more compact to run with their own data and use it on-prem. So that's the offering.

Now in terms of go-to-market, we have a small tiger team that's very focused on working with our customers that we put use cases together. We are also building an ecosystem of ISVs and SI partners that can help us take this to market and expand our scale. So it's still early days, but I'm excited about where this is going.

Pinjalim Bora
Analyst, JPMorgan Securities LLC

Q

Yeah. Understood. Thank you. And one for Rukmini. Rukmini, you talked about ATR slowing this year. Maybe help us understand why would that be the case. Is that just because that new ACV was a little bit slower this year, is that kind of adding up to it? And then, are you baking in any upside from the VMware opportunity in the guidance?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Hi Pinjalim. Thank you for the question. So on the first question on ATR. So we expect continued growth in our renewal ACV business in fiscal year 2024 and our GRR continues to be good at 90-plus percent. But as you noted, and as we said in our prepared remarks, we do expect that the renewals ACV will – is expected to grow at a slower rate in fiscal 2024 than in 2023 due to the shifting of some renewals from 2024 to 2023, largely due to co-terming and some natural variation, right, that we see in the timing of renewals as customers choose to renew based on their budget cycles or other factors.

In fiscal year 2025, we expect renewals [ph] goal to (00:29:38) reaccelerate based on our current view of our available to renew, or ATR. And I think it's important to emphasize also that we continue to believe that this growing mix of renewals, over time, as a proportion of our total billings continues to be a driver of both billings growth and margin expansion over a multi-year period.

And I think your second question, Pinjalim, was around have we baked in any benefit from the VMware spending acquisition by Broadcom. And so, we continue to see significant engagement and opportunities related to potential concerns around that transaction. And in Q4, we did see a few of these opportunities close, including a seven-figure ACV deal with a Fortune 100 company. So while it's difficult to predict the timing of these wins as we've talked about before, just because of some of the dynamics in the market, we do expect some benefit from these deals influenced by this transaction and have factored that into our guidance.

Pinjalim Bora
Analyst, JPMorgan Securities LLC

Q

Got it. Thank you very much.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Thank you.

Operator: And thank you. And one moment for our next question. And our next question comes from Jim Fish from Piper Sandler. Your line is now open.

James E. Fish
Analyst, Piper Sandler & Co.

Q

Hey guys. Nice quarter. Nice guide. [ph] And it's nice to (00:31:06) also see the new customers pick up again, understanding there's some seasonality here. But was anything causing that in particular in this environment to see the 500 net new customers, including anything on the competitive front, to last question? And I appreciate the details on the net retention rate in the quarter here, but can you walk us through kind of how we should be thinking about net retention into next year given kind of what's going on with retention rates? And does this mean with the cash flow guide being close to $300 million of this year that we could be thinking about well north of $300 million for fiscal 2025 or is that just an Analyst Day item that I should be patient for?

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

A

Yeah. I think there were three questions there, Jim. Maybe I'll take the first two which is our new logos and competitive outlook, and then Rukmini can focus on the financial questions.

So on the new logos, we've continued to focus on these higher quality, higher ASP new logos, more so than just new logo count. But seasonally, of course, Q4 is a strong quarter for us [ph] and because we – you know (00:32:09) that you saw the strength in new logos there, relatively speaking. It's also we're focusing on larger, more strategic transactions, and we're seeing success on that front. So that's the new logo piece [indiscernible] (00:32:22).

From a competitive perspective, Rukmini already talked about the VMware dynamic there. Clearly, we've seen the engagement level grow there. Clearly, we've seen some deals starting to close. And there's still a lot of variability in terms of how the pendulum is going to swing on this one from customers who might just use us to get a lower price from VMware to customers who are truly serious about bringing a second vendor in and reducing their risk with an alternative provider. So we'll have to see how that plays out.

The hybrid cloud piece is really starting to work in terms of customers using more of us in the public cloud. So that piece of it is working well. Our partnership with the hyperscalers is actually coming through actually also nicely in that regard. So we feel good about our competitive positioning as we get into FY 2024.

Rukmini, you can perhaps address the NRR and other questions.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Yes, yes. Hi, Jim. So on NRR, we were happy with 123% that we reported for fiscal year 2023. And in terms of fiscal year 2024, Jim, what I say is, I think we should still assume that of our sort of new and expansion business, the majority does come from expansion, right. We talked about that before. We're not giving out a specific number today, Jim, but, you know, more color to come on that at our Investor Day.

And similarly on free cash flow, yeah, we're happy to sort of guide to $280 million to $300 million for fiscal year 2024. And again, more to come at Investor Day. What I will say though is, you know, we continue to be focused on all elements of that profitable growth piece, which means that we do intend to continue to evolve our – grow our margins, free cash flow margins over time while growing the top line, right. So that continues to be the intent. But I'll sort of hold on any specific free cash flow outlook beyond 2024 for our Investor Day.

James E. Fish
Analyst, Piper Sandler & Co.

Q

Fair enough. Just last one for me, Rajiv, on that Cisco partnership. I mean, how much demand were you getting for this? Just, you know, a nice to have as Cisco UCS is a much smaller shareholder of that server market relative to some of your other partners. And understanding Cisco has one of the best sales motions out there with this. But are there any minimums to think about or how should we expect the impacts probably more for fiscal 2025, but any impact for fiscal 2024?

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

A

Yeah. So, again, let me pass it out there. So, Jim, first of all, yes, we have seen customer requests in the past for customers – there are many large customers with UCS deployments. They would like to see this joint solution from us and Cisco. So we're happy that we are able to announce that. Also importantly for us, I say the fact is Cisco has a go-to-market machine that's much bigger than ours. You know, we today have about 20 – call it about 25,000 customers roughly. But our addressable market in terms of customers is at least 100,000. And so Cisco's broad market reach could help us get those initial entries. And, you know, again, we're going to work, co-sell this with Cisco, right?

Cisco is going to be the front in terms of selling this, but we're going to be helping them along the way. And just I look at this as an expansion opportunity for us. It's a much larger customer base and good for the customer in terms of them buying an integrated solution for everything they need in the data center, right? The virtual platform, cloud platform from us, the hardware from Cisco, both in terms of servers and storage, as well as the networking features and the security aspects of this. So we are excited about this.

Now, in terms of the numbers, what we expect is we just literally announced it here and we – there's a whole process of training, enabling [ph] the field (00:36:00), et cetera. So we are factoring in a small amount in the later half of this year, like more likely in our Q4, but we certainly expect the momentum to build here over time.

James E. Fish
Analyst, Piper Sandler & Co.

Q

Helpful. Congrats, guys.

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

A

Thank you.

Operator: And thank you. And one moment for our next question. And our next question comes from Meta Marshall from Morgan Stanley. Your line is now open.

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

Q

Great. Thanks. Maybe just as a first question, understanding kind of the new customer cohort you guys have said is kind of a focus on higher quality and larger customers. Is there any way to quantify just in terms of what that cohort does in terms of kind of initial deal size or anything that kind of mix makes the point on that metric? And then just on kind of the reacceleration and kind of general elongation of sales cycles right now, do you think that, that is kind of the catalyst for that reverting in fiscal 2025 is purely macro, do you need to kind of see more multi-cloud spending like what is it just a matter of macro or what kind of do you think is the main catalyst for that reacceleration? Thanks.

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

A

Let me take a crack at the first part. Rukmini you can add on. So our new ASPs for – for these new logo ASPs are certainly up year-over-year for us given the focus. We haven't put a number on it, but perhaps one of the things we could do take that as an action for a Investor Day to come back to you with looking at, for example, how many customers we have with over $1 million for example of ARR. So we – it's a good question, Meta. We'll come back to you with more color. But in general, yes, new logo ASPs have been going up as a result of our focus.

Rukmini, you want to take the rest?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Sure. Yes. Hi, Meta. Thanks for the question. So I think you had a couple of things in there – woven into your question, Meta. So one was, I think, around just sort of sales cycles, right, which as we've talked about in the past, continues to – we continue to see a modest elongation there and that is really affecting only our sort of new and expansion business, right? And so that's sort of what we continue to see and some of those macro factors are factored into our 2024 outlook in the new and expansion portion.

Now – and then you referenced, I think, the reacceleration that we talked about in 2024 as it relates to our renewals ACV growth rate, so just again to reemphasize renewals, ACV will continue to grow year-over-year for quite a while as we've talked about in the past. What we said was a 2024 renewals ACV growth is at a slower pace in 2023 because of just some timing variations between 2023 and 2024 due to some co-terming but also largely due to just some timing as it relates to when customers choose to make their purchases because their budget cycles and so on. And so, we view that as affecting 2024, but when we look at available-to-renew pool for

2025, we see that reacceleration in 2025. So that's what we were referencing and I just wanted to make sure I was clear on the new and expansion portion versus the renewals, Meta. I hope that answers your question.

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

Q

Yeah, I know. That's perfect. Thank you.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Thank you.

Operator: And thank you. And one moment for our next question. And our next question comes from Mike Cikos from Needham. Your line is now open.

Mike Cikos
Analyst, Needham & Co. LLC

Q

Hey, team. Thanks for getting me on the line here. I did want to come back to the ACV billings for a second. And I know that – congrats on the outperformance on the guidance. I believe you guys cited outperformance stemming from specifically renewals when I think about the ACV billings. What drove that outperformance? Can you put some finer parameters around it? Whether it be – it sounds like macro was relatively stable but was it just better execution, potentially conservatism to the guide, like how do we view the different pieces that contributed to that outperformance you guys were able to generate?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Hi, Mike. Thanks for the question. So there were maybe a couple of components that I will talk to and I welcome Rajiv to – for you to add anything else that you would like. So the first one is that around renewals, right, what – when we – what we say when we mean renewals outperformance is that we see some quarter, I mean, as we've talked about before, which is sometimes more difficult to forecast. And we're also seeing continued improving discipline around renewals economics, which is what we transact the renewals as compared to sort of what the original transaction was, right? So those are the ones that are contributing to improvement in renewals outperformance. And so that was a big driver, I would say, Mike, of the outperformance in ACV billings. So that was really the largest driver of outperformance for Q4 ACV billings.

Mike Cikos
Analyst, Needham & Co. LLC

Q

Great. And I guess a two-parter on a follow-up. One kind of [ph] feeds off (00:41:23) the ACV billings again, but if I think about the guidance that we have today for Q1 ACV billings, it's actually down sequentially. And if I look over the most recent two years, you've gone up from Q4 to Q1. Can you help us think about why it would be down sequentially? Maybe part of it has to do with this co-terming effect or maybe some of those deals that came in, in Q4 from, let's say, the VMware deal that we cited earlier that came to you guys? That's the first question as far as the ACV billings guide being down in Q1 sequentially.

The second is gross margins. I know we cited a benefit from non-recurring savings and the timing of hiring. Can you help us unpack what or quantify what the non-recurring savings were or what that dollar figure was and then the timing of hiring? I guess, we should expect for you guys to hire into that in the out year or is this – this is hiring that's been – you guys can actually prove more efficient versus what you had initially anticipated?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.
A

Okay. Thank you, Mike. Let me take that one by one. So on the Q4 to Q1, our typical seasonality is actually Q1 being lower than Q4, Mike, typically because Q4 is a seasonally high quarter for us given it's the year end, right, and it's sort of – the sellers are motivated to go and have a good Q4. Last year was a bit of an anomaly, right, because if you recall in Q4 2022, we saw some of these impact from supply chain disruptions that were affecting our partners and therefore also impacting us to some degree, right? So the Q4 2022 number was actually probably artificially lower, which led to a sequential increase last year. This is more normal is how I would characterize that, Mike.

And then to your question on gross margin, so we said a few things there, right. So, one was revenue higher than expected. I think that's straightforward. And your question was on the other two. So what we say when we mean timing of hiring is [indiscernible] (00:43:20) attrition happens, normal levels of attrition, but sometimes it takes time to backfill and so on, right. So that can sometimes cross quarter boundaries. And so we saw some of that in Q4, those people we would be expect to be hired and backfilled in short order here, right, really probably in Q1.

And the non-recurring savings were not huge amounts, Mike, but just remember that I think Q4 also is a high gross margin year as well because COGS and operating expenses don't fluctuate as much over the year, but Q2 and Q4 are seasonally higher top line quarters for us, right. You will see that those margins pick up higher in Q2 and Q4 and tick a little bit lower in Q1 and Q3, which is why if you look at our overall fiscal year 2024 guide, we're saying gross margins approximately in that 84% range.

Mike Cikos
Analyst, Needham & Co. LLC
Q

Terrific. Thank you very much. I really appreciate all the color. Thank you.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.
A

Thank you, Mike.

Operator: And thank you. And one moment for our next question. And our next question comes from George Wang from Barclays. Your line is now open.

George Wang
Analyst, Barclays Capital, Inc.
Q

Hi. Hey, guys. Congrats on the quarter. I just want to ask about any update on the repatriation trends, especially given [ph] tougher (00:44:43) macro. Are you guys are seeing sort of increased repatriation to on-prem which may benefit Nutanix?

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

Yeah. So, George, I can't say that we've seen increased repatriation [ph] necessarily (00:44:54). We're certainly seeing instances of repatriation. What I would say is interesting is that we've also seen stuff in the other direction, which is people have committed to some of these large public cloud spend commitments. And what they're saying is they're not able to get their applications really into the public cloud as quickly as they like to see. And so they are now stuck with saying, I have to spend this much money in the public cloud because I committed to it already.

And so we've seen that come to us because now they're looking at [ph] this and saying (00:45:21) we are available through the marketplace of Azure and AWS. And we've seen people purchasing our software through the Azure and AWS marketplace, which helps them retire some of their commitment in public spend. So, yes, I think we see the world being hybrid. Some workloads are being repatriated from the public cloud. I wouldn't say it's necessarily a wholesale trend. We see [ph] that in spots (00:45:45) versus a systemic trend yet at this point. But the world is very much hybrid. People are being much more conscious about how much to put in the public cloud in the first place.

George Wang
Analyst, Barclays Capital, Inc.
Q

Okay. Great. Just a quick follow-up, if I can. [ph] With (00:46:01) simplified portfolio kind of platform approach, can you talk about kind of the attach rate to Nutanix Cloud Platform, Cloud Manager, and the kind of maybe high level commentary on cross-sell and upsell?

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

Yes. So I think two questions there. On the attach rate of the portfolio, for sure, the biggest change that we have seen since we launched our revised portfolio is much higher attach for cloud management along with our cloud infrastructure. In fact, that is the easiest attach sale, really, that everybody who builds a cloud also wants to operate the cloud. So naturally attaching cloud operations, cloud management to an infrastructure. That's the best we've seen.

We've also seen, of course, NC2, which is our public cloud extension is a natural extension, natural attach, and it's really – it ties together with our cloud platform very nicely. So that's another attach that is still relatively small for us, but growing every quarter in terms of customers, number of customers and customer count. Our Unified Storage is the other element of the portfolio that we see reasonable attach [ph] rate (00:47:01) as well.

The one that we have to actually really work with a specialist team to sell is our Nutanix Database portfolio because that's largely sold a level up in the stack to people who are either managing databases or app developers, and that requires more specialist skills and that's much more of a specialist sale.

George Wang
Analyst, Barclays Capital, Inc.
Q

Okay. Great. No, thanks. Congrats, again.

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

Thank you.

Operator: And thank you. And one moment for our next question. And our next question comes from Mehdi Hosseini from SIG. Your line is now open.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

Yes, sir. Thanks for taking my question. I want to go back to your fiscal year 2024 guide. If I just take the midpoint, it seems like OpEx would need to grow by 7%. And I understand your Analyst Day is coming, but would the collaboration or the deal with Cisco actually help ease some of these OpEx growth assumptions built into the model, or does that already take into account – or does that already account for any cost savings as Cisco scales your product [indiscernible] (00:48:28)?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Hi, Mehdi. Thank you for that question. So let me first address the OpEx point, then we'll talk about any potential impact from Cisco. So if you look at our operating expense profile over the last several years, since about three years ago, it was about $1.5 billion and last year it was $1.4 billion, right? [ph] It's (00:48:53) actually we've kind of really kept it sort of flat to down over the last three years while, of course, continuing to grow ACV billings, ARR revenue and so on since over that time. So we've been really sort of cautious about OpEx and in focusing on improved efficiency and productivity.

Where we are now is that we are making some very prudent, I would say, and targeted investments in our go-to-market and in our innovation engine. As we've talked about our market, we believe, is large and growing in order to go and capitalize on that. So we are making some targeted investments on that front.

Now, on the Cisco piece, I think what we expect the Cisco partnership for us to do is to continue to help sort of our productivity go up and really be additive to our overall top line, right? So that's how we should think about operating expenses relative to last year but also relative to any potential impact from Cisco.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

Okay. And one follow up for Rajiv. I just want to go back to your prepared remarks and I'm just trying to better understand, I kind of agree with you that security, privacy, compliance would actually bode well for enterprises to scale AI. But as you think about the train models moving from a cloud infrastructure into on-prem, would that actually require your existing or prospective customer with additional one-time CapEx investment or no?

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

A

Yeah. So that depends on what they have already – I mean, obviously, this AI requires compute resources, right? It requires several platforms with GPUs attached to it. So, clearly, these are new workloads for the customer, they're going to have to buy new hardware, right, and put our software on it. What they would do – just to clarify what they would do, these models, likely our foundational models that are trained on publicly available data in the public cloud. But then when they bring it on-prem, they're going to fine tune this and potentially make it more compact with their own specific data.

A good example just to see how this works, Mehdi, is take support as an example. Even [ph] after the (00:51:11) support – in terms of support, we have a lot of internal documentation that we don't put in the public cloud, internal design documents as well. So imagine using a Generative AI backend to be able to go through all of that and quickly try and arrive at root cause or try and arrive at answers to customer support questions. So we want to run that on-prem or in a secure location where our data is stored. And so, we would typically run that on, again, standard servers with GPU accelerators, running [ph] DCI (00:51:39) models with our stack.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP
Q

And is that where Cisco could come and actually become a partner to facilitate that additional investment required?

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

I think the Cisco piece, by the way, just – let me – I think we should decouple that, right, because this AI piece works with everybody's servers. So customers can buy servers from Dell or HP or Lenovo or any of our server partners, and we have a wide variety of them and [ph] we have been (00:52:06) supporting GPUs for multiple years. So we don't necessarily need this to be only Cisco. So they can buy that from whoever they like their server partner.

What we expect with Cisco is a significant expansion in terms of our go-to-market reach, right, with their go-to-market, their ability to sell into a much broader customer base and their footprint, we should be able to benefit from that in the long term.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP
Q

Got it. Thank you for the [ph] color (00:52:31).

Operator: And thank you.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.
A

Thank you.

Operator: And one moment for our next question. And our next question comes from Erik Suppiger from JMP Securities. Your line is now open.

Erik Suppiger
Analyst, JMP Securities LLC
Q

Yeah. Thanks for taking the question. And congrats on a good quarter. First off, on the GPT-in-a-Box. Are those customers developing their own large language model or are they using third-party software on that box? And then secondly...

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

[indiscernible] (00:53:10)

Erik Suppiger
Analyst, JMP Securities LLC
Q

...in the – well, go ahead.

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

A

Yeah. Erik, I think the answer is most of them would not build their own large language model. They would use foundational models that are available. For example, there's new ones coming out like Llama 2 that are open source. They could, of course, use GPT if they like as well. But there are multiple models. More customers in the enterprise, I don't think, will develop their own models but use what's available out there. They would probably fine tune it with the data that they have.

Erik Suppiger
Analyst, JMP Securities LLC

Q

Okay. That makes sense. And then secondly, in the partnership with Cisco, are the Cisco sales reps getting comped on selling the Nutanix software?

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

A

Yes, they're getting comped on it just as if they were selling a Cisco product. So 100% compensation for that service.

Erik Suppiger
Analyst, JMP Securities LLC

Q

Very good. Okay. Thank you.

Operator: And thank you. And one moment for our next question. And our next question comes from Wamsi Mohan from Bank of America. Your line is now open.

Ruplu Bhattacharya
Analyst, BofA Securities, Inc.

Q

Hi. Thanks for taking the question. It's Ruplu filling in for Wamsi today. I had one question for Rajiv and one for Rukmini. Rajiv, can you comment on a couple of things, specifically demand by vertical? You talked about some share gains this quarter. How is the pricing environment? Is that holding steady or are you seeing any pricing pressure? And then, can you talk about your view on the backlog heading into fiscal 2024? Has that normalized now or is it still elevated?

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

A

Yeah. So on the pricing, we haven't seen any significant change in pricing this quarter compared to our last quarter. And in general, as we, for example, attach more of our products [ph] with our portfolio to our deals, our deal ASPs (00:54:54) tend to go up, right, because we're simply attaching more of the portfolio. So we haven't seen any shift or big change in our pricing dynamics.

Now on the backlog – and with respect to verticals again, you know, I can't say that there's any significant difference. I think it's more a function of volume and deal size that dictate discounts and rather than any particular vertical related factors for us. Now with respect to the backlog, I'm going to let Rukmini comment on that.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Yes. Thank you, Rajiv. And hi, Ruplu. So on backlog, as we talked about, I think last year, fiscal year 2023, you know backlog, it did move around as expected during the course of fiscal year 2023. But despite that, we ended 2023 actually with a slight increase in absolute backlog dollars year-over-year. And we have factored that into the outlook for fiscal year 2024. So we expect some backlog to be consumed over the course of this year. But as is to be expected in an uncertain macro environment like the one we're in, I think the range of possible outcomes are just wider than usual. And more generally, as we continue to grow, the absolute dollar number of backlog could also continue to increase over time.

Ruplu Bhattacharya
Analyst, BofA Securities, Inc.

Q

Okay. Thanks for the details there. If I can ask you, looking at the guidance for fiscal 1Q versus the full year fiscal 2024, it looks like there is operating margin improvement as you go through the year. So what are the drivers for that? And then if you can talk about the seasonality you expect in ACV billings, again, looking to – should we think that going from 2Q to 3Q, should we expect the same level of decline? Your renewables business is growing. So is there any thoughts on how should we model ACV billings in fiscal 2024? Thank you.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Okay. So there were a couple of questions there, Ruplu. I think the first one was on Q1 operating margin versus full year. And so, I think I will just remind folks that again Q2 and Q4 are seasonally – in general seasonally stronger quarter for us, Q2, because you have December in there, which is annual budget flush for many customers. And so, Q2 is stronger for that reason and Q4 is our fiscal year end. And so, Q2 and Q4 seasonally strong quarters, which means that margins, although operating expenses and cost of goods sold don't vary as much, the top line does look stronger in Q2 and Q4, and therefore, margins in general also tend to look stronger in Q2 and Q4 compared to Q1 and Q3, right. So that's sort of one call out on the margin piece on the full year versus 1Q.

And then on seasonality, I think was your second question, Ruplu, more generally, I would just say, I think, as I've said, you should expect some seasonality in top line for a slight decline between 2Q to 3Q and that follow sort of a new and expansion. Therefore, generally renewals ATR also does follow that pattern as well, and to the extent we expect any variation in that, we'll make sure to call that out. But as of now, you should still expect somewhat fairly normal patterns with regard to that.

Ruplu Bhattacharya
Analyst, BofA Securities, Inc.

Q

Okay. Thanks for the details.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Thank you.

Operator: And thank you. And one moment for our next question. And our next question comes from Nehal Chokshi from Northland Capital Markets. Your line is now open.

Nehal Chokshi
Analyst, Northland Securities, Inc.

Q

Yeah. Thank you and congrats on a strong quarter, yet another one. That's fantastic. And nice to see the buyback being announced, could you talk about what is the priority of allocating capital to buybacks relative to say paying down debt?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Hi Nehal. Yeah. Sure. So, I'll just talk maybe more generally, our focus continues to be on sustainable, profitable growth, as we've said and we continue to make prudent and thoughtful investments into our go-to-market innovation engines, as I've said earlier in response to another question. We're happy to have generated over $200 million of cash flow last year and have $1.4 billion of cash and short-term investments. And so, we think of the share repurchase authorization as a reflection of the confidence in our long-term financial outlook by returning capital to shareholders while ensuring that we have optionality to continue to invest in growth and for our other strategic priorities.

And to your question on paying down debt and how, we do take a look at that. Of course, we look at all of the alternative uses of our cash before making any decision. And our public convert, we pay 25 basis points on those and they're not due for another few years. And so it made sense for us to think about that more holistically and sort of we believe that – doing the share repurchase authorization is sort of the best use of our cash given all of the other options available to us.

Nehal Chokshi
Analyst, Northland Securities, Inc.

Q

So, what's your anticipation of the pace of utilization of that buyback authorization then?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

We have not given a specific timeframe, Nehal, and the authorization does not have any expiration date. And so the timing and amount will depend on a variety of factors, as you can imagine, right, including just business condition, stock prices and other factors. And so, I'll leave that there.

Nehal Chokshi
Analyst, Northland Securities, Inc.

Q

Would it be fair to say that you want to return a certain percentage of free cash flow on a go-forward basis?

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

We are not giving sort of a certain percentage at this point, Nehal, but we will just talk more generally about capital allocation and how we plan to use our cash at our Investor Day as well, right? So, I'd be happy this will take more – we'll talk more about that then, but at this point, we're not committing to a specific percentage.

Nehal Chokshi
Analyst, Northland Securities, Inc.

Q

Okay. Great. Thank you and congrats.

Rukmini Sivaraman
Chief Financial Officer, Nutanix, Inc.

A

Thank you.

Operator: Thank you. And I am showing no further questions. This concludes today's conference call. Thank you for participating. You may now disconnect.