Workiva Q3 2023 Earnings Call

Mike Rost, Julie Iskow, Jill Klindt
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Mike Rost

Good afternoon, and thank you for joining us for Workiva's third quarter conference call. During today's call, we will review our third quarter results and discuss our guidance for the fourth quarter and full year 2023. Today's call has been pre-recorded and will include comments from our Chief Executive Officer, Julie Iskow followed by our Chief Financial Officer, Jill Klindt . We will then open the call up for a live Q&A session.

A replay of this webcast will be available until November 6, 2023. Information to access the replay is listed in today's press release, which is available on our website under the Investor Relations section.

Before we begin, I would like to remind everyone that during today’s call, we will be making forward-looking statements regarding future events and financial performance, including guidance for the fourth quarter and full fiscal year 2023. These forward-looking statements are subject to known and unknown risks and uncertainties. Workiva cautions that these statements are not guarantees of future performance. All forward-looking statements made today reflect our current expectations only and we undertake no obligation to update any statement to reflect the events that occur after this call.

Please refer to the company's Annual Report on Form 10-K and subsequent filings for factors that could cause our actual results to differ materially from any forward-looking statements.

Also, during the course of today's call, we will refer to certain non-GAAP financial measures. Reconciliations of non-GAAP to GAAP measures and certain additional information are also included in today's press release.

With that, we'll begin by turning the call over to CEO, Julie Iskow …

Julie Iskow

Thank you, Mike. But before I begin my prepared remarks about our quarterly results, I want to take a moment to acknowledge what's going on in our world. This is an extremely tragic, painful, and uncertain time. It's especially so for those who have a connection to the impacted regions. This may include some of you on our call today. While there is a lot that can be said, it is our hope that resolution is reached and peace will prevail.

I'll now move on to our operating results.

Workiva delivered another solid quarter achieving subscription revenue growth of 21% and a Non-GAAP operating profit that beat the high end of our guidance by nearly 340 basis points.

As highlighted at our September investor day, Workiva continues to stand out from the SaaS crowd given that we solve problems our customers must address. Companies need transparency. They need to comply with regulation. And, they need accuracy in reporting and disclosure.

Workiva provides solutions that are necessary in good times and in challenging times.

Our opportunity AND our technology are such that we are becoming the world's leading platform for transparent reporting and regulatory disclosure. Why? Because OUR strength is where data consistency, and data integrity & accuracy are critical… *and* where narrative is required.

This is highlighted by the deals we're winning and the references our customers are providing. We showcased many of these success stories at our Amplify user conference, including companies like Hershey that shared on the main stage the value they receive from our connected solutions across: financial reporting, GRC, and ESG. [I'd also like to congratulate Hershey for recently receiving the **Innovation Excellence Award for ESG Metrics and Reporting** from Verdantix. This is the second consecutive year that a Workiva customer has won in this category.]

The value our platform provides is also quantified by the continued large-contract-account-expansion that we saw in the third quarter. We continue to see outpaced growth in our large contract customers. In Q3, the number of contracts valued over $100 thousand dollars increased 24%; those over $150 thousand dollars increased 26%; and contracts valued over $300 thousand dollars were up 38% - all compared to the third quarter of 2022.

Our platform is a strong and key differentiator in the marketplace. Workiva remains the only platform that brings Financial Reporting, ESG and GRC together in one secure, controlled, audit-ready environment. We are the platform for Assured, Integrated Reporting.

I'd like to highlight three assured, integrated reporting wins that we signed in Q3:

- **First,** a Fortune 500 energy company purchased three GRC solutions, including audit, internal controls, and risk management. This was to complement their previous investment in SEC, Management Reporting, and ESG. This 11-year loyal SEC customer was engaged with a Big 4 Advisory firm in transforming their GRC program, and the Big 4 Advisory firm recommended Workiva as the technology of choice. This firm will also be providing delivery for the project.
- **Second,** a North American-based airline that purchased SEC in the second quarter of this year, went all-in on the Workiva platform in Q3. They added a 5-solution account expansion that included ESG and 4 GRC solutions. (SOX, Audit, ERM and IT Risk & Controls). This deal was a competitive win over a point solution GRC provider.

The strength of our connected platform and the ability to support both SEC-and- ESG-reporting reinforces Workiva's "Better Together" approach. It also contributed to the competitive differentiation in this platform expansion.

This assured, integrated reporting win was a co-sell with a regional advisory firm that will also be handling the project delivery of both the GRC and ESG solutions.

- **And third,** it's not just about account expansion, we're landing with the platform, including a 3-solution new logo win with a Spain-headquartered utility who purchased ESEF reporting, ESG, and controls management. This assured, integrated reporting win was sourced by a Big 4 advisory firm. There were two other Big 4 firms involved in this deal competing for the implementation work - and all three had a previous relationship with the client and all three have established Workiva consulting practices.

We win deals like these because our customers see the value in our experience, our ecosystem, and our capabilities.

We have unrivaled experience.

- **First,** we've been doing investor-grade reporting for more than a decade.

- **Second,** we have a quickly maturing ecosystem of over 200 partners. Partners want to work with us because of the opportunity for commercial success that it creates for them.
- **Third,** we are the world’s leading platform in XBRL tagging for financial and non-financial data.
- **And finally,** our regulatory reporting expertise is unmatched. We have the expertise on staff so that the day regulatory changes go into effect, our customers can be compliant.

And, we have a diverse and growing portfolio of best-of-breed solutions, and it's all within a true platform.

Let's move on to a top bookings solution, yet again, for the quarter. **ESG**.

Companies continue to purchase ESG well ahead of regulations. As highlighted in recent comments by Chair Gensler from the SEC, 81% of the Russell 1000 are currently disclosing their climate risks. With increased stakeholder focus on sustainability, we’re seeing a more defined ESG technology purchasing process, including formal RFPs and ESG transformation projects.

Our ESG account expansion activity remains strong. And both our differentiated platform and our partner-first strategy are contributing to our win rate in this increasingly competitive environment.

I would like to highlight three ESG wins from the quarter.

- **First,** a Germany-headquartered retail firm purchased our ESG solution to support their broader ESG transformation project that was driven by the CSRD. There were multiple ESG solution competitors vying for this deal, with the customer ultimately choosing Workiva in alignment with their broader project scope. This new logo win was sourced by a Big 4 advisory firm.

- **Second,** a US-based Fortune 500 consumer financial services company expanded their use of our platform during Q3 by purchasing ESG to complement their existing SEC solution. This was a competitive win over an incumbent GRC point solution provider. This opportunity was sourced by a Big 4 advisory firm and was also a co-sell with a climate accounting technology partner. This deal will be implemented by the Big 4 advisory firm.

- **And third,** we signed an account expansion deal with a top U.S.-based private healthcare company. This was a competitive deal that went to RFP with multiple vendors involved. This company had purchased and successfully implemented the Workiva private company financial reporting solution back in 2022. Supporting Workiva with a co-sell in the sales process were both a carbon accounting partner and a Big 4 advisory firm. This project will be implemented by the Big 4 firm.

I'll turn now to Financial Reporting…

In Q3, we continued to see demand in financial reporting in both new logo and account expansion activity.

While ESG was a much-highlighted topic of conversation at our recent Amplify event, many of our long-time customers were there to talk about financial reporting. Financial reporting for Workiva is not just SEC; it also includes, for example, global statutory or multi-entity reporting, private company reporting, management reporting, and our capital markets solution.

The conversations I had with customers focused on topics including investment fund reporting, finance transformations, Workiva's role in ERP projects, and supporting a company's private-to-public journey.

While we continued to win new logos in SEC this quarter, here are three financial reporting deals that showcase the breadth of our Financial Reporting solution:

- **First,** one of the UK's largest financial services firms purchased our banking solution to address the requirements for setting internal capital targets. This risk reporting use case is their 7th regulatory reporting solution that they've purchased since becoming a customer in 2018. This account expansion pushed them over the $1m ARR mark and it highlights how our platform supports many vertical regulatory use cases with standard platform functionality. Workiva supports a wide range of banking-specific use cases, including resolution plans, CCAR and DFAST, Call Reports, CECL planning, and Basel Pillar 3. This demonstrates how, as I described earlier, we are fast becoming the platform for transparent reporting and regulatory disclosure.

- **Second,** we closed a new logo win for fund reporting with a top 10 U.S.-based Private Equity firm. Workiva was selected based on the comprehensive support for data integration, financial statements, prospectuses, shareholder reporting, and XBRL to support SEC filings. This deal was sourced and will be implemented by a regional advisory firm.

- **And third,** we closed a large financial reporting account expansion with a top U.S. public university system. This University system originally purchased the Workiva platform for their annual consolidated financial report back in 2021. This implementation was at the University system level which consolidated results across its network of institutions. The success of the initial implementation led to the customer expanding the Workiva platform across its network of 9 universities and 5 medical campuses. This opportunity was sourced and will be implemented by a regional advisory partner.

I'll talk now about the activity we are seeing in GRC...

With increasing stakeholder scrutiny, establishing an integrated, enterprise-wide governance, risk, and compliance program is a strategic priority for many organizations. Workiva is a recognized leader in GRC, which is a broad market segment that includes internal audit, controls, risk management, and policy management.

I'd like to highlight now two GRC deals that closed during the third quarter…

- **First,** a European global mobility company purchased three GRC solutions including Audit, Controls, and Enterprise Risk Management. This new logo deal was sourced and will be implemented by a Big 4 advisory firm. We were ultimately chosen in this competitive deal over four GRC point-solution vendors. We were the only solution evaluated by the client that could provide capabilities that not only addressed GRC-specific requirements but also supported their ESG and Global Statutory Reporting needs. This is the power of having an assured, integrated reporting platform.
- **And second,** a Fortune 1000 financial services company expanded their investment in Workiva with Policy Management. It was their 10th solution with Workiva! This customer uses solutions across the portfolio including financial reporting, ESG, and banking specific solutions. This product expansion was sourced by a regional advisory firm who previously implemented the Workiva controls and audit management solutions earlier in 2023.

Moving on to capital markets, the IPO market showed some renewed activity during the third quarter. While the number of new IPOs remains limited, we did see an increase in interest in those companies preparing for an IPO and those companies investing in their private-to-public journey. We're pleased with how we’re competing for IPO deals as they emerge.

In Q3, we supported the S1 process for one of the top tech IPOs of the quarter. This is a great example of how we deliver value to companies on their private-to-public journey. This customer first purchased our private company and management reporting solutions back in 2021. Our capital markets solution was initially purchased in late 2022 with the completion of the IPO work in Q3. This company also purchased our SEC solution in Q3 to support their post-IPO process.

While we are seeing some signs of the market opening up, we are not yet forecasting a comeback of IPOs in the fourth quarter.

Moving on to our update on global regulations…

Regulators have been very active since our last earnings call. In Q3, the SEC issued numerous announcements targeted at listed companies and new regulations for private equity firms.

- **First,** on July 26th the SEC issued new cybersecurity disclosure rules, which will significantly increase the pressure on organizations to perform more risk assessments, improve internal controls, and prepare for an increase in external audits.
- **Next,** on August 23rd...new rules for private equity fund reporting were issued. These rules mandate that investment firms provide quarterly statements detailing information regarding private fund performance, fees, and expenses. The rules also require PE firms to disclose fund reports quarterly and obtain an annual audit for each private fund.
- **And,** on September 7th, the SEC issued a sample comment letter-to-companies regarding their XBRL disclosures. We believe that this action by the SEC signals that there may be greater scrutiny over XBRL data quality in filings - which impacts all of our SEC-listed customers. Both our platform and our XBRL services team will support our customers as they continue to navigate through this heightened regulatory scrutiny.

As it relates to the proposed SEC Climate Disclosure Rule…there are no material updates from the past quarter.

- While there had been some discussion on the SEC providing further guidance on the Climate Disclosure rule in October, as of the time of this call no new rules have been communicated. In his September testimony to the **House Financial Services committee**, Chair Gensler was very clear that **there was no guaranteed October date** and that the Commission will potentially issue new rules once all of the comments have been reviewed and the economic impacts have been documented.
- We still believe that the SEC is likely to implement climate disclosure rules in the near future. Chair Gensler's House testimony was specific on the number of organizations that already disclose climate risks. He was also clear about the commission's goal to provide consistency and comparability to those disclosures. Standardized climate disclosure rules would enforce this consistency.

While the SEC is still in the rulemaking process, there ***were*** new climate disclosure laws passed by the state of California that may have **national impact** on ESG reporting. On October 7, Governor Newsom signed into law two important climate disclosure regulations. The laws are:

- SB 253
- SB 261

SB 253 is the Climate Corporate Data Accountability Act. It applies to all U.S. companies with total annual revenues in excess of $1 billion dollars doing any business in California. This is predicted to impact over 5,300 business entities operating in California. These companies must annually report Scope 1, Scope 2, and Scope 3 emissions. Reporting is set to begin in 2026.

SB 261 is the Climate-Related Financial Risk Act. It applies to US companies with total annual revenues in excess of $500 million dollars and that do business in California. It mandates disclosure of climate-related financial risks and measures for risk reduction, aligning with the internationally recognized TCFD framework. Reporting begins in 2026, with biennial reporting instead of annual.

Outside of the U.S., there was continued regulatory activity around the CSRD.

- After approving the Enterprise Sustainability Reporting Standards on July 31st, the **standards setting committee**, EFRAG, was busy at work defining interoperability with the ISSB related to IFRS S1 and S2, and the legacy SASB framework. Interoperability comments were also provided for the frequently used GRI framework.

- **In August,** there was further discussion on the **Draft Materiality Assessment Implementation Guidance**. This has been a priority topic given that there will be many first time filers with this regulation.
- **On October 18** - the European Parliament confirmed in a vote the approval of the E-SRS. They also rejected a resolution calling for limitations to be introduced on these standards. The E-SRS will now be formally adopted before the end of the year and shortly after published in the official Journal of the European Union. Large EU companies will start assessing their operations through the E-SRS criteria starting January 2024 and disclosing their information accordingly by 2025.

Companies are watching these activities closely and they're waiting for implementation guidance on how established ESG frameworks map to the newly set ESRS standards. They are looking to understand what they will need to disclose and how they will have to disclose it.

With all this new regulatory activity with the SEC, the State of California's climate rules, and the European CSRD, we believe that we have a large TAM in front of us and future durable demand for our assured, integrated reporting platform.

I'll move on now to provide some perspective on the macro…and our focus on both growth and productivity.

The geopolitical backdrop and economic uncertainty continue to impact our markets. Throughout Q3, we continued to see elongated sales cycles and increased buyer scrutiny across our portfolio.

We do remain confident, however, in the many growth opportunities in front of us driven by the value our platform delivers to our customers. Our teams will continue to work closely with our customers in solving their most complex reporting and compliance requirements.

Our approach remains to be first and foremost focused on subscription growth and going after our large and expanding TAM.

Across the company, we are focused on driving growth first with a continued eye on productivity and performance. As highlighted by our Q3 operating margin, we're delivering on improved operating leverage and productivity. We're building strong teams, improving our processes, and incenting the right behaviors to drive this productivity.

Areas that contributed to the improvement in our Q3 operating margin were:

- continued strong subscription revenue growth, and
- improved efficiency and productivity across the company

Margins continued to improve throughout the first three quarters and we are guiding to a Non-GAAP operating profit in both 2023 and 2024.

We enjoyed seeing many of you last month at Workiva Amplify - our largest customer user conference to-date.

During the conference we welcomed 5,800 in-person and virtual attendees from almost 2,000 companies - many of them from new logos. We also welcomed nearly 300 advisory and technology partner attendees at our Partner Summit.

We have loyal and devoted customers who are our biggest brand advocates. We hope you were able to hear directly from them about what makes Workiva so special and relevant.

At Amplify, we announced a number of new platform capabilities, including the availability of Generative AI to all customers in North America. We received enthusiastic interest and feedback during our standing-room-only AI sessions - with over 40% of all attendees participating in at least one of these sessions.

We believe that every one of our Workiva solutions can deliver expanded value to our customers with Generative AI— by harnessing best-in-class LLMs embedded directly into our platform.

Our approach to Gen AI has been incredibly well-received by our peers, our partners, and our early adopters due to our responsible implementation. We provide the assurance that no customer data or prompts within our platform are ever stored or used in any way to train Gen AI models. By solving enterprise-grade security we've eliminated one of the top concerns of using tools like ChatGPT.

Our approach to Gen AI has been in tight partnership with our vendors. Including Google, Microsoft, and Amazon. We believe Workiva is the only provider in the markets that we compete in to offer such a comprehensive delivery of Gen AI. In the near term, we believe that monetization of Gen AI will come in the form of solution differentiation and higher win rates.

In closing, I'll leave you with a few final remarks.

- Workiva delivered solid third quarter results, including a transition back to non-GAAP operating profit.

- We continue to win with a multi-solution and account expansion strategy, resulting in strong growth in large contract customers.

- We are confident in our ability to execute on our strategy as we become the world's leading platform for transparent reporting and regulatory disclosure.

- We have a significant edge in experience and expertise with a large install base, and a growing partner ecosystem.

- And, we have a large, relatively unaddressed TAM with the right team in place to go after it. Our opportunity is growing and at the same time we and our platform are getting stronger.

Thank you to our fantastic team of dedicated employees. Workivians all over the world didn’t just help us achieve the solid results that we delivered last quarter, but they’ve helped us once again achieve two important third-party recognitions:

- **First,** Fortune honored Workiva with the #10 ranking on their **Best Workplaces in Technology** list. This is our 7th year on the list and the third year in the top 10.
- **And,** second, MSCI, the top rating tool used by investors to determine which companies are included in ESG investment funds, issued Workiva another AAA rating – this is the highest rating a company can achieve.

None of this is possible without the hard work of our entire team, along with their dedication and commitment to our customers and our mission of powering transparent reporting for a better world.

And with that, I'll turn the call over to you Jill…

Jill Klindt

Thank you, Julie.

Let’s turn to our results. First I will give an overview of our key financial highlights for the third quarter 2023 and then I will provide Q4 and full year 2023 guidance before opening the line for questions.

We're pleased to report that we beat the high end of revenue guidance by $2.2 million, primarily due to strong subscription revenue growth along with higher than expected services revenue growth.

We beat our break-even guidance on Q3 operating results -- generating $5.3 million dollars of operating profit. As Julie mentioned, stronger revenue, coupled with improved efficiency and productivity, were the primary drivers of the beat. Our continued focus on growth and operating leverage is showing in our operating results.

Now let's go through some key results and highlights for the quarter, starting with revenue. We generated total revenue in the third quarter of $158.2 million, delivering growth of 19% from Q3 2022.

- **Subscription revenue** was $143.4 million, up 21% from Q3 2022. Yet again this quarter, both new logos and account expansions helped drive strong revenue growth, with 43% of the increase in subscription revenue coming from customers added in the last 12 months.

- **Professional Services** revenue was $14.8 million in Q3 2023, up by 3.5% compared to the same quarter last year. The growth was driven by higher XBRL services revenue, which outpaced the year-over-year decline in setup and consulting revenue.

As we mentioned in our previous 2023 earnings calls, we are in the process of transitioning more of our lower margin setup and consulting professional services to our partners. As we execute on this plan, we expect setup and consulting services revenue to decline year over year for 2023.

Moving to our performance metrics. We added 85 net new customers in Q3 for a total customer count of 5,945, a growth of 404 customers from Q3 2022.

Our gross revenue retention rate remained comfortably ahead of our 96% internal target metric.

Our net revenue retention rate increased to 112% for the third quarter of 2023 compared to 107% for Q3 2022.

We are very pleased with the strong increase we continue to see in Net Revenue Retention, which improved for the 4th straight quarter. The main driver of this improvement is strong account expansion activity, led by the addition of new solutions.

Account expansions also continue to be a strong contributor to the increase in customers with large contract values. We are seeing momentum and are optimistic that we can continue to expand the number of customers spending over $100k per year. In the third quarter of 2023, we had 1,561 contracts valued at over $100K per year, up 24% from Q3 the prior year. The number of contracts valued at over $150K totaled 851 customers in the third quarter, up 26% from Q3 2022. And, the number of contracts valued over $300k totaled 296, up 38% from Q3 2022.

Moving on to our operating metrics -- gross profit totaled $121.7 million in Q3, up 20% from the same quarter a year ago. Gross margin was flat year-over-year at 77%, as higher cloud computing costs were offset by savings in employee-related spending.

Operating expenses increased only 6% from Q3 2022. This modest increase is due to efforts we are making towards automation and process efficiency as well as thoughtful hiring with a focus on skills needed to drive growth and productivity.

We posted an operating **profit** of $5.3 million in Q3 2023, a continued improvement compared to Q3 2022 operating loss of $8.4 million. As Julie mentioned, we continue to focus on growth and productivity. This focus has helped us improve our operating leverage and stay committed to our goal of delivering improved operating margins and non-GAAP profitability for both 2023 and 2024.

At September 30, 2023, cash, cash equivalents, and marketable securities increased $316 million sequentially to a balance of $782 million, primarily driven by our August convertible note offering.

Our successful issuance of convertible notes raised $700 million at a 1.25% coupon. We used $397 million of the funds to repurchase about 80% of the convertible notes we originally issued in 2019. We plan to use the remainder of the funds primarily for working capital and to support potential future M&A activity.

Operating activities in Q3 2023 resulted in cash provided of $15 million compared with an increase in cash of $5M in the same quarter a year ago.

Turning now to our guidance for Q4 and the full year 2023… As Julie discussed, while we remain encouraged by our opportunities to drive growth, we continue to see elongated sales cycles and increased buyer scrutiny amidst a concerning macro and geopolitical environment. As such, we continue to be prudent with our guidance assumptions.

For the fourth quarter of 2023…

- We expect total revenue to range from $164 million to $165 million.
- By design, we expect services revenue will decline in Q4 at a single digit percent rate.
- We expect Non-GAAP operating income to range from $5.6 million to $6.6 million, a net income of $0.21 to $0.23 on a per share basis. Our share count will be approximately 54 million weighted average shares.

For the full year 2023...

- We are raising the midpoint of our revenue guidance range - expecting revenue to be between $627 million and $628 million. The high end of revenue guidance remains in line with our previously stated 2023 target.

- We expect Services Revenue to decline at a low single digit percent rate.
- We are raising our guidance for non-GAAP operating results, shifting to an income range of $3 million to $4 million or a net loss of $(0.54) to $(0.52) on a per share basis. Our share count will be approximately 54 million weighted average shares.
- The Q3 interest expense recorded in conjunction with the repurchase of the majority of our 2019 notes is driving the gap between our operating results and loss per share guidance.
- We continue to expect we will post positive free cash flow for the seventh consecutive year.

Now to give some directional modeling information for 2024...

- As implied in our Q4 2023 guidance, we will be monitoring the current macro headwinds carefully as we exit 2023, as well as the potential impact on our revenue growth rates as we enter 2024.
- We expect XBRL Services revenue to continue to grow at a modest low-single-digit rate.
- We expect setup and consulting revenue to decline from 2023 to 2024.

- And, consistent with our prior statements, we expect non-GAAP operating profit for the full-year 2024.

In summary, I want to thank all of our employees and partners for their continued support and hard work.

Before we turn to Q&A, I would like to reiterate three key points:

- **First,** We are encouraged by the opportunity ahead of us, our large unaddressed TAM, and the value our platform delivers to our customers.
- **Second,** we delivered a beat on Q3 operating margin guidance and are focused on continuing the momentum of margin improvement and anticipating a Non-GAAP operating profit in fiscal year 2023.
- **And third,** we remain committed to our strategy, long-term growth and improving operating leverage.

In closing, I want to echo Julie's thanks to all Workiva employees. You are an amazing team and I am proud to be working beside you.

We will now take your questions.

Operator, we are ready to begin the Q&A session.