Box Inc.

Third Quarter Fiscal 2023

Conference Call Remarks

November 30, 2022

Introduction

Good afternoon and welcome to Box's Third Quarter fiscal 2023 Earnings Conference Call. I am Cynthia Hiponia, Vice President Investor Relations. On the call today, we have Aaron Levie, Box co-founder and CEO and Dylan Smith, Box co-founder and CFO. Following our prepared remarks, we will take your questions.

Today's call is being webcast and will also be available for replay on our Investor Relations Web site at www.box.com/investors. Our webcast will be audio only. However supplemental slides are now available for download from our website. We'll also post the highlights of today's call on Twitter at the handle.

On this call, we will be making forward-looking statements including:

- Our Q4 and full year fiscal 2023 financial guidance, and our expectations regarding our financial performance for fiscal 2023, fiscal 2024 and future periods, including our free cash flow, gross margins, operating margins, operating leverage, future profitability, net retention rates, remaining performance obligations, revenue and billings, and the impact of foreign currency exchange rates; and

- Our expectations regarding
  - the size of our market opportunity;
  - our planned investments, future product offerings and growth strategies;
  - our ability to achieve our long-term revenue and other operating model targets;
  - the timing and market adoption of, and benefits from, our new products, pricing models, and partnerships;

- our ability to address enterprise challenges and deliver cost savings for our customers;
- the impact of the macro environment on our business and operating results; and
- our capital allocation strategies, including M&A and potential repurchase of our common stock.

These statements reflect our best judgment based on factors currently known to us, and actual events or results may differ materially. Please refer to our earnings press release filed today and the risk factors in documents we file with the Securities and Exchange Commission, including our most recent Quarterly Report on Form 10-Q for information on risks and uncertainties that may cause actual results to differ materially from statements made on this earnings call. These forward-looking statements are being made as of today, November 30, 2022, and we disclaim any obligation to update or revise them should they change or cease to be up-to-date.

In addition, during today's call, we will discuss non-GAAP financial measures. These non-GAAP financial measures should be considered in addition to, not as a substitute for or in isolation from, our GAAP results. You can find additional disclosures regarding these non-GAAP measures, including reconciliations with comparable GAAP results, in our earnings press release and in the related power point presentation which can be found on the Investor Relations page of our website. Unless otherwise indicated, all references to financial measures are on a non-GAAP basis.

With that, let me hand it over to Aaron.

Third Quarter Fiscal 2023 Overview

Thanks Cynthia. And thank you all for joining the call today.

We delivered strong third quarter results with revenue growth of 12% year-over-year, or 17% on a constant currency basis. Our sharp focus on profitability drove **record** non-

GAAP operating margins of 24%, up 330 basis points from 20.7% a year ago. Gross margins remained strong at over 76%, while our net retention rate increased slightly versus the year ago period. We are particularly pleased with these quarterly results, and our substantial year-over-year bottom line improvements, given the increasingly difficult macro environment.

Over the last couple of months, I've had the opportunity to chat with dozens of CIOs and CEOs across nearly every sector, and in companies large and small, and it's clear that companies are facing a very dynamic environment in front of them. In every industry, companies are dealing with a complex mix of economic pressures while at the same time needing to drive significant transformation across their businesses.

My customer conversations and our Q3 results confirm that companies are prioritizing strategic IT initiatives that allow them to better serve their customers, operate with speed and agility, enable an increasingly distributed workforce — all while seeking to reduce complexity of technology stacks and keeping their enterprises secure from threats. These remain the top priorities for nearly any business or technology leader that you talk to today. So, while IT budgets might tighten and some larger deals may require more scrutiny across verticals and geographies, we are in a unique position to help our customers become future-ready.

At the center of the future of work is how companies protect, share, and manage their most important content. Whether it's the creative media that goes into a blockbuster film, the research that goes into producing a new life saving drug or vaccine, the client data used to onboard a new customer, or project files that go into producing a new breakout consumer product – every business runs on content.

Yet we see that today most enterprises are dealing with a mix of legacy enterprise content management solutions, network file shares, and point collaboration and signature tools to work with their content. This fragmentation creates security risks, lowers productivity, and ultimately costs enterprises far more than they need to spend.

The **Box Content Cloud** helps companies drive up productivity, reduce risk, and save substantially in the process.

Examples of Box delivering this value to our customers in Q3 include:

- A global technology leader, who has been a Box customer for more than 10 years, purchased a seven figure Enterprise Plus ELA in Q3 to double down on leveraging Box for their business strategy, which includes M&A. With Box, they plan to retire redundant systems and technology with the goal of saving millions of dollars each year, while also improving productivity and reducing risk by protecting their sensitive data.
- A global entertainment company implemented Enterprise Plus in Q3 to secure and protect content and reduce cost and complexity by consolidating data assets and network file shares from M&A activities into one Content Cloud solution.

Despite ongoing budgetary pressures, it’s clear that enterprises are increasingly making strategic, long-term decisions on how to support a hybrid workforce and digital processes, while maintaining a high-level of security and compliance.

The Box Content Cloud is in the best position to help customers reduce the cost and complexity of their traditional content stack, and we are continuing to double down on powering the full lifecycle of content in a **single platform** and address major trends in the future of work.

In Q3 we drove significant innovation across the platform, which we shared at BoxWorks in October.

We unveiled several major enhancements to Box Shield and Box Governance, our flagship security and data governance solutions. In Box Shield, we’ve extended our Malware deep scan capabilities by adding the ability to scan additional file types, including Microsoft Office, reinforcing Box’s commitment to supporting third-party file types, and helping admins apply critical protection to a wider variety of intellectual property. We also announced Ethical Wall capabilities in Box Shield, which creates re-enforced information barriers within organizations to prevent communication or exchange of information that could lead to conflicts of interest between groups. This can be used to safeguard insider information, especially for our customers in financial and legal services. And finally, we advanced our Box Governance capabilities to support more flexible retention policies to serve a wide range of industry use-cases, with future improvements to come around making it easier to export content under legal hold and providing better reporting and disposition insights, and more.

Across our collaboration and workflow efforts, we launched additional capabilities in Box Sign to help customers move more of their signature transactions to the cloud. These include the ability for users to publish documents online for signature, edit signature requests in flight, enjoy an improved signer experience, and much more. We announced the general availability of the all-new Box Notes, for real-time content collaboration and project management; and we announced the beta launch of Box Canvas, our new visual collaboration and virtual whiteboarding tool, which will begin to roll out this quarter. And we enhanced Content Insights, to ensure users and enterprises have rich insights into how their content is being accessed, consumed, and leveraged for enhanced business intelligence.

Finally, a critical part of our product strategy is our ability to integrate deeply across the SaaS landscape, and we are pleased that our interoperability has enabled us to build strong partnerships with leading technology companies. At BoxWorks, IBM CEO Arvind Krishna discussed how Box and IBM have partnered to drive digital transformation for our customers; Kirk Koenigsbauer, CVP and COO of the Experiences and Devices Group at Microsoft, spoke about the importance of openness and interoperability and Box's ongoing collaboration with Microsoft; Thomas Kurian, the CEO of Google Cloud, shared how the Box and Google partnership enables secure modern collaboration in the enterprise; and finally, Jeetu Patel, Cisco's EVP of Security and Collaboration, discussed how Box and Webex joint customers can now use Box and Webex better together.

And more recently, we launched an enhanced Box app for Zoom that enables customers to automatically save select Zoom recordings directly to Box. With this new feature, joint customers can manage their content in one place while maintaining enterprise-grade security, compliance, and governance all within Zoom.

Now, more than ever, customers are looking to partner with platforms, not point tools, to help them drive greater efficiency, user experience, and security. As we head into Q4 and looking out to next year, we'll be doubling down across our 3 core pillars of innovation.

Across security and compliance, we'll be delivering major enhancements to Box Shield and Governance to protect customers in a very dynamic threat landscape, extend our leadership in compliance, and driving new efforts on the most ambitious security and governance roadmap we've ever had. We will be driving major product improvements for Box Sign to support more advanced signature processes, adding richer features into Box Notes and Canvas, further building out Relay and laying the groundwork for a major year of workflow innovation, enhancing core parts of our main web app user experience, deepening our development of content publishing and other advanced content management capabilities, and much more. And within our platform, we'll continue to double down on our scalability and developer experience efforts like UI elements, in addition to our integrations with other 3rd party applications like Teams, Slack, Zoom, Salesforce, and more.

As we've shared, Enterprise Plus, our multi-product suites offering, is a key strategy to increase the efficiency of our sales motion and bring the full value of the Box Content Cloud to customers. Enterprise Plus brings the full suite of Box's advanced product capabilities into a simple product bundle, and we've seen tremendous uptake from our go-to-market teams and customers. We launched E+ just over a year ago and it has become our most successful Suites launch to date. In Q3:

- Enterprise Plus comprised over 90% of our Suites sales in large deals, and Suites represented 73% of large deals – up from 63% just a year ago.
- And we are now seeing renewal rates of E+ come in higher than our overall company renewal rates.

Our Q3 customer expansions and new wins with Enterprise Plus include:

- A sports marketing and talent management company, who has been a longtime Box customer, purchased an Enterprise Plus ELA in Q3 as Box has become a more strategic and integral part of their business. With this upgrade, they will be replacing their current e-signature provider with Box Sign and will be using Box Shield to safeguard health records and PHI in Box, as well as protect themselves from cyberattacks with threat and malware detection.
- A financial services company providing insurance to thousands of businesses purchased Box with a six figure Enterprise Plus deal in Q3. Prior to Box, they had been running on legacy and on premises systems for their claims agents. They recognized the need to replace this system and after working on a proof of concept proving out several use cases using Box's APIs, they selected Box as their backend content layer for the entire organization to store and work on sensitive client information.

We are pleased with our continued strong adoption of Enterprise Plus, as we know that when a customer adopts our multi-product offerings, we see greater total account value, higher net retention, higher gross margin, and a more efficient sales process.

In summary, we are pleased to have delivered a strong Q3. Since our last earnings call, the FX and macro environment headwinds have increased. However, our operational discipline that led to our Q3 record operating margins will continue. Operational discipline has been built into the core of the company. We are proud of our demonstrated significant margin improvements and we remain committed to our FY23 operating margin target.

The confluence of remote work, digital transformation and cybersecurity challenges is causing enterprises to rethink how they work with their content and these trends are only accelerating. We are confident Box is uniquely positioned to gain from this shift. Our record Q3 gross and operating margins in a very dynamic market once again demonstrates our commitment to increasing profitability. We remain hyper focused on driving growth and profitability as we look to the next billion dollars of Box revenue.

With that, I'll hand it over to Dylan.

<u>Q3 Fiscal 2023 Financial Results; Q4 and Fiscal 2023 Guidance</u>

Thanks Aaron. Good afternoon everyone, and thank you for joining us.

Q3 was another strong quarter for Box, with revenue in line with our guidance and operating margin and EPS above our guidance. Despite FX and macroeconomic challenges, we're on track to achieve the three key financial objectives for FY23 that we laid out at the beginning of this year - accelerating annual revenue growth on a constant currency basis, expanding operating margins, and prudently allocating capital to optimize shareholder returns.

We remain committed to delivering against our FY23 revenue growth plus free cash flow margin target of 37%, a 400 basis point improvement from last year's outcome of 33%. Our ability to expand our operating margins and FCF margins in this environment is a testament to our operational discipline and resilient financial model.

In Q3 we delivered revenue of $250 million, up 12% year-over-year. This was in-line with our guidance, despite the 5 percentage points of FX headwind that we experienced in Q3, which was one point higher than we expected when we set guidance on our Q2 call.

During Q3 we began to see an impact from additional customer scrutiny being placed on larger deals due to the macroeconomic environment. In Q3 we closed 77 deals worth more than $100 thousand dollars annually, versus 97 in the year ago period. We now have 1,586 total customers paying more than 100K annually, representing a 19%

year-over-year increase. It is worth noting that our win rates remain unchanged, and our average price per seat continued to improve year-over-year in Q3.

We also continued to drive a strong Suites attach rate of 73% of these large deals. Roughly 42% of our revenue is now attributable to customers who have purchased Suites, a significant 11 percentage point increase from 31% a year ago. Put simply, Box has continued to execute well albeit in a dynamic environment.

We ended Q3 with remaining performance obligations, or RPO, of $1.1 billion, an 11% year-over-year increase, or 20% growth on a constant currency basis. We expect to recognize more than 60% of our RPO over the next 12 months.

Q3 billings of $258 million grew 12% year-over-year, well ahead of our guidance of a high single digit growth rate. We drove this better than expected billings outcome despite a 8 percentage point headwind from FX, which was 3 points higher than anticipated in our guidance. Our strong billings outcome in Q3 was due to increased early renewals and payment durations.

Our net retention rate at the end of Q3 was 110%, up 100 basis points from the prior year. Our annualized full churn rate was 3%, versus 5% in the prior year, demonstrating stronger product stickiness with our customers. In Q4 we expect full churn to remain at roughly 3%, and our net retention rate to be approximately 108%. We expect net retention will be impacted by lower seat expansion rates as we anticipate customers in certain segments will reduce headcount and budgets amidst macroeconomic uncertainties.

Gross margin came in at 76.5%, up 180 basis points from 74.7% a year ago. This result reflects the efficiencies that we’ve been generating as we transition to running fully in the public cloud, as well as the impact of higher price per seat due to strong Suites adoption. Q3 gross profit of $191 million was up 14% year-over-year, exceeding our revenue growth rate by 200 basis points.

Once again, we demonstrated the leverage in our business and our commitment to delivering higher profitability with a 29% increase in Q3 operating income, to $60M. Our record 24.0% operating margin was up 330 basis points from the 20.7% we delivered a year ago.

We delivered 31c of diluted non-GAAP EPS in Q3, up 41% from 22c a year ago and above the high end of our guidance, despite a negative impact of 6 cents from currency headwinds.

I’ll now turn to our cash flow and balance sheet.

In Q3 we generated free cash flow of $55 million, a significant improvement from $31 million in the year ago period. In Q3 we delivered cash flow from operations of $70 million, versus $46 million in the year ago period. Capital lease payments, which we include in our free cash flow calculation, were $10 million, down from $12 million in Q3 of last year.

Let’s now turn to our Capital Allocation Strategy. We ended the quarter with $403 million in cash, cash equivalents, restricted cash, and short-term investments. In Q3 we repurchased 1.1 million shares for approximately $29 million dollars. As a result, we’ve been able to reduce weighted basic and diluted shares outstanding for 6 consecutive quarters.

We remain committed to opportunistically returning capital to our shareholders. As such, our Board of Directors recently authorized a new $150 million common stock repurchase plan.

In addition to our robust stock repurchase program, we will continue to leverage our strong balance sheet and increasing cash flow generation to invest in key growth initiatives and to fund strategic tuck-in M&A opportunities which enhance and accelerate our product roadmap.

With that, I would like to turn to our guidance for Q4 and fiscal 2023.

The U.S. dollar strengthened significantly versus the currencies in which we transact our international business following our prior earnings announcement on August 25, 2022, resulting in a larger than expected FX headwind to both Q3 and the full year of FY23. As a reminder, approximately one third of our revenue is generated outside of the US, primarily in Japanese Yen. The following guidance ***includes*** the expected impact of FX headwinds, assuming present foreign currency exchange rates.

While our strong business performance this year has largely offset these FX headwinds, we are seeing additional scrutiny in some of our larger deals as companies contend with headcount reductions and budgetary constraints. As a result of these intensifying FX and macroeconomic pressures, we have prudently adjusted our FY23 revenue guidance to reflect these dynamics.

For the fourth quarter of fiscal 2023:

We anticipate revenue of $255 to $257 million, representing 10 percent year-over-year growth at the high end of this range. This includes an expected FX impact of approximately 5 percentage points to our Q4 revenue growth rate.

Based on the increasing FX impact and the volume of early renewals that contributed to our strong Q3 billings result, we now expect our Q4 billings growth rate to be roughly 10 percent on an as reported basis, including an expected FX impact of approximately 5 percentage points. We expect our Q4 RPO growth to be slightly higher than our anticipated Q4 revenue and billings growth rates.

We expect our non-GAAP operating margin to increase to approximately 24.5 percent, representing a 370 basis point improvement year over year.

We expect our non-GAAP EPS to be in the range of 34 to 35 cents, representing a 46% year-over-year increase at the high-end of the range, and GAAP EPS to be in the range of 6 cents to 7 cents. Weighted-average basic and diluted shares are expected to be approximately 144 million and 149 million, respectively. Our Q4 GAAP and non-GAAP EPS guidance includes an expected impact from FX of approximately 5 cents.

For the full fiscal year ending January 31st, 2023:

We now anticipate our FY23 revenue to be in the range of $990 million to $992 million, representing 13% year over year growth, or 17% on a constant currency basis.

We are reiterating our FY23 non-GAAP operating margin guidance of approximately 22.5 percent, representing a 270 basis point improvement from last year's result of 19.8%.

We are raising our FY23 non-GAAP EPS to be in the range of $1.16 to $1.17, up from 85 cents in the prior year, and we expect to deliver our first full year of positive GAAP EPS, in the range of 2 cents to 3 cents. Weighted-average basic and diluted shares are expected to be approximately 144 million and 150 million, respectively. Our FY23 GAAP and non-GAAP EPS guidance includes an expected annual impact from FX of approximately 18 cents.

For the full year of FY23, we now anticipate currency headwinds to impact our billings growth rate by approximately 6 percentage points, or 2 percentage points more than the impact to our revenue growth rate. While we expect our FY23 billings growth rate to be roughly in-line with revenue growth in constant currency, we expect it to lag slightly on an as reported basis.

While we are not yet providing formal guidance for FY24, we thought it would be helpful to provide color on two notable items for FY24 modeling purposes. As we have discussed previously, our public cloud migration strategy will unlock significant financial leverage in our long-term gross margin profile once we fully exit our existing collocated data centers. Our redundant public cloud and data center expenses will peak in the first half of FY24. During Q1 and Q2 of next year, we expect gross margins to dip by a couple hundred basis points from the 76.5% we just reported. We expect to end FY24 with gross margins a few hundred basis points above the result we just reported. We expect this gross margin impact to flow through to operating margins next year, with Q1 and Q2 experiencing a temporary headwind before rebounding, resulting in year-over-year operating margin expansion for the full year of FY24. As a result, Box will be better positioned to continue delivering profitable growth as we scale, exiting next year with an even stronger operating margin model after completing this important transition to the public cloud.

Additionally, due to the material foreign exchange movements we've seen throughout FY23, we think it would be helpful to quantify the impact of FX on next year's revenue growth. At current spot rates we expect a roughly 300 basis point headwind to revenue growth for the full year of FY24, on an as-reported basis, with a more pronounced impact in the first half of the year. As is our custom, we will provide detailed FY24 guidance on our fiscal Q4 earnings call.

I would like to close with how proud we are of our Boxers who have been focused and executing in this dynamic economic environment. We have created the leading Content Cloud platform that allows enterprises to manage the entire lifecycle of their content while lowering costs and keeping their enterprises secure from threats. We are on track to achieve our three key financial objectives for FY23, as the strength and resiliency of our business model has allowed us to deliver revenue growth while expanding operating and free cash flow margins. To sum it all up, we are well positioned to continue to deliver value to our customers and stakeholders in this uncertain macro environment as we scale towards generating the next billion in revenue.

With that, Aaron and I will be happy to take your questions. Operator?