



Qualys Q3 FY2019 Earnings Prepared Remarks

Foster City, Calif., – October 30, 2019 – Qualys, Inc. (NASDAQ: QLYS), a pioneer and leading provider of cloud-based security and compliance solutions, today announced financial results for the third quarter ended September 30, 2019.

Vinayak Rao, Investor Relations

Good afternoon and welcome to Qualys' third quarter 2019 earnings call.

Joining me today to discuss our results are Philippe Courtot, our chairman and CEO, and Melissa Fisher, 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 in 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, investor presentation, and supplemental historical financial spreadsheet are available on our website. With that, I'd like to turn the call over to Philippe.

Philippe Courtot, Chairman and CEO

Thank you and welcome everyone to our Q3 earnings call.

Melissa and I are pleased to report another solid quarter in terms of revenue growth and profitability. We are also very pleased to report strong growth in our paid Cloud Agent subscriptions, with almost 28 million now, 93% growth from prior year quarter. As discussed before, our Cloud Agent is the technology platform for seven security, compliance and IT solutions available now – namely Vulnerability Management, Policy Compliance, File Integrity Monitoring, Indication of Compromise, Patch Management, Asset Inventory and the upcoming Certificate Management – with more to come. In terms of our newer solutions, we saw strong growth again this quarter from FIM and we continue to build a healthy pipeline in Patch Management and Container Security.

At Black Hat this quarter, we launched our Global IT Asset Discovery and Inventory App as a free service. We received very positive feedback from customers and industry luminaries because global IT asset inventory is one of the biggest challenges, if not the biggest challenge, for organizations. Visibility is the cornerstone of security as you simply cannot secure what you do not know or see. With our free service, companies of all sizes can automatically build their global IT asset inventory across on-premises, endpoints, cloud, containers and now, mobile environments as well as identify in real-time everything that connects to their networks. Only two and a half months after the launch, we have approximately 3,650 companies signed-up with over 500 new customers using the service. We have also been rolling out the free service to existing customers since last month and now have almost 300 existing customers using it.

As a result, our goal to make our Cloud Agents ubiquitous is now well on its way and allows us to make the subscription to our paid apps frictionless because no additional infrastructure is required. Distributing such a free solution from our platform to generate meaningful demand of our paid apps is one of the key elements of our profitable growth, driving value for both our customers and shareholders. Furthermore, this multi-product adoption naturally increases the stickiness of our platform and helps make us impenetrable to our competition, who do not offer the same breadth of solutions. This is underscored by the fact that the gross dollar retention rate of enterprise customers who have adopted 4 solutions or more stands at 99%.

We continue to invest in expanding the capabilities of our Cloud Platform and developing additional solutions and we will showcase significant new offerings at our upcoming QSC user conference in Las Vegas on November 20th and 21st. At the conference:

- Our attendees will have the opportunity to listen to industry experts such as Richard Clarke, author of The Fifth Domain, Scott Crawford from 451 Research as well as Ramesh Chinta from Microsoft Azure who will discuss how Microsoft is building security into Azure, and Charles Henderson from IBM XForce Red who will talk about their efforts to automate pen testing and more quickly respond to eliminating vulnerabilities. You will also hear fascinating presentations from our customers who will share their experiences and best practices, their views on how their security needs are evolving and how mission critical Qualys is becoming for them;
- Our President and Chief Product Officer Sumedh Thakar will unveil our next gen Vulnerability Management offering that brings it to its next level and showcase our forthcoming EDR and Data Lake / SIEM initiatives; and
- In addition, among other innovative solutions, we'll discuss:
 - The forthcoming updates to our Container Security solution; and
 - Threat hunting with Qualys.

Click [here](#) to see agenda.

I would like to personally invite you to both our user conference and a dedicated institutional investor and analyst session that will occur during the conference on November 20th. This event will focus on how Qualys is driving sustainable long-term profitable growth and will include a demonstration of our newest applications in the platform as well as a Q&A session with select Qualys customers. You can register [here](#).

Finally, the significant expansion of our Cloud platform, which now delivers an impressive suite of security and compliance solutions, as well as our buildout of operations in Pune, where we have more than 750 employees, was led by our Chief Product Officer Sumedh Thakar and I am delighted to announce his promotion to President and Chief Product Officer; Sumedh started at Qualys in 2003 and through outstanding performance, now runs R&D, QA, Ops, Product Marketing, Customer Support and with the promotion, Worldwide Field Operations. As we continue to lay the foundation for our future growth, we also promoted Laurie MacCarthy to EVP, Worldwide Field Operations; Laurie joined Qualys in 2012 and was most recently, VP Field Operations, Americas. In addition, we promoted Dilip Bachwani to SVP, Cloud Platform, Ops and Dev Ops; Dilip joined Qualys in 2016 and was our VP, Dev Ops. Finally, we welcome the addition of Mustafa Mahudhawala as our VP of Global Customer Service.

Our product and platform achievements and expansion of our management team lays the foundation for our continued progress to enable customers to consolidate their security, IT and compliance stacks while drastically reducing their spend. As importantly, it is core to the highly profitable recurring and growing revenue model we have built.

With that, I'll turn the call over to Melissa to discuss our financial results.

Melissa Fisher, Chief Financial Officer

Thanks, Philippe 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 delighted with our increasing Cloud Agent subscriptions and multi-product adoption, which lays the foundation for future revenue growth and industry-leading profitability. Our Q3 financial and operational highlights include:

- Revenues for the third quarter of 2019 grew 15% to \$82.7 million;
- Platform adoption continued to increase as the percentage of enterprise customers with three or more Qualys solutions rose to 46% from 39% and the percentage of enterprise customers with four or more Qualys solutions increased to 26% from 20%;
- Paid Cloud Agent subscriptions increased to 27.9 million over the last twelve months, up from 23.6 million for the 12 months ended in Q2 2019. Two million additional Cloud Agents were purchased this quarter by a single cloud platform customer;
- New products released since 2015 contributed approximately 33% of total bookings in the quarter, up from 23%; and
- Our average deal size continues to increase, growing 8%.

Our scalable platform model continues to drive superior margins and generate significant cash flow:

- Adjusted EBITDA for the third quarter of 2019 was \$39.2 million, representing a 47% margin versus 45%. We continued to increase our headcount sequentially and we benefited from attracting great talent in Pune as well as lower non-salary headcount costs and lower third-party expenses this quarter as compared to Q2 2019;

- Q3 EPS grew 34%; and
- We generated strong free cash flow for the third quarter of 2019 of \$39.9 million, and year to date, our free cash flow has increased 36% versus the same period last year.

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

- \$5.8 million on capital expenditures, including principal payments under capital lease obligations; and
- \$49.8 million to repurchase 603,417 of our outstanding shares. Our Board has authorized an additional 2-year \$100 million open market share repurchase program, resulting in approximately \$141 million in current share repurchase capacity.

We remain confident in our model driven by our foundation of recurring revenues and expanding suite of applications:

- Our current FY 2019 revenue guidance is now a range of \$321.2 million to \$321.8 million;
- We are raising FY2019 non-GAAP EPS guidance from a range of \$2.03 to \$2.07 to a range of \$2.28 to \$2.30. We now expect to expand EBITDA margins this year and we expect our FY2019 EBITDA margin to be between 42.5% and 43%; and
- For the fourth quarter, we expect capital expenditures to be in the range of \$9 million to \$10 million, which includes approximately \$3.5 million for the first phase of the buildout of a new Qualys office in Pune.

We are very excited by the robust early adoption of our free Global Asset Discovery and Inventory application, which makes it frictionless to enable many of our paid subscriptions. This provides us the opportunity to accelerate revenue growth as well as expand margins in the future. As Philippe mentioned, we look forward to seeing many of you at the analyst and investor luncheon at our upcoming QSC user conference in Las Vegas.

With that, I'll turn the call back to Philippe.

Philippe Courtot, Chairman and CEO

Thanks Melissa. In summary, and as Melissa said, we are really happy with the progress made in expanding our Cloud Platform and the increased adoption of our solutions by our existing enterprise and SME/SMB customer base as well as new customers.

In addition, let me reiterate the invitation we are extending for you to attend both our user conference and investor session. The investor session will also be webcasted for those who cannot attend in person. Please register on our website and peruse the agenda for one or both events. Melissa, Sumedh, Laurie and I all hope you can attend.

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