Axway Software – Full-Year Results 2019 Presentation – Transcript February 20, 2020

Arthur CARLI, Head of Investor Relations, Axway

Good morning everyone. Welcome to Axway's 2019 full-year results presentation. My name is Arthur Carli. I am in charge of Investor Relations for the Group. I am here to remind you that this presentation will be held in English, but a French translation is available too. Just ask for headsets to one of our team members.

On top of that, I would like to remind you that this presentation contains forward-looking estimates. It is recorded and live webcasted on axway.com. With that, I hand over to our CEO, Patrick Donovan.

Patrick DONOVAN, CEO, Axway

Slide 1-3

Thanks, Arthur. Thank you for joining us here today. I am happy to share with you how we finished up 2019 and our outlook for 2020 and a little beyond.

Today, I will start off giving you a few comments on 2019 and some updates on our transformation plan. Then I will ask Roland to come up and join me and talk about the updates on the CSO organisation and the transformation plan there. Then I will come back and share more detail on the 2019 financials, and then give a little bit of a 2020 guidance and some midterm ambitions.

Slide 4

With that, I will remind you that in 2019 we shared with you some guidance for the year and some targets. I will go ahead and give you some updates how those came up for 2019.

Slide 5

For 2019 we had guided that we would be at organic revenue positive, but I had cautioned that it would be just above zero. We are just trying to get the momentum back as part of our strategy. For 2019, thanks to a strong fourth quarter, we finished at a 3.3% organic growth in revenue, or €300 million in total.

If you remember, we also were saying that, as we come out of our transformation journey in 2020, we look to target a €300 million base. I am pleased that we have already reached that target and we will be driving into 2020 quite strong.

Our profit and operating activities, we gave guidance that we were be between 8% and 10%. We finished right in the middle there at 8.6%, or €26 million. We are pleased to be able to keep the profitability, although, as you will see later, we invested strong in various areas to help drive our transformation.

Our Subscription growth for revenue finished at 41% year-over-year, or €60 million of revenue. That was driven with a strong ACV signature as well. We were up 33% for the year over the previous year, signing about €17.5 million of ACV, or Annual Contract Value.

Our signatures growth metric, which this one we track the actual health of our sales activities – in the past, we used to talk about Licenses, is how I am tracking the new business our sales efforts have brought in – it grew 8.3%, crossing the €100 million line to €105 million for the year.

Besides the financial metrics, we had to get some validation in the market that we are progressing towards the hybrid integration platform leadership. We are also doing good things around our API offering, because the API is the doorway to the platform story.

Slide 6

In 2019 we participated in the Forrester Wave. We had debated a little bit if we even go into it. Forrester takes what is called an iPaaS approach to the platform, which we are not fully aligned with. However, we participated and we were happy to see we were a strong performer in the Forrester Wave, which just validates we are one of the significant players in the hybrid integration platform market.

That was a good step to get awareness of Axway associated with the platform space, but more importantly for our strategy. As we are moving our offerings forward, the API is critical for everything. We had to get into the leadership quadrant with Gartner's Magic Quadrant. We achieved that in the second half of 2019. We are happy to see both of these analysts recognising what we are doing.

Slide 7

However, we have talked a lot about being on a transformation journey over these three years. About a year and a half ago I shared a lot of details about what we are trying to do over the next three years, and we kicked all of that off in 2018.

It required a significant amount of effort that Roland and I described would be done around the products, the offerings, the technology, what I call go-to-market, but a lot around the CSO organisation. All of this took investment, time, and effort to change a lot of things within Axway so we can embrace the future.

We have done quite a bit of this over the past 18 months. We have done a lot around the innovation. Over some of the last presentations, I have gone more technology side and talking about the evolution we have made on our products towards the platform. This year, we have focused more on the go-to-market. We have made some good reboots, let us say, of the go-to-market activity. Roland will share, after me, all we have done in this area.

We have also had to get our employees engaged quite strongly. When we started this journey, our employees were not with us, to be frank. We had a lot of attrition in the employee base. They were not fully engaged. I will give you a little more details on what has happened there.

We also have reinforced our management; I will make a few key points on that as well. We have also modernised our organisation. We have had to change the way we think about ourselves so we could attack the market properly.

Slide 8

To go a little deeper on the technology investment, back in the second half of 2018 we had to significantly increase our investment we were making in R&D. Just to remind you, we expense R&D. We do not capitalise anything. When we increase our investment, it goes straight to our P&L.

At the second half of 2018, I realised we were not driving the platform strategy, the API strategy, hard enough. We put some significant investment back into it, which continued on at that pace for 2019. Now we have made some good improvements in the technology and so we could kind of cap the R&D as we go into 2020.

But, you see, we moved from €58 million to €61 million. The first half of 2018, if we would have done that run rate, it would have been significantly below €58 million. The investment was strong over the past 18 months. It will start tapering as we go into 2020.

We additionally took the resources that we were investing and reallocated where they are spending time. We have a lot of legacy and history products. We have had to make a lot of hard decisions about what we do with our portfolio of products and reinvest those resources to help drive the future.

We have been moving the capacity of even the staff we have on hand from mid-60 Service to mid-70%. The additional capacity is allowing us to move stronger towards the platform and move stronger towards the API space. It has been showing returns.

Additionally, we bought some technology in Streamdata to help with the API space and event-driven APIs. All of this – and you will hear me say it constantly through the presentation – software is people, really. The people make the technology.

R&D was the worst for us in attrition back two years ago. We were experiencing in some of our technology centres upwards of 27–28% attrition. We have made significant improvement over the last year, decreasing our attrition by 19%. Now the R&D centres are at the level of the Group, so we are quite pleased with that.

Slide 9

I mentioned also that we have reinforced our management. It was more of a personal objective of mine we were driving quite hard, Roland and I and a few key others. But, we were a small group. We have been able to add some strength in finance with a new CFO. We have added an EVP over People & Culture. I brought on a gentleman to help us with the go-to-market efforts because that was a strong push for 2019. Rounding out the Executive Management team gives us more capacity to drive, which was definitely needed for the year and part of our strategy.

Slide 10

Going a little deeper, besides just the Executive Management, we have done a lot of investment in the top-level management of the Sales and Marketing. That is carried down and it is going down to the next level now. Overall, with our employees as well, we had to make sure all the employees were engaged in our strategy and what we were trying to do so we could continue to push into the market.

We were able to improve our overall engagement score across Axway by 18% in 2019 versus the measurement at the beginning of 2018. Now our employee engagement score is at 58%, which kind of means nothing. But against our survey, our survey target is 60%. At 60%, you have enough of your workforce fully engaged to drive the strategy. We are right in line with where we need to be to push hard to the next phase of Axway.

We have reduced our attrition overall across Axway by 15% over the year, getting it down to a level of about 17.7% per year. My target is 15%. That 15%, that is a healthy software company activity. We have our employees back. We have the resources back to continue to push towards our strategy. Internally, this was a very good metric for us to be able to sustain what we need to do next.

With that, I am going to ask for Roland to come up and give the transformation details of what we have done in CSO, because it is really a validation of what we have had to do in the go-to-market space over 2019. Roland?

Roland ROYER, Chief Customer Officer, Axway

Slide 11

Hello. Thank you, Patrick. Good morning everyone. Very happy to be with you today to give you an update of the transformation journey that we have started in 2018 with the creation of the Customer Success Organisation.

Slide 12

You may remember, for those who are following us, this slide that I used as my first slide in our 2018 July communication. We made the decision to create this Customer Success Organisation based on a few patterns, on a few observations that we were making that required some change within our company.

The first one for that: we were really engaged only with IT, really helping them to manage and control the operations. We recognised that we had to also engage with business lines to help them to transform. The revenue was historically coming very much upfront and transitioning with Subscription. We had to recognise that a big part of the revenue was going to come along the way and along the time of the engagement with our customers.

Our services – support, professional services – were really in a reactive mode, responding to customers when they had some difficulties and some need, contacting us, when today we realised that we need to engage proactively with them, driving adoption and deliver fast customer business outcomes. We created the organisation with a few guiding principles:

- Building this customer-centric organisation with, first, regularly and constantly measuring the customer experience and acting on the customers' feedback.
- The second was to build this organisation to develop the engagement with our customers, align with the 'learn, adopt, expand, and renew' lifecycle of our customers.
- Finally, to have a strong coordination and execution on the regional level, close to our customers and all the customers' interactions.

Today, the Customer Success Organisation is about 800 people from pre-sales, sales, all the services line, support, and the team of Customer Success managers that we created at this time that are engaged with our customers from the start all the way through their engagement.

Slide 13

While we were actually transforming our organisation to better serve our customers, we also recognised that we had to revamp our brand and go-to-market strategy, building up on our Customer Success business outcome over our product features and positioning Axway as a focussed leader.

We have a fantastic customer base. We have more than 11,000 customers. We have an extremely powerful and complete solution offering. We are mission-critical for all these customers. Every day, we are keeping their system running. However, we can have the best solutions, we can deliver great services, but we are not well-known giving the importance we have in their business.

As I often say, great technology alone is not enough. It takes much more than selecting the right software to be successful. That is why we, in 2019, invested and created a team named the Catalyst and creating a consulting services offering to help and guide our customers beyond the technology, through their transformation.

The Catalyst team have business solution and technology experience, and have been engaged and delivered over the last few several years, helping large enterprises to build projects, breaking silos to put the transformation, the project that they have, on the right track for success. They are very well-known in the market. This team and the offering that we have built reposition Axway as not just a one-solution vendor, but a trusted guide in their transformation.

Slide 14

We have the technology. We have the Customer Success Organisation, structure and goal, to be with our customers from the start to forever. We also recognised that we needed to excel in selling the right solution to the right customer. In 2018, we realised that we had to implement some changes in our organisation in that side.

We started early in 2019 by onboarding three strong general managers for the different regions, Europe, US, and the APAC, bringing a high level of experience and expertise in transitioning a business from License to Subscription, being able to bridge this gap between the technology and the business outcome and, I think, being able to build a successful network of partners.

As they came – and they came early in the beginning of the year – they quickly acted and recruited some experience on the API and digital part of the plan. They reinforced the local Customer Success management principle that we have in driving this engagement with our customers. They bring a strong culture and discipline of execution. All of that, and you will all see the impact for that, contributed to a very successful end of the year.

Slide 15

We are measuring success. I will share with you the result of two important financial KPIs and the progress of our signatures on the API, AMPLIFY API Management. Why are we focussing on this one so much? Because, as Patrick said, the API is the doorway to the platform. It is coming from this solution that the customer experiences and extends on the usage of our technology.

The other one will be the Subscription and the transition to Subscription. But, we also measure and use internally other non-financial KPIs. When we created the Customer Success Organisation, we implemented the measurement of customer feedback, customer satisfaction, and loyalty. Since we implemented the CSO, we have constantly seen an improvement in this feedback. Over the last 12 months, we won ten points on that. This is a leading indicator for us, as we know – and we all know – that satisfied promoters of a company will generate and accelerate success.

Slide 16

In July during the last presentation, I presented the API Management pipeline, saying this is a leading indicator of what I hope was going to be the booking of the success and the deals with this product. We drove during the full year lots of initiatives to generate this pipe and drive our team and drive the awareness of Axway on this market.

I mentioned the Catalyst team. We have been around the world, presenting multiple events every week. We recruited the Sales specialists. All of these actions actually generated the fact that our booking year-over-year on signatures, on API Management, grew by 22%. When we looked at the pipeline that we have today for 2020, it is much higher than when we entered in 2019.

The other KPI that I want to share with you is the transition to Subscription. During 2019, we worked to make most of our portfolio available in a subscription mode. Then we enabled our Sales team. We worked with our customers with the possibility to contract with us either as License or with Subscription.

Slide 17

The result of that during the year was we grew our booking by 33%. We grew our revenue on Subscriptions by 42%. The result of this booking is the fact that today is the first year that actually the Subscription revenue overpassed the License. Together, the recurrent revenue of Axway, when we include the Maintenance and Subscription, is just shy of 70% of our revenue. A great transformation that we were explaining at the beginning of the journey in 2018.

Slide 18

In 2020, a couple of weeks back we were launching the year with the Customer Success Organisation. We entered the year with a very strong momentum. The results of Q4 generated very good momentum in the team. We are going to focus for 2020 with three key objectives:

1. Continue to increase our strategic value and positioning with our key customers. Building up on the catalyst and the Axway Accelerate offerings that we build. Creating and strengthening the relationship that we have there. Cross-selling around the platform by being engaged in their transformation.

2. Accelerate the success of AMPLIFY, meaning finding new customers. Building up on the go-to-market investment that we have made. Building up on the Inside Sales team and the bigger team on Sales that we have created to generate more awareness of Axway and more opportunities.

3. Finally, also continue to build and strengthen our partnerships in each region. We just launched this year with Sopra Steria France a very important partnership program around APIM and the digital transformation. We will continue. We have been very successful this year and the year before in APAC or in LATAM to work with our partners. We are actually rebooting the programme in North America where we have not been executing well this last year on the partnership. We recruited the team. We are working with new partners. We have new opportunities and that will be an important part of what we drive in North America.

Slide 19

In conclusion, I will say that we built the Customer Success Organisation and the alignment across the team on the premise that we will work with all customers from start to forever. Axway's mission-critical solution has been crucial for customers for the last 20 years. I have been very, very pleased with the work that we have done in the last 18 months. We will continue in 2020 with the same focus. Together, we will delight our customers for the next 20 years.

With that, I will hand it over, back to Patrick for the financial part.

Patrick DONOVAN, CEO, Axway

Slide 20

Thanks, Roland. I do want to make a little comment before I go into financials. Because it is important to understand we have made the choice here today to not highlight a lot the financials and talk about, 'We are pleased with the financials. We had a good year, hitting our target,' but not to just sit here and throw the numbers up or to throw customer winds up, but to go through a lot of things that are, yes, inward-facing and part of our transformation.

Some of you may not fully understand why, but I will remind you back in 2017 we had a choice to make. Software is an interesting industry because you create an idea, it runs for maybe 10–15 years with success, then it becomes mature. We were starting to hit the maturity in our portfolio with several of our components, except maybe API.

We had choices to make. One choice a lot of our competitors made was to sell to a private equity firm that would do a financial transaction, strip out all the costs, and run it for cash. That gives private equity firms a nice return. It is a model. It works. A lot of the US companies are doing it. We could have bust it up into its pieces and sold for a high value the key assets in the Group and then ran for cash the others, as another change. However, we have taken a much longer-term approach that will hopefully benefit our customers, our employees and all of the shareholders for the long term and not just for a short-term win.

All of these transformation changes are necessary because we are building the foundation, we hope, that is going to be here 10–15 years from now, still a public company, still serving our customers, still delivering value to all our constituents and not just one of them. That is why we are happy with the results. However, we are still on this journey.

As we go into 2020, we have things to do. We have to build this stable company so that as we come out of 2020 we could start being aggressive in the market for the long-term. With that, I will go through and cover some of the financial points. But, remember we are looking at this as a journey.

Slide 21

In 2019 we have finished up, as we said, 3.3% organic to €300 million revenue with a strong Subscription growth. Our gross margin we kept stable at 70%. As always, there is a mix in there, but I am pleased with the gross margin staying at 70%. You will see exactly in the financials what we are doing inside the walls of Axway. 6% growth of R&D finishing at €61 million, where we are investing in our product. We had a 19% growth in Sales and Marketing, finishing at €99 million.

In line with what I have been talking about, as we go into 2020 we have had to do these shocks to the system of Axway to get us moving forward. Our goal was that this is the low year in our margin. In 2020, we start building and coming out of it because we have made these changes and investments now to help benefit the future. We should be able to keep stable, in absolute value, what we are spending on Sales and Marketing, R&D, or even look to opportunistically drop. Because Roland does not like hearing this, but I am expecting more for the investment we are making in our Sales and Marketing for next year.

We should get the return. We did a lot of experiments to see how we could shock the market to view Axway differently, to talk about Axway differently, to engage customers differently. Some are working really well; others have to be revised. We learn from them and we move on. However, these are all the things you have to do to really take a maturing software company and set it on the course to be relevant again for the next 10 or 15 years. We hit a profit on operating activity of 8.6%, or €26 million. This should be a low. Then you will see we are going to forecast driving out of it for 2020. Our net profit finished at €5.4 million, or 25 centimes per share.

Slide 22

Looking a little bit more on the revenue side, as Roland had said, we are pleased to see our recurring revenue go up to 69%. That should continue to go up as we transform our revenue streams. The Subscription revenue surpassing the License, we expected this to happen during the journey. We are not expecting to have it ever go back down below License.

The Maintenance we were quite pleased with, to be able to keep a stable base of Maintenance when you are dropping the License revenue. When you mathematically do the computations with the standard attrition rates, it puts the Maintenance under stress. Being positive was our goal and we achieved that for the year.

We have our Services dropping, as the way the technology is engaging the customers and the way they are buying the License versus a Subscription changes how they use services from a software company versus maybe other consulting firms. Overall our revenue finished at €300 million, up 5.7% in total and 3.3% organic.

Slide 23

Going a little bit further on the Subscription, we had a strong Q4. Again, you are going to hear Roland and I talk about the key pieces in it and what we are learning from it versus absolute numbers. The new ACV growth at 33% is very important to us. The Q4 was really strong and really drove that, but why was Q4 not an anomaly in this system and we just got lucky?

We have done investments all throughout the year, that Roland talked about. We have changed a lot of the leadership. We have changed a lot of the Sales teams. We have engaged customers differently. All this was building pipeline through the year. We had the pipeline there. I got questions from a lot of the investors I talked to at the end of the third quarter results: 'Why do you hold your guidance? You have a tough Q4 to do.' We had the pipeline to do it. All we had to do was do our job. Roland and the team did their job for Q4 and delivered what we expected. The health of the pipeline is now becoming less of a hope and more of just a consistent, reliable mechanism by the changes we are making.

We are pleased that Q4 delivered the results we saw in October. It requires a little faith in software, but you are going to do it and we did it. We are seeing the trend come into Q1. We still have 2020 to do, but all the signs are good that we will.

Slide 24

On License and Maintenance, I created this signatures metric to track new License and Subscription we are bringing in. The License dropping for me is not a problem as long as the signatures metric is growing, because that is going to be an indicator of how overall my revenue should move in License and Subscription. We finished at €52.8 million of License, about an 8% drop. This could be a variability year-over-year.

As a company, we are playing in a league of big fishes, let's say. If you look at the API chart, there is five in the 'leaders' quadrant. We are the smallest of the five, with €300 million of revenue. We have to engage our customers differently and be very strategic. I cannot spend the money they do in Marketing. I do not have the Sales team they do. I have to pick and choose where I am going to fight and win.

We have to engage the customer with a hybrid approach on the contracting model – 'Do you want to buy a license? Do you want to buy a subscription that you run on your premises? Do you want us to run it for you?' We have to be quite flexible. A lot of the work we have done is training and working with our Sales teams, our Marketing teams to provide our offerings so that when we are in the deals, we could talk at how the customer wants to talk to us instead of forcing them down one path.

Slide 25

This is the signatures metric for the year. I have been happy through the transformation. It is at 8.3% for the year. We did 7.8% for the last year. We are seeing the visibility that this positive number continues. What does it translate to? It is taking into account both the License and the Subscription. At a very broad level, if I am going 8% here and this is my License and Subscription and I am holding my Maintenance flat, yes, you could see how we get to a 3% organic growth for the year. We will continue the practice.

To note, this does not include the renewals. Some companies in the market are including renewals when they talk about bookings. This is really new business for us, this is new money. I want to see the new money coming into the business.

Slide 26

The revenue by geography, I just want to make one important point here. If I go back and check every year, I think this might be a first year that we grew every region. That was a nice accomplishment that our leadership teams in each region are pushing from a business level to grow the revenue in the region, whether it's License, Maintenance, Service, Subscription, but focussing on driving the health of the region to continue to grow their region's total revenue.

Slide 27

A quick balance sheet now. We finished at €21 million of cash, down from the €36 million in the prior year. Our net debt is at €22 million. Our DSO remains stable at 77. Our current deferred is at €61 million. Total assets are at €568 million, just up slightly from the prior year. Our equities remain stable at €362 million.

Slide 28

All our banking covenants on a revolving credit facility remained in good shape. Our leverage ratio is below 1. Our leverage ratio is what drives our availability of utilisation of the credit facility. Of the €125 million line, we have about €42 million borrowed. But, we still have some room in this facility, in case we need it.

Our cash flow is a bit challenging with our transformation in the business. To try to make it simple, as we are moving from the License and Maintenance, if you remember the last revenue recognition rules, we had to get paid up front pretty much, or within the first year, to be able to take that revenue up front. The whole industry's behaviour was to shove that cash into the first year. Now, as we are trying to meet our customers and what they are doing, the Subscription economy is almost like a pay-as-you-go economy. The customers, even though they may manage a Subscription or License on premises, if they are contracting with us on a Subscription, they are expecting to pay over time.

Most of our Subscription ACV are annual payments. If I did €17 million of ACV – let's say on average, those are three-year deals, or €50 million or so – I am only getting a third of that cash this year, where I would have almost all that cash up front under the license model. That helps to explain why my change in my working cap is negative this year and why my free cash flow is flat.

This will all start coming back to me. Next year, I build the other third. The year after, I build another third and it layers in a waterfall. However, during the period of transformation, you take this dip for a year or two, whereas since we did good in sales, we take the dip this year. Next year we will layer on, the year after that we will layer on, and we should get back to the €20-plus million we were doing historically in working cap quickly over the next few years.

Slide 29

With that, I will finish up 2019 and give you a few comments on 2020 and beyond.

Slide 30

We have not lost sight of being the leader in the hybrid integration space. We continue to push for this. We expect to be a leader in the API space as well because that is our approach to the platform market. It is an API-first approach.

Slide 31

Financially, we are targeting to continue to organically grow. As I said last year, my expectation is we are now back on a path to where we will be able to grow revenue every year. We are targeting to be at or above the €310 million of revenue for 2020.

Also in line with what we said last year, 2019 should be the low point. We are expecting our margin to be above 10% for 2020. With the improved margin, we are going to drive to start improving our net income as well. To be very technical financially, it is hard to optimise your taxes when you drop your margin. We could start looking to improve our tax position as we come out and start building back our profitability.

Slide 32

Then the midterm ambitions. As we come out of 2020, we have talked about this 2020 ambition constantly. 2020 is the finish of what we are trying to accomplish over the three-year journey. As we start ending the year, we are going to look at what the next three or five years holds for us.

As a company, we are targeting to get back to that target of €500 million of revenue. I want to get back to the range of the profitability we were doing before, between 15% and 20%, and to get back on the EPS over €1 per share. Those are all priorities for us over the midterm. As we go into the planning period, we will be taking those into account.

Slide 33

With that, Roland can join me back up on stage and we will take any questions. There are questions that will come in from the web as well. If you have any questions in the room, just raise your hand and they will bring you a microphone.

QUESTIONS AND ANSWERS

Jean-Baptiste BOUCHET, CIC Market Solutions

Good morning. My first question is, well, where does the performance of Subscription in Q4 come from really? Is there a big contract or any contract recognised up front, or something like this?

My second question is, when you mentioned a medium-term goal, is it more a 2021 or more 2023? Can you give some guidance?

The last question: where do you see the levers to improve the margins to 20%?

Patrick DONOVAN, CEO, Axway

Okay, I will try to go in order. For the ACV in Q4, the mix of it, that was a large transaction. We had some large, seven-figure transactions, but there was no one enormous contract we had. We had a really good volume of transactions. All the teams across the main regions brought in a good amount of business. The health of the business and the ACVs came in for Q4. We are quite pleased with that.

The accounting for the contracts I could spend an hour on. I do not know if you sat through the Capital Markets Day of Software AG; they spent an hour on how you account for all the craziness with the new rules. To make it simple, though, if we are hosting the customers, if we are running it for them, then it is monthly revenue. If they are running it and it is a hybrid – so they take the main portion of the activity in their server room and they may be connecting to the cloud for different components, but the engine, let's say, is on premise – then the rules have changed over the past between IFRS 15 and the prior rules. We have to take a portion of that contract up front. We take about 50% of that contract up front. That is why you cannot get the boost in our Subscription line in Q4. However, it happened throughout the year as well and a little bit in 2018.

Those are what we call customer-managed subscriptions, because they take the primary drivers and the license and only use our cloud services for a little bit. They have a new model of revenue recognition. In the past, those used to be rentals and they would be taken monthly over time as well. Then, there is the pure cloud ones, that are monthly. We had some of the boost in Q4 from that. That helped hit our revenue. That is why I created that signature metric – that, to me, tells whether we are going to grow either now or in the future. It is really trying to strip out, trying to figure out the craziness of the revenue accruals.

Next one, the midterm. For me, as I said, we are looking to target three or five years. Obviously if you do all the math, I am going to have to buy a few companies. Are they available tomorrow or in five years? I do not know. I will have to keep at that midterm level versus trying to say 2021 or a specific year.

Last question, the 20%. As we grow, we have to continue to rationalise our portfolio and pull back R&D or keep it stable while the revenue grows. In Sales and Marketing, we really pushed hard many areas and we should be able to pull back on the spinning there. As long as we maintained that methodology and the revenue is growing, we should be able to gradually increase the margin back to the levels it was before.

Arthur CARLI, Head of Investor Relations, Axway

The first question from the web is coming from **Derric MARCON, Société Générale**. What is the amount of ACV in 2020 that you expect to flow out from the new ACV signing recording in 2019? In other words, last year the €13.1 million new ACV signed were supposed to bring €8 million revenues in 2019. Should we apply the same formula, or the late signing in 2019 makes a big difference in the way we should calculate it?

Patrick DONOVAN, CEO, Axway

The 2019 signing, we had more customers managed than we did in 2018. In 2018 we had a lot that were actually managed accounts. That brought a higher percentage of the new ACV that would flow into the next year. This year is going to be a bit less. I would estimate maybe 20% or 30% of the signings in ACV – maybe a little higher, 30–40% – will flow into 2020.

Arthur CARLI, Head of Investor Relations, Axway

Second question: do you expect the gross margin of your Subscription activity to improve further in 2020?

Patrick DONOVAN, CEO, Axway

Yes. 2019 we had some anomalies on our cost base. We had some technologies that software vendors sometimes will extort you once you are on them. We had some exceptional charging that we were not able to bring down our margin as much as I would have liked in 2019. We will be able to do so in 2020.

Arthur CARLI, Head of Investor Relations, Axway

Last one from Derric: despite the sharp reduction of your Service activity and its repositioning on more added-value services, the profitability of this business remains low. Will you continue to streamline the cost base from here, or are you envisaging other options to turn around this business at a quicker pace?

Roland ROYER, Chief Customer Officer, Axway

Yes, we will, for that question. We are focussing on our higher-level services further. I explained two factors that explain the drag and the decrease. We are working on higher level services, so the amount is less. We are working also in the different regions much more with our partners that we use to deliver long-time engagement with customers that we are less doing right now, as we are partnering.

If you look at some renewals in APAC, that had a big drop because we are actually very successful to work with the local partners there. Yes, we adjust. There is always an upset. However, we adjust also our workforce to the level of activity that we can have on Services.

Patrick DONOVAN, CEO, Axway

That is why the margin lags. If the revenue is dropping, the margin will drop a little faster until you adjust it and find the equilibrium. The margin should come back in 2020 to the levels of the prior year, of 2018.

Arthur CARLI, Head of Investor Relations, Axway

Coming from **Matthias DURNER at Discover Capital**, where would you see your underlying effective tax rate? Why did you see such a significant working capital outflow?

Patrick DONOVAN, CEO, Axway

Yes, the effective tax rate, as I alluded to, is extremely complex when you are changing quickly the profit levels. When you have a steady state profit level over all the countries we participate in with multiple different tax positions and MLLs – in the past, I was able to maintain that quite well and get a low-20s effective tax rate. Not possible this year and will not be possible next year.

But, my target is, as we come out of this and get back into the margin percentage in the 15–20% range, we should be back in the 22–23% effective tax range, especially with the changes made in the tax codes in the US. We see France moving a bit as well. That should help us to stay at that 22–23% level.

Then the working capital I did cover a bit in my presentation. However, with our change in business model, it is really driving the way the customers pay us. It will be over time instead of all up front. We have the financial health to allow that to happen. Some of the smaller competitors had overcompensate their sales guys to get as much cash up front. We have not had to do that. We are not trying to force something onto the customer. We are trying to be a little bit more customer-friendly in the way we engage them.

Arthur CARLI, Head of Investor Relations, Axway

A few questions coming from **Johannes RIES at Apus Capital**. Could we expect some partnership announcements in the coming months? How is your pipeline today? Where do you intend to acquire? Do you have add-ons need?

Patrick DONOVAN, CEO, Axway

I will address the last question, then if you want to take the first two? For the last question, where we look to acquire, I do not believe we need to buy a technology. We should have what we need to drive into the platform market. If we do, it may be another very small acquisition, like Streamdata, where you choose to buy something real quick for a low value instead of add resources and R&D to do it.

However, instead of a large technology buy just for the technology, we would be looking to go in to acquire some customer base or an offering that is complementary to our platform that comes with a customer base, because we want to really drive revenue over the next few years. Roland?

Roland ROYER, Chief Customer Officer, Axway

Pipeline first. Partnerships within pipeline, I will take the pipeline. I shared one of the slides where I was showing a part of the pipeline, but an important one, which was the API Management pipeline. If you looked at it, compared to what it was last year at the same period, it is an increase by 60%. That is just for the API pipeline.

The pipeline has increased. As we said, we invested a lot in in the go-to-market and sales to create this pipeline to have much more opportunities that we can work on and that we can build the success not on one deal, but on real people. That is what happened in Q4, so a good increase on the pipeline.

On partnerships, there are two types of partnerships. We do have partnerships and good partners in terms of technology and in terms of influencers or system integrators. We have worked during the last year with Microsoft. We had a good partnerships with Microsoft, AWS, with some other small products and technology that really complements our offer as well. That has been able to differentiate us and build a stronger solution in terms of technology.

The influencers and integrators, as I mentioned before, that is the relationship that we built on original base. It really depends on our position, our customer presence, and in the local system, in the local areas. We are working currently in APAC with a specific partnership that hopefully will bring in deals. I mentioned the Sopra Steria in France and in Europe. In North America, as I said, we are just at the beginning, but we have the goal to work there and to have some partnerships there.

Arthur CARLI, Head of Investor Relations, Axway

Some questions coming from **Brian NELSON at Long Path Partners**: what would be helpful is to understand the Subscription revenue run rate exiting Q4 2019. The €23 million does not seem to be the right figure, given the revenue recognition explanation you gave. In other words, how much of the €23 million in Q4 Subscription revenue was pulled forward?

Patrick DONOVAN, CEO, Axway

Speaking specifically of Q4 revenue? Okay – I was trying to figure out if he is talking ACV or revenue. On the revenue for Q4, there is a decent portion, probably €8 million to €10 million of one-time, let's call it up front revenue on the ACV signed in Q4.

On the carryover, I am trying to remember the exact figure, but it would be over €50 million will roll forward. We are struggling a bit to communicate, as some of the analysts are struggling a bit with the whole industry. We are facing this. I read Salesforce's communication on Mulesoft. I have seen Software AG's capital market days. All of us in the industry are facing this. The challenge is how do you communicate on something that is recurring that will come back to us in two or three years when a customer signs, but we are forced to take a portion up front. That is where we are at.

We had over €50 million that is going to be recurrent rolling into next year as a base in the add-ons from the new recurrent that we signed in the year, plus whatever we signed next year. It is complicated and we are looking for a way to clarify it a little better. I read deeply Software AG's and I do not agree with how they are doing it. As we come into the half-year presentation, we will see if we could add a little more colour to help out the calculations and the forecasts. However, we are including all of that as Subscription, because to us they are subscriptions or rentals. The customer is not taking the License. They do recur.

The ACV we signed now is very important. They are going to come back to us as renewals. When you compare them to the traditional License, we would get the one-time shot and that would be it. Our relationship would just be Maintenance from then on, unless they buy more from us. Now, they are effectively renting it every year. How we take the accounting is complex, but we are happy it is transitioning to this model because it gives us a very nice stable base, like the Maintenance was in the past model.

Jean-Baptiste BOUCHET, CIC Market Solutions

Two last questions. The first one is if you acquire a company, how would you finance it? Would you be willing to finance it with equity, with only debt, or both? Where do you think you could buy a company? The potential targets are currently pretty expensive. Where do you think you could buy companies at a reasonable price? Is there a region you are looking for? Do you expect mostly synergies from your potential acquisition?

Patrick DONOVAN, CEO, Axway

To finance it right now with dropping intentionally, this is also why I have said I am not doing M&A during this journey for the three years now. Dropping the margin under our current borrowing capacity, that drops my leverage ratio, giving me the ability to borrow. As I bring back the margin, I am going to increase my capacity to use the credit facility or borrow even outside the credit facility. That comes back to me as a vehicle debt in either term debt or the current facility, depending on the size of the acquisition.

Equity is not off the table, but that is more of a discussion we plan as we go into the size of the entity. At this level, I am not going to do anything with equity. We are undervalued in the market. I would be giving away my shares. I am not going to do that. However, it really depends on the size of the acquisition.

Yes, the ones that sound obvious for acquisitions or that could be a target are very expensive. We are going to have to look to the not-so-obvious design value. The market on some technologies just does not make sense how they are getting valued. There are a few out there. Whoever buys them, I am not sure how they will ever get the return unless it is a huge company that could really leverage. Like when Salesforce acquiredMulesoft, they have all the Salesforce customers to go try to sell to. They could force some value there. However, if it is a technology buy at our size, we do not have that leverage. I have to look very specifically at some different technologies that may not seem obvious at first how they fit together, but we do have quite a few targets that are like that.

Regionally, I always would look to help my APAC or UK or European space. However, as you know, in technology there is a lot in the US to look at too. We are not focussed so much on regionally, though.

Arthur CARLI, Head of Investor Relations, Axway

I have the last one from the web, from **Derric MARCON, Société Générale**. How many Axway products are now fully compliant with the SAAS platform (multi-tenant, microservices)? What is your win rate against native cloud vendors like Apigee- Google, MuleSoft-Salesforce?

Patrick DONOVAN, CEO, Axway

As far as internally on our products, most of our core products are compliant. B2B, MFT, API are all on the platform journey. Building every day, it helps them in different ways with the platform. The microservices is a new launch at the beginning of 2019. We pushed that and it is still finding its place in the market. The core products are not fully compliant with the microservices piece yet but will be over time. We will continue to develop that product out over the year.

What is our win rate? I do not have a specific win rate. We are looking to differentiate against players like Apigee and MuleSoft and IBM's offering and Software AG's offering. They all have very specific targets they are going after and we are finding where our target is. We have had to learn. We are not the low-end provider, or some of the companies will come in and have a very quick-to-use, on-the-cloud, try-and-buy system. That is not us. You could solve a quick problem easily like that, but then there is low money in that. Their hope is to expand, but often that product is not capable to expanding to the more complex use cases we sell. In our journey to move and integrate data that I have always talked about, we are taking on the more complex problems that becomes the backbone of a large company's transactions and not just a cute toy on the side. That is where we are focussed to find our space.

When we are in our lane, we have a very good win rate. However, when we get out of it and try to drop down into low-end deals that are just small use cases, we do not have very much success. We are finding our space and way to win.

I think with that, it is 10 o'clock, our time is up. Thank you all for coming.