Qualys Q3 FY2022 Earnings Prepared Remarks

Foster City, Calif., – November 2, 2022 – Qualys, Inc. (NASDAQ: QLYS), a pioneer and leading provider of disruptive cloud-based IT, security, and compliance solutions, today announced financial results for the third quarter ended September 30, 2022.

Blair King, Investor Relations

Good afternoon and welcome to Qualys' third quarter 2022 earnings call.

Joining me today to discuss our results are Sumedh Thakar, our president and CEO, and Joo Mi Kim, our CFO. Before we get started, I would like to remind you that our remarks today will include forward-looking statements that generally relate to future events or our future financial or operating performance. Actual results may differ materially from these statements. Factors that could cause results to differ materially are set forth in today's press release and our filings with the SEC, including our latest Form 10-Q and 10-K. Any forward-looking statements that we make on this call are based on assumptions as of today, and we undertake no obligation to update these statements as a result of new information or future events.

During this call, we will present both GAAP and non-GAAP financial measures. A reconciliation of GAAP to non-GAAP measures is included in today's earnings press release. As a reminder, the press release, prepared remarks, and investor presentation are available on the Investor Relations section of our website. With that, I'd like to turn the call over to Sumedh.

Sumedh Thakar, president and CEO

Thank you Blair, and welcome everyone to our third quarter earnings call. Qualys again delivered another quarter of strong revenue growth and cash flow generation while further executing on a focused investment strategy.

Q3 Business Update

Given the accelerated growth in scope and complexity of cyber threats and an uncertain macroeconomic and geopolitical landscape, CISOs and CIOs continue to broadly prioritize natively integrated security solutions to both fortify their security posture and optimize budgets through a reduction of agents and response times to reduce risk and cut costs.

As a result, Qualys experienced another quarter of steady Vulnerability Management, Detection and Response, or VMDR®, adoption, which is now deployed by 45% of our customers worldwide. Key competitive VMDR wins in the quarter included multiple customers both down market and in the Forbes 1000.

The strength of Qualys' VMDR solution has clear momentum in the market and is garnishing significant industry recognition. As recently announced, Qualys' VMDR application was voted the

best vulnerability management solution at the 2022 SC Awards. This award evaluates vendors based on input from security practitioners worldwide and held in high esteem. We believe Qualys' placement as the number one vulnerability management solution further validates our investments in the platform and represents the standard for securing customer environments today, and in the future.

With multiple long-term growth drivers in our business, I'll take a moment to share some of the early successes we're seeing to broaden platform adoption with customers and partners. On the customer front, in a highly strategic and competitive win, a large government agency entered into a seven-figure upsell agreement to expand its asset count with VMDR, and Patch Management after selecting Cybersecurity Asset Management, Policy Compliance and Multi-Vector Endpoint Detection and Response, as part of an initiative to transform its IT security architecture. This customer selected Qualys because we offer the only security and compliance stack available in the market today that utilizes a FedRamp authorized platform and single light-weight agent to enable full asset visibility and context-aware mapping to prioritize vulnerabilities, proactively reduce technical debt, automate patching and continuously monitor endpoints with high-fidelity telemetry to defend against future Malware and Ransomware events across multiple environments.

In Q3, we also expanded our engagement with a Fortune 100 company in a competitive mid-six figure upsell. This customer selected Qualys' Cybersecurity Asset Management, Policy Compliance and VMDR capabilities. The ability to significantly enhance its security program with comprehensive internal and external asset context, CMDB integration, alerting, prioritization and accurate response capabilities with built-in ticketing and compliance monitoring on a single console while consolidating agents were all key differentiators in this win.

Beyond these wins, we continued to see new customers adopt Cybersecurity Asset Management and Patch Management alongside VMDR. Instead of just being a one-dimensional tool used to detect and produce a list of Vulnerabilities, these new competitive wins underpin Qualys' ability to help customers not only detect, but also prioritize risk across all assets while remediating vulnerabilities much faster than alternative siloed solutions. This is becoming an even stronger value proposition in the current macroeconomic environment as customers increasingly seek multiple security offerings and capabilities out of a single Qualys platform.

Investing in our partner ecosystem continues to be a key pillar in our go-to-market agenda. In the quarter, we expanded our relationships with several MSSPs and entered into a new partnership with a cyber security insurance company to enable reduced premiums for their customers using VMDR with TruRisk. We also extended our strategic alliance with IBM. Through this collaboration, Qualys solutions are being positioned as key platform for securing IBM's zLinux mainframe infrastructure to bring highly accurate vulnerability detection and compliance capabilities to several of the world's largest financial institutions while utilizing the same Qualys agent. Additionally, we continue to see an increase in new customer deal registrations by our partners. We believe the expansion of our partner program since its launch in May reflects our strengthening brand awareness and strategic position in the market.

Platform Innovation

A cornerstone of our strategy is engineering innovation, and we challenge ourselves every day to lead the industry. While we've been focused on helping customers secure their cloud and container environments for some time now, our recent launch of TotalCloud further flexes the

power of our platform by enabling cloud-native VMDR with FlexScan. By pairing agent and agentless zero-touch assessment options with high efficacy vulnerability detection and prioritization capabilities, organizations can now extend the platform to continuously view all cloud assets, visualize the entire external attack surface, and reduce risk by rapidly remediating and preventing misconfigurations and vulnerabilities from build to runtime. With Qualys agents already securing over 30 million workloads in the cloud, we believe this solution provides the most holistic, flexible and accurate approach to modern cloud and container security available in the market today.

We will showcase TotalCloud with FlexScan at our upcoming Qualys Security Conference (QSC) in Las Vegas from November 7th to 10th. We already have over 900 people registered to attend and welcome all of you to access the agenda and register at qualys.com. At this conference our product and engineering teams will showcase the innovation on Qualys platform and our customers will talk about their success with Qualys including focused conversation on how they have been able to save costs in their security program by moving to a unified Qualys platform with single agent.

And, with vulnerabilities proliferating at an unprecedented pace in the face of a growing cybersecurity skills gap, now, more than ever, architecture matters. With the recently announced acquisition of Blue Hexagon, Qualys can now apply cloud scale Artificial Intelligence and Machine Learning capabilities to the Qualys Cloud Platform and its more than 13 trillion data points collected from over 100 thousand network scanners and over 90 million cloud agents. What makes this combination so significant is its ability to discover and identify relationships and patterns within our highly integrated data lake to rapidly predict and detect anomalous activities in customer environments that are invisible and undetectable in traditional security solutions. Specifically, upon integration, this capability will allow Qualys customers to detect active vulnerability exploitation, identify advanced network threats and enable adaptive risk mitigation, including real-time zero-day threat detection across all assets, applications and environments. This is a uniquely powerful new addition to the Qualys Cloud Platform and we're pleased to welcome some of the best security minds and associated innovations in Artificial Intelligence and Machine Learning to the Qualys family.

In summary, we continue to pioneer and define a security cloud category built to solve modern security challenges. And, given the large market opportunity in front of us with multiple growth engines in our business, we anticipate that we can grow at scale long-term, generate cash and continue to invest in key initiatives that will further extend the gap between Qualys and the competition.

With that, I'll turn the call over to Joo Mi to discuss in more detail our third quarter results and outlook for the fourth quarter and full-year 2022.

Joo Mi Kim, Chief Financial Officer

Thanks, Sumedh, and good afternoon. Before I start, I'd like to note that, except for revenue, all financial figures are non-GAAP and growth rates are based on comparisons to the prior year period, unless stated otherwise.

We're pleased to announce another quarter of strong revenue growth and healthy cash flow generation.

- Revenues for the third quarter of 2022 grew 20% to $125.6 million, up from 13% growth in the year ago period. LTM calculated current billings grew 18%.

  - Our net dollar expansion rate speaks to the power of our platform and improving land and expand sales model, driving year-over-year increases over the past several quarters. In Q3, our net dollar expansion rate on a constant currency basis was 111%, up from 104% a year ago.

  - Our LTM average deal size increased 18% as organizations continued to turn to Qualys to solve modern security challenges through cloud-native platforms that aggregate and analyze data in the cloud, operate at web scale, leverage network effects to produce superior outcomes, and are easy to deploy and simple to manage.

- Vulnerability management continues to be a cornerstone of customers' security programs by enabling real-time visibility of their security posture. Qualys' unified platform approach differentiates itself from other vulnerability reporting only solutions through an integrated combination of capabilities, including comprehensive asset discovery, rapid risk detection, prioritization and remediation on a single agent. In Q3, total customer penetration for VMDR was at 45%, up from 32% a year ago.

  - We're also pleased with the continued adoption of our newer products like Patch Management and Cyber Security Asset Management. In Q3, on an LTM basis, the two products combined contributed to 8% of total bookings and 15% of new bookings, with both applications growing over 50% from last year.

- Continued adoption of Qualys solutions increased large customer spend with 151 customers spending $500,000 or more with us. This represents 29% growth from the year ago period and speaks to the strategic role we are playing in our customers' digital transformation initiatives.

We remain focused on leveraging our scalable platform model to continue to drive superior margins and significant cash flow:

- Adjusted EBITDA for the third quarter of 2022 was $54.9 million, representing a 44% margin;

- EPS for the third quarter of 2022 was $0.94; and

- Our free cash flow for the third quarter of 2022 was $40.9 million, representing a 33% margin. Year-to-date margin was 40%.

In Q3, we continued to invest the cash we generated from operations back into Qualys including:

- $1.2 million on capital expenditures; and

- $95.0 million to repurchase 684 thousand of our outstanding shares.

  - With a long history of demonstrated strong profitable growth through times of uncertainty and volatility, we plan to continue to return excess cash to shareholders. As of the end of the quarter, we had $259 million remaining in our share repurchase program.

Shifting now to guidance for the fourth quarter and full year, we are raising the bottom and top ends of our full year 2022 revenue and EPS guidance. While cyber security budgets remain

largely unchanged, this guidance continues to reflect our pragmatic outlook regarding the uncertain global macroeconomic backdrop. Our guidance also reflects the planned increase in investments this year while not losing sight of the importance of optimization as we remain committed to driving long-term profitable growth. Specifically, these investments continue to include the expansion of our partner programs and enhancing our relationships to leverage their large distribution networks. Alongside this, we will continue to invest in digital marketing initiatives and expand product management capabilities as well as sales capacity and support functions. Additionally, as Sumedh touched on earlier, shortly after quarter end, we announced the acquisition of Blue Hexagon. This is expected to have a de minimis impact on full year results. With that:

- Full year revenue is expected to now be in the range of $488.6 million to $489.6 million, representing a 19% growth. This compares to prior full year revenue guidance of $488.0 million to $489.5 million.

- In terms of profitability, we are raising our full year EPS guidance to now be in the range of $3.60 to $3.62 from the prior range of $3.50 to $3.55. This implies an EBITDA margin in the mid-40s.

- For the fourth quarter, we expect revenues to be in a range of $129.7 million to $130.7 million, which represents 18% to 19% growth. We expect EPS to be in a range of $0.89 to $0.91.

- Our planned capital expenditures in Q4 is approximately $2.5 million to $3.5 million and for the full year 2022, we expect investment in the range of $15 million to $17 million.

In conclusion, we believe our product differentiation will enable us to improve our competitive edge and drive durable top-line growth while leveraging our highly scalable model to maintain strong cash flow and industry-leading profitability. We believe that with customers becoming more cost-conscious with heightened scrutiny of their security spend, we will continue to see higher levels of customer interest associated with the value proposition of consolidating vendors on a single agent and see that dynamic playing well for Qualys long-term.

With that, Sumedh and I are happy to answer any of your questions.