

BASE Earnings Call Transcript

Date: 2024-09-04

Quarter: 2

Operator: Greetings, and welcome to the Couchbase Second Quarter 2025 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Edward Parker at ICR. Thank you. You may begin.

Edward Parker: Good afternoon, and welcome to Couchbase's second quarter 2025 earnings call. We will be discussing the results announced in our press release issued after the market closed today. With me are Couchbase's Chair, President and CEO, Matt Cain; and CFO, Greg Henry. Today's call will contain forward-looking statements, which include statements concerning financial and business trends and strategies, market size, product capabilities, our expected future business and financial performance and financial condition and our guidance for future periods. These statements reflect our views as of today only and should not be relied upon as representing our views at any subsequent date, and we do not undertake any duty to update these statements. Forward-looking statements by their nature address matters that are subject to risks and uncertainties that could cause actual results to differ materially from expectations. For a discussion of the material risks and other important factors that could affect our actual results, please refer to the risks discussed in today's press release and our most recent annual report on Form 10-K or quarterly report on Form 10-Q filed with the SEC. During the call, we will also discuss certain non-GAAP financial measures, which are not prepared in accordance with generally accepted accounting principles. A reconciliation of these non-GAAP financial measures to the most directly comparable GAAP financial measures as well as how we define these metrics and other metrics is included in our earnings press releases, which are available on our Investor Relations website. With that, let me turn the call over to Matt.

Matt Cain: Thank you, Edward, and good afternoon, everyone. I'm pleased to report that in Q2 we made strong progress in our full-year objectives, delivering excellent new customer logo growth, strong new business, meaningful growth in Capella consumption and ARR mix, and continued progress on the growth, efficiency and leverage across our organization. Annual recurring revenue or ARR was \$214 million, up 18% year-over-year and 19% in constant currency. Revenue in the second quarter was \$51.6 million, up 20% year-over-year and above the high end of our guidance range. Non-GAAP operating loss in Q2 was also above the high end of guidance at \$4.1 million, representing a negative operating margin of 8%, 2.2 percentage points above the midpoint of our implied operating margin guidance range. We added 62 net new logos up from 12 in the second quarter of fiscal 2024 and 19 from last quarter, not including the additional 39 customers added due to our change in methodology made in Q1 to include on-demand customers. Capella now represents 31% of our customer base and 13.5% of our total ARR, both up 2 points sequentially. Over the past several quarters, I've discussed the leverage that we've seen building across our business as a result of our efforts to improve operational rigor and efficiency. We made further progress on this front in Q2 with our second quarter Rule of 40 score improving 14 points year-over-year. Driving efficiency across go-to-market, R&D; and all aspects of our operations will continue to be one of our highest priorities for the balance of fiscal 2025. I'm proud of the strong execution of the entire Couchbase team and what continues to be a challenging macroeconomic environment. In Q2, we saw new customer wins across a variety of industries, including healthcare, financial services, manufacturing, retail, technology and

communications, and travel and hospitality. We saw strong gross new ARR growth across new and existing customers and strong Capella migrations and new logo additions, including a mid six-figure Capella [land], the largest in our history. Customer uptake in consumption of Capella continues to grow nicely. Our pipeline of large strategic opportunities continues to expand and we are well positioned to have a very strong second half of the year. And thanks to the hard work of our go-to-market teams, we successfully closed all of the significant deals that slipped from Q1. We delivered one of the best gross new ARR quarters in company history and we were able to do so despite a renewal pool, which as I discussed last quarter is disproportionately weighted toward the back half of the year. Offsetting the strong execution was a higher level of customer loss and downsell, which resulted in an unanticipated headwind to our ARR performance in Q2. While we experienced some churn and downsell in any given quarter, the impact to Q2 was higher and more concentrated than what we normally experience. Not reflected in this quarter's results, however, was the significant progress we are making with a large number of strategic accounts where we are participating in multi-year initiatives to support the next-generation of enterprise applications. Greg will discuss our outlook in more detail in a few moments, but the strong visibility we have across the size, scale, and diversity of these opportunities gives us confidence in our ability to achieve our full-year objectives. Our customers continue to demonstrate a growing commitment to the Couchbase platform. As the demand for rich, hyper-personalized and real-time AI applications accelerates, we believe the core tenants of our value proposition are only becoming more relevant. In parallel, we are witnessing and participating in an increasing number of strategic projects across our customer base, focused on evaluating, architecting, and building the next phase of data infrastructure to support our customers AI and application requirements. And it's becoming clear that many alternative approaches and solutions are failing to meet the long-term demands of enterprises looking to scale their infrastructure to support their next-generation application roadmap. Couchbase was deliberately architected to be the foundation for mission-critical applications, delivering the world's most scalable, performant and flexible modern database. We've intentionally build our platform to combine uncompromising performance with the flexibility of deployment and usage models from cloud to on-premise and to the edge and everything in between. And with the introduction of Capella, we do so in an easy-to-use and familiar way, while at the same time rapidly enhancing our platform with new services. As enterprises endeavor to build the next-generation of adaptive applications, we are seeing the need to combine the ever increasing volumes of data from [disparate] and traditionally siloed sources, whether it's structured or unstructured data, broad-based internet data or proprietary enterprise data with extremely low latency and a highly connected and performant way. This need will only become more urgent. Our strategy continues to be focused on seizing this moment. It's driven by our architectural foundation that supports a broad range of use cases and workloads complimented by the low TCO of Capella, enabled by our go-to-market motion and focused on developers, system architects, and other key stakeholders across our large enterprise target market. Now turning to product specifics. We are continuously extending our platform with new features and services that are purposely designed to advance the capabilities of developers to build next-generation applications. This quarter, we announced the general availability of Couchbase Mobile with vector search, which makes it possible for businesses to offer similarity and hybrid search in their applications on mobile and at the edge. We also introduced Capella Free Tier, a perpetual free developer environment, which empowers developers to evaluate and explore products and test new features without time constraints as they develop next-generation production-ready applications on Couchbase. Developers now have the access, convenience, and simplicity to learn, develop and deploy applications on Capella into production. On top of all of this, we [GAID] Capella Columnar during the quarter. This powerful innovation empowers our customers to unify operational and analytical workloads on a single platform. Our approach reduces complexity, lowers TCO, and accelerates time to market positioning our customers with a strong foundation in their AI-driven transformation journeys. As modern applications are increasingly being built on higher performance semi-structured formats like JSON, application teams and IT organizations face growing challenges. The flow of real-time data at scale is severely constrained by the architectural limitations of relational systems. This introduces latency, impacts productivity and performance due to rigid and complicated ETL operations and impedes real-time operational write-backs, disrupting critical tasks in today's data-driven environments.

Overcoming these obstacles is crucial for organizations aiming to harness the full potential of their data in real-time. Couchbase has intentionally architected to solve these challenges through its innovative Columnar data format, which eliminates the inefficiencies of legacy, rigid and outdated systems. Our approach paves the way for AI-powered applications to seamlessly integrate operational data with real-time analytics, enabling our customers to deliver more agile, personalized and cost effective solutions. We believe the strategy aligns strongly with the application agendas of enterprises where the demand for real-time AI-driven insights is rapidly accelerating. Capella Columnar is a transformative achievement for us, and I am thrilled to share that Q2 saw fast adoption and positive feedback from early users across various industries. This strong market response underscores the significant value our customers see in integrating advanced analytics directly with their operational environments. And by combining Capella Columnar with advanced vector search capabilities with a unified cloud database platform, we enable enterprises to further reduce costs, simplify operations, and put both the operational and analytical power directly in the hands of developers to create reliable adaptive applications that scale effortlessly from cloud to edge. What gives us confidence in our strategy is that we continue to see it resonate with our growing customer base. A new Capella customer in Q2 is a financial service company that chose Capella to power their client reporting service in its data hub. We were selected because of our ability to enable greater transparency and reporting precision to its commercial clients, including providing intraday reporting and full transaction detail availability. Another new Capella logo this quarter was an aviation and aerospace component manufacturing company that provides in-flight entertainment and communication solutions to airlines. Requiring a database that would provide performance at scale with the flexibility to power content management of its business critical in-flight entertainment system, this customer selected Couchbase because of the compelling mobile offering and edge capabilities. Turning to expansion. This quarter, a global leader in unified retail commerce solutions, Aptos expanded its investment in Capella to continue supporting its cloud native point-of-sale system Aptos ONE. Aptos originally selected Couchbase for its mobile and offline first capabilities and was able to reduce infrastructure costs and improve operational efficiencies by migrating to Capella and has continued to invest in Capella for easier deployment of new products and features while reducing database administration. Another Capella expansion came from an automobile trading company, Toyota-Astra Motor. This customer is leveraging Capella to deliver an application to improve customer experience end-to-end and decided to expand its investment in Capella because of its performance advantage. This comprehensive mobile application will serve all of Toyota's clients' needs. A global leader in the convenience, foods and beverages space also expanded their Couchbase investment this quarter. Initially needing a database solution with offline available functionality for its sales application used by field representatives, this customer again expanded with Couchbase because of our databases superior offline first capabilities, flexibility and ability to process a high number of transactions. We also had an important new relationship with a large ISV, which contributed a significant number of new logos in the quarter. Partner-led sales continue to be a key component of our go-to-market strategy and ISVs can be a force multiplier to our existing motion and reinforces the value proposition that we bring to customers. Finally, I'm excited to welcome Josh Harbert as our new Chief Marketing Officer. Over his 20 years in marketing roles at both private and public software and technology companies, he has demonstrated a strong track record of accelerating growth and achieving strategic outcomes. Josh's experience will be instrumental in leading all aspects of our marketing strategy and execution. We are thrilled to have Josh as part of our world class team. In conclusion, I'm pleased with how our teams have responded and executed in the second quarter. We made progress across our strategic priorities, delivered strong new customer growth, meaningfully increased our Capella mix, successfully launched Capella Columnar and continue to drive efficiency across our model. Our customers and prospects are focused on building the next-generation of adaptive applications while addressing the growing data challenges of an increasingly AI powered world. Our foundation rests upon a carefully architected platform, purpose built to enable these mission-critical applications, and I'm honored that Couchbase is serving as a strategic partner helping customers navigate this journey. We are not fully satisfied with our net new ARR performance in the first half of the year. That said, we are making rapid operational progress across the business inclusive of several key strategic accounts where we are emerging as a strategic and long-term critical platform

provider. This robust pipeline of exciting opportunities gives us confidence in our ability to drive substantial wins and expansions going forward. This dynamic taken with other important levers in the business reinforce our confidence in delivering the year. We will work tirelessly to support our customers and acquire new ones, enhance and extend our technology leadership, deliver new capabilities and services, and drive increased Capella adoption and will do so in a more efficient manner and with a dedicated focus on a Rule of 40 trajectory. As I have said many times, at Couchbase, we attack hard problems driven by customer outcomes. With that, I'll now hand the call over to Greg to discuss our results in more detail. Greg?

Greg Henry: Thanks, Matt, and thanks, everyone for joining us. I'm pleased with the progress we've made in the quarter, including our top and bottom line performance, new business generation, logo ads, and strong execution across all aspects of our business. Despite ongoing macroeconomic headwinds, we continue to see strong demand for our platform and remain confident in our trajectory and ability to achieve our 2025 goals and the objectives we laid out at our Analyst Day. I'll now walk you through our second quarter financial results in more detail before providing our guidance for the third quarter and fiscal year. Total ARR was \$214 million, representing growth of 18% year-over-year and 3% sequentially at the midpoint of our guidance range. Foreign currency fluctuations added approximately a 1 point headwind to our ARR growth rate. We entered the second quarter with \$28.9 million of Capella ARR, up 20% sequentially and representing 13.5% of our total ARR, up 2 points from 11.5% last quarter. As Matt mentioned, while Q2 was among our strongest quarters from a new business perspective, we experienced unexpected loss and downsell from a few large customers, which impacted our ending ARR balance. While there is no commonality to any of these, we note that one of the losses was due to ceasing of operations following its acquisition by a larger entity. I'll discuss our outlook in more detail in a moment, but we remain confident in our ability to retain and expand our customer base and more specifically, our largest customers. Turning to revenue. Second quarter total revenue was \$51.6 million, up 20% year-over-year and 1% from last quarter. Second quarter software revenue was \$49.3 million, also up 20% year-over-year and 1% sequentially. The remaining \$2.3 million came from professional services revenue up 5% year-over-year and flat sequentially. Our second quarter ARR per customer was \$246,000 down from Q2 2024 and down from \$257,000 in the first quarter, largely driven by our strong new logo additions in the quarter. As a reminder, ARR per customer growth could moderate or decline as our Capella mix continues to grow in contribution. Our dollar-based net retention rate, or NRR, continues to exceed 115%. We exited the quarter with 869 customers, an increase of 62 net new customers from last quarter. Our Capella customer logo count grew by 37 in the quarter and continue to be encouraged by our solid retention metrics, strong Capella ARR growth and ability to consistently expand new logos. In discussing the remainder of the income statement, please note that unless otherwise stated, all references to expenses, results of operations and share count are on a non-GAAP basis. We remain focused on efficiently growing our business. I'm pleased with our efforts on this front once again resulting in outperformance against our operating loss outlook. Our second quarter gross margin was 88.3%. This compares to 87.2% from Q2 of last year and 89.9% last quarter benefiting from sustained enterprise gross profit margin strength and lower services revenue mix offset by growing Capella mix, which inherently carries a lower gross margin. Exercising expense discipline and finding opportunities for cost efficiencies continues to be a priority. Second quarter sales and marketing expenses were \$29.6 million or 57% of revenue. This is down from 65% of revenue in Q2 of fiscal 2024. Like last quarter, increasing sales and marketing efficiency was a priority of ours in Q2. Research and development expenses were \$13 million or 25% of revenue down from 29% from Q2 of last year. General and administrative expenses were \$7.1 million or 14% of revenue compared to 15% of revenue a year-ago. Operating loss for the second quarter was \$4.1 million or a negative 8% operating margin. This compares to a loss of \$9.2 million or a negative 21% operating margin in Q2 of last year. Net loss attributable to common stockholders was \$2.9 million or negative \$0.06 per share. Turning to the balance sheet. We entered the second quarter with \$156.1 million in cash, cash equivalents and short-term investments. We continue to remain well capitalized for executing against our long-term strategy. Our remaining performance obligations or RPO was \$215.8 million at the end of Q2, up 27% year-over-year. We expect to recognize approximately 63% or \$136.2 million of total RPO as revenue over the next 12 months, representing growth of 19% year-over-year.

As a reminder, we experienced fluctuations in our RPO balances due to a host of factors, including renewal timing as well as changes in average contract duration. Operating cash flow for the second quarter was negative \$4.9 million. Free cash flow was negative \$5.9 million or a negative 11.5% free cash flow margin. We remain committed to being free cash flow positive for fiscal 2026. Now, I will provide our guidance for Q3 and the full-year fiscal 2025. As Matt discussed, we saw strong momentum across our business in Q2 and are pleased with the execution of our teams. We continue to expect Capella to be an important growth driver for our business, complimented by investments, enhancing our product capabilities, partner ecosystem, and go-to-market motion. As we have previously discussed due to our customer base of large enterprises, the mission-critical nature of many of the applications we support and the sensitivities that our renewals upsells and Capella migrations have on our reporting metrics, including ARR, quarterly timing is always an important element of our business and sometimes difficult to predict. As such, given the composition of our renewal pool and pipeline of large opportunities, we continue to expect our net new ARR growth to be disproportionately weighted towards the back half of the year and in particular Q4. In addition, I'd like to mention a specific ARR dynamic that is having a more pronounced impact on our outlook relative to prior years. On occasion, given strategic nature of our customer engagements, our contracted deals can include future increasing ARR, which can contribute to our ARR visibility typically in a quarter where we have any pre-contracted ARR is relatively modest. However, we currently have a substantially larger than normal amount of contracted ARR with start dates in Q4, which is contributing both to our strong second half visibility and greater than normal weighting of net new ARR discussed above. Finally, we remain mindful of the macroeconomic headwinds and continue to carefully monitor their outlook on our business. As such, our outlook assumes a consistent degree of conservatism to account for these variables, as well as lack of visibility into how the macroeconomic environment may impact upsell and migration timing, as well as consumption trends for our emerging as a service offering. With these factors in mind, for the third quarter of fiscal 2025, we expect total revenue in the range of \$50.3 million to \$51.1 million or year-over-year growth of 11% at the midpoint. We anticipate ARR in the range of \$218.5 million to \$221.5 million, representing 17% growth year-over-year at the midpoint. We expect non-GAAP operating loss in the range of negative \$5.5 million to negative \$4.5 million. For the full-year of fiscal 2025, we are raising our revenue outlook while maintaining our ARR guidance and decreasing our operating loss guidance. We are encouraged by the pipeline, opportunities and overall business momentum heading into the second half of the year. As such, we remain confident in our ability to achieve our full-year ARR guidance. We now expect total revenue in the range of \$205.1 million to \$209.1 million or year-over-year growth of 15% at the midpoint. We continue to expect ARR in the range of \$235.5 million to \$240.5 million, representing 17% growth at the midpoint. And finally, we expect a non-GAAP operating loss in the range of negative \$24.5 million to negative \$19.5 million. With that, Matt and I are happy to take your questions. Operator?

Operator: Thank you. And ladies and gentlemen, at this time, we'll conduct our question-and-answer session. [Operator Instructions] Our first question comes from Matthew Hedberg with RBC. Please state your question.

Matthew Hedberg: Hey guys. Thanks for taking my questions. Maybe I wanted to start with the kind of the unexpected churn and downsell that you talked about. It sounded like – Greg, you said there wasn't really a commonality to those. I guess, I wanted to double click on that. And is there a way to think about the magnitude of that on your Q2 net new ARR?

Greg Henry: Yes. Hey, Matt, it's Greg. Yes. Look, again, like we said, there was just a few of them. One, we knew about – one in particular, we got, I would call a little surprise at the end where we're in negotiations and they went a different direction. But there is no commonality and we called it out because it's a little bit more pronounced and we see – we're very sort of within a pretty tight range on loss and downsell. If I go back the last three years of being public, this one was a little bit outsized and we wanted to add a little bit of color, which is why we noted that the gross ARR add was one of our best in company history. It just was offset by slightly higher loss and downsell than we had expected, which is what sort of impacted the net ARR for the quarter. Otherwise, we felt pretty good about how the quarter ran.

Matthew Hedberg: That's helpful. Thank you. And then Matt, I mean, the new customer adds was a real

highlight. And it sounded like you had quite a bit of success from the partner add perspective, some of the partners that you called out. I guess, I'm wondering, you guys have had a lot of focus on increasing sales and marketing focus on partners. Could you maybe talk a little about why you're seeing some success there and how repeatable is that, especially as we look towards what seemingly sounds like a strong second half pipeline for you guys?

Matt Cain: Yes. Matt, certainly 62 net logo adds is a highlight of the quarter. And I'd say it's aligned with several of our strategic initiatives on the go-to-market side paying dividends. As we've talked about, we made particular investments to cover strategic accounts, ensure that we're increasing Capella momentum and of course, increasing the pace of new logo adoption. I'd say the partner motion is pervasive across the entirety of our business and extends our reach and relevance with strategic customers. I think partners realize the unique role that we play with our differentiated platform and our partner types range from the hyperscalers to different types of service providers and ISVs has and continues to be a really important channel for us. We're excited about this and think it speaks to the strategic nature of our platform, aligning with strategic partners unlocking new opportunity with really exciting next generation applications. So we fully expect to continue to derive benefits from that and quite frankly, with the platform that we have and the momentum of the business, I think it's going to only increase over time.

Matthew Hedberg: Thanks a lot guys.

Matt Cain: Thanks, Matt.

Operator: Our next question comes from Kash Rangan with Goldman Sachs. Please state your question.

Kasthuri Rangan: Hi. Thank you very much. Matt, you talked about the Columnar database. I'm curious to get your expanded thoughts on it. I always thought GenAI was more on the unstructured side of things. Obviously, databases have a huge role to play with the structured data. But can you expand – is this something that you're hearing from your customers? Are you proactively doing this [Columnar] database? Because I still want to understand how the Columnar database fits with the broader GenAI enablement of your customers. And then one for you, Greg, can you talk a little bit about the Q4 upcoming net new ARR growth that you expect within the customer base? What exactly is driving that? Is that from Capella or from the core platform? Thank you so much.

Matt Cain: Kash, let me talk about the Columnar database. Let me start first with kind of our very high level view on our role to play in AI. We have an opportunity to be the single source of truth to store index and search, structured, semi-structured and unstructured data. The highlights that we talked about in the quarter are advancing the platform for developer reach, developer productivity, and the Columnar announcement is a big part of enabling that AI strategy. If you think about a JSON application, the capability surrounding that JSON application from an ETL and analytics perspective are relational by definition. We have essentially shattered that barrier and built a native JSON analytics set to complement what we do on the operational side. This allows us to have zero ETL for JSON, ingest multiple data sources, open up conversational analytics for developers, and critically important – importantly, provide operational write-back for the application set. And so Columnar is the advancement that opens up these capabilities and data ingest. But it's really an extension of the platform that is very much in service of our AI strategy to be that single source of truth and bring AI technology into applications and really embed those capabilities to take application attributes to the next level. So exceedingly strategic for the pursuit of us as a data platform and in the AI world that we're living in. And for those reasons, we're getting tremendous customer feedback and already uptake since GA with the feature alongside the rest of the platform.

Kasthuri Rangan: Awesome. Thank you.

Greg Henry: Kash on your Q4 ARR question. So obviously this is the first time we've guided to Q3 and based on giving the full-year guidance, you have an implied Q4 guide, if you will. And what we want to call out is we do these large strategic deals, and we've been doing these for years now, where we build in growth over time within a contract. So for example, if you recall like last Q4, we had a big nice RPO jump because we did a couple of very large deals. Those were multi-year deals. So this is in some cases the second or third year kicking in and based on our definition of ARR where we look at what's at the end of the quarter plus 12 months forward, some of that will now get – it will – is getting pulled into

Q4 and resides there. We wanted to give some context that we have this from time to time. Some quarters it's zero, some quarters it's a modest amount. Q4 in this particular case is a bit outsized. We want to call that out. Given that now that you see the implied guidance of Q4 to give some confidence that – the confidence that we have that we can deliver the second half and particularly Q4 because there is a healthy amount of ARR that's already contracted in Q4 specifically.

Operator: Thank you. Our next question comes from Brent Bracelin with Piper Sandler. Please state your question.

Brent Bracelin: Thank you. Good afternoon. Matt, I wanted to double click into Capella net new ARR. They're more than doubled sequentially, highest you've ever seen. Could you just walk through what drove that? Obviously it sounds like there were a lot of new customers. Was there also a contribution from some migrations of existing customers? Just walk us through what drove the outside momentum just given it was so strong this quarter? And I have a quick follow-up.

Matt Cain: Yes. Look, we have high expectations for Capella and I think we've had a quarter where those are proving out. And I'd say it's balanced across all aspects that you talked about. We increased customer count, which is now up to 31%. We increased the ARR mix, which is now 13.5%. That's a combination of net new applications as well as migrations. We also talked about the single largest Capella lan that we've ever had. And so Capella continues to be a significant growth vector for us. Customers value the service. Developers want to focus on building great applications and offloading a lot of data management to Couchbase, and we're seeing that play out across accounts of all sizes, quite frankly and all geographies across the world. So we anticipate that this is going to continue. Some of those levers are going to be dependent on pace of migrations. But over the kind of normalizing for time, we expect this to be a significant lever of growth for us on a go-forward basis and are seeing nothing, but positive leading indicators across all aspects of how we track Capella.

Brent Bracelin: Helpful color there. And then Greg, as you just think about churn and downsell. Can you just remind us what the gross retention of the business has been over the last, let's say, two, three years. And then maybe walk through the logic of what you're baking in on a go-forward basis? Do you think there might be a slightly more elevated churn assumption you're baking into the back half of the year? Any additional color there would be helpful. Thanks.

Greg Henry: Yes. Hey, Brent. So yes, we don't really disclose growth retention. I can tell you it's a healthy enterprise level growth retention that we've experienced ever since we've been a public company. And we are not anticipating the additional elevated levels of loss and downsell in the second half. We think it normalizes. We think Q2 is anomalous, obviously with what's going on at the macro we're watching closely. But we've gone through and looked very closely at what's up for renewal in the second half and evaluated that and we do not see where there's going to be again anomalous loss and downsell and should have get back to the healthy growth retention renewal rates that we've been seeing historically.

Brent Bracelin: Got it. Helpful color. Thank you.

Greg Henry: Thanks, Brent.

Operator: Your next question comes from Mike Cikos with Needham & Company. Please state your question.

Mike Cikos: Hey guys. Thanks for taking the questions here. I was just hoping to see if we could get a little bit more color. I know we're all circling around the churn and downsell. But is there any way you can kind of discuss – were these customers potentially [newer] cohorts into the Couchbase customer base, or have they been around for a while? And really the reason for the question is, if I just look at the momentum that you guys have from a product velocity and innovation standpoint, whether it's the GA, Mobile with vector search where you guys just recently announced Columnar now. It's just a bit striking or counterintuitive to hear about this churn and downsell and just want to make sure that we're thinking about this appropriate as far as this is an anomaly here in Q2?

Matt Cain: Hey, Mike. This is Matt. I appreciate you calling this out. Let take our time with this. Anytime we enter a fiscal period, a significant driver for the financial year is our renewal base. And we study the shape of the renewal base and the health of the renewal base. Shape obviously being winter accounts up for renewal and the health renewal base, really looking at a specific account, how strategic are we with our deployment, with that customer? How many services are they leveraging with respect to the

database? How many applications do we have deployed? And as we've talked about coming into the year, this year's renewal base is disproportionately allocated to the second half. What is proving also to be true is that the relative healthy upside is also seemingly sitting in the back half with what we were talking about these large strategic accounts. And just to give some perspective on large strategic accounts. We've often referred to our business as a land and explode model. These are multi-year, very strategic accounts that have the potential to be up to eight-figure ARR that at the point of transaction deliver disproportionate ARR growth. Offsetting that is kind of the natural part of our business, which is loss and downsell. What we called out in the second quarter is as normal kind of course of business. We can predict a certain amount of loss and downsell. But there were really a couple accounts that delivered more meaningful as in outside the norm downsell. One of them that was an acquisition where they shutdown the business into the seven-figures that we were prepared for and the one that came a little late. What we didn't have in the quarter is one of those strategic accounts transact that would've completely offset that. Now as we look at the kind of makeup of the year, we can't lose sight of the strategic accounts that we're highlighting. And the opportunity that has, which reinforces our confidence for the year. And as I look at kind of the fiscal year in the entirety, we look at the predictability of our enterprise business renewal rates, expansion rates. And we fully expect that to continue. The upside is often derived with how we execute on big accounts. And the health of the pipeline in the back half is quite frankly one of the best we've ever seen in terms of the number of accounts, the size of expansion that can come and the geographic distribution. Again, all part of our strategic investments. What isn't reflected in the quarter is the progression that we've made with those strategic accounts that again, further underpins our confidence for the year. So loss and downsell, we believe isolated more one-offs. The map converges over time offset by those strategic opportunities. And we have very good visibility in the second half, which kind of completes the full picture.

Mike Cikos: Great. Thank you very much for the thorough answer there, Matt. Definitely appreciate it. And I guess for the follow-up, if I could just tack on. First, great to hear the reiteration on the view that next year will be free cash flow positive. Just wanted to double check on the OpEx. The expense discipline shown in Q2, really was across the board. It hit every line item there. And I'm trying to think, you guys obviously have these go-to-market initiatives, whether it's tapping more heavily into partners, engaging with them, offering incentives. So over the remainder of the year, I guess, can you just give us a reminder, how should we think about the partners continuing to beat the drum on behalf of Couchbase? Where does the – I guess, what is the partner contribution to deals today versus where we expect this to scale to?

Matt Cain: Look, Mike, I think we called out the partner activity on the ISV because of the outsized new logo edition. But I'd say partners has been a persistent part of our business and we've scaled investments there to align with other investments as we've grown the company. It has been and continues to be an important lever for us. But it's not as if we haven't already invested in an adequate level or on an appropriate slope to drive the growth that we're committed to. Look, I think, a lot of this is about getting more efficiency. We talked a lot about having built a great foundation and getting to the Capella inflection, which is going to lead the leverage. What I would point out is, our ability to get more out of our spend. Our innovation team is firing at a level that quite frankly they never have. With Capella as a platform, our ability to do that more efficiently and extract appropriate amount of value from the market with that offering is going up. Go-to-market teams increasing their sophistication on finding new customer prospects and efficiently getting them through the funnel. So we remain committed on kind of Rule of 40 and free cash flow progress. And we're able to do that it by investing in quite frankly, a more efficient way as our platform matures and market dynamics remain extremely attractive for us. So I'd say all of those things factor into the financial commitments and partners being one part of that.

Mike Cikos: Great. Thank you very much guys.

Operator: Our next question comes from Sanjit Singh with Morgan Stanley. Please state your question.

Theodor Thun: Great. Thank you. Theo Thun on for Sanjit. Maybe just start with one higher level question. I mean, you've obviously at least spoken to some of the downsell and churn dynamics within your base. You've also spoken about the opportunity of buying for that single source of truth in AI. You're obviously not the only company buying for that, and clearly the hyperscalers are playing a big role in this new wave of AI applications. So could you just sort of contextualize what you are seeing in

your partnership, but also in your competition with the hyperscalers? Are there any meaningful shifts in terms of your competitive intensity or win rates that you would call out? And then the second question sort of on your billings and free cash flow. You spoke to the slipped deals from Q1 closing, yet it seems like your billings and your free cash flow was slightly below where the Street expected to be. Anything that you can kind of highlight on what drove that as well?

Matt Cain: I'll start and then I'll turn it over to Greg. Look, at a very high level, we are here to build a database for enterprise applications, which increasingly are going to be driven and enhanced with AI. And if we look at our core architecture and what we've been building for the future for this moment and the one that we are going to experience. The core attributes that make us great, scale, performance, flexibility, cloud to edge architecture, native JSON, SQL compatibility, have never been more relevant. And if I step back and put myself in the shoes of our enterprise customers and think about what they're going to need from a data platform and define the attributes, you'd be hard pressed in my opinion to find a better starting point than Couchbase. And our teams wake up and ensure that we're building the next-generation of capabilities and services to enable our enterprise customers to be successful with these enterprise applications. If we're doing that, we're going to have to solve problems in a unique and differentiated way relative to other solutions that are out there, which include native services from the cloud providers. And I'd say that's a dynamic that we've been dealing with and will deal with for some time. But we pride ourselves at solving customer problems and doing it in a compelling and differentiated way that includes hybrid-cloud, edge deployments, some core capabilities that the hyperscalers don't have in their offering. At the same time, we really value those relationships as we go-to-market and we deploy Capella and their cloud, and we partner with other services within their spec. And so I'd say this is an ongoing dynamic on the margin. If I were to comment on kind of the co-opetition dynamic, I would say partnership momentum and development, particularly in emerging geographies is very positive. And I'd say the competitive dynamic on a platform level remains unchanged. And that's a competitive dynamic that we take on every day. So it's a complicated relationship as you can appreciate just based on their scale. But it's one that we lean into for the reasons that I mentioned.

Greg Henry: Yes. Just following up on the billings and free cash flow. While we recognize they're very important metrics, we have never guided to those. And we in particular would say billings is not the best measure of our business by any means. It can be very lumpy, and particularly with Capella, with the rebuy activity, it can be less, far less frequent than on the subscription side of the business. So that's why we've been really trying to have people focus on ARR as one of our key metrics. I'd say also RPO and revenue obviously are good ones to look at. But billings and free cash flow can be a little bit lumpy for us. Although I will say on the free cash flow side, a year ago at this point, we were minus \$10 million of free cash flow, and this year we're minus \$5 million. So I do feel good about the progress we're making there.

Theodor Thun: Got it. Very well articulated. Thank you so much.

Greg Henry: Thank you.

Operator: Your next question comes from Ittai Kidron with Oppenheimer & Co. Please state your question.

Ittai Kidron: Thanks. Not to beat a dead horse here on the churn. What gives you confidence – is there any way to associate this for sales execution? I mean, I understand the customer got acquired and the division shutdown, that's part of life that happens. But clearly, there were other cases of down sales. What is it that makes you comfortable that this is not a sales execution issue rather than just bad coincidence of a customer decision?

Matt Cain: Well, Ittai, you can appreciate, I would imagine that we study this pretty hard. We're talking about two big ones, one that we were prepared for, and one that came with a little bit of a surprise. Without getting into too much detail, the leading indicator on that account suggested that we were doing the right thing from a go-to-market perspective. We haven't yet talked about macro on the call. I think there were some cost pressures at play within the account, where quite frankly we're not as strategically deployed as we are in healthy accounts. Now we're aware of where we're vulnerable. And we study that pretty hard and it represents a very, very small minority of our ARR base. This happened to be one of them where we were thought – we thought we were beyond the vulnerability approved not

to be true. And so that's something that we're going to go look at and see if there's anything we need to tighten up. But I do not think it's indicative of the rest of the business by any stretch whatsoever. And we deal with this dynamic on a quarterly basis. These two just again, in the quarter without a strategic deal to offset them kind of played out, which is why we're spending the time on it. And so again, we don't think it changes anything for the year. I'm pleased with sales execution. We talked about that in Q1, we learned a lot from that. Some of the highlights from the quarter were really strong. And my confidence in the fiscal year remains intact. And quite frankly, with the progress we're making in strategic accounts sets us up really well for a strong fiscal year, all things taken into account.

Greg Henry: Yes. Ittai, if I could just add on to just one other thing that's why we call it out is. To Matt's point, we closed nearly all the deals from Q1 that slipped. That's a non-issue. And that also led to us delivering, what was the third highest gross ARR achievement in company history. So again, the demand and our ability to close deals were very strong. As Matt talked about, unfortunately, we were one deal or one signature away from the net number being closer to where we were expecting it versus what we delivered, which we still feel is good. It's right down the middle of the guidance range, but obviously we have higher expectations than that as we move through the quarter.

Ittai Kidron: Appreciate that. So I guess as we look into Q4, we're clearly, as you mentioned, have a large contracted business. But also you're clearly are chasing several strategic projects. Can you qualify to us what is the number of strategic projects you hope to close? And by the way, what is your definition of strategic project? Is that a 100k plus lan? Is this – help us understand the parameters around this. Why spending so much time on it? What is the near-term impact of such deals and the long-term potential of such deals?

Matt Cain: Ittai, I'd say there are many, many of these strategics. And for us to call it out at that level, I think seven-figure plus ARR increases. I've mentioned a few of these can be become eight-figure ARR customers for us over time. These are going to be felt across the financials. And quite frankly, really drive our business. We work so hard to build a strategic platform that is so well aligned to enterprise projects. These are multi-year transactions where some of the biggest companies in the world are making decisions to invest it in us as a true strategic partner. Figuring out the mix between license and Capella and exactly what structure is going to work for them. They can be complicated, but they're very worthwhile. And when we lan these, we talk about the – how exciting they are, like one that we had in Q4, which drives a lot of benefits for us for some time. So it is many of those accounts that kind of were set up where we're making great progress on customer negotiations and discussions and strategic planning and well beyond technical wins. And so we would be remiss if we didn't spend the time on them because of how critical they can be for us in the back half. But they are significant and we have a very robust pipeline of these strategic accounts, which I'll remind everyone was a point of emphasis for us coming into the year because we understand the potential they have and the value unlock that's in front of us.

Greg Henry: Yes. And Ittai, I'll just add one more thing is, the large majority of these strategic deals we're talking about either have a renewal point in the second half or another compelling event. There are a few that are even talking to us that are early fiscal 2026 renewals that are talking about potentially getting deals done. I wouldn't call those in the same category because they don't have the exact compelling event of a renewal right now. But again, large majority our renewals are compelling. Some fiscal 2026 deals are up. Customers are already starting to talk to us about potentially doing something in the second half of 2025.

Ittai Kidron: Appreciate it.

Operator: Our next question comes from Jason Ader with William Blair. Please state your question.

Jason Ader: Yes. Thank you. I guess, first question is, do you think it's possible that you could be operating breakeven by the end of next year? I know you've talked about free cash flow positive next year. But just on the operating line, non-GAAP operating income, do you think that could be – you think you could turn positive or breakeven at some point maybe late next year?

Greg Henry: Yes. Hey, Jason, it's Greg. I certainly know, I mean, our commitment that going back to the Investor Day was fiscal 2027 for the full-year. Could there – you see a quarter maybe, but again, we're not committing to that other than the free cash flow piece at this time. I'm glad you asked though. You can see we are driving hard towards that and really committed to doing that. But we do not expect

to be non-GAAP op income flat or positive in fiscal 2026 for the year.

Jason Ader: Okay. Good. All right. And then, I think what my observation from some of the other questions is just I think people are scratching their heads on the ARR guidance just because it doesn't feel like it's de-risked. You've had a challenging first half of the year on that new ARR and now you basically didn't change the ARR guidance for the year. And I think you explained why do you feel good about Q4. But it also doesn't feel like it's de-risked. So what was the debate internally on lowering ARR guidance versus keeping it where it is?

Matt Cain: Well, Jason, I'd say that we've approached this as we always do with the utmost amount of analysis and studying every leading indicator and trend and account information that we have. And I'll state that we feel very comfortable with the guidance that we've provided. When we look at the fundamentals of the business, we have a very predictable enterprise model that plays out over time. The discussion that we're having is around some of the lumpiness in big accounts on a quarterly boundary that have happened to play out in the quarter, which we fully expect to offset on a multi quarter basis. On top of that, we have the Capella business, which is driving financial benefits throughout the financials that we don't have in the rear view mirror. But we're talking about the highlights that layer on top of it. And so we understand where these levers sit and the contracted ARR, which Greg has articulated in Q4, which is material. So if we look at the balance of the back half, everything that we're calling is well within the normal ranges of quarterly seasonality, execution, pipeline conversion. And what give us gives us a confidence is the cover that this very unique and well-earned pipeline of strategic opportunities provides where we don't have to chop all that wood in the back half to have a great result. But we have a lot of wood to get after, which we feel great about. So when we build the business from enterprise renewal rates, expansion rates layer on Capella contracted ARR. Again, we have confidence in the back half number and set up with kind of the entirety of the fiscal year.

Greg Henry: Yes. And Jason, I just add too. Again, if we have the visibility, obviously what's in the renewal pool, and we've talked about, it's disproportionately weighted in the second half. If you take that, if you take the fact, like Matt was saying, you take the contracted ARR and sort of, again, we can see it and back it out. The math for us internally all holds together in terms of what we can do in terms of expanding the population of renewal base, generating ARR from that, as well as from the Capella momentum that you see as well. So for us that's what gives us the confidence that Matt put out. And that's why again, we wanted to call this contracted ARR amount out because without that, I could see how someone from the outside would think that it looks a little bit outsized. But it's very much within the norms of what we've delivered historically.

Jason Ader: Could you give us the magnitude of that ARR contract – the growth in that contract?

Greg Henry: Not specifically, but I'll say it's several million dollars. And again, much more significant than we would see in any historical quarter, which is again why we're calling it out.

Jason Ader: All right. Thank you, guys.

Operator: Your next question comes from Raimo Lenschow with Barclays. Please state your question.

Raimo Lenschow: Hey, perfect. Thank you. Two quick questions and thanks for squeezing me in. First one is staying on that subject. Is that like a – just the Q4 having these kind of future ARR commitments. Was that a function of you kind of changing how you kind of working with customers and deal structure? And then just it's something that just came together, but it seems odd that kind of it's coming together now. And then, can you also mention what's driving the downsell? So we all talked about the customer loss and I get it. Doesn't look under your control. But what's driving downsell? Is that like economic activity [at the] customer. Have they overcommitted and now kind of rightsizing? What's driving that? Thank you.

Greg Henry: Yes. Let me answer the first question. No, we haven't changed how we do and structure deals to generate this contracted ARR. This is always part of our business. And again, it ebbs and flows based on timing. Some quarters, like I said, it'll be zero. Others be a modest amount. I think what's driving this is last Q4 in particular, we renewed two of our largest customers into multi-year transactions with substantial amounts of growth that were just built in because of the growth that they are experiencing and the investment that they're willing to make with Couchbase. So that's really the only driver of the dynamic. Otherwise it's pretty much in line. But those were two extremely large accounts

we had last Q4.

Matt Cain: Yes. Raimo, with respect to the downsell, I'd say with the exception of two big accounts, one that was planned and the one that we've talked about, everything's within the norms of our predictable business. We need to call those out for the reasons that we've talked about. But I don't think there's much more to it than those being one-off situational things for all the reasons we've talked about. We feel very comfortable with our ARR base, the strategic nature of our platform, our ability to compete and grow. And so with respect to a multi period outlook, nothing has changed. And we feel confident in the year. I don't – there is no kind of broader pattern beyond those two big outliers.

Greg Henry: Yes. And I would just add that those two outliers were losses, which was really the driver. We we're calling it loss and downsell. But the loss – those two are the losses that are driving it. And Raimo to your question, the downsell, they just happen from time to time where customers will spin up an app or spin down an app or something changes with the environment or they're not typically, again, very large and significant. It's the losses that were the ones that – are the ones this quarter.

Raimo Lenschow: Okay. That's great to hear. Thank you.

Greg Henry: Thanks, Raimo.

Operator: Thank you. And we have time for one last question. Our next question comes from Howard Ma with Guggenheim Securities. Please state your question.

Howard Ma: Great. Thanks. Greg, I have a question for you. Just to drive the point home on back half ARR. I thought that your ARR definition is based on contracted ARR. So I mean, I could be mistaken, but when you talk about the higher than normal amount of ARR that's contracted to start in Q4, wouldn't that already be baked into your reported ARR today? And quickly just on a related note, when you talk about the back half expansions is that – or the net new ARR being back half weighted? Are you talking just expansions or are you baking at a good amount of net new right from new logos that's in there as well? Thanks.

Greg Henry: Yes. Howard, I'll start with your second question first. So what's weighted towards the back half is the renewals. We have significantly larger renewal pool in the second half than we did in the first half. We knew that coming into the year. We've talked about that previously. We tend to upsell at the time of renewal. It just gives us a better opportunity from an upsell perspective to drive new business. But we are not assuming higher upsell rates, higher – new logos that we've experienced. Everything is within the range. But again, that's why we're calling out this contracted ARR because that is material in this quarter. And yes, we take anything at the end of a period plus 12 months forward. So if you do a multi-year deal, a three-year deal, when you sign it the first-year, and you'll look out 12 months, you may get into year two. But then when you get to the end of year one, beginning of year two, then you'll look into year three and take that value. And again, during these contracts all three years have different values. So year one can be a \$1 million, year two can be \$2 million, year three can be \$3 million. And depending on which year you're in, you'll pick up – you might pick up a \$1 million at the signing of the deal. But you still have growth from \$2 million to \$3 million the following year and you'll get that as well. That is the dynamic that's happening. So these deals are done. There is – it's 100% going to happen. It obviously has no revenue impact immediately. But we do have the ARR coming in Q4 from what's contracted a year or even sometimes more though.

Howard Ma: Got it. Super clear. I understand now. Thanks, Greg.

Greg Henry: You're welcome.

Operator: Thank you. And that concludes our Q&A; session. I will now hand the floor back to Matt Cain for closing comments.

Matt Cain: Thanks, operator. Thank you all for joining us. We look forward to speaking with you all again soon. Have a great day.

Operator: Thank you. This concludes today's call. All parties may disconnect. Have a good day.