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Teradata Corp. (TDC)

Q3 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. My name is Cameron and I'll be your conference operator today. At this time, I would like to welcome everyone to the Teradata Third Quarter 2024 Earnings Call. All lines have been placed on mute to prevent any background noise. After the speakers remarks, there will be a question-and-answer session. [Operator Instructions] .

I would now like to hand the conference over to your host today, Chad Bennett, Senior Vice President of Investor Relations and Corporate Development. You may begin your conference.

Chad Michael Bennett

Analyst, Teradata Corp.

Good afternoon and welcome to Teradata's 2024 third quarter earnings call. Steve McMillan, Teradata's President and Chief Executive Officer, will lead our call today followed by Claire Bramley, Teradata's Chief Financial Officer, who will discuss our financial results and outlook.

Our discussion today includes forecasts and other information that are considered forward-looking statements. While these statements reflect our current outlook, they are subject to a number of risks and uncertainties that could cause actual results to differ materially.

These risk factors are described in today's earnings release and in our SEC filings, including our most recent Form 10-K and in the Form 10-Q for the quarter ended September 30, 2024, that is expected to be filed with the SEC within the next few days.

These forward-looking statements are made as of today, and we undertake no duty or obligation to update them. On today's call, we will be discussing certain non-GAAP financial measures which exclude such items as stock-based compensation expense and other special items described in our earnings release.

We will also discuss other non-GAAP items such as free cash flow, constant currency comparisons and 2024 revenue and ARR growth outlook in constant currency.

Unless stated otherwise, all numbers and results discussed on today's call are on a non-GAAP basis. A reconciliation of non-GAAP to GAAP measures is included in our earnings release, which is accessible on our Investor Relations page of our website at investor.teradata.com. A replay of this conference call will be available later today on our website.

And now I will turn the call over to Steve.

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

Thanks, Chad. And thanks, everyone, for joining us today. In Q3, Teradata grew our cloud business, delivered enhanced technology innovations that strengthen our hybrid trusted AI position and added to our partner ecosystem all core elements of our strategic plan.

Cloud ARR grew 26% year-over-year as reported in Q3, with a solid cloud net expansion rate of 120%. And we have already closed one eight figure cloud deal in the fourth quarter.

Despite strong growth in cloud ARR, we have recently seen a change in our large transformational deals. Customers are planning to migrate workloads to the cloud in a more staged process.

The total customer spend with Teradata is unchanged and there is no impact on our total ARR. However, this shift results in a reduction to our cloud ARR and we are therefore lowering our 2024 outlook to 18% to 22% for the full year.

We see an ongoing healthy growth in our cloud business and continued migrations, which we anticipate is going to help us increase the mix of cloud in the future and help drive total ARR growth in 2025.

The strength and the fundamentals of our business is clear; serving customers needs across both our cloud and our on-prem businesses. We are increasingly seeing customers leverage our hybrid capabilities as they look to transform and commit to Teradata technology for the long-term.

As we have shared, we see that Teradata is increasingly becoming more strategic. The very large organizations we work with, have both data in the cloud and on-prem, and we believe we are uniquely positioned to address their needs with our differentiated hybrid platform.

We remain comfortable in closing deals over time, as evidenced by the eight figure deal I mentioned. We're seeing signs of greater engagement with both customers and prospects and improvement in renewal rates. These are primarily the result of our go-to-market restructuring.

We're in the early stages of our go-to-market reorganization and expect to see improving execution as we move into 2025. Our teams are taking AI to our customers and more than 20% of our pipeline includes an active AI sales engagement.

In the third quarter, we continue to add new logos and grew our new logo pipeline. Teams are actively working on closing the large deals in the pipeline. Teradata remains true to being customer and market-driven, and we have adjusted the timing of deals to align with our customers extended decision making on these strategic opportunities.

Teradata remained highly profitable in the third quarter. Profitability increased with non-GAAP earnings per share of \$0.69 versus \$0.42 in Q3 of 2023, and free cash flow of \$69 million compared to \$36 million in Q3 of 2023.

We will uphold our commitment to maintain margins, protect and grow free cash flow and return capital to shareholders. When we look ahead, we see opportunity. As companies embrace AI, they need data at scale.

Data at scale is the foundation of Gen AI applications, and data at scale has always been at the core of Teradata. We've made great strides advancing our perception and our innovations, as I'll now explain.

I'll start with recognition received for our market position in trusted AI. Ventana Research rated Teradata as an overall leader and a top rated analytic data platform company and is one of the best in meeting product and customer experience requirements.

Ventana also ranked Teradata as exemplary in Ventana's AI and MLOps platform gains. We're also very pleased with the response from our recent possible events in London and Los Angeles, where we received positive feedback from customers, prospects, partners and analysts.

We heard consistent comments on our clear strategy, differentiation on trusted AI and in partnerships that strengthen our open and connected ecosystem approach that customers want.

Across the board, we heard from attendees that they were impressed with the breadth of customers who shared their insights and the value Teradata brings to their organizations.

One analyst noted that customers and partners alike continue to view Teradata as their strategic vendor around analytics and called out the potential we bring to help them with Gen AI workloads.

Another noted our strong pace of innovation, our differentiated hybrid capabilities, and our superior pricing economics for customers. It was from these customer events that we announced a sweeping set of innovations that support and advance our differentiated position in trusted AI.

Starting with enhancements to ClearScape Analytics, our analytics engine for AI innovation. These enhancements are designed to enable organizations to maximize the return on investment of their AI and ML investments.

They are also intended to boost data science productivity to achieve business outcomes faster and more efficiently. We have brought Spark to ClearScape Analytics. Data scientists are now able to easily convert PySpark code to Teradata machine learning, eliminating the need for reengineering or data movement.

This significantly reduces complexity and costs. Customers can leverage VantageCloud's enterprise-grade workload management, security and data integration that is designed to operationalize trusted AI at scale.

In one example, a large Latin American bank recently trialed a migration of some Databricks workloads to VantageCloud using this capability. The workloads were to perform daily data analytics for 16 million credit card records and 75 million consumer transaction records.

The results were dramatic; 56% faster processing with VantageCloud and 47% cost savings with VantageCloud compared to Databricks, all without moving data in and out of their data warehouse.

In October, we announced our new bring-your-own or BYO LLM capability designed to enable customers to simply and cost effectively deploy Gen AI use cases at scale. Organizations are recognizing that larger language models aren't best suited for every use case and can be cost prohibitive.

Bring-your-own language model allows companies to choose the best model for their specific business needs, including small or medium domain-specific language models from open source providers like Hugging Face. Many models are free to use, inexpensive to run and can be tailored to industry and horizontal use cases for real world value.

For customers with more complex generative AI needs, including training or fine-tuning, ClearScape now also provides them with the flexibility to strategically leverage either GPUs or CPUs depending on the complexity and size of the large language model.

Teradata's ability to leverage GPUs can allow customers to develop and operate LLMs for purpose-built Gen AI business applications and not be constrained to siloed AI tools that require complex workflows or large amounts of data movement.

In addition to these models being easier to deploy and more cost effective overall, we bring the language models to the data, so that organizations can also minimize the expense of data movement and maximize security, privacy and trust.

With these ClearScape announcements, we are continuing to deliver what we see as the most powerful, open and connected AI and ML capabilities in the market today. All VantageCloud customers have access to ClearScape Analytics with these new features.

Our focus on driving innovation has never been stronger, and I'm pleased to report that we have appointed Louis Landry as our Chief Technology Officer. I'm excited that Louis will bring his expertise in advanced engineering and emerging technologies to help accelerate the pace of innovation at Teradata.

Louis has led our technology and innovation office and his knowledge of Teradata technologies, deep engineering and years of experience leading technology innovations at larger enterprises make him an excellent CTO for Teradata. Hillary Ashton, our Chief Product Officer, will be leaving Teradata at the end of the year and will facilitate a smooth transition out of her role.

As we build on our innovations and strengthen our open and connected ecosystem, our focus on partnerships remains front and center. We recently announced the integration of NVIDIA's AI Accelerated Computing Platform with our Vantage platform for the development and deployment of Gen AI applications to accelerate trusted AI workloads both large and small.

VantageCloud Lake's Integration with NVIDIA's is platform is designed to enable our customers to more affordably deploy everyday Gen AI use cases faster and their environment choice for immediate return on investment.

We also announced that the Teradata platform is now integrated with dbt Cloud. We bring our ability to manage complex, large scale datasets with enterprise-grade reliability, robust security and governance, and combine that with dbt's transformation tools to turn raw data into actionable insights.

Together, we believe that we can enable unparalleled data management and agile analytics, empowering engineering teams to transform data at scale with less manual effort, all in service of helping organizations accelerate their AI and ML initiatives.

Finally, we introduced a generative AI-driven Customer Complaint Analyzer solution built on VantageCloud Lake in concert with EDGE Solutions & Consulting. Customer Complaint Analyzer is designed to continuously capture data signals in order to identify, address and prevent customer complaints.

The powerful solution is designed to help companies improve their customers experience and reduce churn. And we already have a healthy opportunity pipeline for this new AI use case.

We've had great customer reaction to our announcements. For example, our team demonstrated how we can help companies more effectively integrate signals from customers into their workflows and quickly act on them.

We used Hugging Face models, leveraging the bring-your-own model feature in ClearScape Analytics to analyze and summarize customer calls for classifying the output and automating treatment of next-best-action, all in a single integrated analytic workflow without moving data.

This AI-driven solution provides faster responses to customers, and we demonstrated how an entity could analyze and address 300,000 calls a day, up from 30,000 a day with their manual process.

We are seeing great interest as the benefits can be far reaching, including cost savings, improving customer satisfaction and increasing the lifetime value of the customer. These announcements and our customer engagement events are executed with one goal, help our customers achieve massive value, trusted data and trusted AI.

I'll wrap up with a sampling of some of our recent wins that should illustrate that goal in action. A US insurance company and member of the S&P 500 migrated to the cloud with VantageCloud Lake on AWS.

The account had implemented the cloud strategy and migrated its Hadoop data lake to Snowflake years ago, before we had a cloud offering. Our team introduced VantageCloud Lake and demonstrated that Teradata was the best and most cost effective solution for the company's complex workloads and we won this business back.

Our Lake offering on AWS will support the customer's business, insurance division and more. We're collaborating with Cognizant on the migration.

We also had a significant win with one of the largest banks in Asia Pacific. In this competitive win, the bank chose Teradata on AWS to achieve the robust performance and reliability needs. It runs risk, compliance and regulatory reporting on Teradata.

We will also integrate VantageCloud's Lake as an innovation platform so that the bank can develop AI/ML use cases without the constraints of working with production data. This move marks a significant evolution to enhance their agility and innovation capabilities.

And finally, a Fortune 500 insurance giant added VantageCloud Lake on AWS to run additional analytic workloads for its finance department.

As I close, I'll reiterate that we remain committed to accelerating growth and innovation. We see strong market opportunity that aligns to our strengths, and we are delivering AI innovations and value for customers.

We have proven that Teradata can and does evolve with changing market dynamics as we've grown our ARR business to more than \$0.5 billion in under four years, while aggressively returning capital to shareholders.

We believe we are well positioned with our hybrid trusted AI platform as enterprises begin to commercialize AI uses. We have been and will continue to take actions to improve growth. We have made meaningful leadership changes in products and go-to-market.

With Rich now in the CRO role for two quarters, we have made material changes in our go-to-market organization designed to improve execution. We believe we are taking the right actions to return us to growth. And while it's still early in seeing the results from those changes, we firmly believe in our differentiated technology, our people and in our future.

Now I'll pass the call to Claire.

Claire Bramley

Chief Financial Officer, Teradata Corp.

Thank you, Steve, and good afternoon, everyone. In the third quarter, cloud ARR grew to 38% of our total ARR, up from 30% at this time last year. We continued to demonstrate strong improvement in operating margin, profitability and free cash flow generation. Year-over-year free cash flow nearly doubled and our operating margin increased over 800 basis points.

As Steve mentioned, we anticipate a different migration path within our large transformational cloud deals. The durable nature of our business model remains intact, with over 80% of our revenue being recurring, delivering a gross margin of over 70% and a total operating margin of 20%.

With the reiteration of our total ARR outlook, we continue to expect improvement in our overall retention rates going forward.

Let me now share more details on our quarterly financial results, starting with revenue. Third quarter recurring revenue was \$372 million, up 3% year-over-year, as reported, and 5% year-over-year in constant currency.

Recurring revenue was driven by the strong growth in cloud revenue. We saw a small net benefit from upfront revenue in the quarter. Recurring revenue as a percentage of total revenue was 85%, up from 82% from the prior year period.

Third quarter total revenue was \$440 million, flat year-over-year, as reported, and up 2% in constant currency. The year-over-year constant currency growth in recurring revenue was partially offset by lower consulting revenue.

Moving to profitability and free cash flow. Total gross margin was 61.6%, up 130 basis points year-over-year, driven by our strategic focus on recurring revenue. Operating margin was 22.5%, up over 800 basis points year-over-year.

Non-GAAP diluted earnings per share was \$0.69, exceeding the top end of our guidance range. The primary drivers for the EPS outperformance were currency and upfront revenue. We generated \$69 million of free cash flow in the quarter, which is a \$30 million increase sequentially, and nearly double on a year-over-year basis.

In the third quarter, we repurchased approximately \$15 million or 500,000 shares. Year-to-date, we have returned 144% of free cash flow in the form of share repurchases, and we remain committed to returning at least 75% on a full year basis.

Moving to our full year 2024 outlook. As a reminder, our outlook ranges are in constant currency for the ARR and revenue metrics. We reaffirm our previous outlook for total ARR, total revenue, recurring revenue and free cash flow.

Although total ARR is unchanged, we are seeing a different mix between cloud and on-prem. For cloud ARR, we now expect more staged migrations for the large transformational deals and anticipate growth of 18% to 22%.

We are increasing the non-GAAP earnings per share outlook. It is now \$2.30 to \$2.34. Additional full year outlook assumptions include weighted average shares outstanding of approximately 98 million. Other expense of

approximately \$48 million. We project a non-GAAP tax rate of approximately 25%. Our net expansion rate, we anticipate a slight deceleration, but to still be in line with historical levels.

Regarding our outlook for the fourth quarter of 2024. We anticipate non-GAAP diluted earnings per share to be in the range of \$0.40 to \$0.44. We project the non-GAAP tax rate to be approximately 22.1% and the weighted average shares outstanding of 97.5 million.

Previously announced cost reduction actions remain on track and ensure the durability of our margin profile as we return to total ARR growth next year. Free cash flow growth remains our focus and we are committed to return 75% of free cash flow to shareholders in the form of buybacks. We will provide an update to our fiscal 2025 outlook during our Q4 earnings call in February.

Thank you very much for your time today. Now please open the call for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] . Your first question comes from the line of Matt Hedberg with RBC. You may proceed.

Matthew Hedberg
Analyst, RBC Capital Markets LLC

Q

Great. Thanks for taking my questions. Maybe one for Steve and then one for Claire. You noted, sort of, at the top of your remarks, there was a change in how customers are thinking about cloud migration. I'm curious if you could just maybe double click on that a bit more. Is this an industry wide thing?

Do you think it's something that's unique maybe to your base and I'm just curious, does it change the medium-term outlook on cloud mix and kind of overall growth when obviously that cloud mix is a big part of the total company acceleration?

Steve McMillan
President, Chief Executive Officer & Director, Teradata Corp.

A

Thanks, Matt, for that question. And I'll let you come back to ask Claire a question afterwards. Fundamentally, we are seeing strength in our business, both from a cloud perspective and from an on-prem perspective.

But as I said in my prepared remarks, we have seen recently a material change in the buying behavior in a handful of our large conversion deals. The way these customers are approaching their cloud strategy is in a more staged nature. They're breaking down that cloud migration into smaller deals. And as they are doing that, they're actually leveraging the hybrid nature of our platform where they can run both in the cloud and on-prem.

So, to your point, we are seeing a mix change of commencing in the cloud and on-prem. And so while initially we're left in the cloud, we don't see a change to the total commitment or opportunity.

And that's why we reiterated our full year 2024 total ARR guide. And in 2025, we talked about returning to growth from a total ARR perspective. So, we saw a handful of eight figure deals essentially in some cases convert into a set of seven figure deals.

Matthew Hedberg

Analyst, RBC Capital Markets LLC



Got it. That's super helpful, Steve. And then maybe a related question for Claire. To me, it feels like, there's a bit more higher priority on Q4 on-premise spending within your base. And I guess I'm wondering, I think a lot of us are wondering, do we see maybe a bit more of a December budget flush this year?

And I'm wondering, did your guidance contemplate maybe a bit more of that, given that historically, budget flush I think tends to impact more on-prem than cloud. And then, when you think about cloud growth and maybe even re-acceleration, what are the building blocks of that essentially?

Claire Bramley

Chief Financial Officer, Teradata Corp.



Hi, Matt. Yeah. So, just on your first part of your question, with regards to budget flush, we haven't factored any uplift from a budget flush. We've done a customer by customer pipeline analysis.

And as Steve said, looking at what we expect to close in 2024 and factor that into our updated assumptions for both total ARR and cloud ARR. So, no budget flush assumed for on-prem at the end of 2024 in December.

With regards to, as you look forward into the future, but I think just generally on 2025, I would say, we're still driving towards the metrics that we talked about last quarter.

As Steve just mentioned, that means total ARR growth in 2025 and also growth in our free cash flow year-over-year in 2025. And we continue to anticipate a robust growth in cloud ARR in 2025 as well.

So, naturally we're not providing detailed guidance in this quarter. We'll provide it at our Q4 earnings, which is in line with when we would normally provide it, which is in February of next year.

Matthew Hedberg

Analyst, RBC Capital Markets LLC



I appreciate the answers from both of you. Thanks a lot.

Claire Bramley

Chief Financial Officer, Teradata Corp.



Thanks, Matt.

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.



Thanks, Matt.

Operator: Your next question comes from the line of Chirag Ved with Evercore ISI. Your line is open.

Chirag Ved

Analyst, Evercore ISI



Thank you so much for taking the question. Steve, as you think about the business over the next couple of quarters, given the mix change and customer approach to cloud, does this change how much you're indexing on

cloud versus on-prem in terms of your approach to innovation, contracts, renewals at this point? And what are you seeing to support and guide that decision making process?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

Thanks, Chirag for the question. So, I just want to reiterate, we are completely committed to our cloud first strategy. We believe it continues to reposition Teradata in the marketplace as modern and relevant for our customers.

And we believe that the innovations that we develop from a cloud perspective, they actually enable additional capabilities on-prem. So, as an example, I was talking about being able to bring your own language model, and we are actually able to leverage our technologies and technology development to actually deliver that capability both in the cloud and on-prem.

So, the focus from a strategic perspective is very much to keep on that cloud first mission, cloud first, but not cloud only is absolutely our strategy. I would say as well that as we look forward, the strength of our cloud pipeline still remains intact.

We expect these customers to continue a migration path for the cloud with Teradata, and we have continuously demonstrated that we are the least risk path to the cloud for some of the largest organizations in the world to move that complex, large workload to the cloud and utilize the Teradata technology set in the cloud.

Because we're not seeing that, we're not seeing any deterioration overall in the pipeline, we're just seeing that timeline of migration pushing out into the future. We remain committed to that cloud strategy and cloud execution. And we believe that it'll still remain a fundamental part of our growth strategy as we move forward.

Chirag Ved

Analyst, Evercore ISI

Q

Great. And then, Claire, maybe one for you. Recurring revenue came in ahead of where the Street was at for Q3 and you maintained the full year guide. Can you talk through what happened in Q3 and what you're expecting in Q4 from the recurring revenue point of view?

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

Yeah. So, I think it's just more of a linearity in the modeling, Chirag. So, not a big difference in terms of what we're expecting internally. We did see a slight benefit from more upfront revenue, which hits both total revenue and recurring revenue, but that was more of a linearity change. So, no overall change to what we're expecting, just a slight shift between Q3 and Q4, which is why the full year guide remained unchanged.

Chirag Ved

Analyst, Evercore ISI

Q

Perfect. Thank you both.

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

Thank you.

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

Thanks.

Operator: Our next question comes from the line of Tyler Radke with Citi. Your line is now open.

Tyler Radke

Analyst, Citigroup Global Markets, Inc.

Q

Yeah, thanks for the question. Steve, wanted to go back to the commentary you made around the staged migration that you're seeing with customers in terms of moving to cloud. I guess why do you think this is happening and why now?

I mean, is this a macro budgetary-driven decision? I mean, it would seem like budgets have been tight for a while. So, what's kind of your theory on why this is happening and why now?

And just to clarify, is this only customers that you saw in Q3, what makes you think that this was just a function of the sample size versus a broader trend that extends in the next year?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

Yeah, Tyler, thanks for the question. So, over the past couple of months, we've ran our customer marketing events both in London and L.A. It gave us the opportunity to talk in depth with a number of our customers regarding what their plans are and how they plan to move forward.

Now, we've seen an impact in a handful of our really very large deals, so looking at those eight figure deals where we've had appetite for customers to make a migration path which is to migrate their entire real estate to the cloud.

And one program just like the deal that we signed early in the fourth quarter, the eight figure deal that we signed. But we are seeing a handful of customers that are choosing to essentially take from their perspective, a less risk approach to these major transformational programs that they are executing.

They're still committing to Teradata, and in many cases, they're committing incremental spend with Teradata across both on-prem and the cloud. But for the cloud deals, we expect those to close in a more staged process. So, instead of one eight figure deal, we'll close multiple seven figure deals over a longer time period.

Tyler Radke

Analyst, Citigroup Global Markets, Inc.

Q

Very helpful. And follow-up on that for Claire. So last quarter, you talked about seeing similar cloud growth as your prior guide in 2025 as 2024, which I think was around 30% and \$1 billion in cloud in 2026. Do you still expect \$1 billion in 2026 or does this sort of change the trajectory of that cloud business ramping to \$1 billion?

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

I guess, Tyler just on that. I would say we still see a path to the \$1 billion for cloud ARR in 2026. Naturally, we're working with these customers on a detailed timing of their staged processes. So, we will obviously update the cloud ARR for 2025 in February.

We don't anticipate to recover all of this in 2025, but definitely we anticipate, as Steve mentioned, some of these additional stages to close in 2025. So, we'll come back on the 2025 cloud ARR. But we do still see that path to the \$1 billion, because as Steve said, they're still committing to migrate with us over time.

Tyler Radke

Analyst, Citigroup Global Markets, Inc.

Great. Thank you.

Q

Claire Bramley

Chief Financial Officer, Teradata Corp.

Thank you.

A

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

Thanks.

A

Operator: Your next question comes from the line of Erik Woodring with Morgan Stanley. Your line is open.

Erik W. Woodring

Analyst, Morgan Stanley & Co. LLC

Great. Thanks so much for taking my question, guys. Steve, maybe I'll start with you. It feels like Teradata has faced a bit of a perfect storm of headwinds this year between some on-prem erosion, some deal elongation, and now some cloud migration timing dynamics.

Q

And I'm just wondering, how can you be sure that the headwinds that you have encountered this year have nothing to do with competitive pressures for example, elongating sales cycles are taking longer to migrate to the cloud.

Is there a sign that those are risk that those customers are potentially evaluating maybe other cloud native platforms? Just help us gain some comfort that this isn't a competitive risk and this is more just related to timing and maybe company-specific issues. And then I have a quick follow-up. Thank you so much.

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

Yeah, thanks, Erik. Look, we absolutely would like conversion opportunities over time that are in the pipeline and I wanted to refer to the fact that those customers are actually making commitments to us from both an on-prem and a cloud perspective.

A

So, we expect them to start those cloud journeys with us. So, we're just seeing essentially a more staged approach to the execution. From a competitive perspective, I'm very proud of how we are doing from a competitive perspective.

I mentioned in my prepared remarks, one customer that had migrated to Snowflake, but has recently made the decision to come back to utilizing the Teradata platform in the cloud.

But I'm also really happy with how we're doing from a competitive perspective against newer players like Databricks. I made the reference to a Latin American bank that had migrated workloads from Databricks and actually they are utilizing Teradata and they're doing it twice as fast in terms of processing speed and at half the cost. And we're continuously building up that catalog of competitive execution with competitive win backs.

We are absolutely convinced of our lowest cost per query comparison to the competition. I think what we see is, we look at these very large deals and some of the largest organizations in the world, it's really all about risk appetite and what they see with Teradata as the least risk way of actually migrating to the cloud and getting the benefits of cloud technology.

So, I think the way that they're using and deploying our technology set in terms of our hybrid capabilities is something that none of the other competition can actually deliver against. And so leveraging that hybrid capability as they execute through in a migration gives us a differentiated position. So, that's how we can be more assured that we're doing well from a competition perspective.

Erik W. Woodring

Analyst, Morgan Stanley & Co. LLC

Q

Okay. Thank you, Steve. That's really helpful. And then maybe my follow-up is for you Claire, which is, can you maybe just talk a little bit more the changing gross margin profile of your recurring revenue base, given some of these mix shifting dynamics?

And really, when you expect that recurring revenue gross margin to kind of bottom and stabilize and start to expand, has that timeline changed as you've now kind of thought about the different underlying mix between on-prem and cloud in your business? Thanks so much.

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

Thanks, Erik. Yeah. So, just with regards to gross margin, we've actually been very stable with our total gross margin and our recurring gross margin over the last couple of quarters. And I'm pleased that even though we've been increasing the mix of cloud ARR, we've been able to offset the negative impact that that has by an improvement in our cloud margin rate.

So, seeing a continued improvement in cloud margin rate year-over-year and quarter-over-quarter and expecting that to continue and we're seeing that offset the negative impact from the mix change. And I think as we look out into the future and we continue to increase the mix of cloud ARR, we will continue to maintain that stability.

Erik W. Woodring

Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks so much. Good luck, guys.

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

Thank you.

Operator: Your next question comes from the line of Howard Ma with Guggenheim. Your line is open.

Howard Ma

Analyst, Guggenheim Securities LLC



Thanks. Steve, I want to understand you gave a pretty thorough explanation of these staged migrations, but what can you point to further? So, I was just brainstorming, I was thinking maybe it's verbal customer commits around the timing of migration expansions, even if it's not contractual right, maybe you can share some data on conversations or maybe it's telemetry data that support the stickiness on Teradata or maybe you have a pronounced on-premise renewal base next year. So, really anything more concrete that could instill confidence that that slower cloud migrations or what you're calling staged migrations won't translate into future competitive losses?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.



Thanks for the question. Look, I'd start off by saying, like, we are strategically positioned in all of these accounts that we're talking about, and overall, our pipeline remains strong and our deal opportunity hasn't really changed at the aggregate level. It's just changed shape in terms of timing of execution.

I'd also – to the point we were just talking about, we've not had any lost cloud opportunities from that large deal set. And in fact, our total ARR remains unchanged. So, the total customer commitment and spend commitment with Teradata has remained unchanged.

If I look specifically in second half in terms of our execution, we've actually got better renewal and retention rates in the second half of 2024, and that's going to help power some of our total ARR growth as we move into 2025.

Howard Ma

Analyst, Guggenheim Securities LLC



Got it. And for Claire, speaking of 2025, I respect that you're not giving any discrete guidance so far, but you're making some pretty big initiatives. I mean, there is product initiatives at your recent customer conference, your go-to-market reorg is underway. Can you just paint a picture for us and help us understand when these initiatives will kick in?

I mean, we're in November already, so as we look around the quarter to next year, how will they kick in into the numbers and on the back of that, why should we not expect significant acceleration next year?

Claire Bramley

Chief Financial Officer, Teradata Corp.



Yeah. So, we are committing to total ARR growth in 2025, Howard. So, we are committing to an increase, an improvement compared to 2024. And there are three main drivers of that, that supporting that total ARR growth in 2025 include a higher percentage of cloud. So, that obviously drives more growth. So, we are anticipating robust growth in 2025 and that will increase the percentage of cloud.

The other things as well is we are expecting a meaningful improvement in our retention rates for the full year in 2025. And finally, we expect on-prem expansion improvement year-over-year as well.

So there's multiple things, including robust cloud growth that will be helping us to move back to total ARR growth next year, which obviously I would say is a meaningful improvement compared to where we are in 2024.

Howard Ma

Analyst, Guggenheim Securities LLC

Okay. Thank you.

Q

Claire Bramley

Chief Financial Officer, Teradata Corp.

Thanks.

A

Operator: Your next question comes from the line of Nehal Chokshi with Northland Capital Markets. Your line is open.

Nehal Chokshi

Analyst, Northland Capital Markets

Yeah. Thank you. Help us understand what it means in terms of change in year-end total workloads on Teradata given takedown cloud ARR, but no change in total ARR?

Q

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

Hi Nehal. Thanks very much for the question. As we've been executing these customer events recently, I had the opportunity to talk to a lot of our customers. And what we see is that, they still have the requirement to operate data at an enormous scale and do that in the most effective and efficient way. And Teradata is definitely the platform that can enable them to do that.

A

When we talk to them about the most recent capability developments that we've had, both from an analytics perspective or analytic capabilities and database or in-platform or utilizing the analytic capabilities of the environment in which they're working, these are all ways that our customers want to utilize the Teradata technologies.

The thing that really resonated with our customers is the fact that we meet our customers where they want to be met. So, if they want to leverage the Teradata platform in the cloud, they can do that. If they want to leverage on-prem, they can do that. And if they want to do that in a hybrid environment, that's something that Teradata can deliver uniquely in the marketplace in terms of given that one platform across those environments. So, we still see a real demand in terms of utilizing the Teradata platform for these modern workloads and in modern environments.

Nehal Chokshi

Analyst, Northland Capital Markets

So, the reason why I asked that question is because I thought that when an on-premise customer converts a certain amount of their on-premise estate to cloud, there's an expansion associated with that. So, if you have a slowdown in the cloud migrations, you would actually have less total ARR, is that not correct?

Q

Claire Bramley

Chief Financial Officer, Teradata Corp.

Yeah. So, Nehal, it's a good point. So, we do, normally and on average, see an uplift at the point of migration. In the grand scheme of things in terms of our total ARR range that we guided, we were able to absorb that in that

A

range. So, yes, there is an impact linked to the reduction of the cloud ARR, but we've been able to absorb that in our total ARR previous numbers.

Nehal Chokshi

Analyst, Northland Capital Markets

Q

I see. Understood. Okay. And then of the \$50 million takedown for cloud ARR for calendar 2024, is there significant concentration within that \$50 million to like just a couple of customers?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

I mentioned in the prior questions, but there is a handful of customers where the deals have moved from eight figures to seven figures. And clearly, you just need a few of those and you've quite rapidly built up that cloud ARR number.

What I would say is, and it goes to the question about, is it something systemic inside the marketplace, we are still seeing our customers committed to executing that cloud migration with us. And we'll clearly capture the expansion that we've been talking about.

But we are also seeing those customers actually looking to expand their overall spend with Teradata and the combination of both on-prem and cloud and many cases.

Nehal Chokshi

Analyst, Northland Capital Markets

Q

Got it. And then if I can sneak one more in. Steve, you cited a few customer wins in the quarter boomeranging back to Teradata, either from Databricks or Snowflake. What's the frequency of this type of customer case and any change in that frequency that you're seeing relative to a quarter or a year ago?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

Yeah. We're definitely seeing that as our platform becomes more and more performant, and also the capabilities in our platform from an analytics perspective enabling us to compete for those data science workloads, for example, from, Databricks. So, as we continue the development in our cloud first strategy, it's an enabling us to go back with a win back message and the ability to address customer requirements and customer needs that we haven't been able to in the past. So, I believe our competitive positioning will continue to improve over time.

Nehal Chokshi

Analyst, Northland Capital Markets

Q

Thank you.

Operator: Your next question comes from the line of Wamsi Mohan with Bank of America. Your line is open.

Wamsi Mohan

Analyst, BofA Securities, Inc.

Q

Yes, thank you. Steve, can you perhaps just address the broader macro trends as well. Where are you seeing maybe just in terms of expectations of spend going into 2025? And large deal cadence, are you seeing any

changes in the way those are progressing, not just in these cloud migrations that you've spoken about, but just in the base business as well? And I have a follow-up.

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

Yeah. Wamsi, I'll just reiterate that, I think the fundamentals of our business remain very strong. We don't see increased competitive pressures. I talked in my prepared remarks about winning a bank in the Asia-Pacific region in a highly competitive environment.

But we see the customer spend commit to Teradata remaining strong at both now and into the future and clearly, you know our business very well, we deal with some of the largest organizations in the world.

So, having that commitment has given us the confidence to say that we're going to return to total ARR growth next year. From a spend perspective, we are working to increase our addressable market with the capabilities that we're developing from an AI perspective.

We're working with some large banks in the US where we're actually deploying generative AI use cases in the Teradata platform using Hugging Face language models as an example.

So, we're starting to expand not only make sure that we maximize our presence in enterprise, data warehousing and data lake and data lake house, but also in terms of the analytical workloads that we can operate against. So, I'm confident in terms of the opportunity that we will have as we move into the future.

Wamsi Mohan

Analyst, BofA Securities, Inc.

Q

Okay. Thanks, Steve. And I guess just to follow-up on your point around AI also, you said 20% of your pipeline includes active AI sales engagement. What do you think about the rate and pace of this business? Is there something that's got pretty long proof of life, proof of concept, like timing or do you think that you have something that will translate faster and this 20% pipeline will significantly grow a quarter from now?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

A

Yeah. I think as we look at AI and Gen AI, those data science projects, a number of them are failing. A recent study said that, more than 50%, 60% of AI and Gen AI workloads are not moving out of proof of concept into production.

One of the reasons for that is operating at scale. What we're able to demonstrate for our customers is that we can actually take them from that idea and concept and then operationalize that at scale with all of their trusted data inside their ecosystem.

And so I think as we look at our pipeline of opportunities and we are able to prove that out to our customers, that we can take them and not just deliver on a proof of concept, but actually help them deploy these solutions at scale in the production environment that's really going to act as a tailwind for us as we move into the future.

Operator: Your next question is from the line of Derrick Wood with TD Cohen. Your line is open.

Derrick Wood

Analyst, TD Cowen



Great. Thanks. My first question, Steve, there's a lot of talk about growing adoption of Iceberg and the broader data analytics ecosystem. What are you guys seeing from your customers and do you think this changing cloud migration behavior has anything to do with companies contemplating data storage movements to Iceberg?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.



Yeah. I think, we talk to nearly every single one of our customers about how they plan to leverage an open table format on Native Object Store. And we see that as a great opportunity for us. Our Cloud Lake platform supports open table formats, and we don't lock our customers into one particular open table format. We have a strategy that we want to support both Iceberg and Delta Lake as an open table format.

Now when you look at that from a Teradata perspective, we see that again as looking to increase our TAM. As we look at the amount of data that is in Native Object Stores and putting structure around that data and Native Object Stores, that's something that the Teradata ecosystem only touches in a light way just now.

As we look to the future, we look at that as an opportunity to again expand our addressable marketplace and the opportunity that we have in terms of that unstructured data is often an order of magnitude larger than the structured data in say an organization.

Operator: Your next question comes from the line of Patrick Walravens with Citizens JMP. Your line is open.

Pat Walravens

Analyst, Citizens JMP Securities LLC



Oh, great. Thank you. So, Steve, I think you mentioned in your remarks that Hillary is going to be moving on and you're looking for a new Chief Product Officer. What are sort of the top characteristics that you're looking for in that individual?

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.



Hi, Pat. Thanks. Just to be clear, Hillary is going to move on, but we're taking this opportunity to actually leverage the bench strength that we have inside the organization from both a product management, a product engineering and a Chief Technology Officer perspective.

So, I announced that Louis Landry is appointed as our Chief Technology Officer. As we move into the future, I'm actually elevating the product management focus we have inside the company and the product engineering focus that we have inside the company to have those roles report directly to me.

Operator: Your next question comes from the line of Raimo Lenschow with Barclays. Your line is open.

Raimo Lenschow

Analyst, Barclays Capital, Inc.



Perfect. Thanks for squeezing me in. Two quick questions, Claire on the cash flow side, you outperformed this quarter, but the full year is unchanged. Anything around timing of things that came in, in Q3, etcetera, that you want to point out? And then I have one follow-up for Steve.

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

Yeah. To your point, Raimo, we were pleased with the performance of free cash flow. We anticipate there to be a slight linearity impact with regards to our working capital as they slightly over performed on DSO and DPO compared to our previous expectations.

And so that would just be a linearity impact between Q3 and Q4. But we feel good about the meeting being in the range of our free cash flow guide for the full year, and it will be similar increase in cash flow that we saw this time last year.

Operator: Your next question comes from the line of Austin Dietz with UBS. Your line is open.

Austin Dietz

Analyst, UBS Securities LLC

Q

Hey, Steve and Claire. I know we've spent a lot of time on migrations and their more staged nature on the call so far. But the cloud net expansion rate this quarter, it seemed to slow several percentage points. And I believe it's a trailing 12-month metric to where the in-quarter piece would have slowed by more than that. So, do you mind just unpacking what you saw from a net expansion perspective this quarter? And then how should we think about that cloud net expansion rate over the near to medium-term?

Claire Bramley

Chief Financial Officer, Teradata Corp.

A

Yeah. Thank you, Austin, for the question. So, as you mentioned, net expansion rate was 120% in Q3 and it is a trailing 12-month metric. So, that's a deceleration and that was mainly driven by our healthcare vertical and also some of our European business.

We do expect further deceleration into Q4 given the mix of migrations versus expansions. And as we look forward, we will obviously continue to monitor with the stage migrations that we see what the impact will be in 2025.

So, as a reminder, expansion at the point of conversion for the first 12 months is not included in our net expansion rate. So, we're also impacted by that as we update the migration timing of our customers migrations.

Operator: There are no further questions at this time. I will now turn the call back over to Steve McMillan for his final remarks.

Steve McMillan

President, Chief Executive Officer & Director, Teradata Corp.

Thank you, and thanks everybody for the questions. The fundamentals of our business are strong and we firmly believe in Teradata's differentiated technology and future growth. We will remain focused on improving execution and accelerating that growth, and we remain committed to protecting and growing our free cash flow and returning that capital to our shareholders. Thank you all.

Operator: This concludes today's conference call. You may now disconnect.

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