Zoom Q3 FY24 Earnings - Prepared Remarks

Slide 1 – Zoom Q3 FY24 Earnings

Tom McCallum, Head of IR

Thank you, Kelcey.

Hello everyone, and welcome to Zoom's earnings video webinar for the third quarter of FY24. I'm joined today by Zoom's Founder and CEO, Eric Yuan, and Zoom's CFO, Kelly Steckelberg.

Slide 2 – Use of non-GAAP financial measures

Our earnings press release was issued today after the market closed and may be downloaded from the Investor Relations page at investors.Zoom.us. Also, on this page you'll be able to find a copy of today's prepared remarks and a slide deck with financial highlights that, along with our earnings release, include a reconciliation of GAAP to non-GAAP financial results.

Slide 3 – Safe Harbor statement

During this call we will make forward-looking statements, including statements regarding our financial outlook for the fourth quarter and full fiscal year 2024; our expectations regarding financial and business trends; impacts from the macroeconomic environment, our market position, opportunities, go-to-market initiatives, growth strategy and business aspirations; and product initiatives and the expected benefits of such initiatives.

These statements are only predictions that are based on what we believe today, and actual results may differ materially. These forward-looking statements are subject to risks and other factors that could affect our performance and financial results, which we discuss in detail in our filings with the SEC, including our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q. Zoom assumes no obligation to update any forward-looking statements we may make on today's webinar.

And with that, let me turn the discussion over to Eric.

Slide 4 – Zoomtopia

Eric Yuan, Founder and CEO

Thank you, Tom! Thank you everyone for joining us today.

In early October, we hosted Zoomtopia, our yearly customer and innovation-focused event, and it was awesome! Like last year, we ran it hybrid on Zoom Events. Thousands joined us in person and many multiples of that virtually. Among the in person attendees were 40 customer presenters such as JP Morgan, MIT, Boston Consulting Group, HubSpot and Kohls, who spoke about their amazing experiences on Zoom and excitement about the future.

We also showcased newly-released innovations like Zoom AI Companion, as well as Zoom AI Expert Assist and Quality Management for the Contact Center. Zoom AI Companion is especially noteworthy for being included at no additional cost to our paid plans, and has fared tremendously well with over 220,000 accounts enabling it and 2.8 million meeting summaries created as of today. Remarkable growth in less than three months.

At Zoomtopia, I also had the pleasure of sharing the stage with Flex, a global manufacturing and supply chain leader, who spoke about how they use Zoom to connect their large, distributed workforce of 170,000 employees across 30 countries. Flex started using Zoom Meetings in 2017, quickly followed by Rooms and Team Chat. Since then, Flex increased Team Chat users by 200% and Zoom Rooms by 245%. They also became power users of Zoom Whiteboard, creating over 13,000 Whiteboards. And moving to Zoom Phone allowed them to eliminate 50 to 70% of circuits and infrastructure across the globe, and reduce total cost of ownership. We were so happy to have Flex share their journey at Zoomtopia, and cannot wait for what is in store for our partnership next.

Slide 5 – Customer wins highlight the appeal of our customer and employee experience solutions

Now moving on to some of our customer wins in Q3.

First, let me thank Dropbox, who has been an amazing customer for many years starting with Meetings and then extending to Rooms, Phone and Events. In Q3, they selected Zoom Virtual Agent and Zoom Contact Center to provide world-class AI-enabled support to their global user base.

Let me also thank Amynta Group, a premier insurance services company, who initially adopted Zoom Phone and Zoom Contact Center on a limited scale in Q1 of this year. Seeing how our modern solution offered superior agility, customization for CX flows and administrative functionality, in Q3 they decided to standardize their customer-facing sales support on the Zoom stack and add Workforce Management, leading to a nearly 5x increase in their monthly spend with us.

I'd also like to congratulate the Virgin Group on their launch of Workvivo to bring together 60,000 employees across almost 40 Virgin companies on one platform. The "Virgin Family" Workvivo platform is helping to drive social connection, encourage collaboration and boost brand knowledge. It's inspiring to see how the Virgin Group is bringing the platform to life and strengthening culture with Zoom's Workvivo.

These wins are a testament to the investments we are making in our customer experience offering, with the rapid pace of new innovations like Workforce Management, Quality Management, Zoom Virtual Agent and AI Expert Assist. They also highlight our progress with employee experience, especially with integrating Workvivo into the Zoom client.

Thanks to Dropbox, Amynta and Virgin Group. I love you all. And with that I'll pass it over to Kelly.

Slide 6 – Q3 Milestones

Kelly Steckelberg, CFO

Thank you, Eric. And hello everyone. We are pleased that we beat our top-line and profitability guidance in Q3. Here are a few milestones:

First, Zoom Phone reached approximately 7 million paid seats.

Second, Zoom Contact Center reached approximately 700 customers as of quarter-end, while Zoom Virtual Agent customers nearly doubled quarter over quarter.

And finally, the number of customers on Zoom One bundles that include Zoom Phone grew approximately 330% year over year.

These proof points demonstrate our customers' willingness to entrust us with their critical CX and EX processes, and their commitment to grow with us as we expand our platform.

Slide 7 - Continued top-line expansion in Q3 with positive trends in Enterprise and Online

In Q3, total revenue came in at $1.137 billion dollars, up 3% year over year and 4% in constant currency. This result was approximately $17 million dollars above the high end of our guidance.

Our Enterprise business grew 8% year over year and represented 58% of total revenue, up from 56% a year ago.

We continued to see improvement in Online Average Monthly Churn, which decreased to 3.0% from 3.1% in Q3 of FY23. This is the lowest churn we have ever reported.

Slide 8 – Growth with new and existing Enterprise customers

The number of Enterprise customers grew 5% year over year to approximately 219,700. Our trailing twelve month Net Dollar Expansion rate for Enterprise customers in Q3 came in at 105%.

We saw 14% year-over-year growth in the up-market as we ended the quarter with 3,731 customers contributing more than $100,000 dollars in trailing twelve months revenue. These customers represent 29% of revenue, up from 27% in Q3 of FY23.

Slide 9 – Growth in Americas, macro headwinds in ROW

Our Americas revenue grew 5% year over year, while EMEA and APAC declined by 2%, each. On a constant currency basis, APAC grew slightly year over year.

Slide 10 – Q3 FY24 expenses and margins

Moving to our non-GAAP results, which exclude stock-based compensation expense and associated payroll taxes, acquisition-related expenses, net gains or losses on strategic investments, and all associated tax effects.

Non-GAAP gross margin in Q3 was 79.7%, an improvement from 79.5% in Q3 of last year, but slightly lower than the first half of this year. The strong performance in gross margin was primarily driven by the optimization of usage across the public cloud and our co-located data centers, partially offset by our additional investments in new AI technologies. For the full year, we expect non-GAAP gross margin to be approximately 80%.

Non-GAAP operating income grew by 17% to $447 million dollars, exceeding the high end of our guidance of $405 million dollars. This translates to a 39.3% non-GAAP operating margin, a meaningful improvement from 34.6% in Q3 of last year.

Non-GAAP diluted earnings per share in Q3 was $1.29, on approximately 310 million non-GAAP diluted weighted average shares outstanding. This result was 20 cents above the high end of our guidance and 22 cents higher than Q3 of last year.

Slide 11 – Growing future revenue under contract

Turning to the balance sheet. Deferred revenue at the end of the period was 1.32 billion dollars, down approximately 3% from Q3 of last year. This was roughly one percentage point better than the high end of the guidance we provided last quarter. For Q4, we expect deferred revenue to be down 6 to 8% year over year, partially driven by shorter billing frequencies on Enterprise deals arising from the high interest rate environment.

Looking at both our billed and unbilled contracts, our RPO increased 10% year over year to approximately $3.6 billion dollars. We expect to recognize approximately 58% of the total RPO as revenue over the next 12 months, as compared to 59% in Q3 of last year, indicating lengthening contract durations on a year-over-year basis. As a reminder, our renewal seasonality peaks in Q1 and declines throughout the rest of the year.

Slide 12 – Strong cash flow and position in Q3

Operating cash flow in the quarter grew 67% year over year to $493 million dollars. Free cash flow grew 66% year over year to $453 million dollars. The sharp increase in our cash flow metrics was due to stronger collections, targeted expense management and higher interest income. Our operating cash flow and free cash flow margins expanded to 43.4% and 39.9%, respectively.

We ended the quarter with approximately $6.5 billion dollars in cash, cash equivalents and marketable securities, excluding restricted cash.

Given the strength in profitability and collections, we are increasing our free cash flow outlook for FY24. We now expect free cash flow to be in the range of 1.34 to 1.35 billion dollars, which at the midpoint would represent 13% year over year growth.

Slide 13 – Q4 and Full Fiscal Year 2024 outlook

Turning to guidance. For Q4, we expect revenue to be in the range of 1.125 to 1.13 billion dollars, which at the midpoint would represent approximately 1% year-over-year growth. Adjusting for currency impact, this projection is slightly higher than the previously implied guidance from our Q2 call. We expect non-GAAP operating income to be in the range of 409 to 414 million dollars. Our outlook for non-GAAP earnings per share is $1.13 to $1.15 based on approximately 312 million shares outstanding.

We are also pleased to raise our top-line and profitability outlook for the full year of FY24. We now expect revenue to be in the range of 4.506 to 4.511 billion dollars, which at the midpoint represents approximately 3% year-over-year growth. We expect our non-GAAP operating income to be in the range of 1.74 to 1.745 billion dollars representing an operating margin of approximately 39%. Our outlook for non-GAAP earnings per share for FY24 is $4.93 to $4.95, based on approximately 308 million shares outstanding.

Thank you to the entire Zoom team, our customers, our community, and our investors for your trust and support!

Slide 14 – Q&A

Kelcey, please queue up the first question.