

NASDAQ:PENG Q3 2025 Earnings Call Transcript

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Cameron | Conference Call Operator:

Good afternoon. Thank you for attending the Penguin Solutions Third Quarter Fiscal Year 2025 Earning Result Conference Call. My name is Cameron and I'll be your moderator for today. All lines will be muted during the presentation portion of the call with an opportunity for questions and answers at the end. If you would like to ask a question, please press star 1 on your telephone keypad. And I would now like to pass the conference over to your host, Suzanne Schmidt with Investor Relations. You may proceed.

Suzanne Schmidt | Investor Relations:

Thank you, Operator. Good afternoon and thank you for joining us on today's earnings conference call and webcast to discuss Penguin Solutions' third quarter fiscal 2025 results. On the call today are Mark Adams, Chief Executive Officer, and Nate Olmstead, Chief Financial Officer. You can find the accompanying slide presentation and press release for this call on the investor relations section of our website. We encourage you to go to the site throughout the quarter for the most current information on the company. I would also like to remind everyone to read the note on the use of forward-looking statements that is included in the press release and the earnings call presentation. Please note that during this conference call, the company will make projections and forward-looking statements, including but not limited to statements about the company's growth trajectory and financial outlook, business plans and strategy, and existing and potential collaborations. Forward-looking statements are based on current beliefs and assumptions, are not guarantees of future performance, and are subject to risks and uncertainties, including, without limitation, the risks and uncertainties reflected in the press release and the earnings call presentation filed today, as well as in the company's most recent annual and quarterly reports. The forward-looking statements are representative Only as of the date they are made and except as required by applicable law, we assume no responsibility to publicly update or revise any forward-looking statements. We also discuss both GAAP and non-GAAP financial measures. Non-GAAP measures should not be considered in isolation from, as a substitute for, or superior to our GAAP results. We encourage you to consider all measures when analyzing our performance. A reconciliation of the GAAP to non-GAAP measures is included in today's press release and the accompanying slide presentation. And with that, let me turn the call over to Mark Adams, CEO. Mark?

Mark Adams | Chief Executive Officer:

Thank you, Suzanne. I'd like to welcome all of you to our third quarter fiscal 2025 Penguin Solutions earnings call. We are pleased with our Q3 financial results. Our revenue was \$324 million, an increase of 7.9% compared to Q3 of fiscal year 2024. Non-GAAP gross margins came in at 31.7%. Non-GAAP diluted earnings per share was 47 cents, a 25% increase year over year. We achieved non-GAAP operating income of \$38 million, up 15% from the prior year, And we delivered non-GAAP operating income margin of 11.9%. All in all, our Q3 results attest to our progress in transforming Penguin Solutions into a leader in high performance, high availability, enterprise infrastructure solutions. We continue to see signs of early stage enterprise AI adoption across vertical markets, such as financial services, energy, defense, education, and neo-cloud segments. As we have mentioned in the past, our belief is that the investment of AI pilot systems deployed throughout the industry in 23 and 24 would lead to growth in full production installs in 2025 and 2026. We are now seeing signs that we have entered the initial stages of that growth in corporate build-outs at scale. Penguin Solutions helps customers manage the complexity of AI adoption by leveraging both our

proven know-how and advanced cluster build-outs and our portfolio of hardware, software, and managed services. We work with our customers to design, build, deploy, and manage these environments with a focus on time to revenue and reliability, while also targeting the highest level of performance and availability. Our products and services are primarily marketed to hyperscalers, NeoCloud service providers, and Fortune 500 companies. Historically, we have sold directly to our end customers. However, we are also investing in channel partnerships that we believe will provide new opportunities for growth over the long term. The foundation of Penguin Solutions' success is our expertise in large-scale deployments, which has been developed over a 25-plus year history implementing complex data-centered clusters beginning with our early days in high-performance computing, or HPC. Our expertise integrating advanced technologies such as power, cooling, AI compute, memory, storage, and networking enable us to deliver high-performance, high-reliability enterprise infrastructure solutions for our customers. As we've mentioned at the beginning of our fiscal 2025, we have transitioned from providing a quarterly financial outlook to providing a full year financial outlook. We believe that a full year outlook provides a broader perspective of our business, especially with regards to AI infrastructure engagements, where the timing of actual deployments and associated revenue recognition can be unpredictable and concentrated. This approach aligns well with our focus on long-term strategic objectives. At the same time, We know that our stakeholders appreciate commentary on our progress each quarter, and we will offer that today as well. On our Q2 fiscal year 2025 call in April, we raised our full year revenue growth outlook from 15% to 17% at the midpoint. Today, we are reaffirming that outlook. In addition, we are raising our full year non-GAAP diluted earnings per share outlook from \$1.60 to \$1.80 per share at the midpoint. As a reminder, we have shared previously that revenue and profits are likely to be weighted more towards the first half rather than the second half of fiscal 2025. I'd like to now provide additional detail on our business segments. Our advanced computing revenue for the third quarter of fiscal 2025 was \$132 million, down compared to the prior quarter as expected. As we often highlight on our earnings calls, revenue recognition in advanced computing tends to be lumpy. This is due to factors like customer concentration, the timing of large project implementation for our major customers, and the timing and discretionary nature of our customer renewals. The decline in Q3 when compared to the prior quarter was largely due to the timing of a major deployment at a large hyperscale customer where we recognized the revenue in our second quarter. That said, this quarter we had some exciting wins at our existing customers and closed five new customer bookings, highlighted by wins in the federal, energy, and biotech segments. We continue to see increased interest at enterprise customers, as well as in NeoCloud customer opportunities, exemplifying the increased investments being made in large-scale AI infrastructure. Our core competency in successfully managing large-scale AI infrastructure build-outs helps customers accelerate their time to a live production environment. We believe our customers value our technology-agnostic approach, which allows us to create a unique overall solution that meets their specific AI infrastructure needs. Beyond our hardware building blocks, we are investing in the development of Penguin Ice Clusterware, a software platform that helps customers manage their infrastructure assets. Our Penguin Solutions Service Organization can assist companies in managing their post-deployment operations, supporting the high performance and high availability of their systems. Overall, we have seen growth in new customer bookings and have continued to expand our pipeline during the first three quarters of FOI 2025. Integrated memory under the Smart Modular brand achieved \$130 million in revenue in Q3, up 24% compared to the prior quarter. We saw strong demand from our computing, networking, and telecommunications customers. Pricing in both DRAM and NAND appears relatively stable, and inventory levels appear balanced at our major customers. We are optimistic about memory demand in the near term, as large enterprises seek out higher performance and higher reliability memory to support both established workloads and new complex AI workloads. In line with this increasing demand for improved memory bandwidth and availability, we are seeing early adoption of our Compute Express Link or CXL family of products. Thanks in part to positive momentum in our customer qualification efforts, We have received early production orders of CXL from OEMs and an AI computing customer, which reinforces our optimism about CXL's appeal to new types of customers. From an R&D perspective, we are focused on products that enable higher bandwidth and larger memory access to and from a GPU via memory pooling. We continue to invest in the design of smart optical memory appliance, or OMA, with first product shipments targeted for late 2026, early 2027. Given the importance of memory to the AI ecosystem, we feel confident that smart modular

continued to play a key role fulfilling our customers integrated memory requirements in the future. Optimized LED operates under the Cree LED brand. Cree's revenue came in at \$62 million of slightly compared to the prior quarter. Our top line was constrained during the second half of Q3, largely due to increased cost and uncertainty related to tariffs on products shipped out of our Weizhou, China facility. Despite macro uncertainty in the LED market, we remain confident in our high-performance product portfolio, our strong intellectual property, and our cost-effective capital light operating models. In December of 2024, we closed a \$200 million investment from SK Telecom. At the time, we explained that in addition to the investment, the opportunities to partner with SK Group and more specifically, SK Telecom and SK Hynix could offer strategic commercial benefits as well. We are making progress with SK Telecom on opportunities related to their AI strategy, including their AI data center infrastructure initiatives. The already strong relationship between SK Hynix and Smart Modular is evolving as we look at new ways to address markets with system level products and custom high value add memory related segments. Since our last call, there have been two other company developments that I would like to mention. First, on June 26th, we announced a refinancing that further strengthens our balance sheet by reducing our gross leverage and extending our overall debt maturity while establishing a \$400 million credit facility. Nate will provide more details in his comments. Second, on June 30th, we completed the re-domiciliation of Penguin Solutions, Inc. from the Cayman Islands to the United States as a Delaware corporation. While our past structure served us well, we look forward to being a U.S.-based company as we continue our transformation. In closing, I want to thank our team for delivering strong results during a time of macro uncertainty. For Q4, we remain focused on short-term execution while also continuing to invest for longer-term growth. Penguin's value proposition of solving the complexity of AI infrastructure for our customers positions us well to address the increasing market opportunity being created by enterprise adoption at scale. Let me stop here and hand the call over to Nate, who will provide more color on our performance and outlook for the remainder of fiscal 2025. Nate?

Nate Olmstead | Chief Financial Officer:

Thanks, Mark. I will focus my remarks on our non-GAAP results, which are reconciled to GAAP in our earnings release tables and in the investor materials on our website. Now let me turn to our third quarter results. Total Penguin Solutions net sales were \$324 million, up 7.9% year over year. Non-GAAP gross margin came in at 31.7%, which was down year over year and up sequentially. Non-GAAP operating margin was 11.9%, up 0.8 percentage points versus last year, and non-GAAP diluted earnings per share were 47 cents for the quarter, up 25% from Q3 last year. In the third quarter of fiscal 2025, our overall services net sales totaled \$66 million, down 3% versus Q3 last year. Product net sales were \$259 million in the third quarter, up 11% versus the prior year. Third quarter net sales by business segment were as follows. Advanced computing, \$132 million, or 41% of our total net sales, and down 9% year over year. Integrated memory, \$130 million, which was 40% of our total net sales and up 42% year over year. And optimized LED, \$62 million or 19% of our total net sales and down 4% year over year. Non-GAAP gross margin for Penguin Solutions in the third quarter was 31.7%, down 0.6 percentage points year over year, driven primarily by a higher mix of integrated memory net sales compared to last year. partially offset by improved margin rate in integrated memory and optimized LED. Gross margin was up 0.9 percentage points sequentially, with higher margin rates in advanced computing partially offset by a higher mix of integrated memory net sales. Non-GAAP operating expenses for the third quarter were \$64 million, up 1% year-over-year and up 2% sequentially. Operating expenses as a percentage of net sales were down year over year, driven by higher net sales volumes and stable spending levels. Non-GAAP operating income was \$38 million, up 15% year over year and down 22% versus last quarter. The combination of top line growth and operating expense discipline translated into a 0.8 percentage point increase in operating margin versus Q3 last year. This is our fourth consecutive quarter of non-GAAP operating margin expansion year over year. Non-GAAP diluted earnings per share for the third quarter of fiscal 2025 were 47 cents, up 25% versus the prior year and down 10% versus prior quarter. Adjusted EBITDA for the third quarter was \$45 million, up 15% year over year. Turning to balance sheet highlights, For working capital, our net accounts receivables total \$293 million, compared to \$212 million a year ago, with the increase driven by higher sales volumes. Days sales

outstanding came in at 47 days, up from 42 days in the prior year quarter, due to variations in sales linearity across the quarters. Inventory totaled \$184 million at the end of the third quarter, UP FROM 177 MILLION AT THE END OF Q3 A YEAR AGO DUE TO HIGHER SALES VOLUMES. DAYS OF INVENTORY WERE 36 DAYS DOWN FROM 44 DAYS A YEAR AGO PRIMARILY DUE TO THE TIMING OF RECEIPTS AND CHIPMENTS. ACCOUNTS PAYABLE WERE \$272 MILLION AT THE END OF THE QUARTER UP FROM 192 MILLION A YEAR AGO DUE PRIMARILY TO HIGHER SALES VOLUMES. DAYS PAYABLE OUTSTANDING WAS 53 days compared to 47 days last year due to the timing of purchases and payments. Our cash conversion cycle was 30 days, an improvement of 8 days compared to last year due to faster inventory turns. Consistent with past practice, days sales outstanding, days payables outstanding, and inventory days are calculated on a gross sales and gross cost of goods sold basis. which were \$563 million and \$468 million, respectively, in the third quarter. As a reminder, the difference between gross and net sales is primarily related to our memory businesses, logistics services, which are accounted for on an agent basis, meaning that we only recognize the net profit on logistics services as net sales. Cash and cash equivalents and short-term investments total \$736 million at the end of the third quarter, up \$268 million from Q3 last year and up \$89 million sequentially. The year-over-year fluctuation was due primarily to proceeds from the issuance of preferred shares and cash generated by the business. Third quarter cash flows generated from operating activities totaled \$97 million compared to \$80 million generated from operating activities in the prior year quarter. The increase year-over-year was due primarily to improved working capital efficiency. We spent approximately \$30 million to repurchase 1.8 million shares in the third quarter under our share buyback program. Since our initial share repurchase authorization in April 2022, we have used a total of \$113 million to repurchase 6.6 million shares through Q3 of fiscal year 2025, and we have \$37 million remaining in our authorization. We did not make any debt prepayments in this past quarter, and the principal on our term loan was at \$300 million as of the end of the quarter. Our net debt at the end of Q3 was negative \$66 million. Subsequent to the end of the quarter, we completed a refinancing of our existing credit facility. We paid off the \$300 million remaining on our term loan using \$200 million of cash from our balance sheet and \$100 million of borrowing from a new revolving credit facility. This refinancing transaction significantly reduced our leverage, extended our debt maturities, and is expected to reduce our debt service costs as we reduced our total growth debt by \$200 million. For those of you tracking capital expenditures and depreciation, capital expenditures were \$2 million in the third quarter and depreciation was \$5 million. And now turning to our outlook. Given our strong year-to-date performance, we are maintaining the midpoint of our net sales outlook for the year at 17% year-over-year and tightening the range to plus or minus two percentage points. By segment, our full-year net sales outlook reflects the following. For advanced computing, we continue to expect full-year net sales to grow between 15% and 25% year-over-year. For memory, we now expect net sales to grow between 25% and 30% year-over-year. And for LED, we continue to expect net sales to be approximately flat year over year. Our non-GAAP gross margin outlook for the full year remains 31% with a tighter range of plus or minus 0.5 percentage points. We now expect our non-GAAP operating expenses for the full year will be \$260 million plus or minus \$5 million. We are also raising our outlook for our non-GAAP full year diluted earnings per share which is now expected to be approximately \$1.80 plus or minus 5 cents. This is up from our prior outlook of \$1.60 plus or minus 10 cents. And finally, our non-GAAP diluted share count is now expected to be approximately 54 million shares for the year. Due primarily to changes in our geographic mix of our earnings, we are lowering our FY25 non-GAAP tax rate to 25%. which reflects currently available information. While we expect to use this normalized non-GAAP tax rate through 2025, the long-term non-GAAP tax rate may be subject to changes for a variety of reasons, including the rapidly evolving global and U.S. tax environment, significant changes in our geographic earnings mix, or changes to our strategy or business operations. Our outlook for fiscal year 2025 is based on the current environment, which contemplates, among other things, the global macroeconomic environment and ongoing supply chain constraints, especially as they relate to our advanced computing and optimized LED businesses. This includes extended lead times for certain components that are incorporated into our overall solutions, impacting how quickly we can ramp existing and new customer projects and higher tariffs in our optimized LED business. We believe we are continuing to manage our operations in a prudent manner as we navigate a challenging environment while also investing in our long-term growth. Please refer to the non-GAAP financial information section and the reconciliation of GAAP to non-GAAP measures tables in our earnings release and

the investor materials on our website for further details. With that, operator, we are ready for Q&A.

Cameron | Conference Call Operator:

Thank you. We'll now begin the question and answer session. If you would like to ask a question, please press star followed by 1 on your telephone keypad. If for any reason you would like to remove that question, please press star followed by 2. Again, to ask a question, press star 1. And as a reminder, if you are using a speakerphone, please remember to pick up your handset before asking a question, and we will pause here briefly as questions are registered. The first question is from the line of Kevin Cassidy with Rosen Securities. You may proceed.

Kevin Cassidy | Analyst, Rosen Securities:

Yes, thanks for taking my question. Congratulations on the good results. And in particular, the five new customer bookings. I wonder if you could give us a little more details on that. Are these, you know, customers that you got through partnerships? maybe how long they've been working on booking these new customers, and is it software and services or hardware or both? Maybe just a few questions about that.

Mark Adams | Chief Executive Officer:

Hey, Kevin. Thanks. It's Mark. Let me see if I can break this down for you. The length of these sales motions typically are in the 12 to 18-month range from the time we engage the customers to the time we ship and the bookings kind of come somewhere around the 12-month mark. And I would say some of the new bookings were kind of along that framework. And you asked specifically about software and services relative to hardware. And we've mentioned on previous calls that the hardware is typically something that we recognize revenue upfront. And the way software and services, that category is recognized as more ratified over time. And so when we get these bundled solutions, so to speak, these integrated solutions of hardware, software, and services, they typically are hardware upfront and have characteristics of being lower margin in nature. And then the software and services come to us over time. And that's consistent with some of our more recent bookings.

Kevin Cassidy | Analyst, Rosen Securities:

Okay, great. And maybe you said a little bit about the SK Telecom collaboration. I mean, maybe generating new customers. Can you talk more about where you're seeing that? Sure.

Mark Adams | Chief Executive Officer:

Yeah, absolutely. You know, at the time of the investment, when we closed it back in December of 24, we highlighted that this was really a relationship that was transcending, you know, the financial investment element of it. And we were excited about working with SK and more specifically SK Telecom and SK Hynix. We've had some early wins on the memory side, and we look forward to broadening that relationship with Hynex over time, more system-related products and helping enable some of their memory technologies to new application environments. We've talked about higher bandwidth opportunities like the OMA we mentioned, but we've actually had some early success on business opportunities with Hynex to date. We are making really good progress with SK Telecom as well. We are certainly very optimistic about the opportunities ahead with them in terms of AI data center infrastructure solutions. By the way, you know, the efforts that we have there are really global in nature, not just domestic, but also in other parts of the world. And, you know, again, we're pleased about the progress we're seeing on their AI data center initiatives, and we're exploiting

multiple joint opportunities with them. So, overall, the relationship with SK is positive, and we're pleased with the progress. Okay, great.

Kevin Cassidy | Analyst, Rosen Securities:

Thanks for answering the question.

Cameron | Conference Call Operator:

The next question is from the line of Tom O'Malley with Barclays. You may proceed.

Tom O'Malley | Analyst, Barclays:

Hey, guys, thanks for taking my questions. My first is on the memory side. I think that's the one segment that you're actually taking a bit higher for the full year. You saw some strong growth in the May quarter. August for your full year guide is implied kind of down in the mid single digits range. Can you kind of talk about the dynamic of potential pull forwards? If we look at some other companies in the ecosystem, you've seen some really strong consumer demand in the most recent quarter. You didn't call that out. You kind of called out abroad. breath of strength. But do you know if you're seeing any pull forwards? Are you protecting against that with the guide in August? Any color there would be helpful.

Mark Adams | Chief Executive Officer:

Sure. And, Tom, I think just one correction. I think if you said that memory was the only one that was growing in the year, did I misunderstand?

Tom O'Malley | Analyst, Barclays:

No. You raised memory from, I think, prior. Your range for the full year, I think, moved a little higher from 25% to 30%. Correct. So you took that up a little bit.

Mark Adams | Chief Executive Officer:

Right. Okay. Yeah. And advanced computing is up in the range, I guess it's 15 to 25%, I believe. So on the memory side, we are not seeing any necessary pull forward, so to speak. As we commented on back in the fall, there was some inventory that we were working through. And this quarter, I think we were really pleased with the growth opportunities as people started to get back in ordering. But we don't see any significant inventory builds or what have you. And yeah, we watch that from a customer discussion standpoint on their ordering patterns and what their requirements are and their forecasts. And our pipeline in Q4 remains pretty healthy. So we're generally very pleased with the direction of the business overall.

Tom O'Malley | Analyst, Barclays:

And then on the advanced computing side, you know, historically these are big projects, big customers. They tend to slide around one to two quarters, which is, you know, why I think the four-year guidance is useful. But when you look at the fourth quarter, is the big acceleration again important? a timing of an order, or are you seeing kind of broad-based strength across different customers kind of implied in your full-year guide as a nice mid-teens growth sequentially into the August quarter? So just trying to understand what's contributing to

that strength in Q4.

Mark Adams | Chief Executive Officer:

You know, we're doing, as we mentioned, we're seeing some uptick in terms of bookings, some of which we'll be looking to recognize the revenue through deployments by the end of the quarter. But this quarter isn't necessarily one major deployment. That's not what we're suggesting. We've got a little more diversity in the quarter, although I'll let Nate talk to a specific outlook. But this quarter is not like we commented on in Q2 earlier in my script. This is more a number of customers. And again, we run into the situation where the bookings come at a certain time, our supply chain goes out and acquires accordingly. And we look to install and it's really done at the customer and our pace relative to the business we do with them and not necessarily to the end of a fiscal quarter. So this is where we run into that same lumpiness in terms of revenue. Having said that, As I want to reinforce, it's not about one customer per se. It's a little more diversified.

Cameron | Conference Call Operator:

The next question is from the line of Sameek Chatterjee with JP Morgan. You may proceed.

Sameek Chatterjee | Analyst, J.P. Morgan:

Hey, guys. Thanks for taking my questions. Maybe if I can start on advanced computing, and you talked about sort of the deployments for fiscal 4Q not being driven by like one lumpy deployment but more broad-based. But can you talk about the mix a bit in terms of what you're seeing in those incremental deployments? I know you've talked about the neocloud opportunity, but any sense that you can give us in terms of what you're incrementally seeing in the mix sort of rotating more towards the neoclouds or any more visibility as you look forward into that? And I will follow up. Thank you.

Mark Adams | Chief Executive Officer:

Sure. I think as I commented on earlier in my preferred comments, we've seen, in addition to neocloud, we've seen some strength in federal and energy how to win in biotech, and we're seeing a lot more inbound signals relative to interest in the financial sector as well. Those are kind of the top segments that we're playing in today.

Sameek Chatterjee | Analyst, J.P. Morgan:

Okay, got it. And then maybe on the sort of, I know it's too early to talk about the next fiscal year, but when you think about sort of the new customers that you've signed up, that you talked about, the five new customers, as well as the opportunity that you're now seeing in the pipeline, just help us think about maybe from a fiscal 26 perspective for advanced computing, what should we keep in mind relative to fiscal 25, the growth rate that you have in that sort of 15 to 25% range, how should we think about what are the puts and takes for fiscal 26?

Mark Adams | Chief Executive Officer:

Yeah, unfortunately, we're not providing any of that guidance today. It's just too dynamic an environment with all the puts and takes. There's a number of factors that we and other companies are dealing with right now. One good example is the tariff situation and how dynamic that changes over time. Certainly, you know, very happy and proud of the way the team navigated that in Q3 and delivered strong results. But we're going to stop from commenting on FY26 in any way, shape, or form today. Okay. No, I appreciate it.

Sameek Chatterjee | Analyst, J.P. Morgan:

Thank you. Thanks for taking the questions.

Nick Doyle | Analyst, Needham:

Thank you.

Cameron | Conference Call Operator:

The next question is from the line of Nick Doyle with Needham. You may proceed.

Nick Doyle | Analyst, Needham:

Hey, guys. Thanks for taking my questions. First, could you give any details on the CDW agreement or partnership? Just maybe talking about how that approach is different than with Dell and if you expect any kind of, you know, similar contributions or customer-type wins in fiscal 26. Thanks.

Mark Adams | Chief Executive Officer:

Sure. Again, we're going to – sorry, Nick. We're going to hold up on any 26 commentary, but the framework that we're – working on right now is we're starting to invest in partnerships outside of our direct customer engagement. And you've mentioned two of them today. The idea being that we can scale to a larger set of customers through some of these partnerships and really focus on our value add. And we've seen some early proof of concept success stories in in both partners that you mentioned. But again, it's early stage and it's the right thing for us to be thinking about as we expand, not just in terms of customers here in the US, but as we think about a broader go-to-market internationally.

Nick Doyle | Analyst, Needham:

Got it. For my second question, services revenue grew quarter over quarter, you know, while overall advanced compute declined sharply. So was that driven more by these point-in-time services, or did those larger hardware deals in the first half translate to this, you know, kind of slower, steady revenue growth that we saw this quarter?

Mark Adams | Chief Executive Officer:

You know, I think that it's a mixture of everything what you just said. It is a mixture of, you know, Service revenue ratified over time and recognized over multiple periods, so to speak. And the mix of hardware in Q3 was lower than, say, Q2. And so the combination of that contributes to the services mix. As you know, we

recognize services the way we do, but they are renewed annually. And then in the middle of the fiscal year, if we get a new order, we begin that recognition at the time of a shipment slash signed order for those services. And so that's a positive, and we continue to try to add to that quarter to quarter. Thank you.

Cameron | Conference Call Operator:

Brief reminder, if you would like to ask a question, please press star followed by one on your telephone keypad. If for any reason you would like to remove that question, please press star followed by two. Again, to ask a question, press star one. And as a reminder, if you are using a speakerphone, please remember to pick up your handset before asking a question. The next question is from the line of Brian Chin with Spiegel. You may proceed.

Dennis (for Brian Chin) | Analyst, Spiegel:

Hi, this is Dennis on for Brian. Thanks for taking our questions. My first one is on advanced compute. For the five new customers that you want, are you expecting any change in the hardware and software mix proportions over the life of these customers?

Mark Adams | Chief Executive Officer:

Well, typically what happens or what we've seen happen with our customer engagements with new customers is, again, the revenue recognition for the new customers up front is hardware-related. just because that's what we install and that's what we design a solution for. And then our services and software mix happens over time. Now, we've had a number of instances where customers increased the footprint of their rollout or of their implementation, and that can be a time when they actually order more hardware along the way, But typically, the flow of revenue recognition and type of product is hardware early on in the cycle of a new customer acquisition and software and services over time. And we continue to try to be very disciplined and making sure that we're not doing any hardware-only deals. As you all can see from our competitor announcements, without being specific, The hardware market itself is super competitive from a margin standpoint. And quite frankly, I think our value add is in the services area and the software and services that we offer our customers. And, you know, of course, our hardware is best in class from a design and performance standpoint. But the hardware market tends to be lower in gross margin. And thus, we tend to propose and look at our business from a solutions standpoint. mindset, not in any one component of hardware-only sales.

Dennis (for Brian Chin) | Analyst, Spiegel:

Would you say that the majority of this 66 million of services sales comes from advanced computing, or is there a good bit from the other segments too?

Mark Adams | Chief Executive Officer:

A majority of the services, like a healthy majority, I'll let Nate see if he can give me the actual number here, but the majority of services is all advanced computing.

Nate Olmstead | Chief Financial Officer:

Yeah, the great majority. Got a little bit in memory, but it's really mostly advanced compute.

Dennis (for Brian Chin) | Analyst, Spiegel:

Great. And then for my second question, so for memory, could you discuss the strength in this quarter from a product and a vertical perspective? And how does the strength in DRAM pricing impact your memory gross margins? And then maybe you could also talk about the attach rate of your memory products to your advanced computing products.

Mark Adams | Chief Executive Officer:

Okay, so the first, the pricing in DRAM has been relatively stable in the quarter. What I would say is the memory gross margin question, ironically, when memory pricing goes up, the gross margins are impacted slightly in a negative way because DRAM then becomes a higher percentage of the whole value add that we give. Um, but it's just a directional, uh, trend, but the, um, uh, the mix of products, um, uh, and the unit growth was substantial as well in the quarter, which led to a combined, uh, high growth quarter in memory. Um, on the attach rate, we continue to work, um, and use smart modular and the penguin platform, uh, that we do sell. And, um, We're continuing to develop on new products that we think will be very valuable in terms of the AI ecosystem, as we've talked about, CXL and our optical memory appliance development, which is a long-term initiative for us to help provide better memory, advanced memory solutions for advanced workloads. So it is a priority of ours, and we do a good job on the Penguin systems itself, and we're looking to develop more sophisticated, higher bandwidth memory end products going forward.

Dennis (for Brian Chin) | Analyst, Spiegel:

That's it for me. Thank you.

Cameron | Conference Call Operator:

Thank you. And for our last question, we have a follow-up from Nick Doyle with Needham. You may proceed.

Nick Doyle | Analyst, Needham:

All right. Thank you. Just kind of a bigger picture question. We're hearing about this idea of production inference, and I think that really requires this truly tier one grade, high availability, you know, server solution. So if you take out the hyperscalers just because that's not where you generally play, how much market capacity today is operating at that level and kind of ready to service production inference today? and how much is left, where you guys can go in and really increase that utilization and get the high availability ready to go.

Mark Adams | Chief Executive Officer:

Thanks. Nick, I'm not sure I totally understood your question. We have a high availability edge server platform that we use. We've talked about developing products for inferencing over time. In the data center, you know, we're starting to see more of the trend line to be a hybrid training and inferencing demand thesis. But I'm not sure, again, if I'm quite getting your question. Can you restate it?

Nick Doyle | Analyst, Needham:

Yeah, just pointing out that when guys want to do this kind of production level inference, there's a thinking that it really requires high availability versus more traditional cloud. And, and to do that, you know, you need a, a higher level server and that's what you guys can provide. So maybe the market just isn't there and you can kind of help the market move towards a solution that, you know, works for everybody and wonder.

Mark Adams | Chief Executive Officer:

Great. Got it. So I understand. I apologize. I misunderstood because we, when you said inferencing, I initially went to, our edge platform and what we're trying to build for future edge implementations. But in the environment you're talking about, you're exactly right. There's, and by the way, that's a lot of has to do with our software and services that we provide to be able to make sure that not only is the design performance we get up front in our systems critical, but it's also the availability and uptime through diagnostics and fault, fault repair capabilities in the data center that allow us to have the maximum uptime. And that's a really critical metric when you think about the capital investments into AI infrastructure, making sure people have high reliability, high availability, along with the high performance. And quite frankly, when you come from a high performance compute background like us, we've seen the levers that allow for the most optimal performance in a data center. And I think that has played well and will continue to play well for us as true enterprise rollout production environments for inferencing.

Nick Doyle | Analyst, Needham:

Thanks, Mark.

Mark Adams | Chief Executive Officer:

Thank you.

Cameron | Conference Call Operator:

That concludes the Q&A session. I would now like to pass the conference back over to Mark Adams, the CEO, for any closing remarks.

Mark Adams | Chief Executive Officer:

Thank you, Operator. And just in closing, we are pleased with our results. through the third quarter. On today's call, we reconfirmed the midpoint of our revenue guidance, which we raised to 17% on our last call. And we raised today our earnings per share guidance range for fiscal 2025. We have strengthened our balance sheet and remain committed to our long-term investments in hardware, software, and services, positioning us to address the rapidly growing market demand for AI infrastructure solutions on premise, in the cloud, and at the edge. Thank you all for joining today's call.

Cameron | Conference Call Operator:

That concludes today's call. Thank you for your participation and enjoy the rest of your day.