Appian Q3 2024 Earnings Call Prepared Remarks Transcript

Jack Andrews, VP of Investor Relations

Good morning and thank you for joining us. Today, we'll review Appian's third quarter 2024 financial results. With me are Matt Calkins, Chairman and Chief Executive Officer and Mark Matheos, Chief Financial Officer. After prepared remarks, we'll open the call for questions.

During this call, we may make statements related to our business that are considered forward looking. These include comments related to our financial results; trends and guidance for the third quarter and full year 2024; the benefits of our platform, industry, and market trends; our go-to-market and growth strategy; our market opportunity and ability to expand our leadership position; our ability to maintain and upsell existing customers; and our ability to acquire new customers.

These statements reflect our views only as of today and don't represent our views as of any subsequent date. We won't update these statements as a result of new information unless required by law. Actual results may differ materially from expectations due to the risks and uncertainties described in our SEC filings. Additionally, non-GAAP financial measures will be discussed on this conference call. Reconciliations of GAAP to non-GAAP financial measures are provided in our earnings release.

With that, I'd like to turn the call over to our CEO, Matt Calkins. Matt?

Matt Calkins, Chairman and Chief Executive Officer

Thanks, Jack. In the third quarter of 2024, Appian's cloud subscription revenue grew 22% year-over-year to $94.1 million. Subscriptions revenue grew 19% to $123.1 million. Total revenue grew 12% to $154.1 million. Our cloud subscription revenue retention rate was 117% as of September 30th. Adjusted EBITDA was positive $10.8 million.

Appian continues to grow even as we become more efficient. Growth remains our top priority. We now project positive adjusted EBITDA for the full current year *2024*, an improvement from our breakeven forecast last quarter. Mark will provide more details.

Appian has pivoted to a more efficient cost structure. We did that with minimal short-term impact and without losing *any* long-term growth potential. We've streamlined our priorities, focusing on high-value implementations in core verticals and use cases. We've become more closely engaged with our very-happy customer base. We've reorganized some departments to become leaner and more effective. And we're seeing the first results.

Our advisory-service attachment rates are rising. Our existing-customer renewal uplifts are also up. Under our new system, we're realizing higher pricing. Our pipeline shows a larger median deal size. These are the first fruits of our efforts, the first indications that our strategy can work. We're early in this process. There's a lot more we can achieve in this direction.

We're in the amusing position of being an analyst-designated leader in a diversity of markets, though we offer only one product. Depending on whether you consult Gartner, Forrester, Everest, or somebody else, Appian leads in process automation, or orchestration, or mining, or low code, etc. This linguistic confusion has been a weight on our market, which wants clarity. I'll try to offer some here.

Appian is a process company – sometimes we call ourselves *the* process company – but anyway we've been focused on processes for a long time. A process is anything an organization does thousands of times. It typically involves multiple steps, multiple participants, organization-specific customization, and evolution over time.

Every organization is full of processes. Many of them are unique and require customization. Those processes do some of the most important things, like spending money, handling customers, and creating products or services. These behaviors are the signature of their firms, their outward and inward expressions, shaping reputation and identity.

When we say we're 'the process company', we mean that we sell a software platform for processes, but also that we have the expertise, solutions, executive partnership, and organizational commitment to provide great *process* outcomes. As I like to say, Appian isn't a product, it's an experience. We're very proud of our 99% GRR.

Here's where I'm going with this. Commentators today, with all their various names for the same thing and trend-chasing, are underestimating the value of process. My example is the recent trend around Agentic AI.

Agentic AI means using AI to respond to stimuli and take actions, autonomously. For a complex action, that means AI must inform itself, collaborate with other actors, and take actions independently. Process is a better way to do all three of those things. AI is more effective working *within the structure of a process*, where data fabric provides enterprise-wide data access, where human and digital collaborators are available, and where powerful actions are pre-defined and launchable. This is *especially* true when the job is complex and the tolerance for error is low. It's also true if you need to audit AI's actions and tune them for future accuracy or efficiency.

You could think of process as a frame for AI, giving it the support and structure it needs to be effective. Appian uses AI *in a process* to create a superior version of Agentic AI.

I say all this to rebut the theory that AI will obsolete process because AI can do everything by itself. (You know, you've heard this one: write the code, take the actions, etc.) As I hope I've explained, the opposite is true, at least at our end of this market. Process is a perfect home for AI, and the two are highly complementary. I'll return to this theme in future earnings calls.

This quarter, Appian saw the highest yet quarter-on-quarter increase of our AI usage. For example, a top Latin American bank is modernizing its enterprise to increase operational agility and optimize margins. It named Appian its platform standard earlier this year after we embedded AI into its processes within just a few weeks. The bank can initiate and complete various consumer-related actions on Appian based on the insights our AI provides. Now, the bank intends to replace an incumbent's inflexible system with Appian and improve operational efficiency by 40%.

Q3 is big in the Public Sector, a very important sector for Appian, where we continue to expand. We signed a contract with a Federal cabinet-level agency that manages US national parks and resources. It purchased several of our government acquisition management solutions, from the GAM suite, last quarter and became a new Appian customer. The group chose Appian because we've successfully digitized procurement operations at several peer organizations. In fact, with this new win, we're proud of this one, all 15 US cabinet-level agencies are now Appian customers.

Another federal agency uses sophisticated technological systems to support national security and defense. It became a new Appian customer earlier this year when it purchased a few of our government acquisition management solutions, again the GAM suite. It purchased a seven-figure software deal this quarter to replace a few of our competitor's systems with Appian. Now, the org will run HR management and annual planning processes on Appian.

Next an update from another of our primary verticals, Financial Services. We did a deal with a global financial services provider that oversees quadrillions of dollars in annual transactions. It decided to modernize its client lifecycle management processes using Appian and became a new customer this quarter. Our platform will consolidate several systems into a single application to manage processes like pre-qualifying applicants, onboarding new clients, and managing lifecycle events.

My second Financial Services story is with a top global bank*.* The firm runs internal audit and call center operations on our platform. This quarter, it purchased fifteen-hundred additional user licenses for a payment exceptions application. Appian will manage the process for approving an organization's transaction request when it doesn't have enough cash on hand to make the payment. This heavily regulated process can result in major fines if a bank falls out of compliance. Appian won this deal because we have a strong track record of managing similar high-risk processes across other major banks.

I'll close my remarks with a few personnel updates. First, we welcomed Mark Dorsey as our new Chief Revenue Officer. Mark has 25 years of experience leading sales teams at cloud and SaaS companies, including Oracle, IBM, and most recently Alteryx. Next, Appian elected Boe Hartman and Michael Beckley to our Board of Directors. Boe is the first member of the board to understand Appian from the client's perspective. He successfully ran a multi-million dollar Appian deployment for one of the world's premier banks. He's an expert at turning functionality into value who will help us define our solutions. Michael Beckley is one of our founders, and currently our CTO, and is returning to the board after an absence of several years. Finally, our CFO Mark Matheos is leaving Appian. We appreciate his 8 years of good work, and we wish him well. Our former CFO and current Board Member Mark Lynch will return as interim CFO while we search for a full-time replacement.

With that, I'll hand the call over to Mr. Matheos – for the last time -- for a deeper discussion of our financials.

Mark Matheos, Chief Financial Officer

Thanks, Matt, and thank you to everyone joining us today. I'll review the financial highlights for the quarter, and then will provide guidance for the fourth quarter and full year 2024.

Our key metrics of cloud revenue, total revenue, and adjusted EBITDA all came in above the high end of our guidance ranges. Cloud subscription revenue was $94.1 million, an increase of 22% year-over-year. Our cloud subscription gross renewal rate remained stable at 99%, up from 97% a year ago, and consistent with the prior quarter. Our cloud subscription revenue retention rate was 117% as of September 30, 2024, compared to 117% a year ago, and 118% in the prior quarter. We continue to target a cloud subscription revenue retention rate between 110% and 120% on a quarterly basis.

Approximately 88% of our total net new software bookings this quarter was for the cloud, compared to 71% in the prior year's third quarter. Total subscriptions revenue was $123.1 million, an increase of 19% year-over-year.

Professional services revenue was $30.9 million, down 7% year-over-year. As we've previously stated, professional services revenue can fluctuate quarter to quarter, due to the timing of large projects. We continue to leverage our professional services to enable partners and drive customer success. Over the long-term, we expect professional services revenue to continue to decline as a percentage of total revenue.

Total revenue was $154.1 million, an increase of 12% year-over-year. Subscription revenue represented 80% of total revenue, compared to 76% in the year ago period, and 77% in the prior quarter. We continue to see global demand for our platform, with our international operations contributing 36% of total revenue, compared with 35% in the year ago period. Foreign exchange movements provided a small revenue tailwind of slightly less than 1% this quarter.

Turning to profitability metrics:

- Non-GAAP gross margin was 77%, compared to 75% in both the year ago period and prior quarter.
- Subscriptions non-GAAP gross profit margin was 89%, consistent with both the year ago period and prior quarter.
- Professional services non-GAAP gross margin was 30%, also consistent with both the year ago period and prior quarter. Our goal is to enable customers and help them achieve strong

outcomes. We continue to invest in non-billable areas of our services organization to ensure customer success and drive adoption of our platform.

Total non-GAAP expenses were $110.2 million, a slight decline from $110.5 million in the year ago period.

Adjusted EBITDA was positive $10.8 million for the quarter, which is well ahead of our third quarter guidance of between breakeven and positive $3 million, and significantly improved from an adjusted EBITDA loss of ($5.3) million in the year ago period.

Non-GAAP net income was $11.4 million, or $0.15 cents per diluted share, compared to a non-GAAP net loss of $(14.6) million, or $(0.20) cents per diluted share for the third quarter of 2023.

In the third quarter, we had approximately $9.2 million of foreign exchange gains, compared to $4.3 million in foreign exchange losses in the same period a year ago. As a reminder, we do not forecast movements in FX rates. Therefore, FX movements are not considered in our guidance.

Turning to our balance sheet, as of September 30th, 2024, cash, cash equivalents, and investments were $140.0 million. This provides us with sufficient liquidity to operate and invest in our business. For the third quarter, cash used by operating activities was ($8.2) million, a significant improvement compared to the use of ($65.0) million in the same period last year. As a reminder, last year's figure included a one-time payment of $57.3 million for our judgment preservation insurance policy.

Finally, total deferred revenue was $227.6 million as of the third quarter of 2024, an increase of 15% from the year ago period. As a reminder, while the majority of our customers are invoiced on an annual upfront basis, we also have some large customers that are billed quarterly or monthly. Consequently, we continue to believe cloud subscription revenue is a better indicator of our business momentum than deferred revenue, billings, or remaining performance obligations. These latter metrics can fluctuate based on the timing of invoicing, seasonality of on-prem license revenue, and the duration of customer contracts. The true scale of Appian's business is represented by subscriptions revenue, which includes support and all software subscription revenue, regardless of whether the customer deploys to the Appian Cloud, a private cloud, or on-prem.

We previously forecasted adjusted EBITDA breakeven in 2024. Now, we're pleased to share that we expect positive adjusted EBITDA for the full year 2024.

Let's turn to the specifics of our guidance.

- For the fourth quarter of 2024, cloud subscription revenue is expected to be between $95 and $97 million, representing year-over-year growth between 14% and 17%.
- Total revenue is expected to be between $163.5 and $165.5 million, representing year-over-year growth between 13% and 14%.
- Adjusted EBITDA for the fourth quarter of 2024 is expected to range between positive $6 million and positive $8 million.
- Non-GAAP net loss per share is expected to range between $(0.03) cents and breakeven. This assumes 74.0 million diluted weighted average common shares outstanding.

There are three reasons why we anticipate our adjusted EBITDA to decline sequentially from Q3. First, we expect Q4 sales commissions to increase, reflecting a seasonally stronger quarter for bookings. Second, we are hosting a number of marketing events during Q4. These include Appian Government and

Appian Europe. Third, we are making incremental investments in Appian's cloud capabilities to better serve the public sector.

For the full year 2024, we are raising our cloud revenue and total revenue guidance. We are also raising our full year adjusted EBITDA guidance.

- Cloud subscription revenue is now expected to be between $364 and $366 million, representing year-over-year growth of 20%.
- Total revenue is now expected to be between $613 and $615 million, representing year-over-year growth between 12% and 13%.
- We now expect adjusted EBITDA to range from positive $5 to positive $7 million. This is an improvement of $28.5 million from the midpoint of our guidance range at the beginning of the year.
- We're also updating our expected full year 2024 non-GAAP net loss per share to a range between $(0.38) cents and $(0.35) cents. This assumes 73.0 million diluted weighted average common shares outstanding.

Our guidance assumes the following:

- First, as previously disclosed, the variability in our services revenue can be impacted by a few large transactions. We expect professional services revenue to be flat to down sequentially in Q4.
- Second, we expect on-prem license revenue in Q4 will increase sequentially and track to seasonality that is consistent with prior periods.
- Third, total other income and interest expenses are expected to be between $4 and $5 million in Q4, and between $20 and $21 million for the full year 2024.

- Fourth, capital expenditures are expected to be approximately $1 million in Q4, and between $4 and $5 million for the full year 2024.
- And fifth, our guidance assumes FX rates as of November 4th, 2024.

In closing, we expect to continue driving more efficient growth in the business. We're pleased about our ability to guide for positive adjusted EBITDA in 2024.

I'd like to express my appreciation for my time at Appian and will cheer for the company from the sidelines.

And with that, we will open the line for questions. Operator?