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OTEX.TO - Q1 2020 Open Text Corp Earnings Call

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OVERVIEW:

Co. reported 1Q20 total revenues of $696.9m, GAAP net income of $74.4m, and GAAP EPS of $0.27.

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PRESENTATION

Operator

Thank you for standing by. This is the conference operator. Welcome to the OpenText Corporation First Quarter Fiscal 2020 Conference Call. (Operator Instructions) The conference is being recorded. (Operator Instructions) I would now like to turn the conference over to Harry Blount, Senior Vice President, Investor Relations. Please go ahead.

Harry Blount - *Open Text Corporation - SVP of IR*

Thank you, operator, and good afternoon, everyone. On the call today is Open Text's Chief Executive Officer and Chief Technology Officer, Mark J. Barrenechea; and our Executive Vice President and Chief Financial Officer, Madhu Ranganathan. We have some prepared remarks, which will be followed by a question-and-answer session. This call will last approximately 60 minutes with a replay available shortly thereafter.

I would like to take a moment and direct investors to the Investor Relations section of our website, investors.opentext.com, where we have posted 2 presentations that will supplement our prepared remarks today. First, our strategic overview titled open Text Investor Presentation, and the second titled Q1 FY 2020 Financial and Business Results includes information and financials specific to our quarterly results, notably our updated quarterly factors on Page #7.

In November and December, Open Text management is pleased to meet with investors throughout Canada, the U.S. and Europe, and we look forward to attending the following conferences: the Bernstein Technology Innovation Summit on November 6 in New York; the TD Securities Technology Conference on November 14 in Toronto; the RBC Capital Markets TIMT Conference on November 19 in New York; the Credit Suisse Technology conference on December 3 in Scottsdale; and the NASDAQ Investor Conference held in association with Morgan Stanley on December 4 in London; and also, the Barclays Global Technology, Media and Telecom Conference on December 11 and 12 in San Francisco. Please feel free to reach out to me or the IR team for additional information.

And now I'll proceed with the reading of our safe harbor statement. Please note that during the course of this conference call, we may make statements relating to the future performance of Open Text that contain forward-looking information. While these forward-looking statements represent our current judgment, actual results could differ materially from a conclusion, forecast or projection in the forward-looking statements made today. Certain material factors and assumptions were applied in drawing any such statement.

Additional information about the material factors that could cause actual results to differ materially from a conclusion, forecast or projection in the forward-looking information as well as risk factors that may project future performance results of Open Text are contained in Open Text's recent Form 10-K and 10-Q as well as in our press release that was distributed earlier this afternoon, which may be found on our website. We undertake no obligation to update these forward-looking statements unless required to do so by law.

In addition, our conference call may include discussions of certain non-GAAP financial measures. Reconciliations of any non-GAAP financial measures to their most directly comparable GAAP measures may be found within our public filings and other materials, which are available on our website.

And with that, I'll hand the call over to Mark.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Thank you, Harry. Well, good afternoon to everyone, and thank you for joining today's call. Let me start with an additional thank you to those who participated in our annual investor conference last month in New York City. We asked for and appreciate your feedback. We listened, and the Open Text leadership team presented our strategic vision and operational plans for a stronger Open Text. Our trust is earned every day with our customers, and it's our planning that gives us confidence in our strategy and operational delivery.

This is our 19th consecutive quarter of year-over-year growth in constant currency led by our double-digit Cloud growth. The strong Q1 results we are announcing today is a continuation of that long-term perspective and the team's continuous commitment to excellence. 19 consecutive quarters of year-over-year growth is the textbook definition of durable.

We laid out a clear, purpose-driven strategy during Investor Day to help companies unlock their information advantage; be the leading platform for enterprise information management; deliver the best hybrid cloud for customer experiences; a relentless focus on operational excellence and efficiency; and continue to hire, develop and retain the best, most diverse inclusive talent in our workforce. In today's digital era, enterprise information management is a strategic and mission-critical platform for enterprise customers.

We also laid out a value-creation playbook during Investor Day. That playbook includes recurring revenue growth; margin expansion, with margin gains above 40% adjusted EBITDA, reinvested for future growth that includes innovation, products, sales capacity and customer coverage; accretive and strategic acquisitions; strong cash flows; customer-driven innovation; and a disciplined capital structure and approach to dividends.

In addition to our purpose-driven strategy and value creation playbook, we presented our fiscal 2020 business profile that included: low single-digit organic growth plus additive M&A revenues; high single-digit cloud growth; customer support with constant to low single-digit growth; license business, constant year-over-year; and professional services, constant year-over-year; and continued optimization for margin; continuing to expand EBITDA margin; and a longer-term view for fiscal 2022 aspirations of 38% to 40% adjusted EBITDA; and $1 billion to $1.1 billion of operating cash flows.

The Open Text Business is an annual business. We view it annually. We ask you to view it annually, and I'm pleased with our start to fiscal year 2020. In constant currency, with approximate numbers, total revenues of $707 million and 6% growth. The team delivered the highest Q1 revenues in the company's history. We also had positive organic growth within the quarter. Annual recurring revenues of $557 million were up 7% year-over-year, representing 79% of total revenues driven by our cloud revenues of $239 million, which increased significantly by 15% year-over-year.

Customer support was up 2% to $317 million. License was up 3% to $79 million. PS was constant year-over-year. Our adjusted EBITDA dollars are up 5% to $259 million, and trailing 12-month cash flows are up 4% to $842 million.

Let me spend a moment on some key customer wins within the quarter. The U.K. Department of Work and Pensions has depended upon OpenText Exstream since 2009 to create multichannel notifications to the U.K. benefit system. Having successfully used the software now for over a decade, the DWP has further modernized their extreme environments now into the OpenText Cloud.

AAA, the Auto Club Group, represents over 9.4 million members and is one of the largest AAA clubs. After selecting OpenText Identity and Access Management in May of last year, AAA has recently expanded that partnership with Open Text to manage 16 million digital identities to support growth and expansion, all in the OpenText Cloud.

Third win I'd like to highlight is the Deutsche Bank, a German multinational investment bank and financial services company, selected OpenText Magellan to provide the ability to seamlessly transform complex data into compelling visualizations and graphs and charts and tables and diagrams for all their lending businesses.

I'd also like to highlight Daiichi Jitsugyo, a leading Japan consulting firm, offering customer solutions that combine manufacturing, marketing and services, which selected OpenText Extended ECM for their pharmaceutical business unit due to its complexity with SAP and ability to effectively manage the creation, review and approval of new pharmaceutical trials.

And lastly, the International Committee of the Red Cross based in Geneva, Switzerland selected OpenText Media Management to capture, store, manage, distribute, retrieve and archive its multimedia assets with the ability to support its mobile workforce in areas with poor network connectivity while also providing a very high level of security for confidential assets.

Look, the cloud and hybrid are the dominant themes here. The cloud migration is a once-in-20-year shift within enterprise software. Our hybrid cloud strategy is resonating with customers, and I'd like to expand on that a little bit. First, it's about providing customer's choice in completing the need, as I like to say. That is about focusing on running anywhere and allowing customers to consume any way. Run anywhere. Consume any way. By run anywhere, we mean off cloud, our cloud, somebody else's cloud. By consume any way, we mean to consume by license or subscription. And it's all integrated both off cloud and on cloud. Combined, this is hybrid, and it completes the need for our customers.

Second, it's about modernization and offering customers the latest enterprise-class solutions in a seamless API-agnostic, compelling user experience managed by Open Text, managed by a third party or managed by the customer themselves.

At Enterprise World at Investor Day, we detailed our next-generation platform called Cloud Editions or CE and OT2. OpenText Cloud Editions is our EIM software native to the cloud, and OT2 is the EIM platform services available for direct consumer consumption. We're on track for the delivery in Q4 of this fiscal year. CE and OT2 is a cloud-first approach. We have successfully transitioned into a modern cloud company, servicing the information needs of the world's largest enterprises and governments.

Let me turn my remarks to Q2. Q2 is historically a strong quarter for the company, and our Q2 outlook is favorable. While we have not seen any material impact to our business due to macro-related factors, we have taken prudent steps regarding customer spending environments in the U.K. due to Brexit uncertainty, Central Europe due to a slowdown in manufacturing and China due to trade tensions. Our U.S. business is looking solid. Over 50% of our revenues and profits are located in the United States. U.S. dollar also remains very strong compared to other currencies, and this has caused a short-term FX revenue headwind.

I'd just like to recall that in fiscal 2019, the FX revenue impact was a negative $53 million. In Q1 fiscal '20, this most recent Q1, the FX revenue impact was a negative $10 million, and Madhu will get into that in more detail. And we now expect a total revenue impact of a negative $35 million to revenues in fiscal '20. This is an industry challenge, not an Open Text-specific challenge.

Let me add some additional Q2 financial color. We are expecting Q1 to Q2, sequentially, high single-digit revenue growth, and this includes a negative $10 million of FX revenue impact; low to single-digit operating expense increase; and flat adjusted EBITDA dollars, year-over-year (Corrected by Company after the call), as we complete the integration of Catalyst and Liaison customers, infrastructure and employees. We'll have the integration of these 2 acquisitions complete within the quarter. You will see these items presented in the Quarterly Factors section of our investor materials.

Again, Q2 is a seasonally strong quarter for Open Text. Our outlook for the second quarter is favorable.

I'd like to leave you with a few key thoughts before I turn the call over to Madhu. First, our Q1 results are a continuation of our long-term planning and execution, another strong data point to the long-term durable nature of the Open Text business. We delivered the strongest Q1 revenue in the history of the company and our 19th consecutive quarter of year-over-year revenue growth in constant currency.

Second, in constant currency, we had growth in all the right places, with 15% growth in the OpenText Cloud, 7% growth in recurring revenues, and our adjusted EBITDA dollars expanded by 5%. This is growth in all the right places.

Third, our balance sheet continues to strengthen. Trailing 12-month OCF is up 4%. We had approximately -- we ended the quarter with approximately $1 billion in cash and a $750 million undrawn revolver, supporting our total growth strategy. Our net debt is $1.6 billion. Our trailing 12-month adjusted EBITDA dollars is $1.1 billion. And that leaves our net debt to adjusted EBITDA ratio, just dividing the 2 numbers, at 1.5x.

Fourth, the company is ready for all scenarios. The continued adoption of hybrid cloud by our customers. We're well positioned to capture EIM share both in the United States and globally. We are the market leader in content services and business networks. We're focused on gaining share with our upcoming Cloud Editions and OT2. Balanced and natural hedging in our cost structure that reduces FX volatility to earnings. We are a patient and disciplined strategic acquirer, and our balance sheet is strong.

We are confident in executing to our long-term fiscal '22 aspirations while delivering to our shorter-term fiscal '20 targets that we outlined at Investor Day just last month.

Open Text is durable in both up and down economies.

With that, it's my pleasure to turn the call over to Madhu Ranganathan, Open Text's Chief Financial Officer. Madhu?

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Thank you, Mark, and hello, and thank you all for joining us today. Our first quarter of fiscal '20, it reflects a focus on operational performance, strong expense management and continuing to build on our balance sheet strength. And turning to the details of our quarterly results, similar to prior quarters, my references will be in the millions of USD and compare to the same period in the prior fiscal year. Also, as a reminder, during our first quarter fiscal '20, the impact of foreign exchange was once again meaningful. In our press release, you will see the impact of FX across the entire P&L in all revenue streams and our earnings.

Let me start with revenues and earnings. There was a $10 million FX impact to revenue during the quarter. Total revenues for the quarter was $696.9 million, up 4.5% or $706.6 million, up 5.9% on a constant currency basis.

On earnings per share, GAAP earnings per share for the quarter was $0.27 per share, up from $0.13 per share for the same period last year. And let me outline the reasons. Now first of all, higher revenues this quarter; and second, lower depreciation and completion of the required amortization period of certain technology assets and accounting purposes and restructuring charges as well as higher interest income. Our tax provision was also lower due to certain reversals during the quarter. This led to an increase in net income of $38 million year-over-year, up 105%.

Non-GAAP earnings per share for the quarter was $0.64 on a diluted basis, up from $0.60 per share for the same period last year, or $0.65, up $0.05 per share on a constant currency basis.

And let me now share with you all the details of our results. The geographic split of total revenues in the first quarter was Americas, 60%; EMEA, 30%; and APJ, 10%. The main vertical sectors, financial services, business services, consumer goods, technology, public sector and health care, contributed 85% of our annual recurring revenue.

Our annual recurring revenues were $549.6 million for the quarter, up 5.8% or $556.6 million, up 7.1% on a constant currency basis. Annual recurring revenues as a percent of total revenues increased 79% for the quarter and reflecting similar seasonal strength to our first quarter last year and inclusive of contribution from our cloud-based Liaison and Catalyst acquisitions.

Our cloud revenues are particularly strong in the quarter at $237.3 million, up 14%, or $239.3 million, up 15% on a constant currency basis. Customer support revenues were $312.3 million for the quarter, up 0.2% or $317.3 million, up 1.8% on a constant currency basis. Our customer support renewal rate was up slightly to approximately 92%. Our license revenues for the quarter was $77.9 million, up 1.3% or $79.1 million, up 2.9% on a constant currency basis. Our professional services revenues were $69.4 million for the quarter, down 1.7% or $70.8 million, up 0.2% on a constant currency basis.

Turning to margins. GAAP gross margin for the quarter was 67.2%, up 110 basis points compared to the same period last year. Our adjusted gross margin for the quarter was 73.1%, down 30 basis points compared to the same period last year and primarily due to dilutive margin impact of Liaison and Catalyst. Also on an adjusted basis, cloud margin was 57.1% during the quarter, down from 58% in Q1 last year and reflecting our integration activities with Catalyst and Liaison. Customer support margin was 90.7% during the quarter, up from 90.3% in Q1 last year. Our license margin was 97% during the quarter, up from 95% in Q1 last year. Our professional services margin was 22.1% during the quarter, up from 20.3% in Q1 last year. Our goal remains to optimize the professional services business for high margins.

Adjusted EBITDA was $254.2 million this quarter, up 3.2% year-over-year or $258.6 million, up 5% on a constant currency basis. Adjusted EBITDA margin was 36.5%, down 40 basis points compared to 36.9% in Q1 last year and continuing to reflect seasonality as well as integration of the Liaison and Catalyst acquisitions. Our GAAP net income for the quarter was $74.4 million, up from $36.3 million in the same period last year, again primarily as a result of the reasons I mentioned earlier when discussing the year-over-year increase in GAAP EPS. Our adjusted net income in the quarter was $173.5 million, up 7.4% from last year or $177.2 million, up 9.8% on a constant currency basis. As a reminder, the fiscal 2020 target model range for adjusted EBITDA margin is 38% to 39%. It is important to continue to look at our margins on an annual basis.

Turning to operating cash flows for the quarter. We generated $137 million compared to $171 million in the same period last year. There were 2 primary reasons which I will outline here. A strong license quarter in Q3 2019 and even stronger collections in Q4 both resulted in annual operating cash flows of $876 million during fiscal 2019. And with the strong performance in Q3 and Q4, we saw a lower opening AR, accounts receivable, in Q1 F '20 versus Q1 fiscal '19 by 5% or $24 million. In addition, as we acquired Liaison and Catalyst during fiscal 2019, we carried higher expense into Q1 '20 compared to Q1 '19.

Our operating framework is more efficient than same quarter last year with DSOs at 54 days, lower by 2 days compared to Q1 2019. We are on track to grow OCF in fiscal 2020 and remain focused on achieving operating cash flows of $1 billion to $1.1 billion in fiscal '22 as we continue to apply automation and human-based efficiencies into our working capital framework.

Turning to balance sheet. We ended the quarter with approximately $1 billion in cash compared to $941 million at June 30 at fiscal year-end or 6% higher. Our consolidated net leverage ratio was 1.5x and remains the strongest level in 2 years and well within our external covenant ratio of 4x.

In terms of our ongoing IRS matter, we are in the appeals phase. The standard IRS process continues, and our resolve remains strong as we vigorously defend our position.

On the revolver, as mentioned in our earnings release, we have amended our revolving credit facility to increase the capacity to $750 million, up from $450 million and restate the 5-year maturity from 2022 to 2024. This amendment is aligned with Open Text's size and ensures we have ample capacity to support our total growth strategy.

On the shelf, you will also note in our press release that we are renewing our universal Canadian Shelf Prospectus as part of ordinary course renewal timing. Under Canadian rules, a shelf prospectus is effective for 25 months, and our previous shelf expired in September 2019. We are renewing with a $1.5 billion capacity under the Canadian shelf, and again, simply aligning with Open Text growth since our last filing during August 2017.

Turning to our dividend program. Today, we announced a quarterly dividend of $0.1746 per share payable on December 19, 2019. As a reminder, our dividend rate is based on distributing approximately 20% of our trailing 12-month operating cash flows.

Turning to fiscal 2020 target operating model and long-term aspirations. Our fiscal 2020 target model remains unchanged. As a reminder, the model is included in our Q1 investor presentation posted on our IR website. We remain on track to meeting our fiscal 2022 long-term aspirations of 38% to 40% adjusted EBITDA, with margins above this rate reinvested back into the business for future growth, including products, sales capacity and coverage. $1 billion to $1.1 billion operating cash flow during fiscal 2022 remains our long-term aspiration.

So let me summarize and reiterate the quarterly factors that we anticipate for our upcoming fiscal Q2. I would refer you back to Mark's commentary as well as Slide 7 in our quarterly business and financial highlights on our IR website. As we look at where foreign currency rates are today as well as geographic components of our business, we know that the FX headwind was $10 million to revenues in Q1, and we expect FX headwind in Q2 to also be $10 million. We're also expecting approximately $35 million annual FX headwind for fiscal 2020. We expect operating expenses in Q2 to be up low to mid-single digits compared to Q1, and our adjusted EBITDA in dollars to be flat year-over-year as we complete the integration of Catalyst and Liaison.

So in summary, Q1 results came in line with our expectations, and we continue to progress into a seasonally strong Q2 and remain focused on our fiscal 2020 and long-term targets. We are very pleased with how we have further strengthened the balance sheet to execute against our total growth strategy.

And finally, I'd like to thank you, our shareholders, whose trust and confidence we greatly value, and the Open Text team for their deeply committed efforts.

I would now like to turn the call for your questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Raimo Lenschow of Barclays.

Raimo Lenschow - *Barclays Bank PLC, Research Division - MD & Analyst*

Congratulations to a great start. I have 2 questions. Mark, last -- in Q4, when you talked a little bit about the uneven performance especially outside of the U.S., and this quarter, the license number looks really good, the overall numbers look really good, can you see a little -- talk a little bit to what you're seeing in terms of end demand at the moment? And then I have one follow-up.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. Yes, thanks for the question. We're in the end of October, right? And it's 60 days to the end of the calendar year and our Q2. And Q2 is our -- is a seasonally strong quarter for us. As I said in my prepared remarks, we were -- we feel pretty confident coming into Q2, our seasonally strong quarter and ending the year with a fair amount of confidence.

U.S. pipeline and demand, despite the headlines, if you will, was strong. The issues in Europe are, I think, well chronicled for most companies at this point. And we see similar things, which is basically German manufacturing. And I think there's just a new normal in Asia Pacific. Most companies have sort of set themselves into a strategy of if you're in China, servicing China, you have your manufacturing plan, fueling for for more capacity. You've -- you're well on your way of migrating to another location. I'd like to say, if you don't know your landed cost, you can't plan a supply chain. So I think most folks know their landed costs right now.

So I think it's -- the world's got a bit more defined, and we're -- we've been able to build our strategy along that, what's more defined than it was 90 days ago. And that gives us the confidence going into Q2.

Raimo Lenschow - *Barclays Bank PLC, Research Division - MD & Analyst*

Perfect. Okay. That's really helpful. And then the last couple of days, there was a lot of noise around M&A with MicroStrategy and all that sort of stuff there. Can you maybe remind us again -- like you talked about the capacity you have, but also like what's driving your decision making? Like what are the criteria that we should really look out for?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. So well, let me kind of address the first part, which is the rumor and speculation. I -- we don't respond to rumor and speculation, but in this case, we did very uniquely because I think it's very important that we provide clarity of our position if there's any uncertainty, and you can always expect that from me and the team. So as a rule, we don't respond to rumors and that sort of thing. But it was important, and you can always expect it from me and the team to provide clarity. So we did in our press release.

In terms of our strategy, look, our balance sheet has -- is amazingly strong with $1 billion in cash, $750 million undrawn revolver, a net debt to adjusted EBITDA ratio of 1.5x compared to our covenants of 4x trailing, a trailing 12-month cash flows. And we have a slide in our investor deck that shows the self-funding nature of our M&A. And if you just look back over the last 12 months, we've generated $600 million of available cash that could have been used for M&A on a self-funded basis.

I like our value playbook, and nothing is changing our value playbook. The balance sheet is strong. We're going to remain patient and strategic buyers. And as equity and valuations decline in a volatile market, we'll be in a much better position. But we're not changing our value playbook, and we're patient and strategic allocators of capital. And I do expect in this fiscal year, in fiscal '20, to deploy capital and get deals done.

Operator

Our next question comes from Richard Tse of National Bank Financial.

Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Yes. At your recent Investor Day, you laid out a bunch of sort of objectives for 2020, I think, increasing wallet share in the base and then penetration to the Global 10,000. So either today or going forward, are you going to be able to share metrics in terms of the performance on those objectives?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Richard, thanks for the question. Let me -- we'll take that under consideration. I think it's a good ask. And I think on, at least, an annual basis, we can provide a bit more insight into the Global 10,000. So leave that with us, and we'll think about it.

Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Okay. Great. And then with respect to the last question, I guess, from the previous analyst, can you maybe give us a sense of what the acquisition environment is like today and the valuations from that standpoint?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. I'll sort of reemphasize some comments I made last month in New York, where it felt as if valuations had peaked, and we're on the -- just turning to the back side. Just the curve has been -- we're just over in the backside of the curve of valuations, and it still feels that way. Our top of the funnel pipeline is very active. We're engaged on a volume basis on more deals, and it feels like we're on the other side of the peak of some valuations.

Counter to that, right, I mean, money still remains pretty inexpensive. I think negative interest rates push people to putting money to work and not putting it into banks, if you will. But our data, the Open Text data that we've tracked pretty -- very disciplined, shows activity up and stages progressing.

Richard Tse - *National Bank Financial, Inc., Research Division - MD & Technology Analyst*

Okay. And just one clarification. I think in your prepared comments, you said that Q1 to Q2 was going to be a single-digit increase in revenue. And I think you referred to it on a quarterly basis, sequential. I think in your presentation, it sort of implies it's year-to-year. Can you clarify that?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. My comments are sequential. Is that right, team? Yes. They're sequential, Q1 to Q2.

Operator

Our next question comes from Daniel Jester of Citi Research.

Daniel William Jester - *Citigroup Inc, Research Division - VP*

Just sticking with the M&A theme, the upsizing of the revolver. Should we read into anything of that in terms of your desire or willingness to maybe do a little bit of a larger transaction than you have historically?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Daniel, Mark here. Thanks for the question. No, I wouldn't read anything into it. It's that the timing is just good for us as we kick off the year. Our shelf needed renewing, so we made it commensurate with the shelf. And we are in the market looking at all sizes, small -- as I like to say, small, medium and large. The larger transactions are usually a bit more strategic, and there are opportunities in the market of that size. But I wouldn't read into the revolver of kind of changing our playbook or our historical deal size. We continue to run a value playbook. We think ROIC is the most important metric. At the end of the day, if it's 2 things, it's got to be the right company at the right price that yields the right return as measured by return on invested capital.

Daniel William Jester - *Citigroup Inc, Research Division - VP*

And then just to follow up on some of the comments on margins. The integration of Liaison and Catalyst, you called that out as something that might be a bit of a headwind on margins sequentially. We're 10 or 11 months past those acquisitions. So is this the last quarter where we're going to see maybe a little bit of incremental cost there? And maybe just help us frame how we should be thinking about that over the next couple of quarters?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. Thanks, David. Insightful question. This is the last quarter for us to integrate Liaison and Catalyst, and both of these businesses are cloud businesses. And they come with infrastructure. They come with servers and storage. They come with a large networking environment, redundancy, disaster recovery, systems, migrating vendors from one -- third-party vendors from one cost structure to our cost structure. So this is the last quarter of all that work, so we will be complete with Catalyst and Liaison by the end of December. So this is the last quarter where we're going to have that work and that expense, and they will see a little of that expense in the quarter and thus are quarterly factors. But we'll be complete. We're well on track.

As an acquirer, we set out to get to synergies in 12 months. Many other acquirers, it takes them 24 to 36 months to get to that point of synergies. We get there rapidly within 12 months. So we'll be done with Liaison and Catalyst integration by the end of December, and then we'll be on the new cost structure starting in the -- starting in January.

Operator

Our next question comes from Thanos Moschopoulos of BMO Capital Markets.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Analyst*

Madhu, would you happen to have the sequential impact that FX had on revenue for the quarter?

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

The sequential impact, yes I do. We called out approximately $10 million in Q1.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Analyst*

Sorry, I thought that was the year-over-year impact. Was that the impact -- I'm talking about Q4 FX rates relative to Q1 FX rates.

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

Understood. It is a year-over-year impact, and the sequential impact, I think, it was around $6 million.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Analyst*

$6 million, okay. And then secondly, if I look at your cloud revenue, I think you may have dipped a little bit sequentially on an FX-adjusted basis, if I'm doing the math correctly. And any color on that? Is there some Q1 seasonality with respect to B2B messaging transaction volumes, for example?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes, I'll take that. On reported currency, cloud up 14%. In constant currency up 15%. I think you need to look at recurring revenues in total. And recurring revenues, ARR year-over-year up 6%. So you put a little FX in there, you put a little mix in there as well, and it just creates that variance sequentially, if you will. So we're on target for our growth targets -- we're on target for our growth objectives for cloud this year, but I would just point to mix and FX in the sequential nature of the cloud. I wouldn't point to seasonality.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Analyst*

Okay. And then finally, you start implementing a significant maintenance price increase several months ago. Can you provide any color as to what proportion of the customer base might be on the new maintenance pricing at this point?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes, I won't get into what percent, but all new business is on that new rate now going forward. So we're on the other side of all new business. And we're now in -- kind of hitting the -- kind of getting to 1 renewal cycle. This is roughly -- on the maintenance side, it's about a 1-year contract. So all new renewal contracts also have that price being built into it.

And customers negotiate, and we defend our position, and we defend the position because we've added new services. We are getting 24/7. You're getting all our digital access for that increased price. So the reaction has been very favorable actually, that it's not just a price increase, but we're finding new capabilities and services for those additional charges. So we're in a really good position to see the benefit of that in the coming quarters.

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

And Thanos, this is Madhu. Just chime in, and I stand corrected. So when you look at comparison to prior quarter rate and not the year-over-year rate that we shared, which I believe was your question.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Analyst*

Yes.

Madhu Ranganathan - *Open Text Corporation - Executive VP & CFO*

The negative impact was $2.5 million.

Thanos Moschopoulos - *BMO Capital Markets Equity Research - VP & Analyst*

$2.5 million, okay.

Operator

Our next question comes from Paul Steep of Scotia Capital.

Paul Steep - *Scotiabank Global Banking and Markets, Research Division - Analyst*

Mark, maybe you could talk a little bit about the maintenance line here? We've seen it, I guess, static for sort of 6 or 7 quarters. Can you talk maybe a little bit -- it relates presumably to some of the discussion around cloud, as to what you're doing to either move maintenance higher? Or has there been -- focus more to actively transition or shift some of the revenues towards the cloud line?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. So thank you for that. We're not interested in flipping maintenance to cloud, so we're not interested in substituting revenue. We're interested in new revenues. So customers understand that if they're making a long-term deployment choice, and I highlighted a couple of customers who made a decade-long choice, that it is more cost effective to continue to license the technology than to subscribe to it.

In constant currency, our maintenance was up 1.8%, right, 1.8% in the quarter, and that's reflective of our strategy of we don't provide guidance nor do we allow customers to flip maintenance in the cloud. Rather, you must buy additive to new revenues. So again, we're up 1.8% in maintenance.

Also look at the renewal rate of low 90s, and it was up, right, to 92%. So you got the confidence. You got the renewal rate. You're seeing maintenance grow. And that's all aligned to our strategy that if you're going to own the technology long term, maintenance is a better way to go than a subscription, and it's reflected in our numbers.

Paul Steep - *Scotiabank Global Banking and Markets, Research Division - Analyst*

Great. One quick clarification just on M&A., how should we be thinking about maybe legacy deals you would have thought of versus the mix of a higher focus on maybe newer SaaS-based business? How is the pipeline looking in terms of the shift towards more cloud-based deals?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes, interesting question. At the end of the day, we like recurring revenues, right? So -- and that can come in 2 forms. So maintenance or pure cloud, those are recurring revenues. Some PS businesses look very recurring to us as well. And if you just look at the kind of the first 24 or 25 years of our history, most of our acquisitions were off-cloud.

But if you look at starting with EasyLink, GXS, ANX, Covisint, Liaison, Catalyst, these were all -- Hightail. These were all cloud-based companies. We're building the capability to be a cloud consolidator just as we have been historically regarded as an off-cloud consolidator.

I think one of the things I'm going to use this opportunity to highlight again from EasyLink, GXS, ANX, Covisint, Liaison, Catalyst, Hightail, we are building this capability of being a cloud consolidator. That is unique in the marketplace. And to be able to have a cloud business, as we highlight, we feel we'll be -- we're at a $1 billion run rate, and having this infrastructure that's our own and the teams to be able to operate this is phenomenal. It's really a long-term differentiator for us.

Paul, nothing changes our view of ROIC of whether it's a SaaS-based asset, private cloud or recurring revenue. It's going to be the right company at the right price with the right return.

Operator

(Operator Instructions) Our next question comes from Stephanie Price of CIBC.

Stephanie Doris Price - *CIBC Capital Markets, Research Division - Director of Institutional Equity Research & Software and Business Services Research Analyst*

So Open Text is holding a 24-city Cloud Summit this fall. I was hoping you could talk a bit about the uptick on the summit and how clients are thinking about the move to the cloud and feedback on OpenText Cloud offerings right now?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. Thanks, Stephanie. Yes, we're doing a major city tour and expo. And the focus of that, what we're calling the Cloud Summit, we got a code name for it, which is Destination Innovation. Migrating to the cloud is not about cost out, right? It's about your next platform. It's about innovation, agility, speed, modernizing the platform. So a big focus of the Cloud Summit is targeting that kind of meet of our installed base that are running off cloud and migration and modernization to the OpenText Cloud.

So we're looking at our installed base plus new clients, come join us at the Cloud Summit, and we're going to outline a migration and modernization path to either private cloud or to our SaaS workloads, things like core, federated content services, our new Cloud Editions, OT2 services, e-signature now live, integration to video and collaboration with Hightail, modern capture in the cloud, archive in the cloud, record management in the cloud, business network in the cloud, SAP integration in the cloud, support for Google, support for SAP in their recent announcement with Microsoft in the cloud.

So the Cloud Summit is really meant to go into our installed base and provide these kind of clear journey maps to go from off-cloud to cloud. And in terms of attendance, it's phenomenal, the response we're getting into the 4-continent, 24-city tour coming up over the next 3 to 4 months.

Stephanie Doris Price - *CIBC Capital Markets, Research Division - Director of Institutional Equity Research & Software and Business Services Research Analyst*

Great. And then I wanted to focus for a minute on the partner channel, and I was hoping you could talk a little bit about it and how you think about the growth on that side of the business as you target the G 10,000.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Sorry, Stephanie, could you repeat that, please? I'm sorry.

Stephanie Doris Price - *CIBC Capital Markets, Research Division - Director of Institutional Equity Research & Software and Business Services Research Analyst*

Sorry, I was asking about the partner channel and how you think about the growth on that side of the business as you target the G 10,000.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. It's -- it remains healthy and strong, and there are multiple kind of layers to this. There are kind of the value-added partners who can bring us into an industry or into a set of clients, and it's really where they have relationships.

We don't have a kind of a volume channel. That's not what our channel is about. It's really about -- I like to emphasize the V part, capital V, value. And if you got a relationship or know an industry, then we get close to you, kind of a company called Iron Capital. We have [Foresight]. These are partners who are more midsized SME, but they have a relationship with clients and industries. You then have where we have OEM relationships like McKesson, Cerner, Canon, who are developing IP on top of our technology. And then way up on top, you have the global system implementers, and we're focused on about a dozen of them. And then lastly, relationship with the new hyperscalers who are just out there trying to build as much demand as they can. So we want to be real close to them, both with the demand capability and as well as key capabilities they can provide like Google Cloud Platform.

So we're not -- don't look at our partner channel for volume but really for value in those areas.

Operator

Our next question comes from Paul Treiber of RBC Capital Markets.

Paul Treiber - *RBC Capital Markets, Research Division - Associate*

It's nice to see organic growth -- positive organic growth this quarter. Among your core products, were there any ones that were particularly stronger contributors to organic growth this quarter that you'd like to call out?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Hey, Paul, thanks for joining the call, and thanks for the question. I'd point to where we have leadership and scale. I would look towards content services and how we really modernized the platform both off-cloud and cloud. And also, I'd look towards our value-added network as businesses have been moving supply chains around in locations. That core part of our value-added network and ODM, volumes are certainly up. So I look towards kind of the core, more business and content services and kind of the network side of business networks.

Paul Treiber - *RBC Capital Markets, Research Division - Associate*

And then also could you provide that or elaborate additionally on SAP after the announcement, the partnership, the expanded partnership you announced earlier this year? How are you seeing pipeline and customer interest to build related to that on the cloud side? And then also just in regards to the license side business at SAP, how that's tracking ahead of the rollout of the new cloud products?

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes. And Paul, I just want to make sure I didn't hear you wrong on your previous question. I think you asked, did we have positive organic growth? And the answer is yes. So we did have positive organic growth within Q1. So I just want to make sure I heard your question right and make sure I answered it. We had positive organic growth in the quarter.

Paul Treiber - *RBC Capital Markets, Research Division - Associate*

Yes. No, you heard that right. I was asking what drove the positive organic growth this quarter.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

Yes, I wasn't sure if you said it was good to see positive growth or if you asked did we have positive growth. I just wanted to reinforce, we had positive organic growth within the quarter. So thank you.

In relation to the question -- to SAP, as I've always said it this way, that products come and go, relationships endure. And our relationship with SAP endures. And they've had a leadership change at SAP, but we have relationships all throughout and in their new leadership. We have great relationships with the team.

SAP has selected us for their next-generation content services platform in the SAP cloud, and that work is going along great. So they remain a strategic partnership. Our plan remains great. No disruption based on the leadership changes. And in fact, with their recent partnerships, with some other hyperscalers, we see it as great news because it's just going to continue to reinforce our installed base and the pace of their migration to the plan. So we see that all as positive.

Operator

This concludes the question-and-answer session. I will now hand the call back over to Mr. Barrenechea for closing remarks.

Mark J. Barrenechea - *Open Text Corporation - Vice Chairman, CEO & CTO*

All right. I'd like to thank everyone for joining the call today. And look, I'm going to end where I sort of started with Investor Day and using one word, which is durable. And we like the durable nature of our business, and it's been 19 consecutive quarters of year-over-year growth in constant currency.

Thanks for joining the call today, and we'll speak soon. Thank you.

Operator

This concludes today's conference call. You may disconnect your lines. Thank you for participating, and have a pleasant day.
