NASDAQ:PLUS Q3 2025 Earnings Call Transcript

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Operator | Host:

call is Mark Marin, CEO and President, Darren Ragwell, COO and President of E-Plus Technology, Elaine Marion, CFO, and Erica Stoker, General Counsel. I want to take a moment to remind you that the statements we make this afternoon that are not historical facts may be deemed to be forward-looking statements and are based on management's current plans, estimates, and projections. Actual and anticipated future results may vary materially due to certain risks and uncertainties detailed in the earnings release we issued this afternoon, and our periodic filings with the Securities and Exchange Commission, including our most recent annual report on Form 10-K, quarterly reports on Form 10-Q, and other documents we might file with the FCC. Any forward-looking statement speaks only as of the date of which the statement is made, and the company undertakes no responsibility to update any of these forward-looking statements in light of new information, future events, or otherwise. In addition, we will be using certain non-GAAP measures during the call. We've included a GAAP financial reconciliation in our earnings release, which is posted on the investor information section of our website at www.eplus.com. I'd now like to turn the call over to Mark Maron. Mark?

Mark Marin | CEO and President:

Thank you, Clay. Good afternoon, everyone, and thank you for joining us. I will give a recap of our fiscal third quarter 2025 highlights and an update on our business overall. Elaine will follow with the discussion of our financial results, and I will then conclude with an update of our current outlook. We continue to execute on our strategic priorities of expanding our footprint and customer base and broadening our suite of solution and service offerings as we are investing in the most promising growth areas. We continue to see the evolution of our industry transition to our more ratable consumption and subscription-based model, which has impacted the comparability of our quarterly results. As noted last quarter, our revenue trends reflects an acceleration of gross billings recorded on a net basis, as well as a move towards more ratable revenue models. Software subscriptions orders have continued to increase year over year, with these deals being recognized on a net basis or ratably. While this evolution helped to contribute to a flat year-over-year revenue, we delivered solid growth in gross billings, gross profit, and gross margin. It is also a solid forward indicator for growth with our subscription orders up 51.4% year over year, accounting for almost 46% of our open orders currently compared to 31.7% last year and growth of over 100 million. On a consolidated basis, total revenues were flat as lower product sales were partially offset by faster growing high margin service revenue. which is partially reflected in our gross profit being up 5.3%. We believe customers are still digesting purchases from last year's inventory flush, primarily impacting our networking and data center cloud sales. The main factor, though, was that we had a much higher gross to net adjustment this year, which was up 840 basis points from the prior year and impacted our top line revenues by approximately $60 million. This year-over-year increase in SG&A expenses was primarily due to increased headcount from the Bailiwick acquisition, as well as investments in the business. Of note, much of the increased headcount were customer-facing employees. Adjusted EBITDA decreased 15% as higher earnings in the finance segment were offset by a decrease in our technology business adjusted EBITDA. We continue to see softer than expected hardware sales, and lower demand from some enterprise customers. As we have moved towards a services-led model, our services revenues continue to grow nicely, increasing 52% year-on-year and reaching a new high of $114 million, with services gross profit up 45% year-over-year. Revenue in the quarter benefited from the acquisition of Bailiwick early in the year, which is integrating well, and organic managed services revenue increased 28% year over year. Our finance segment delivered another solid quarter with revenue increasing 20%, primarily due to an increase in proceeds from the sale of equipment, as well as higher portfolio earnings and transaction gains. As we look at our longer-term growth drivers, AI is a good place to start. In an E-plus AI survey, 76% of IT leaders have said their organizations have yet to reach AI maturity. They noted the top challenges they are facing are a skills gap, security concerns, and cost. There is a disparity between AI aspirations and AI readiness, and most companies are in the early stages of their AI journey. With that, we continue to build out our AI Ignite and SecureGen AI programs that deliver services and solutions our customers need to make informed decisions. Our SecureGen AI program is a platform developed by ePlus utilizing leading AI technology from our strategic partners to deliver a SecureGen AI chatbot experience. This allows customers to test use cases and convert them into actionable plans with built-in guardrails. Ultimately, our secure GenAI program helps our customers more quickly make informed decisions and adopt GenAI safely. We're also leveraging the benefits of AI internally to create efficiencies that improve customer satisfaction and we expect will provide cost savings long term. With our internal use of AI, we're seeing an increase in quality due to automation and an ability to resolve inquiries and tickets faster. As such, we expect that AI will help us deliver enhanced customer experiences. Security is key to customers' long-term roadmap, especially related to AI initiatives around data strategy, governance, and risk. Our security offerings also continue to be a solid performer for us. Our security gross billings accounted for 21.2% of our trailing 12 months gross billings. We continue to benefit from very attractive cash flow characteristics. In turn, our balance sheet provides financial flexibility to support future growth initiatives. We will continue to be disciplined and strategic with our deployment of capital as we prioritize investing in the business to drive long-term growth, both organically and via M&A transactions, as well as return excess cash to our shareholders. I will now turn the call over to Elaine to discuss our financial results in more detail. Elaine?

Elaine Marion | CFO:

Thank you, Mark, and thank you, everyone, for joining us today. I will now review our financial performance for the third quarter of fiscal 2025. Consolidated net sales of $511 million were modestly above the $509.1 million reported in last year's third quarter. In our technology business, sales were flat year over year as a decline in product sales was more than offset by continued strength in services demand. The decline in product sales reflects a shift towards sales of third-party software and services, resulting in higher netted down revenues, as Mark mentioned, as well as lower sales of product as a result of last year's supply chain easing, particularly from enterprise customers. Notably, growth fillings growth of 6.6% year-over-year outpaced net sales growth, highlighting continued demand for Eplus's offerings and the netting down effect. Our strategic focus on services continues to deliver results as service revenue grew 52% in the quarter with strong contribution from both professional and managed services. The professional services segment benefited from the bailiwick acquisition while growth in the managed services segment was broad-based. Within our technology business, our two largest markets continue to be telecom, media, and entertainment. and technology representing 24 and 17% respectively of technology business net sales on a trailing 12-month basis. SLED healthcare and financial services accounted for 16, 13, and 10% respectively with the remaining 20% from other end markets. Our financing segment posted a solid quarter with revenues of 17.8 million up 19.8% from 14.9 million in last year's third quarter due to higher proceeds from sales of equipment and portfolio earnings. Consolidated growth profit grew 5.3% faster than our revenue growth to $140.9 million, representing a consolidated growth margin of 27.6%, up from 26.3% in the prior year. The 130 basis point expansion was primarily driven by higher product margins, which benefited from a shift in mix to third-party maintenance and subscriptions. While product margins were higher than last year, a higher proportion of product sales to certain enterprise customers at lower overall margins weighed on product margins, but this was offset by contribution from the netting effect I've mentioned. Professional services gross margin declined to 40.1% from 43.3%, due to a shift in mix of services provided, while managed services gross margin declined to 29.8% from 31.8%. Consolidated operating expenses increased 17.3% year-over-year to $112.4 million, primarily reflecting increased headcounts due to the bailiwick and peak resource acquisitions, as well as continued investments in our business to support our growth. Our headcount at the end of the quarter increased to 2,291 from 1,897 a year ago, primarily reflecting additions of customer-facing professionals acquired in the bailiwick transaction. Operating income was $28.5 million, down from $38 million, and earnings before taxes declined to $32.2 million from $38.4 million in the prior year quarter. During the third quarter, we realized interest income of 1.8 million and foreign exchange gains of 1.9 million, resulting in other income of 3.7 million. Our effective tax rate was 25% versus 29% a year ago due to lower state taxes. Third quarter consolidated net earnings were 24.1 million, or 91 cents per share, down from net earnings of $27.3 million or $1.02 per share in last year's third quarter. Non-GAAP diluted earnings came in at $1.06 per share compared to $1.18 per share last year. Our diluted share count at the end of the quarter was $26.6 million compared to $26.7 million in the prior year third quarter. Consolidated adjusted EBITDA amounted to $39.2 million versus $46.2 million in the third quarter of fiscal 24. For the nine months ended December 31, 2024, our consolidated net sales totaled $1.57 billion, down from $1.67 billion in the prior year. The decrease primarily reflects lower product sales in the technology business, partially offset by growth in services and stronger performance in our financing segment. Technology business net sales were 1.52 billion year-to-date compared to 1.63 billion last year. Despite the decline in net sales, gross billings in the technology business were essentially flat year-over-year at 2.49 billion. Year-to-date consolidated gross profit rose 0.7% to 423.4 million, while gross margin rose 180 basis points to 27%. Gross margin expansion was driven by higher product margins, which benefited from an increase in netted-down revenues partially offset by lower upfront margins. For the nine months ended December 31, 2024, consolidated net earnings were $82.8 million, or $3.10 per diluted share, compared to $93.8 million, or $3.52 per diluted share in the comparable period last year. and non-GAAP earnings per share were $3.56 versus $3.99. Adjusted EBITDA was 134.4 million, down from 153.6 million in the comparable period last year. We ended the quarter with cash and cash equivalents of 253.1 million, consistent with the balance at the close of fiscal 2024. Operating cash flow for the first nine months was $141.2 million compared to $143.5 million last year and included cash used to fund working capital, the bailiwick acquisition, and share repurchases. We ended the quarter with $99 million in inventory down from $139.7 million at the end of fiscal 2024. Inventory turns were 13 days, down significantly from 27 days in the third quarter of fiscal 2024. As a result, our cash conversion cycle improved to 32 days, down meaningfully from 54 days in the prior year. During the first nine months of the year, we repurchased approximately 380,000 shares under our repurchase plan at a cost of 30 million. Our strategy continues to focus on our core priorities driving organic growth, expanding through accretive acquisitions, and returning capital to shareholders through our repurchase program. With that, I will turn the call back over to Mark. Mark?

Mark Marin | CEO and President:

Thank you, Elaine. We are investing both organically and inorganically to develop a portfolio that provides us with multiple levers for growth across a broad range of verticals to drive growth and diversification. Growth of our gross profit and services are key indicators of the success of our go-to-market plans and being a trusted advisor for our customers. Our recent results reflect both the fast growth of our services-led business model and the accelerating shift towards ratable subscription and as-a-service revenue recognition models. This has resulted in mixed results for the quarter, and we will continue to adapt and adjust as the market transitions. As a result, we are adjusting our fiscal 2025 financial outlook. Turning to guidance, we now forecast revenue range of 2.07 billion to 2.11 billion for fiscal year 2025 and an adjusted EBITDA range of 165 million to 171 million. Our guidance reflects higher gross to net adjustments than previously expected and also factors in the near-term potential of tariffs and how this might affect short-term decisions. We will continue to monitor this closely and expect to share more insight at the time of our year-end conference call. We are making investments in the business, focusing on high-growth areas where we seek the best return opportunities, and we are confident this will support our commitment to growth in 2025 and beyond. Our balance sheet and financial condition are healthy, which gives us a solid foundation for expansion. In conclusion, we remain confident in the growth opportunities for our business moving forward and our ability to execute. Operator, please open the line for questions.

Operator | Host:

Thank you. Ladies and gentlemen, we will now begin our question and answer session. If you have dialed in and would like to ask a question, please press star followed by the number one on your telephone keypad. If you would like to withdraw your question, simply press star one again. Your first question comes from the line of Maggie Nolan with William Blair. Please go ahead.

Maggie Miller | Analyst at William Blair:

Hi. Thank you. Can you talk a little bit about your expectations for product sales that are included in the guide and maybe a couple of quarters beyond that?

Mark Marin | CEO and President:

Sorry, Maggie. Did you say we didn't hear you? Expectation for product sales in the quarter and then going forward or?

Maggie Miller | Analyst at William Blair:

Maggie Miller, The yeah that's the fiscal fourth quarter, and if you can go a couple quarters beyond that kind of flesh out the you know trends you're seeing given that it's been a weak spot.

Mark Marin | CEO and President:

James Meeker, yeah it's it's actually I think we noted it on the last earnings call as well Maggie. James Meeker, That there's a softening in the market around some of the hardware or product demands, if you will, we specifically sort with some select enterprise accounts in this quarter, we would expect it to continue into next quarter. The other things that affected are, I'll say bottom line, not so much top line, was some of the upfront gross margins on product sales. That was more of an anomaly, but that was offset by the netted down revenues. The other interesting thing in play here, Maggie, is the market is really changing. The OEMs are going more to as a service consumption subscription models, so they're recognized on a net and ratable basis. I think you may have seen our netted down revenues product sales were actually affected by 840 basis points. To put that in perspective, that's about 60 million in net sales that would have went to our top line if it were flat the last year. So it's a moving target. I would expect that they continue to be a soft demand for Q4 and then would expect it to start to pick up a little bit as we move into our Q1.

Maggie Miller | Analyst at William Blair:

So on that last point, Mark, I mean, we've talked about this shift toward net of down product revenues. Are you calling an acceleration? Do you have an idea of maybe what might be driving that trend to accelerate at this moment in time?

Mark Marin | CEO and President:

Yeah, we've seen a couple different things, Maggie. One, we still don't know if it's a new trend. If you look at just the last two quarters, Last quarter's netted down revenues for product sales was affected by 940 basis points. This quarter was 840 basis points. That's significantly higher than last year and higher than what we were projecting in the beginning of the year. So there is that play. What's really happening here is the OEMs are changing how they're going to market. As we sell more software, that subscription, normally recognized on a net or maybe an annual basis, So it's really the product mix and solutions that we're selling that's affecting this right now.

Maggie Miller | Analyst at William Blair:

Okay. Thank you.

Mark Marin | CEO and President:

No problem. Good hearing from you, Maggie. We'll talk to you soon.

Operator | Host:

Your next question comes from the line of Greg Burns with Sidoti. Please go ahead.

Greg Burns | Analyst at Sidoti:

Good afternoon. So I just wanted to talk, I guess, a little bit more about the demand environment. I know you've been kind of calling out this digestion of some of the product that's in the channel from the supply chain kind of improving over the last year. That seems to be lingering longer than probably we would have expected. So is there anything else going on? What are you hearing from your customers? Is it beyond that at this point? Is there other things driving the soft demand or is it really just kind of this digestion of product in the channel?

Mark Marin | CEO and President:

yeah it's the digestion greg we can see it specifically in the networking space and a few select enterprise customers so uh it is around supply chain for the most part uh there are things going on overall uh in the industry i think as you know with tariffs and doge and everything else that's going on i do think the election actually slowed things down a little bit for us in the beginning of the quarter we did see our billings were flattened down uh in the october november time frame and picked up in december But we didn't pick up a lot of what I call the year-end flush or what we normally expect in this quarter. So those are still the cases there. We still, from a, I'll say a customer set standpoint, both sides and by vertical, we're pretty diversified. In fact, we've actually diversified more with the Bailiwick acquisition with some of their customers or expanded the verticals we were in, in some cases. So we feel

Greg Burns | Analyst at Sidoti:

somewhat protected long term but there are some things going on that are affecting decisions right now okay um and then in terms of this ongoing shift towards more software subscription ratable models can you just talk about like what the value proposition for a for a bar is in that type of model is there an increased risk of maybe disintermediation over time if can they go more easily direct uh to customers with that model?

Mark Marin | CEO and President:

No, no, Greg. In fact, it's actually an opportunity for us to build up our services. So in a lot of cases with the subscription, there's add-on services, there's renewals, there's what they call lifecycle management. So you try to get them to adopt the technology or software, if you will, upsell additional features, add in incremental services, maybe provide some type of staffing and or managed service. So No, it's not. It's no different in terms of with the subscription versus hardware. I believe that would affect the channel.

Greg Burns | Analyst at Sidoti:

Okay, great. Thank you.

Mark Marin | CEO and President:

No problem.

Operator | Host:

Thanks, Greg. I'd like to turn the call back over to Mr. Mark Myron for closing remarks.

Mark Marin | CEO and President:

All right. Thank you, everybody. Hey, look, I will reiterate, we still feel very strongly about our strategy and our focus areas that we're in. We're going to continue to build out our services-led model. Our services were up 52%. They were approximately 23% of our net sales this quarter. We'll continue to leverage our customer base and customer segments. Our strong balance sheet gives us flexibility to make inorganic and organic moves. So we feel good where we're positioned. And we've been in business for a long time, so we will adapt and adjust to this new norm short term and be able to make the moves that we need to make. So I want to thank everybody for joining us today and look forward to seeing or hearing you on the next call. Thank you.

Operator | Host:

That concludes today's meeting. Thank you for your participation. You may now disconnect.