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## Microsoft Cloud Revenues Powered by Office 365

Posted on January 31, 2024 by Tony Redmond

Reading Time 4 mins

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### Office 365 Reaches 400 Million Paid Seats

**Microsoft reported** revenue of \$62 billion and operating income of \$27 billion for the second quarter of their FY24 fiscal year. Emphasizing the importance of cloud computing to Microsoft, almost 55% of their revenue (\$33.7 billion) came from the “Microsoft Cloud,” an amorphous term for a collection of cloud products including Office 365, Azure, LinkedIn, and Dynamics 365.

## Quarterly Commercial Highlights

Investor Metrics	FY23 Q2	FY23 Q3	FY23 Q4	FY24 Q1	FY24 Q2
Commercial bookings growth (y/y)	7% / 4%	11% / 12%	(2)% / (1)%	14% / 17%	17% / 9%
Commercial remaining performance obligation (in billions)	\$189	\$196	\$224	\$212	\$222
Commercial revenue annuity mix	96%	96%	97%	96%	96%
Microsoft Cloud revenue (in billions)	\$27.1	\$28.5	\$30.3	\$31.8	\$33.7
Microsoft Cloud revenue growth (y/y)	22% / 29%	22% / 25%	21% / 23%	24% / 23%	24% / 22%
Microsoft Cloud gross margin percentage	72%	72%	72%	73%	72%

Growth rates include non-GAAP CC growth (GAAP % / CC %).

#### Commercial business

- Commercial bookings increased 17% (up 9% CC) year-over-year driven by strong execution across our core annuity sales motions and growth from large, long-term Azure contracts
- Commercial remaining performance obligation of \$222 billion, up 17% (up 16% CC) year-over-year
- Commercial revenue annuity mix of 96% was relatively unchanged year-over-year

#### Microsoft Cloud

- Microsoft Cloud revenue of \$33.7 billion, up 24% (up 22% CC) year-over-year
- Microsoft Cloud gross margin percentage of 72% was relatively unchanged year-over-year. Excluding the impact of the latest change in accounting estimate for useful lives, gross margin percentage increased roughly 1 point driven by improvement in Azure and Office 365, partially offset by scaling our AI infrastructure.

Microsoft Cloud includes Azure and other cloud services, Office 365 Commercial, the commercial portion of LinkedIn, Dynamics 365, and other cloud properties. Includes non-GAAP constant currency (“CC”) growth. See Appendix for reconciliation of GAAP and non-GAAP measures. Growth rates in GAAP and CC are equivalent unless otherwise noted.

Figure 1: Microsoft FY24 Q2 Results

A year ago, the number was \$25.7 billion. Growing quarterly revenue by \$8 billion in a year is pretty special. The annualized run rate for the Microsoft Cloud is now \$134.8 billion.

### Copilot Optimism

Microsoft didn’t comment about any impact on Microsoft Cloud revenues generated by the Copilot products they have released to date. They said that 10,000 organizations use Copilot Studio to create add-ons for Copilot for Microsoft 365 and that Copilot for Microsoft 365 had “*faster adoption than either our E3 or E5 suites.*” However, they didn’t give any comparative data to prove the point. Anyway, it’s impossible to compare the adoption rate for a product introduced to an installed base of 400 million users against a new product like Office 365 E3 that had to cope with the initial inertia of moving from on-premises systems to the cloud.

We heard once again that “*Copilot for Microsoft 365 users were 29% faster in a series of tasks like searching, writing, and summarizing.*” What Microsoft didn’t say is that your mileage will vary depending on the quality of the user interaction and the data available in your tenant. Interestingly, Satya Nadella spoke about his own experience of Copilot and the value he gains from **summarization of Teams meetings** email, and documents. He said that summarization “*has become a big deal.*” I agree. I think summarization is a way people can get immediate value from AI that’s just harder to achieve with generated text.

My recommendation is to ignore the **ongoing hype around Copilot for Microsoft 365** and focus on a hard-nosed assessment of what the technology can and cannot do in your environment.

### Office 365 News

Microsoft said that Office 365 commercial seats grew 9% year over year, “*driven by small and medium business and frontline worker offerings.*” Satya Nadella said that the growth put the number of paid Office 365 seats at “*over 400 million*”. It seems like they have been at or around this number for the last few quarters. **In April 2023**, Microsoft reported 382 million Office 365 paid seats. For years, Office 365 has grown at around 2.5 million seats per month. Adding 22.5 million to the 382 gives 404.5 million. Microsoft didn’t give a figure for the number of active Office 365 users, so it’s hard to do an apples-to-apples comparison against the data available for years before FY22. Even so, the interesting thing is that Office 365 active users continue to grow at a reasonable rate.

- April 2017: 100 million.
- October 2019: 200 million.
- December 2021: 300 million.
- January 2024: 400 million.

CFO Amy Hood continued to emphasize the increased expansion of average revenue per user (ARPU), meaning that Microsoft extracts more money per user. They do this by selling add-ons like Teams Premium and convincing customers to upgrade licenses to more expensive packages such as Microsoft 365 E5. In an answer to an analyst question, she also said that the new seats being added come from small to medium organizations and so are “*lower RPU seats.*” However, they are new seats, and the opportunity exists to sell upgrades to those seats, including Copilot (either the new Copilot Pro for individual users or Copilot for Microsoft 365).

### EMS Reaches 268 Million

Microsoft has reported a number for active Enterprise Mobility and Security (EMS) users over the last few quarters. In **FY24 Q1**, the number was 259 million. Now it’s 268 million. Growing by nine million in a quarter is better than the three million achieved between FY23 Q4 and FY24 Q1, but as I noted last time round, I suspect that the **FY23 Q4** number was a glitch.

### The Remarkable SLA Performance of Office 365

Another recent statistic is the **99.996% performance against the Office 365 SLA** during the last quarter of 2023. The last time Microsoft had any kind of dip in performance against the Office 365 SLA was the first quarter of 2013, when they achieved 99.94%. So much for all the fears about the reliability of cloud services.

This doesn’t mean that Microsoft’s cloud services are perfect because they are not. Outages happen all the time and some outages affect hundreds of thousands of users. However, the distribution of tenants across multiple datacenter regions and the availability features incorporated into services like Exchange Online, SharePoint Online, and Teams means that an individual problem seldom has any impact on the SLA.

On to the next quarter – and the next hundred Office 365 seats.

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