



Qualys Q2 FY2024 Earnings Prepared Remarks

Foster City, Calif., – Aug 6, 2024 – Qualys, Inc. (NASDAQ: QLYS), a leading provider of disruptive cloud-based IT, security, and compliance solutions, today announced financial results for the second quarter ended June 30, 2024.

Blair King, Investor Relations

Good afternoon and welcome to Qualys' second quarter 2024 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

Thanks, Blair, and welcome to our second quarter earnings call.

In Q2, we witnessed organizations increasingly optimize spend within an already tight IT spending environment. Given this dynamic, organizations are standardizing on trusted platforms to consolidate security stacks, leverage automation, and achieve expedient remediation of risk. Qualys has a unique, organically built platform to address this need. Nevertheless, crisp execution is required to fully capitalize on this opportunity. While we've made meaningful progress on several fronts, including growing our Sales and Marketing team, building momentum with partners, and growing new business, we have work to do in addressing our upsell execution in the current environment, which resulted in lower-than-expected bookings growth this quarter. With the upcoming departure of our Chief Product Officer later this month, I plan to directly oversee the product and marketing teams to position us for forward success. I am confident in our ability to re-accelerate growth in the long-term with sharpened execution on product-led growth and improved alignment between our product messaging and marketing activities to drive operational efficiencies in our go-to-market motion. At this time, I'd like to thank Pinkesh Shah, our Chief Product Officer, for his contributions during his tenure at Qualys.

Although Q2 was a challenging upsell quarter for us with continued increase in deal scrutiny, we're

fortunate that many of our customers have already begun a long-term transformation journey with us. Through the conversations I've had with many CISOs over the past several quarters, their message is clear; they are looking to pivot to a natively integrated risk management solution. In the face of a sluggish macro, escalated threat environment, and cyber security skills gap, organizations need to reduce complexity and costs while presenting measurable risk reduction initiatives to Boards and C-level executives.

Against this backdrop, Q2 was another quarter of rapid innovation for Qualys, reflecting our ongoing commitment to technology leadership and customer success.

Platform Innovation:

Qualys' mission has been to bring innovative new security solutions to market fueled by customer insights. As a result, we have established a strong track record of converting operational challenges into structural competitive advantages while maximizing lifetime value, ensuring frictionless outcomes at scale, and driving immediate ROI on security spend.

For example, Qualys pioneered a patching category for security teams. Building on this success, we commenced development of our TruRisk Eliminate capabilities several quarters ago. I'm now pleased to announce that some of these increasingly popular solutions amongst our beta customers will soon enable organizations to respond to zero-day threats and mitigate top exploitable vulnerabilities even when a patch is nonexistent or cannot be deployed. This new subset of our broader TruRisk Eliminate roadmap, which we call TruRisk Mitigate and TruRisk Isolate, empower security teams to apply flexible, automated, and intelligent risk-based response solutions to address cyber risk based on an organization's own unique operational characteristics, remediation timelines, and business objectives. With these new capabilities soon going GA, strong customer support, and over 45 million patches deployed year-to-date on Qualys agents, we're increasingly confident that we're once again transforming our customer's security operations while further magnifying our competitive differentiation in the market.

Continuing our innovation to help our customers address risk coming from use of latest technologies like AI/Large Learning Model (LLM), we are pleased to announce our newest capability, which we call Qualys TotalAI. As organizations rapidly deploy AI/LLM technologies, the security teams are looking for help to quickly find and comprehensively assess vulnerabilities in these models. With seamless AI Security Posture Management (AISPM) integration, these new adaptive capabilities discover AI/LLM usage within customer environments, scan for vulnerabilities, and prevent data leakage for comprehensive risk assessment, prioritization, and remediation across the entire attack surface with a single click of a button.

In addition, we are pleased to announce an extension to our TotalCloud Cloud Native Application Protection Platform (CNAPP), which now discovers and assesses the risk of all known and unknown in-use Kubernetes container images. Leveraging our own AI and Machine Learning (ML) technologies, we are establishing a baseline of normal behavior for each host, container, serverless function, and other objects. Now, through real-time observation of file systems, processes, and network activity, our newest runtime security tools provide organizations with predictive and threat-based protection to actively detect anomalous activities, prevent zero-day attacks, automate response, and help ensure Payment Card Industry Data Security Standard (PCI DSS) 4.0 compliance in both containerized and legacy environments. These new container runtime insights, combined with toxic risk factors within a unified, actionable dashboard allow for immediate threat quantification, prioritization, and remediation from code to cluster. We believe

this new capability uniquely sets us apart to enable secure and compliant cloud consumption at scale.

Turning to our federal agenda, we recently received FedRAMP Moderate certification for our TotalCloud CNAPP and Endpoint Detection and Response (EDR) solutions, marking another key milestone for the company. We continue to expect our pending FedRamp High certification for several key applications later this year, making Qualys the only modern alternative to legacy on-prem scanners for federal, state, and local government agencies at the High Impact level. Our investments to establish a public sector presence are starting to yield results, supporting our confidence to address this new vertical and drive incremental growth in the business over time.

Finally, with respect to our upcoming Enterprise TruRisk Management solution, we remain on track for GA later this year. This extension to our platform is currently in private beta with select design partners. The ability to bring first and third-party data into our platform to holistically detect, quantify, prioritize, and remediate vulnerabilities with automated workflows on a unified dashboard across on-prem, cloud, and multi-cloud environments is evolving into the go-to risk management solution for enterprises, especially within the context of a tight spending environment. The early customer feedback we're receiving is very positive, and it's great to see CISOs from around the world actively attend and engage in the many risk quantification workshops we've been conducting over the past several months.

These innovative new approaches to cybersecurity risk management, along with several others we're showcasing at Black Hat this week, allow our customers to reduce complexity and cost; and, of equal importance, create multidimensional paths for durable long-term growth in our business.

Q2 Business Update:

Moving to our business update. We believe that with continued deal scrutiny comes greater opportunity for Qualys over the long term as our natively integrated risk management platform helps customers consolidate technologies and achieve better outcomes with less time, fewer resources, and immediate ROI.

With many of our customers already embracing Qualys to help rearchitect and consolidate their stack, Qualys' Vulnerability Management, Detection, and Response (VMDR®) solution has translated into an enviable customer base, deep penetration, and significant industry recognition. As recently announced, Qualys' VMDR with TruRisk was voted the best vulnerability management solution at the 2024 SC Awards Europe for the second consecutive year. We believe Qualys' placement as the number one vulnerability management solution further validates our investments in the platform and continues to represent the gold standard for securing customer environments today, and in the future.

Given Qualys' blueprint for delivering greater value to customers, our VMDR solution with TruRisk is not only fueling new logo lands, but also helping to increase platform adoption, especially in the areas of Cybersecurity Asset Management with External Attack Surface Management (EASM), Patch Management, and Cloud Security. Let me share a couple of recent wins with new customers, which illustrate why companies turn to Qualys to help consolidate their security tools and improve their security posture.

In Q2, a large federal government agency became a customer of Qualys. This new customer was previously using multiple legacy and next-gen solutions to manage a variety of risk

management use cases across their security, IT, and DevOps teams. In addition to the complexity of using multiple point products, this government agency was frustrated with increasing costs associated with on-prem deployments. Looking to migrate to a natively integrated, cloud-based, FedRamp High Impact level Ready solution that meets the Cybersecurity and Infrastructure Security Agency (CISA) Binding Operational Directives (BOD), they replaced two of their existing vendors in a high six-figure bookings Phase One deployment using multiple Qualys modules right out of the gate. These initial deployments included Cybersecurity Asset Management with EASM, VMDR with TruRisk, and Patch Management. Through this highly strategic and competitive win, this customer is now able to leverage unified dashboards that provide them with greater insights and automation than any of the competitive products they evaluated, while taking full advantage of the speed and scale of an integrated platform. This win is a further testament to the investments we're making to expand our federal business, and we were also pleased with the turn-out and encouraging feedback from many large government agencies at our first public sector cyber risk conference in May.

In a second new high six-figure customer win, a hyper-growth Cloud Native SaaS business standardized on the Qualys Enterprise TruRisk Platform. This company's security team struggled with managing multiple consoles, lack of integration, complex workflows, missed detections, and extended remediation times, which restricted their ability to protect themselves. This customer is now consolidating on the Qualys Enterprise TruRisk Management Platform, replacing several competing vendors through a natively integrated multiproduct solution including Cybersecurity Asset Management with EASM, VMDR with TruRisk, Patch Management, and our TotalCloud CNAPP applications. Now, with a comprehensive multi-sensor solution, single user interface, and single platform, they have complete visibility and automated remediation across their endpoints and multi-cloud environments.

With seamlessly integrated solutions delivered natively on our platform to solve modern security challenges, more and more Qualys customers are beginning to understand how cybersecurity transformation drives better security outcomes, saves time, and costs less. As a result, customers spending \$500,000 or more with us in Q2 grew 18% from a year ago to 199.

Beyond these wins, we're also increasingly gaining leverage from our partner ecosystem. Our pipeline of business opportunities with partners continues to grow, and our partner-led win rates increased again in Q2. As our market perception and brand awareness continue to strengthen, we anticipate partner integration with our platform will continue to increase, further strengthening our strategic position, expanding our ecosystem, and broadening our reach.

In summary, our rapid innovation engine underscores our growing thought leadership and the value proposition we deliver to customers seeking to transform, consolidate, and fortify their security posture. Given the large market opportunity in front of us and multiple growth drivers in our business, we anticipate that we can grow at scale long-term, generate cash, and 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 second quarter results and outlook for the third quarter and full year 2024.

Joo Mi Kim, Chief Financial Officer

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

period, unless stated otherwise.

Turning to second quarter results, revenues grew 8% to \$148.7 million with channel continuing to increase its contribution, making up 46% of total revenues compared to 43% a year ago. As a result of our continued commitment to leverage our partner ecosystem to drive growth, we were able to grow revenues from channel partners by 17%, outpacing direct, which grew 2%. By geo, 14% growth outside the US was ahead of our domestic business, which grew 5%. US and international revenue mix was 58% and 42%, respectively.

As for calculated current billings, we would like to note that our Q2 calculated current billings were negatively impacted by the sunset of our embedded solution for Microsoft Defender as of May 1st. Earlier this year, we announced that we will be retiring our integration on Microsoft Defender and transitioning to BYOL model. Since this went into effect in Q2, we have been fielding inbound calls from former Qualys on Microsoft Defender users and working closely with them to ensure that they understand the value of our Cloud Security solution, TotalCloud CNAPP. Normalized for this change, our calculated current billings growth would have been 1%.

In Q2, with a continued challenging spend environment resulting in lower performance in upsell, our net dollar expansion rate declined to 102% from 104% last quarter. Conversely, we continue to see strong returns on our new business initiatives and achieved double digit new bookings growth for the fourth consecutive quarter. With this momentum in new customer bookings growth, we believe we're building a stronger foundation to drive expansion and share gains over time.

In terms of product contribution to bookings, Patch Management and Cybersecurity Asset Management combined made up 13% of LTM bookings and 22% of LTM new bookings in Q2. Cloud Security solution, TotalCloud CNAPP, made up 4% of LTM bookings.

Turning to profitability, reflecting our scalable and sustainable business model, adjusted EBITDA in Q2 was \$69.9 million, representing a 47% margin, compared to a 48% margin a year ago. Operating expenses in Q2 increased by 10% to \$59.0 million, primarily driven by a 22% increase in Sales and Marketing investments aimed at capturing the market opportunities in front of us. As we continue to increase our investment intensity and focus on Sales & Marketing enablement, customer success, and productivity, we believe we will be able to drive wallet share and long-term returns.

EPS for the second quarter of 2024 was \$1.52, and our free cash flow was \$48.8 million, representing a 33% margin, compared to 37% in the prior year. In Q2, we continued to invest the cash we generated from operations back into Qualys, including \$1.0 million on capital expenditures and \$35 million to repurchase 233 thousand of our outstanding shares. As of the end of the quarter, we had \$230.7 million remaining in our share repurchase program.

With that, let us turn to guidance, starting with revenues: For the full year 2024, we are now expecting our revenues to be in the range of \$597.5 to \$601.5 million, which represents a growth rate of 8%. This compares to revenue guidance of \$601.5 to \$608.5 million last quarter. For the third quarter of 2024, we expect revenues to be in the range of \$149.8 to \$151.8 million, representing a growth rate of 5% to 7%. This guidance assumes continued deal scrutiny and no improvement to our net dollar expansion rate through the back half of this year.

Shifting to profitability guidance, for the full year 2024, we expect EBITDA margin of 43% to

44%, and free cash flow margin in the mid-to-high 30s. We expect full year EPS to be in the range of \$5.46 to \$5.62, up from the prior range of \$5.06 to \$5.30. For the third quarter of 2024, we expect EPS to be in the range of \$1.28 to \$1.36. Our planned capital expenditures in 2024 are expected to be in the range of \$12 to \$16 million; and, for the third quarter of 2024, in the range of \$4 to \$7 million.

Consistent with prior guidance, for the remainder of 2024, we intend to align our product and marketing investments to focus on specific initiatives aimed at driving more pipeline, supporting sales, including enhancing our partner program, and expanding our federal vertical. As a percentage of revenues, we expect to prioritize an increase in investments in Sales & Marketing as well as related support functions, systems, and people with more modest increases in engineering and G&A.

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