HD **Q2 2015 8x8 Inc Earnings Call - Final**

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OPERATOR: Good afternoon, ladies and gentlemen, and welcome to the 8x8 second quarter FY15 earnings conference call.

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(Operator Instructions)

As a reminder, this conference call is being recorded. I would now like to turn the conference over to your host, Ms. Joan Citelli, Director of Corporate Communications.

JOAN CITELLI, DIRECTOR OF CORPORATE COMMUNICATIONS, 8X8 INC: Thank you, and welcome, everyone, to our call. Today I'm joined by 8x8s Chief Executive Officer, Vik Verma; our existing Chief Financial Officer, Dan Weirich; and our newly appointed Chief Financial Officer, Mary Ellen Genovese to discuss our results for 8x8's second fiscal quarter of 2015 ended September 30, 2014.

If you have not yet seen today's financial results, the press release is available on the Investors tab of 8x8s website at www.8x8.com. Following our comments, there will be an opportunity for questions. Before I turn the call over to Vik, I would like to remind all participants that during this conference call any forward-looking statements are made pursuant to the Safe Harbor provision of the Private Securities Litigation Reform Act of 1995.

Expressions of future goals including financial guidance and similar expressions, including without limitations, expressions using the terminology may, will, believe, expect, plans, anticipates, predicts, forecasts, and expressions which reflect something other than historical fact are intended to identify forward-looking statements. These forward-looking statements involve a number of risks and uncertainties including factors discussed in the Risk Factors sections of our annual report on Form 10-K, and our quarterly reports on Form 10-Q and in our other SEC filings and **Company** releases.

Our actual results may differ materially from any forward-looking statements due to such risks and uncertainties. The **Company** undertakes no obligation to revise or update any forward-looking statements in order to reflect events or circumstances that may arise after this conference call, except as required by law.

Thank you. And with that, I will turn the call over to Vik Verma, Chief Executive Officer of 8x8.

VIK VERMA, CEO, 8X8 INC: Thank you, Joan, and welcome, everyone, to 8x8's second quarter of FY15 earnings call. Before we begin, I would like to introduce our newly appointed CFO Mary Ellen Genovese. As previously announced, Dan is leaving 8x8 to join a non-competing cloud-based big data startup here in the Bay Area called Treasure Data.

Maryellen, who has been working with 8x8 in various capacities for over two years and has a proven track record as a CFO, will become our new CFO effective November 1, 2014. To facilitate this transition, Dan will be working with Mary Ellen through the remainder of 2014 in an advisory capacity. On behalf of all of us at 8x8, I wish Dan the best in his new role, and thank him for his service to 8x8 over the past decade.

Dan has played a very significant role in our growth over that time and has been key in our efforts to capture the mid-market segment and launch our global reach initiative. We are fortunate to have Mary Ellen join us as CFO. I have known Mary Ellen for more than a decade. In fact, she was my CFO at Savi Technology prior to acquisition by Lockheed Martin.

Prior to Savi, she was CFO of Trimble Navigation where she played a leadership role in helping them transform from a horizontal GPS technology provider to becoming the dominant player in targeted vertical markets. Under her watch as CFO, Trimble's revenue more than doubled from $271 million to $669 million while she maintained strong operational margins and positive cash flow.

In her previous CFO positions, Mary Ellen completed numerous acquisitions, complex joint ventures, secured financings, led cost reduction programs, and built global financial reporting capabilities. Dan has built a deep and experienced finance organization here at 8x8, and I'm confident that Mary Ellen is ready to help take us to our next level of growth.

I would like to begin by reviewing some of the high-level financial results and business activities for the quarter. Following my remarks, Dan will discuss the results and metrics in greater detail and we will then be happy to answer any questions that you may have for us today.

As you can see from our FY15 Q2 results, the momentum we generated in a very strong fiscal Q1 continued this quarter with 29% year-over-year growth in total revenue to a record $39.6 million, and non-GAAP net income of $4.3 million, or 11% of revenue.

We remain committed to profitable growth and strong cash flow, and this is the 18th consecutive quarter in which 8x8 has generated non-GAAP net income alongside increasing revenue. Driving this growth is the continued mid-market adoption of our cloud telephony, contact center and unified communication services we saw during the second quarter of FY15. New monthly recurring revenue from channel and mid-market sales increased 59% year-over-year, and represented 44% of new monthly recurring revenues **sold** in the quarter compared with 33% in the same period last year.

Revenue from mid-market customers represented 41% of total service revenue compared with 35% for the same period a year ago. Customers are choosing 8x8 for our comprehensive one-stop shop product suite which includes cloud-based telephony, contact center, mobile apps and Web conferencing. Our ability to rapidly deploy these solutions on a worldwide basis is accelerating time to value for our customers, enabling them to very quickly begin realizing the benefits of transitioning their communication infrastructure to the cloud.

A few noteworthy highlights from the quarter. First, our ability to offer a broad range of cloud-based mission-critical communication services is bringing us larger and larger deals where we continue to displace incumbent premise-based systems from Avaya, Cisco, ShoreTel and others. Having a single cloud-based solution is a tremendous advantage for our customers as it enables them to eliminate the cost and hassle associated with deploying, integrating, and managing disparate multi-vendor technologies.

During the September quarter, our top two wins and four of our top 10 deals were from new mid-market customers subscribing to both our Virtual Office and Virtual Contact Center solutions. One of these customers, a leader in cloud-based supply chain management solutions, will be deploying approximately 800 Virtual Office and 100 Virtual Contact Center seats to employees in two primary locations in the coming weeks.

Second, our intense focus on customer support is yielding continued low revenue churn at just 0.9% during the quarter compared with 1.2% in the same period a year ago. In addition to building a personalized and responsive mid-market customer service organization, we have implemented a rapid customer deployment model that I believe is unparalleled in our industry.

Yesterday's press release announcing the full deployment of our customer, ChenMed, clearly illustrates this accomplishment. In just five weeks, we successfully rolled out our service across their entire organization of 1,400 employees, 36 healthcare centers and two corporate offices.

Third, we are continuing to invest in product development to ensure that our entire suite of service offers all of the features and capabilities our customers are relying on to grow and be competitive in their respective industries. During the quarter, we expanded the omni-channel capabilities of our cloud contact center solutions with the release of Virtual Contact Center 8.1. We also announced a new partnership with Conversocial, the leading provider of social customer service solutions to enable contact centers to engage with customers over social media channels.

Additionally, we are continuing work on two very significant R&D projects which we expect to complete by the end of our current quarter. First, we are currently in beta with our VCC 9.0 global platform release with a handful of select customers. We are very excited about this new global dimension we are adding to our Virtual Contact Center solution and believe ours will be the only cloud-based contact center service to enable a seamless follow-the-sun operating model. With our next-generation global platform, Virtual Contact Center will have the ability to manage and serve all agents on a single distributed platform irrespective of their geographic location.

The global platform architecture eliminates the need for multiple distinct instances to manage traffic from different continents. Now an agent logging in from North America can service customers not only from North America but also from Europe, Asia, and beyond with optimized call quality and call routing, shared queues, and consolidated reporting, all from a fully cloud-based solution.

Next on the product development front is a much deeper level of integration between our Virtual Office and Virtual Contact Center solutions. This is an extremely complex engineering task due to the tremendous amount of software and intellectual **property** associated with each of our core services. As we combine these services into a single integrated platform and user experience, we are distancing ourselves technologically from our single dimension competitors who specialize in only one of these distinct service areas.

Fourth, we continue to make good progress on the international front, building a geographically distributed worldwide presence that enables us to provide seamless connectivity and superior quality of service to our multi-national customers using a proprietary geo-routing call handling technology. We're about to launch our service platform at a new data center in Sydney, Australia and have engaged with a partner there to work with several current customers.

And our UK office has been busy with some significant wins of their own, including a world-renowned public research university that will soon be deploying our Virtual Contact Center solution with Zendesk Integration. We believe that we are well ahead of any of our competitors in terms of our ability to offer and very quickly deploy a complete suite of services with dedicated customer support.

The mid-market and enterprise segment is very different from the SMB segment. The solutions required by this market segment demand a much more robust product, a stronger sales force, and a world-class customer service and support effort and these capabilities cannot be built overnight.

For the third consecutive year Gartner, the leading information technology research and advisory **firm**, positioned 8x8 in its leaders quadrant of its August 28, 2014 Magic Quadrant for unified communications as a service multi-regional. We believe Gartner's recognition is a testament of our ongoing leadership in the industry.

Given our continued strong quarterly performance, we're increasing our revenue guidance of FY15 to approximately 26% and non-GAAP net income as a percentage of revenue in the 8% to 10% range. Previously, we had stated that range as 6% to 9% of revenue. Now considering the quarter's results and where we stand in our investments to date, we are comfortable stepping that up a bit to 8% to 10% of revenue for the remainder of FY15.

With that, I will now turn the call over to Dan Weirich who will provide you additional details on our financial results.

DAN WEIRICH, CFO, 8X8 INC: Thank you, Vik. Our second quarter revenue growth was strong, with a 30% increase in service revenue and 29% increase in total revenue compared with the same period last year. 41% of our total service revenue in the second quarter was from customers who generated more than $1,000 in monthly recurring revenue, or MRR, compared with 35% in the same period last year.

As Vik noted, our sales were robust in the quarter with new monthly recurring revenues **sold** by our channel and mid-market sales increasing 59% year-over-year, representing 44% of new MRRs **sold** in the quarter compared with 33% in the same period last year. All of our sales channels experienced an increase in MRR **sold** in the quarter.

GAAP net income was $1.3 million, or $0.01 per share. Non-GAAP net income was strong at $4.3 million, or $0.05 per share, and 11% of revenue compared to $4.1 million and $0.05 per share in the same period a year ago. Sequentially, non-GAAP net income as a percentage of revenue increased from 8% to 11% due to approximately 1% expansion in gross margin, 1% related to better optimization of our sales and marketing spend, and 1% related to capitalized software.

During the quarter, we received a $1 million licensing payment related to a family of patents we **sold** in FY13. We removed the $1 million benefit from our non-GAAP net income because we consider this to be an isolated **transaction** that is not reflective of our ongoing operations. 8x8 continues to innovate and was awarded three patents, our 93rd, 94th, and 95th patents, in the quarter.

Gross margin was strong at 72%, the highest since the first quarter of FY14. Service margin was 79% and product margin was negative 8%. This compares with 71% gross margin, 81% service margin, and negative 27% product margin in the second quarter of FY14.

Cash, cash equivalents, and investments were $186 million at September 30, 2014, up $3.6 million in the quarter, and $7.2 million in the first half of the fiscal year. Cash flow from operating activities was $8.6

million year-to-date. Capital expenditures were $1.5 million in the quarter, or 3.9% of revenue, and $2.6 million, or 3.3% of revenue in the first six months of FY15.

We ended the quarter with 40,434 customers, an increase of 1,094 in the quarter compared to an increase of 1,407 in the first quarter of FY15. The primary reason for the reduction in net customer additions between the first and second quarters of FY15 is because we instituted a price increase on our one- and two-line customers effective September 1, 2014. The price increase has been net MRR positive as we are able to more than offset cancellations and fewer customer additions with higher MRR.

Average revenue per customer was a record at $299, up $6 sequentially, and $31, or 12%, compared to the same period a year ago. Monthly business service revenue churn was strong at 0.9% in the quarter compared with 1.2% in the same period a year ago. As Vik indicated, we expect annual revenue growth of approximately 26%, with non-GAAP net income as a percentage of revenue in the 8% to 10% range for this fiscal year. We are building a **Company** focused on sustainable growth with attractive margin potential.

Finally, I want to thank everyone in the financial community for attending the 34th consecutive 8x8 earnings calls I've participated in. 8x8 has never been as strong as it is today and its best days are yet to come. I am very proud of what we accomplished over the 10.5 years I've been at 8x8 and look forward to watching the **Company** continue to prosper from the outside.

Mary Ellen and I have been working together for the past two and half years and I have first hand experience to know that the **Company** will be in great hands under her leadership. That concludes my prepared remarks, and I'll now turn the call over to Vik.

VIK VERMA: Thank you, Dan, and, again, thank you for your decade-long service to 8x8. Before we close our prepared comments, I'd like to have Mary Ellen address you and introduce herself directly.

MARY ELLEN GENOVESE, INCOMING CFO, 8X8 INC: Thank you, Vik, and thank you also, Dan. I have had the pleasure to speak to many of you listening on today's call since we announced my new role earlier this month. I am very excited and honored to step into 8x8's CFO role. Dan has built a world-class finance organization and I enjoy working with his team.

As many of you know, I am familiar with the **Company** as I have been working with the 8x8 **Board** since April 2012, and have been a member of the executive staff since September 2013. I see great opportunity ahead for 8x8. I believe we are in a position of strength in the market compared to our competitors.

I am ready to help take 8x8 to the next level, and I believe my experience with profitable worldwide growth, acquisitions and integration with both domestic and international businesses, as well as my experience with developing vertical markets will help 8x8 as we continue to capture increasing market share. I am looking forward to working with Vik and the rest of the management team to continue our domestic and international growth. I look forward to meeting many of you in my upcoming travels for investor conferences and road shows.

VIK VERMA: Thank you, Mary Ellen. You have our full support and confidence in your new role.

In summary, we have had a strong quarter characterized by continued growth and profitability. We're executing on the plan we have laid out to you previously, expanding our mid-market customer base while increasing customer size and ARPU. While others in this space are targeting the mid-market, 8x8 has demonstrated proven success with a viable strategy and sustainable business model.

With that, we'll be happy to take on any questions you may have for us today. Operator, please open the line for any questions.

Questions and Answers

OPERATOR: Thank you, Mr. Verma. (Operator Instructions) Amir Rozwadowski from Barclays.

ARINDAM BASU, ANALYST, BARCLAYS CAPITAL: Hey, this is Arindam Basu on behalf of Amir. Great results. A couple of questions for me. First, this improvement in churn, is this more like a quarterly trend or are you seeing a structural shift as you move to larger customers?

And then a follow-up to that is also on the margin guidance. Again, is this a result of the ongoing mix shift in the type of customers, or is that a function of tighter cost control, as well? If you could just break that down a bit, that would be very helpful?

DAN WEIRICH: Hi, Arindam, it's Dan Weirich.

On the churn question, last quarter we had a phenomenal figure of 0.4%. We stated to consider it to be approximately 1% until further notice. If you go back a few years, we were 1.7% in FY13. We were 1.3% in FY14. We put up 0.4% in the June quarter and 0.9% in this most recent quarter.

It's primarily due to the mix shift as greater percentage of our revenues coming from mid-market customers is why you've seen this trend. But in addition to that, we just continue to improve our product, improve our deployment of our product, as well as the customer success in support of our product. So it's a combination of many, many things. We definitely think there is more room for improvement.

If you look at it on just a macro view, the mix difference is a mid-market customer is going to churn at the neighborhood of 0.3% or so, from a logo count, and it does not always tie that close in at revenue. But it is significantly lower than a smaller customer who is going to turn at like 1.7% or something like that. Over time, mix shift is going to bring it down to consistently sub 1%.

But as we noted in the past, we are still comfortable at the approximately 1% range. On the overall margin side, if you look at the two different types of revenue streams from SMB, which are customers that spend less than $1,000 a month and mid-market distributed enterprise, which spend more than $1,000 a month, we talk about something called contribution margin which essentially is our GAAP service margin less customer service and billing related expenses.

For the quarter, the combined Company was 63% contribution margins this quarter. Very consistent to prior quarters. The delta is tiny between the two, between SMB and mid-market. SMB is a touch more profitable, primarily because the customer service and deployment is lower on that today because we're in a very much a growth mode for the mid-market side.

But the delta I'm talking about is a 300-basis-point delta on it. The primary difference on the two is the lifetime value of the mid-market customers is much, much greater because the customers are with us for so much longer than an SMB customer. The mix on that is between the two is not the reason for moving up the guidance. It's just that as we progress through this year we've just done a little bit better than we expected on the bottom line, specifically in this quarter.

And it was related to three things. One is we optimized the sales and marketing spend a bit this quarter. So we picked up about call it 100 basis points or so of improvement from the prior period. Two is gross margin has been moving upwards and with got a lot of good visibility on gross margin and have a lot of confidence in where that's going in the future.

And the third is we did capitalize two software-related projects this quarter which represented a little bit less than 100 basis points in improvement sequentially. It's just a combination of many things is the reason why we've moved up the range and we tightened the range a bit for the balance of the year.

ARINDAM BASU: Got it. Okay. Perfect.

VIK VERMA: Thank you.

OPERATOR: Catharine Trebnick from Dougherty & Company.

CATHARINE TREBNICK, ANALYST, DOUGHERTY & CO.: Hi, thank you for taking my question. Could you provide any more detail on the mid-market in terms of segmentation? Are you having any more particular success in the financial versus healthcare? And then what would be the reasons for that driving that? Do you see some of your security sweet spot that you have or sweet spot adding to that? Thanks.

VIK VERMA: That's a great question. Security, it is reliability, it's compliance. I think is the key things that we bring to the party. As you know, we have 99.997% reliability.

We have FIPS, FISMA and every other alphabet soup of compliance. And just generally, we take our security element and we architect to the product to be highly scalable, highly secure. We've seen traction in the financial sector, we have seen traction in healthcare.

We've seen traction surprisingly in recruiting, as well as law firms. Those have been the four verticals that we are starting to see quite a bit of traction in. But there are others that are jumping on board, including transportation and a few others. But as I said, the first few, financial, healthcare, law firms, and recruiting offices are definitely starting to take off for us.

CATHARINE TREBNICK: Okay, thank you very much.

OPERATOR: Michael Huang with Needham & Company.

MICHAEL HUANG, ANALYST, NEEDHAM & **COMPANY**: Thanks very much. Thanks for all the help, Dan, and welcome aboard, Mary Ellen. Look forward to working with you. Just a few, a couple of questions for you.

First of all, drilling into the net add number, so obviously, on the lower end it seems that the price increases drove some churn there, but it's great to see some replacement of higher MRR customers. When you look at just the mid-market segment, is there any color you can share with us that kind of helps us understand the number of mid-market customers that are being added and what is the trend with respect to previous quarters?

DAN WEIRICH: Yes, Mike, just on your first point, on the net add increase, it was down sequentially, effectively on purpose by us. So we sell to businesses that have one employee and we sell to businesses that have thousands of employees. What we did is we started looking at our small customers defined as one- and two-line customers. They were calling customer service a whole lot more than bigger customers, and a combination thing and their contribution margin is materially lower than the balance of the organization.

They were chewing up lots of time on installs and various things like that. We looked around the market and saw that some folks that compete in that size customers' range were charging a lot more than we were charging. And so we did two things. One is we raised the pricing on all of our customers that have been with us for more than a year that were one- and two-line customers effective September 1. And, two, our SMB sales team for new one- and two-line customers had to sell at a higher price effective September 1 than they were selling pretty much for the years prior to that.

And so it's a combination of -- we had a few cancellations related to the higher price increase that was completely immaterial relative to the overall price increase. And we had a few lapsed signups that effectively is the explanation for the net add piece. On the mid-market customer additions, it's something that we're not breaking out primarily for competitive reasons. Historically, we have provided a tremendous amount of information relative to some of our competitors in the market and it's something that we keep pretty close to our vest.

We did note last quarter that the figures as of last quarter and FY end 2014 we had in the neighborhood of 1,200 mid-market customers that were spending $3,500 per month on average, 60%-plus contribution margin and 0.3% churn rate. So the LTV on those customers is enormous. And we are doing really well on adding those customers.

We're up 59% in the amount of monthly recurring revenue that we **sold** through our mid-market and channel sales efforts in the quarter. But just on the numbers of new logos we're adding, we're not breaking out that figure, but we are giving you a little insight as to what some of these look like. So last quarter we talked about an urgent care operator in numbers and things like that. And yesterday we just announced who that customer was. So you can see the type of customers that we are targeting, how quickly we're getting them deployed, and what services they are buying from us.

MICHAEL HUANG: Got it. Directionally, if you looked at the number of mid-market customers that you added, was it up sequentially or are you able to qualitatively share with us that?

VIK VERMA: Yes, it was up sequentially. I think in essence we were up in terms of percentage, I think it was 60 basis points sequentially, and then as I said, every quarter you're starting to see that number keep trending up.

MICHAEL HUANG: Got you. And my second question, so thanks for sharing some thoughts around the innovations that are upcoming. Could you share any detail around some of the beta customers that are working with you on VCC 9.0?

How big are these contact centers, and are they customers already, or are they prospects who are ultimately kind of playing around with VCC and ultimately accepting 8x8 once this is generally available? Maybe just provide a little color around that? Thanks

VIK VERMA: So, one, they are big. That's always a good thing. Second, I think part of the point that you start to see is a steady stream of new product and new features. 8.1, I think talked to you a little bit about everything from local language translation, multi-chat, et cetera, et cetera. You are starting to see some of the other such functionality with this VCC 9.0.

We have a handful of customers that we are using to basically beta. We brought in approximately 18 CIOs and senior IT-level folks here that had international offices, as well as domestic offices, and what we were noticing is that we rent them through our product road map and several of them then signed up for additional beta. So we are trying to do this in a very interactive process, which is exactly what you do with mid-market. You find a handful of representative customers, you work very tightly with them, and then you keep innovating very, very quickly. And I think you are starting to see the pace of our product releases is picking up pretty significantly.

MICHAEL HUANG: Thanks so much.

OPERATOR: Mike Crawford from B. Riley & Company.

MIKE CRAWFORD, ANALYST, B. RILEY & CO.: Thank you. I was glad to see you raise the guidance on the operating margin to 8% to 10% this year. I'm wondering what your thoughts are, if you dare look out a year or two or three given likely very probable top line growth what that might translate to in terms of potential operating leverage, given that you already have much of your mid-market channels now in place?

VIK VERMA: We're midway through the year, Mike, so we just raised our guidance, as you know, to 8% to 10% exactly, I think, 15 minutes ago. I'm probably not ready to look at 2016 and beyond. We will probably provide that you towards the latter half of this year. But suffice to say, we're starting to feel good about our business, and I think, hopefully, you're getting the sense we tell you what we're going to do and then we make sure we try to give you a good sense of what it is going to be and keep trying to meet our expectations.

MIKE CRAWFORD: Okay. Thank you. Maybe I will try to follow up, just to be a little less specific, but are there any factors that would prevent there from being more operating leverage as the top line grows from here?

VIK VERMA: Not that I can think of, Mike. I think as you can see we are starting to get improvements across the board in everything from overall spend, as well as gross margin. I think we have the industry's leading gross margin and we see that actually getting better.

MIKE CRAWFORD: Great, thank you very much.

OPERATOR: Greg Burns from Sidoti & Company.

GREG BURNS, ANALYST, SIDOTI & COMPANY: Good afternoon. I just had a question on what your thoughts are in terms of uses of cash, evaluations in the space of coming in over the last six months or so, so I would imagine that things are getting more -- potentially more attractive out there. What are your thoughts on M&A or other uses of cash?

VIK VERMA: That's actually a great question. I think hopefully you recognize the process that we follow. We've been pretty darn disciplined on price. As you know, we had a reasonably decent M&A pipeline and we have kept churn in there what we are finding as people are starting to be a lot more amenable to different prices, and by different I mean lower prices.

We will continue to go through a rigorous process, but the intent is to keep adding bolt on technologies that can keep enhancing our platform. I think you keep hearing the same common vision. We have a global unified platform with multiple capabilities all built in, one-stop shop, and we will keep adding to that as we go on. And that's essentially our M&A pipeline. But what we are trying to make sure is we keep paying a very fair price for what we get we get full value for.

GREG BURNS: Okay, and in terms of the investments you're making to support the expansion into the mid-market. Do you feel like you have increased bandwidth now to handle more customers or more incoming volume? Like could we potentially see accelerated growth at some point based on the investments you have put in? Or do you feel you need to make incremental additional investments in certain areas of the business to continue to pursue the mid-market?

VIK VERMA: All of it is, as you know, a work in progress in the sense that -- and it's all incorporated in the guidance we just provided. We just took up our guidance on revenue to approximately 26%. We took up guidance on net income to 8% to 10% for the whole fiscal year. And that incorporates the fact that we will continue to be investing in R&D, as well as in other areas.

I think the key part for us is, I think we would like to feel we have now a differentiated platform and we're going to keep adding more and more features and functionalities to it so can put non-trivial distance between us and our various competitors. But, again, it's all incorporated in the guidance that we have already given you.

GREG BURNS: Okay, thank you.

OPERATOR: Nikolay Beliov from Bank of America.

NIKOLAY BELIOV, ANALYST, BOFA MERRILL LYNCH: Hi. Good call. Thanks for taking my question. Vik, you took the helm of the Company about a year ago. When you look back over the last one year, what were the surprises? Where did you do better than you expected? (Inaudible) like coming out like as a CEO like a year ago and versus where you might be under performed and what you can do better?

VIK VERMA: That's actually a very good question. So a couple of thoughts. One, I think the way we went after mid-market was SMB-plus, and I think that was where we had to make some changes in the way we approached it. Mid-market is a very different type of sales.

You need a very different type of sales person, you need a very different type of sales engineer, and you need a very different type of deployment, a different level of documentation, a different level of customer support. A different standard and reliability, et cetera. It's not just a larger SMB customer.

I think that is an area we made some non-trivial progress on. I think you can see it in two very distinct areas. We have put together a dedicated customer success team that basically has partnered with all of our major customers and we're starting to see the fruits of that both in the fact that they are providing us input on new products that they want and need, plus they are also upselling significantly, and then also you are starting to see churn stabilize.

The other area we've invested very significantly in is this rapid deployment capability. As you know, everybody wants to go from SMB to mid-market, and I think I've made this comment that it's more than just putting it on a PowerPoint. You have to put very detailed design documents, you have to make sure that the customer's expectations are very clearly set, acceptance criteria is defined. Billing happens in a very structured way. Those are things that don't just happen, and is not just a simple as, okay, connect a phone and we will bill you.

And so I think to a large degree, as you know, a lot of our competitors in this space are known for having large bookings, which then somehow never seem to translate into deployments. I wanted to give you very concrete example where a 1,400-person facility went live from start to finish in under five weeks. Actually, the bulk of the deployment was done in three weeks.

So that is another area I think that we've added to and enhanced. What I will tell you, and I think this is one of the great surprises and the most pleasant surprise, some of the technology we have out here is unbelievable. And I think over the next few quarters you will start to see us add additional features and functionalities. We've had a core **group** of engineers working for years, and when all is said and done, at heart, we are technology **Company**. And our products are pretty amazing.

I think you'll start to see more and more stuff that I think people will have a tough time kind of replicating. Where we can definitely do better is sales and marketing. I will tell you that we're still so-so. We're still learning how to sell at mid-market. We're still not at the capacity I would like, so I see a non-trivial amount of headroom in being able to make our mid-market sales get much, much better. So I view all of these as generally positive.

NIKOLAY BELIOV: And to your last comment, just to clarify, you talked about on the call about optimizing sales and marketing investment. So you got some leverage out of that. What did you specifically do?

VIK VERMA: In essence, everything from pay different quotas for new logos versus upsells to having very dedicated teams of sales engineers and account executives to changing quotas. It is a standard blocking and tackling sales 101 type stuff, and I think it's just very different from SMB to mid-market. And as I said, I'd like to think we've got a non-trivial amount of headroom where we can continue to get our sales productivity better.

NIKOLAY BELIOV: Thank you.

OPERATOR: Dmitry Netis from William Blair.

DMITRY NETIS, ANALYST, WILLIAM BLAIR & **COMPANY**: Okay, thank you. Nice print, gentlemen, and, Mary Ellen, welcome to the team. Good luck with the new role, and, Dan, thanks for a good ride and good luck with Treasure Data.

DAN WEIRICH: Thank you, Dmitry.

MARY ELLEN GENOVESE: Thank you.

DMITRY NETIS: Okay, real quick, a couple of questions. What was your accrued backlog at the end of the quarter, and how did it grow from last month, or from last fiscal Q1, I guess?

DAN WEIRICH: Dmitry, we mentioned last quarter that we weren't going to provide that anymore. We provided it in Q4. We provided in Q1, just to illustrate to folks that we're in a transitional period of time. We are migrating from the vast majority of the revenue going live within 30 days to a situation to where it didn't go live in 30 days, it went live in two to six months or so.

We're starting to see very, very good successes of customers installing very quickly. So ChenMed is an example of that where they installed in 35 or so locations, 1,400 seats in a very short period of time. And so we just felt that the backlog figure was something we could let the folks know that we're in a transitionary period of time. The revenue was delayed a little bit, but we're in a situation that now that we're very comfortable with it and it's nothing that is great news or bad news in any form or fashion. It something we're just not disclosing.

DMITRY NETIS: Okay, good, well, thanks for the color, though. And then, if I were to remove your international revenue, are you able to tell us how the growth looked like here in the US?

DAN WEIRICH: Yes, so once again we have stated that acquisitions are part of our strategy. We haven't broken out the organic from inorganic revenue growth in the past. We do have in our tables and in our 10-Q revenue from Europe and Asia. There is revenue that was 8x8 customers, which are two different types.

Legacy customers, there are Fortune 500 customers, there are these young, rapidly growing, recently public, typically Internet-based companies who grow internationally and some of that revenue is starting to get recorded in Europe and in Asia today. So it is not like a clean cut on exactly what was organic revenue from the acquired revenue, as a lot of our sales now are cross-border and various things like that.

But in the March quarter the acquisition we fully annualized and you will be able to clearly see it. And as we've stated, and you can figure it out in our guidance that the acceleration in revenue should appear very loud and clear at that point in time.

DMITRY NETIS: Is it fair to say your international revenue is accelerating, or the growth of that revenue is accelerating?

DAN WEIRICH: Yes. We are seeing increases across all elements of the business. Whether it's our SMB, our mid-market, our international, or domestic, anywhere you look we're seeing good growth across the business.

VIK VERMA: I'll add a little more color, Dmitry. I was just at if I just in the UK on our QBR. I think I talked to you about this very large deal, this is another signature deal that they won which is a very large public university that you have heard about. The UK market is actually a very interesting market and we're starting to see good growth there, and as Dan pointed out, all our channels are seeing good growth.

DMITRY NETIS: Okay, very good. And last, if I may, squeeze that in, on the ARPU side you have had very nice sustainable at quarter-over-quarter of about $6. How should we think about that going forward? Are you comfortable with that $6 number going forward? Or is it going to fluctuate? Give us a sense on that.

DAN WEIRICH: So we were in the $5 range for a while and we've moved it up to roughly $6 or so. Yes, I think pretty much, if you look at it from a net add standpoint and ARPU standpoint, it's got to be at like $6-plus to maintain the growth figures that we're talking about.

It's not something that we like monitor and manage or quota on or commission on, it's how many new logos are coming in the door, but our overall emphasis is just moving the average size of the customer up, so ARPU is a derivative of that, and it is where the rubber really meets the road in a business like this. That's why we provide the metrics that we do provide and this is one of the handful or so that is extremely important to the business.

DMITRY NETIS: Great, thank you very much. Excellent quarter.

DAN WEIRICH: Thank you, Dmitry.

MARY ELLEN GENOVESE: Thank you.

OPERATOR: George Sutton from Craig-Hallum.

GEORGE SUTTON, ANALYST, CRAIG-HALLUM CAPITAL GROUP: Thank you. Vik, when you were discussing the focus on the mid-market and the strength you're seeing there, I wonder if you could specifically talk about the channel partner contribution to that, and your happiness or lack of happiness with respect to how the channel partner program is going?

VIK VERMA: That's a great question. One, we are seeing huge pent-up demand in the channel partner program. I think we'll see a non-trivial contribution. It is still relatively small and early stages for us on the channel.

But we're starting to see several big deals come through our channel, and I think increasingly that will be a bigger contribution to our revenue. I actually -- it is early days yet in the sense that I think what I've been doing is decreasing the number of channel partners that we have. We had a lot of channel partners. I would rather have much more productive and much more engaged channel partners and we're starting to see that, and we're starting to see channel partners spend a non-trivial amount of time really learning our product, us training the sales force, joint marketing, all of those kinds of things. But we want to do it with less channel partners than more, and I think it seems solid growth; I think it can grow much faster.

GEORGE SUTTON: As my follow-up, you mentioned Sydney for the first time that I've heard Sydney mentioned. What specifically happened there that encouraged you to move into that market, as well?

DAN WEIRICH: Hey, George, it's Dan. On Australia, it's what happened, a couple of things. One is we have a partner that we picked up in the Contactual acquisition three years ago who had been distributing the product in -- the contact center product in Australia.

They wanted to get a lot bigger, and so that was something that was pulling, and then we had one very large Fortune 500 customer of ours who was using this globally in a very big way. Kind of gave us the ultimatum like, get a presence in Australia or we've got to go **buy** from somebody else and we don't want to **buy** from someone else. Those were the two main ones, and then we do have a number of other customers who have a lot of call flow that occurs in Australia.

And is a little bit away from **Hong Kong** where we have our Asia-Pacific data center. And so just a combination of those factors as to where we put our next deployment. It is going to be live imminently.

GEORGE SUTTON: Perfect. Thank you.

VIK VERMA: By the way, one of the things -- that is starting to be a huge competitive differentiator. We're seeing this more and more where one of the interesting things is a lot of companies that are approaching our UK office are actually US companies that have UK presence or UK subsidiaries. And then there are others that have, for example, Australian subsidiaries or **Hong Kong** subsidiaries, and they will basically approach us and say can you put this particular office and/or they will dictate to that office, and that gives us that much more tentacles into that particular customer.

OPERATOR: Mike Latimore with Northland Capital.

JIM FITZGERALD, ANALYST, NORTHLAND CAPITAL: Thank you. This is Jim Fitzgerald standing in for Mike Latimore. My question is regarding organic growth. The March quarter is going to be all organic growth, not including that acquisition revenue. Would you expect somewhat slower growth in that quarter, the March quarter, regarding total revenue as compared to earlier in the year?

DAN WEIRICH: Yes. Definitely if you're comparing it to the quarter we just reported there is not an apple and orange comparison of acquired revenue to organic revenue. But as what we're saying is that the last time we provided organic revenue growth rate was in the December 2013 quarter. We gave the specific revenue for the UK business in the month of December that we acquired it. We closed the acquisition November 29, 2013. And so you've got the organic figure there, and is what we're saying is that the growth rate in the quarter ending March 31, 2015 will be higher than that.

JIM FITZGERALD: Okay, great. And then one other quick question. I might have missed this. Are nine out of 10 mid-market deals still against the on-premise system vendors?

VIK VERMA: Yes, actually more often than not we see on-premise as the primary competitors.

JIM FITZGERALD: Okay, great. Thank you.

OPERATOR: I am showing no further questions at this time. I would now like to turn the conference back to Mr. Vik Verma.

VIK VERMA: Thank you, everybody, for listening to our presentation today. I look forward to seeing you all in the coming months at upcoming financial conferences and other industry events. Again, thank you very much.

OPERATOR: Ladies and gentlemen, this concludes today's conference. Thank you for your participation and have a wonderful day. You may all disconnect.

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