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QMCO.OQ - Q2 2025 Quantum Corp Earnings Call

EVENT DATE/TIME: NOVEMBER 13, 2024 / 10:00PM GMT

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PRESENTATION

Operator

Good afternoon and welcome to Quantum Corporation's second-quarter fiscal 2025 financial results conference call. (Operator Instructions) Please note, today's conference call is being recorded for replay purposes.

I will now turn the conference over to your host, Brian Cabrera. You may begin.

Brian Cabrera - Quantum Corp - Chief Administrative Officer

Good afternoon and thank you for joining today's conference call to discuss Quantum's second-quarter fiscal 2025 financial results. I'm Brian Cabrera, Quantum's Chief Administrative Officer. Speaking first today is Jamie Lerner, our Chairman and CEO; followed by Ken Gianella, our CFO. We'll then open the call to questions from analysts.

Some of our comments during the call today may include forward-looking statements. All statements other than statements of historical fact, should be viewed as forward-looking, including any projections of revenue, margins, expenses, adjusted EBITDA, adjusted net income, cash flows or other financial, operational, or performance topics. These statements involve known and unknown risks and uncertainties we refer to as risk factors. Risk factors may cause our actual results to differ materially from our forecast.

For more information, please refer to the detailed descriptions we provide about these and other additional risk factors under the Risk Factors section in our 10-Qs and 10-K filed with the Securities and Exchange Commission. We do not intend to update or alter our forward-looking statements once they are issued whether as a result of new information, future events or otherwise, except of course, as we are required by applicable law.

Please note that our press release and the management statements we make during today's call will include certain financial information in GAAP and non-GAAP measures. We include definitions and reconciliations of GAAP to non-GAAP items in our press release.

Now I would like to turn the call over to our Chairman and CEO, Jamie Lerner. Jamie?

Jamie Lerner - Quantum Corp - Chairman of the Board, President, Chief Executive Officer

Thank you, Brian, and thank you all for joining us. Earlier today, we announced our results for our second quarter fiscal 2025.

Turning to slide 3. Here are some brief highlights from the quarter. We finished Q2 '25 with \$70.5 million in revenue, GAAP gross margin of 41.5% and adjusted EBITDA approximately breakeven. Sales bookings and customer win rates were largely in line with our expectations as we continue our business rotation toward our long-term initiatives and growth of profitable revenue streams. This quarter's execution resulted in a higher-than-anticipated backlog of approximately \$14 million and \$4 million above typical run rate.

Evidence of our transformation can be seen in the progress of gross margin improving 490 basis points sequentially to above 41%, as well as non-GAAP operating expenses being reduced by approximately 9% year over year.

These actions contributed to our achievement of breakeven adjusted EBITDA for the quarter and have set a positive operating path towards EBITDA growth for the remainder of the year. Quantum continues to focus on business efficiency by enhancing operations and driving more automation into the business.

Combined with this quarter's actions, our restructuring and operational improvements are expected to result in almost \$40 million in total savings as of the end of our fiscal year 2025 compared to fiscal 2023. These actions are also improving our free cash flow, which is expected to be positive in the back half of fiscal year 2025 and driving fiscal 2026 to be cash flow positive for the first time in 5 years.

Turning to slide 4. Let me share some proof points to our go-to-market strategy and how our innovation agenda continues to center on accelerating future growth. First example is this quarter, a leading broadcaster in the Americas and an existing quantum customer for over a decade, selected Myriad and significantly grew their existing ActiveScale environment with ActiveScale cold storage.

This deal also leveraged our Quantum Go subscription solution, highlighting our plans to empower our customers to innovate and allow them to focus on their data rather than their storage infrastructure costs.

Another example of innovation yielding near-term results is our new DXi T-Series All-Flash data protection appliance we recently launched. We've had multiple strategic wins against competition this quarter based on its superior data reduction and recovery rates.

These deals have been closing rapidly. The majority in under 30 days from deal discovery demonstrating the critical importance of cyber resilience in today's market and the compelling value proposition that our DXi solutions provide.

While our future growth is led by Myriad and ActiveScale, it remains important to maintain a strong base with our traditional data protection offerings. The Scalar i7 RAPTOR our latest tape innovation to support growing AI use cases is now shipping under limited availability. Built to handle advanced AI workflows for hyperscale customers, MSPs and large enterprises, the Scalar i7 RAPTOR delivers the most efficient, dense and low-cost solution for AI data lakes.

Demonstrating its leadership in the market, we already have a multimillion dollar purchase order in-house from one of the world's leading cloud platforms. These are just some examples of our go-to-market progress and how our innovation can help accelerate our growth.

Now let me hand the call over to Ken for a financial update.

Kenneth Gianella - Quantum Corp - Chief Financial Officer

Thank you, Jamie. Please turn to slide 6, and I'll provide an overview of the GAAP financial results for our fiscal second quarter. Revenue was \$70.5 million, a decrease of approximately 7% year over year and down approximately 1% from the prior quarter.

Sales bookings for the quarter were consistent with our overall business expectations as we continue to transform the company, even though operational headwinds related to the supply chain continued in the most recent quarter.

The year-over-year decrease in revenue reflects lower contribution from our primary storage solutions. Backlog in the quarter remained elevated at approximately \$14 million, and above our target run rate of \$8 million to \$10 million as higher supply chain lead times continue to persist.

Our GAAP gross margin for the period was 41.5% and compared to 43.3% in the year-ago quarter and 36.6% in the prior quarter. The year-over-year driver was predominantly from revenue mix towards lower-margin product lines.

Sequentially, we saw higher margins due to operational efficiency gains and improved product mix. GAAP net loss for the second quarter was \$13.5 million, or a loss of \$2.82 per share, which included approximately \$4.7 million of one-time expenses related to our debt and restructuring activities. Importantly, we anticipate the one-time related to our restructuring activities will significantly subside in the back half of our fiscal year.

Now turning to slide 7 for non-GAAP metrics. Non-GAAP operating expenses were \$30.4 million in the second quarter, an approximate 9% reduction from the \$33.3 million last year and effectively flat against the prior quarter.

This decrease in operating expenses was the result of our proactive actions to improve process and productivity, and we anticipate lower operating costs at or below these levels as continued cost actions begin to take hold in the back half of our fiscal year.

Adjusted EBITDA in the second quarter was essentially breakeven at a negative \$300,000 compared with a positive \$1.7 million in the prior year second quarter and a negative \$3.1 million in the prior quarter. This quarter's sequential EBITDA improvement primarily reflects the benefits of our operational cost controls despite revenue being at the lower end of guidance.

As Jamie mentioned, we remain focused on streamlining our processes and enabling automation to reduce our ongoing operating and overhead costs. This is evidenced by our total expense savings of almost \$40 million since the end of FY23.

Our focus remains on improving EBITDA and total profitability. EBITDA improvement over the coming quarters will be accelerated from not only our global restructuring, but from the rollout of our updated product portfolio and enhanced go-to-market model.

An area of focus for us, in particular, is Annual Recurring Revenue, where we anticipate our efforts will continue to deliver sequential and year-over-year improvements in profitability in the second half of FY25 and beyond.

Moving to slide 8. I want to provide an example of where our focus towards recurring revenue and subscription-based selling is taking hold with an update of our Annual Recurring Revenue and Subscription metrics.

Total Annual Recurring Revenue, or ARR, for the trailing 12 months was approximately 51% of our total revenue at \$146 million. With the gross margin on the combined businesses, being approximately 67%. As a company, we continue to focus on our total ARR by maximizing our Quantum Subscription opportunities in both our partners and customers globally.

The best way to demonstrate our progress is through our Subscription ARR, where in the second quarter, the subscription portion of our total ARR increased approximately 28% year over year and approximately 5% sequentially to \$19.6 million, with over 88% of new unit sales in the quarter being subscription-based. Continuing this rotation and focus on ARR is a key element towards our long-term business model.

Now please turn to slide 9 for an overview of debt and liquidity at quarter end. Cash, cash equivalents and restricted cash at the end of the second quarter were approximately \$17 million. Outstanding debt split between term and our revolver was \$104.7 million and \$28.3 million, respectively. At quarter end, the company's net debt position was \$114.6 million.

Over the last several years, the company has had significant cash spend on onetime consulting, a new ERP, updated infrastructure, new product introductions and restructuring expenses. We are pleased to announce that we are substantially complete with these efforts and anticipate the back half of FY25 returning to operating cash flow positive with a full year cash improvement year over year.

Turning to slide 10. Let me close out with the company's guidance for our fiscal third quarter and an updated view of fiscal 2025. First, we anticipate total revenue in the third quarter to be approximately \$72 million, plus or minus \$2 million. This reflects management's view of ongoing operational headwinds including transition to a new manufacturing partner during the quarter.

We expect non-GAAP operating expense to be \$31 million, plus or minus \$1 million, reflecting aggressive cost reductions over the last two years. As a result, non-GAAP adjusted net loss per share for the third quarter is expected to be negative \$0.75, plus or minus \$0.05 per share. based on an estimated 4.8 million shares outstanding.

Adjusted EBITDA for the third quarter is expected to be approximately \$2 million. While the Q3 '25 guidance at the midpoint is essentially flat year over year, the adjusted EBITDA guidance is almost \$5 million improvement from the prior year.

Turning to our fiscal year FY25 outlook. While we are exceeding our expectations on product mix, gross margin and cost improvements, we need to continue to focus on improving our overall revenue execution. We see improvements in second half of FY25 continuing into FY26. However, having factored into our updated annual guidance, the operating impacts in the first half and the Q3 outlook.

With this information, we have adjusted our fiscal year FY25 outlook, to a target of \$280 million, plus or minus \$5 million, with adjusted EBITDA expected to be \$3 million, plus or minus \$2 million. While our revenue is lower year-on-year at our current guidance midpoint, the operational actions we have taken have improved our adjusted EBITDA by almost \$10 million over the prior year. We have substantially completed our operational and infrastructure improvement efforts in the first half of fiscal 2025.

And Quantum remains focused on returning to growth by driving new and innovative products into the marketplace. -- improving our customers' experience and leveraging our global footprint to improve our overall service model. We anticipate these efforts to yield growth in revenue, profitability and free cash flow in the second half of FY25 and beyond.

With that, I'll now hand the call back to Jamie for closing remarks.

Jamie Lerner - Quantum Corp - Chairman of the Board, President, Chief Executive Officer

Thank you, Ken. As Ken mentioned, our strategy remains intact as we reallocate resources towards high priority growth initiatives, particularly Myriad and ActiveScale. The go-to-market approach for our new solutions is a key element of the company's growth strategy as we ramp up new cutting-edge solutions. One area in particular that we're evolving is our sales model to focus dedicated sales resources on select product lines.

This approach will enhance our geography-based sales reps, allowing a deeper focus on how our growth solutions provide customer value, enhanced support to our channel partners and expand collaboration with product management and marketing. Combining our latest innovations with these go-to-market enhancements is a key part of executing on our business model.

These actions are already producing green shoots across our more modern products. while at the same time, solving the critical needs of our customers in today's data era. We anticipate this trend to accelerate pipeline growth in the second half of our fiscal year 2025 and continue into fiscal year '26.

In summary, we have completed the heavy lift on the operational model. We have fully refreshed our product portfolio, and we are now actively engaged in reenergizing our go-to-market approach. All of these combined create positive momentum in the coming quarters and beyond. Thank you for your time today.

Operator, we are ready to open the call to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Eric Martinuzzi, Lake Street.

Eric Martinuzzi - Lake Street Capital Markets - Analyst

Yeah. I wanted to touch on the revenue shortfall and the linkage with the supply chain issue. I understand the backlog at \$14 million is roughly \$5 million higher than what you guys would typically finish out a quarter with. But just given that you are aware of the issues, what steps did you take to try and correct the issue and what's ongoing with trying to get that supply chain issue fixed?

Jamie Lerner - Quantum Corp - Chairman of the Board, President, Chief Executive Officer

Sure. The way I'd characterize is the sales team brought in the purchase orders needed to meet guidance. As you know, some of the purchase orders come in late in quarter and we've been rotating our portfolio more to high-speed all-flash offers.

And as you've been watching, high-speed all-flash systems, particularly those from Super Micro, have long lead times. So, we've been finding that the lead times on SSDs and high-speed servers that use SSDs just have longer lead times. And so we used to have about two- to three-week lead time on that type of server. Now it can be up to 10 weeks.

Now one way we solve for that is we purchased them 10 weeks in advance. But it gets pretty dangerous buying a lot of that equipment in advance because your customer - if the configurations change during the quarter, you can end up buying the wrong equipment and have inventory you can't get rid of.

So we're doing our best job to preorder systems, but we're not ordering them so far in advance that we end up with scrap material. So, I think you'll see a little elevated backlogs for a period of time. But what I felt good about is the bookings were on target. And all-flash systems just have longer lead times right now.

Kenneth Gianella - Quantum Corp - Chief Financial Officer

And we anticipated some of that, Eric, going into the quarter. It was just still way elevated from where we planned.

Eric Martinuzzi - Lake Street Capital Markets - Analyst

Sorry. Could you repeat that, Ken?

Kenneth Gianella - Quantum Corp - Chief Financial Officer

Yeah. We anticipated some of the longer lead times coming into the quarter. It just persisted much deeper than we had planned for.

Eric Martinuzzi - Lake Street Capital Markets - Analyst

Got you. And your comment about the decline in primary storage, that is the same issue we're talking about here, right? It's not like the demand wasn't there. It was just we didn't -- we weren't able to fulfill the orders?

Jamie Lerner - Quantum Corp - Chairman of the Board, President, Chief Executive Officer

Our primary storage is where you see the predominant all-flash systems.

Eric Martinuzzi - Lake Street Capital Markets - Analyst

Okay. All right. And then you talked about some positive proof points in the business. Is there any metrics you can put around key performance indicators regarding Myriad and ActiveScale, either revenue or number of units just showing that progress between Q1 and Q2 and what's got you so excited about the back half?

Kenneth Gianella - Quantum Corp - Chief Financial Officer

Yeah. I mean I'll start -- I can start, Jamie, with the pipeline. When you look at the pipeline growth and what we're seeing, Eric, it's jumped considerably quarter-over-quarter. And we're seeing the focus from our teams and what we're seeing in the field. of that growing into the second half and in FY26.

Jamie, anything else you want to add to that?

Jamie Lerner - Quantum Corp - Chairman of the Board, President, Chief Executive Officer

Yeah, I think the other metric that we're pretty proud of is we crossed over 1,000 customers on subscription with us on subscription software.

Eric Martinuzzi - Lake Street Capital Markets - Analyst

Okay. All right. And then the cash, you had talked about Q2 that you were anticipating a challenging cash usage quarter that looks like the burn was about \$14.8 million. You also said that's going to reverse that we'll get to positive free cash flow in the back half. Do you have a dollar amount for in Q3 that you're targeting as far as cash from ops?

Kenneth Gianella - Quantum Corp - Chief Financial Officer

No, we're not putting the exact number out there, but the signpost that we want to give to folks is, if you think about the CapEx spend that we've been talking about the last few years, particularly on putting a new ERP system in having a new R&D facility.

Over the last two years, that was about \$30 million worth of CapEx one time. Then you add into the restructuring costs for this year, along with what we've seen for us getting back on file and the cash spend there. A lot of those bills in costs covered over Q1 and Q2. That total cost is somewhere within another \$15 million to \$20 million spent.

So as you start in the back half of the year and start looking to FY26 and you get out of those headwinds that we've had of refreshing our product line, refreshing our processes and our systems, restructuring globally to operate more effectively and efficiently. That's where you see the pickup in the back half of the year even at lower revenue levels. That's where you see the pickup on free cash flow, going cash flow positive as well as FY26 being a full year of positivity just from these actions we've taken.

Eric Martinuzzi - Lake Street Capital Markets - Analyst

Got it. Okay. That covers the questions for me. Thank you.

Jamie Lerner - Quantum Corp - Chairman of the Board, President, Chief Executive Officer

Thanks, Eric.

Operator

(Operator Instructions) Nehal Chokshi, Northland Capital Markets.

Nehal Chokshi - *Northland Capital Markets - Analyst*

Yes. Thank you. Good to see the bookings were where you were expecting in the proof of the backlog there. What conversion rates relative to historical levels are needed to reach a breakeven free cash flow in fiscal 2H '25 that you're talking about?

Kenneth Gianella - *Quantum Corp - Chief Financial Officer*

Conversion rates on what? I didn't understand the question.

Nehal Chokshi - *Northland Capital Markets - Analyst*

Of your pipeline, of the pipeline that you guys have developed? The demand pipeline.

Kenneth Gianella - *Quantum Corp - Chief Financial Officer*

Yeah. I don't know if I have an exact answer of one-to-one. I can say that our pipeline is growing and our win rates, while they're slightly down from prior years. We expect that to go up. The way I really look at it is about the rotation of the product mix, right, getting and slowing down the service declines year over year and getting that recurring revenue, as we talked about on the call, back up and guaranteeing that, as well as getting a real new baseline of our OpEx.

If you look at the cost downs we had, we're down 8% year over year on the OpEx side of things on a non-GAAP basis. Those indicators are two great ones to say, if you can have a recurring revenue in an OpEx base that you can be near breakeven on your cash flow, then you start seeing the top line one-time sales really carry and grow that. That's the inflection point that we're in.

So I don't have an exact number of pipeline to win rate to free cash flow. I look at it that even at these -- if we stayed flat year over year at what we guided at a midpoint \$280 million, we would be positive operating free cash flow next year is the best pinpoint I could give you.

Nehal Chokshi - *Northland Capital Markets - Analyst*

Understood. And then are you seeing different conversion rates of your pipeline by products, i.e., do Myriad, ActiveScale have materially different win rates relative to your older products?

Kenneth Gianella - *Quantum Corp - Chief Financial Officer*

Yeah. So I think it's still early days to say was whether they're higher or lower. I'd say, ActiveScale was on par with prior years. We did see a bit of a dip down in our enterprise tape business. That's why we're super excited about the i7 coming out and being a category killer to get those win rates back up.

But everything else, we're seeing flat to slightly up in every other category. Our traditional categories our legacy products tend to be in.

Jamie Lerner - *Quantum Corp - Chairman of the Board, President, Chief Executive Officer*

DXi is significantly up, and we think that trend is going to continue. Myriad's up just coming off a tiny base. But DXi is really a thing that is surprising us the most with our T10 and T20 all-flash products. Those seem to be accelerating faster than they have in the past and accelerating faster than we actually planned internally. And I think a lot of it is just from the innovation we've been doing around the products when our larger peers in the space, particularly Dell, just hasn't been a lot of innovation or activity in their product lines.

Nehal Chokshi - *Northland Capital Markets - Analyst*

Yeah. And when you said refer to Dell, you're really referring to guys as main products?

Jamie Lerner - *Quantum Corp - Chairman of the Board, President, Chief Executive Officer*

Yeah.

Nehal Chokshi - *Northland Capital Markets - Analyst*

Okay. All right. Got it. Okay. That's great. And are you guys expecting the elevated backlog to persist into the March quarter? Because I believe that your updated fiscal year '25 guidance implies typical March Q seasonality, which would beg the question, why wouldn't that be buffered with the elevated backlog that you have right now?

Kenneth Gianella - *Quantum Corp - Chief Financial Officer*

Well, we're snakebit on that front in two ways going into this quarter. One is the -- we're expecting that those headwinds to persist where we thought they were dying down. The second one is we're doing a factory transition. We're consolidating our manufacturing operations into one new location. And that's happening at the end of the quarter. So, we're buffering that along with it in our guidance.

Nehal Chokshi - *Northland Capital Markets - Analyst*

Okay. Thank you.

Operator

Thank you. There are no further questions at this time. I'd like to hand the floor back over to Jamie Lerner for any closing comments.

Jamie Lerner - *Quantum Corp - Chairman of the Board, President, Chief Executive Officer*

All right. Thanks, everyone, for joining us. And we will be speaking again in 90 days. Thank you.

Operator

This concludes today's conference call. You may disconnect your lines at this time. Thank you for your participation.

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