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Q2 Holdings, Inc. NYSE:QTWO

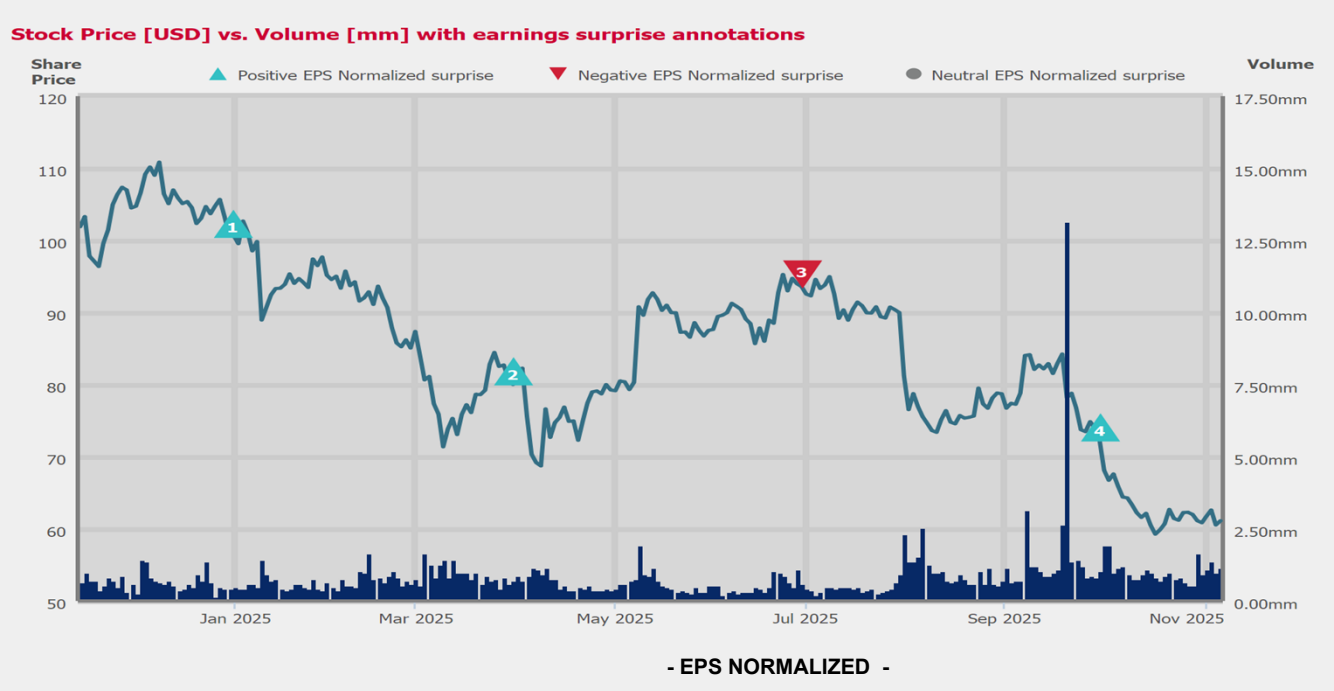
FQ3 2025 Earnings Call Transcripts

Wednesday, November 5, 2025 10:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2025-			-FQ4 2025-	-FY 2025-	-FY 2026-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.56	0.64	14.29	0.62	2.41	NA
Revenue (mm)	197.77	201.70	1.99	204.05	791.48	NA

Currency: USD
Consensus as of Nov-06-2025 12:00 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2024	0.47	0.48	1 2.13 %
FQ1 2025	0.48	0.50	2 4.17 %
FQ2 2025	0.53	0.52	3 (1.89 %)
FQ3 2025	0.56	0.64	4 14.29 %

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Presentation

Operator

Good afternoon. My name is Tyler, and I will be your conference operator today. At this time, I would like to welcome everyone to the Q2 Holdings' Third Quarter 2025 Financial Results Conference Call. [Operator Instructions]

I will now hand the call over to Josh Yankovich, Investor Relations. Sir, please begin.

Josh Yankovich
Investor Contact

Thank you, operator. Good afternoon, everyone, and thank you for joining us for our third quarter 2025 conference call. With me on the call today are Matt Flake, our CEO; Jonathan Price, our CFO; and Kirk Coleman, our President, who will join us for the Q&A portion of the call.

This call contains forward-looking statements that are subject to significant risks and uncertainties, including among other things, with respect to our expectations for the future operating and financial performance of Q2 Holdings and for the financial services industry. Actual results may differ materially from those contemplated by these forward-looking statements, and we can give no assurance that such expectations or any of our forward-looking statements will prove to be correct.

Important factors that could cause actual results to differ materially from those reflected in the forward-looking statements are included in our periodic reports filed with the SEC, copies of which may be found on the Investor Relations section of our website, including our quarterly report on Form 10-Q for the third quarter of 2025 and the press release distributed this afternoon and filed in our Form 8-K with the SEC regarding the financial results we will discuss today.

Forward-looking statements that we make on this call are based on assumptions only as of the date discussed. Investors should not assume that these statements will remain operative at a later time, and we undertake no obligation to update any such forward-looking statements discussed in this call.

Also, unless otherwise stated, all financial measures discussed on this call other than revenue will be on a non-GAAP basis. A discussion of why we use non-GAAP financial measures and a reconciliation of the non-GAAP measures to the most comparable GAAP measures is included in our press release, which is available on the Investor Relations section of our website and in our Form 8-K filed today with the SEC. We also have published additional materials related to today's results on our Investor Relations website.

Let me now turn the call over to Matt.

Matthew P. Flake
CEO & Chairman of the Board

Thanks, Josh. I'll start today's call by sharing our third quarter results and highlights from across the business. I'll then hand it over to Jonathan to walk through our financial performance and guidance.

In the third quarter, we delivered strong financial results with revenue and adjusted EBITDA, both above our guidance. We generated revenue of $202 million, representing 15% year-over-year growth and adjusted EBITDA of $49 million or a 24.2% margin. We also generated free cash flow of $37 million in the quarter. In addition to the strong financial performance, we had the best third quarter in company history from a booking's perspective.

As we shared earlier this year, we expected our larger deals to be weighted toward the second half, and we saw that begin to take shape with 7 total Tier 1 and enterprise deals in the quarter. This concentration, combined with a solid mix of new and expansion wins, drove the record third quarter bookings activity. Several of the Tier 1 and enterprise wins were net new, showcasing continued momentum in acquiring new customers, and all 3 major product lines contributed to the quarter's performance.

On the digital banking front, we saw continued success upmarket, including a net new win with a bank exceeding $80 billion in assets that will begin by using our platform for retail and small business. We also signed a major expansion with a $60 billion bank that started with commercial and will now add retail. As demonstrated by these wins, our single platform approach, unifying retail, small business and commercial continues to differentiate Q2, help us compete more broadly and creates meaningful expansion opportunities over time.

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During the quarter, we also had 2 instances where a Q2 Bank was acquired by a larger institution. And in both cases, the acquiring bank selected Q2's platform to serve the combined entity. This is an indicator of our competitiveness and the scalability of our technology, especially as bank M&A activity continues.

Our fraud solutions continued to gain traction as well. We signed the largest fraud deal in company history during the quarter, a significant expansion with an existing $200 billion digital banking customer. This win was for our check and ACH fraud solution, which continues to see robust demand in the market. With the cost and complexity of fraud growing, customers are increasingly turning to Q2 as a strategic partner to help them manage risk more efficiently and effectively.

We also had our strongest relationship pricing quarter of the year, highlighted by multiyear renewals with 2 top 10 U.S. banks. Our relationship pricing solutions continued to be an important lever for financial institutions seeking to optimize yield, profitability and growth across both loans and deposits.

Beyond our strong sales performance, we also recently hosted Dev Days 2025, our second annual conference for partners, customers and employees, who build on the Q2 platform using our APIs and SDK. While our annual client conference, Connect, is our venue to showcase production-ready innovation and customer adoption proof points, Dev Days is an event where we share architecture and technology enhancements and explore the next frontier of our platform.

At this year's event, AI was front and center, and we showcased several ways we intend to bring leading AI capabilities to our platform for the benefits of bankers, account holders, developers and our fintech partners. We demonstrated a range of planned AI offerings that illustrate the breadth of our strategy. The first was an AI Copilot that can help account holders and bank staff alike, enabling account holders to receive guidance and manage money through natural language prompts and customer service representatives to retrieve and summarize information.

We demonstrated AI-assisted coding in our SDK, which makes all of our developer documentation available via conversational developer tools and will help customers, partners and even Q2 go from idea to execution faster. We shared a customer-facing extension of our internal AI assistant that indexes the vast archives of our internal Q2 knowledge and makes it available through an LLM, which we believe will help our customers self-serve and get faster customer support outcomes.

And finally, we shared a new partner data integration strategy that is intended to enable us over time to turn our wealth of 1,000-plus back-end integrations and more than 200 fintech partners into a unified data and capabilities ecosystem that will empower agentic innovation. The key takeaway from Dev Days was our customers need to invest in innovation, which requires mission-critical partners with expertise in handling highly regulated data and managing complex integrations to enable AI adoption.

We believe we are well-positioned to be that partner of choice, as we have a proven track record of innovation, can leverage our network of customers, partners and integrations to build new capabilities on our platform, strengthening it with every generation of innovation. Our platform and the ecosystem that surrounds it can facilitate AI innovation in financial services. As technology and financial services continue to evolve, we believe advancements in AI will flow through Q2, not around it.

Looking ahead, we feel very good about the success we've had heading into the final quarter of the year. Our pipeline remains solid. We expect demand to remain strong as we close out 2025. And as Jonathan will share in a moment, we're raising our financial outlook, reflecting our confidence in our ability to deliver on the full-year expectations we set earlier this year.

Before I hand the call over to Jonathan, I wanted to share some exciting updates to our leadership team, which we believe will better align our talent and efforts with our long-term strategy. First, Hima Mukkamala has been appointed as our Chief Operating Officer, expanding his role to include our service delivery and customer experience functions. In Hima's time overseeing our engineering team since 2023, he has demonstrated operational excellence and an extreme focus on AI enablement, both to drive internal efficiencies as well as external innovation.

In conjunction, Kirk Coleman will continue to lead our go-to-market functions as Chief Business Officer, reinforcing his focus on sales and customer success, leveraging his deep industry expertise to advance our product strategy and next phase of growth.

I want to thank Mike Volanoski, our Chief Revenue Officer, for his contributions during his time at Q2, and he will remain with us through December 12 to ensure a smooth transition.

With that, let me pass it over to Jonathan.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

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Thanks, Matt. Our third quarter results demonstrate continued strong execution across several key metrics, including revenue and adjusted EBITDA, both of which exceeded the high end of our previously issued guidance. These results highlight the progress we have made towards our profitable growth strategy, reinforced by the strongest third quarter of bookings in our history and sustained margin expansion.

I will now discuss our financial results in more detail and conclude with our guidance for the fourth quarter and full year 2025, as well as an updated financial outlook for 2026. Total revenue for the third quarter was $201.7 million, an increase of 15% year-over-year and up 3% sequentially. Our revenue growth was primarily driven by subscription-based revenues, which grew 18% year-over-year and 4% sequentially. Subscription revenue as a percentage of total revenue continued to increase, ending the quarter at 82%, highlighting the ongoing shift in our revenue mix towards this higher-margin revenue stream.

The year-over-year and sequential revenue growth was primarily driven by a combination of new customer go-lives and expansion with existing customers. Our services and other revenues increased 5% year-over-year, reflecting an improvement compared to the prior quarter's year-over-year trends. This growth was driven by an easier comp versus the prior year as we lap the impact from First Republic Bank, which we indicated on the prior call.

In addition to the easier comp, we benefited from higher professional services revenues from core conversions. These increases helped offset ongoing declines in more discretionary professional service offerings, which remain under pressure. Total annualized recurring revenue or total ARR grew to $888 million, up 12% year-over-year from $796 million at the end of the third quarter of 2024, driven by strength in our subscription ARR, which grew to $745 million, up 14% year-over-year from $655 million in the prior year period.

Total ARR growth was fueled by continued strength in subscription-based bookings across both new and existing customers. As expected, subscription ARR growth also benefited from a normalization in churn following a concentration of churn in the second quarter, and we continue to expect churn in the second half to be more favorable than the first with full year levels remaining in line with or better than historical averages.

Our ending backlog of approximately $2.5 billion increased by $161 million sequentially or 7% and $485 million year-over-year, representing 24% growth. Year-over-year and sequential increases were primarily driven by expansion with existing customers as well as solid net new activity and was broad-based. We entered the year expecting enterprise and Tier 1 opportunities to be more heavily weighted towards the back half, and that proved out with strong third quarter performance in those segments, which represented the majority of our booking's growth for the quarter. And as we have mentioned previously, the sequential change in backlog may fluctuate quarter-to-quarter based on the number of renewal opportunities available within that quarter.

Gross margin was 57.9% for the third quarter, up from 56% in the prior year period and above the 57.5% we saw in the previous quarter. The year-over-year and sequential increases in gross margin were driven by an increasing mix of higher-margin subscription-based revenues. We continue to expect gross margin to expand in Q4 with full-year 2025 gross margin expansion of at least 200 basis points.

Total operating expenses for the third quarter were $76 million or 37.7% of revenue compared to $73 million or 41.5% of revenue in the prior year quarter and $75 million or 38.2% of revenue in the second quarter. The year-over-year improvement in operating expenses as a percent of revenue was driven by G&A, which benefited from lower personnel-related costs and higher revenues, which impacted all categories.

Total adjusted EBITDA was a record $48.8 million, up 50% from $32.6 million in the prior year period and up 7% from $45.8 million in the previous quarter. We ended the third quarter with cash, cash equivalents and investments of $569 million, up from $532 million at the end of the previous quarter. As we indicated on the prior call, the third quarter included a material cash payment, which drove the slight sequential decline in cash flow.

In the third quarter, we generated $46 million in cash flow from operations, driven by improved profitability and continued effective working capital management and delivered $37 million in free cash flow. We continue to anticipate the fourth quarter will be our strongest free cash flow quarter of the year, consistent with typical seasonality.

As announced in our press release, Q2's Board of Directors authorized a share repurchase program for an amount up to $150 million. Given the significant progress we have made on improving the balance sheet and our cash flow generation, we believe we are in a strong position to exercise all components of our capital allocation strategy. These priorities include investing in the business to elongate our subscription growth trajectory, evaluating opportunities for highly synergistic inorganic growth, retiring our convertible debt and opportunistically utilizing the share repurchase program over time.

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Let me finish by sharing our fourth quarter and updated full year 2025 guidance. We forecast fourth quarter revenue in the range of $202.4 million to $206.4 million, and we are raising full year revenue to the range of $789 million to $793 million, representing year-over-year growth of 13% to 14% for the full year. We forecast fourth quarter adjusted EBITDA of $47.2 million to $50.2 million and are raising our full year 2025 adjusted EBITDA guidance to $182.5 million to $185.5 million, representing 23% of revenue for the full year.

Looking ahead, we are also providing an updated financial outlook for 2026. We expect full-year subscription revenue growth of approximately 13.5%, which is up from the approximately 13% we previously provided, reflecting the strong bookings momentum we've seen year-to-date and the durability of our subscription model. Total non-subscription revenue is expected to decline in the mid-single digits year-over-year in 2026, driven by ongoing secular pressure in bill pay and discretionary services revenue.

In addition, we expect our full year 2026 gross margins to be at least 60%, and we expect adjusted EBITDA margin expansion of approximately 250 basis points. As a result, we are increasing our 2024 to 2026 3-year annualized average adjusted EBITDA margin expansion target to 450 basis points, up from our previous expectation of 360 basis points.

Finally, based on our performance to date and anticipated second half strength, we reiterate our full year free cash flow conversion outlook of at least 90% for 2026.

In summary, we delivered a strong financial performance, which exceeded the high end of our previously issued guidance. This performance, coupled with our outlook for the remainder of the year, has given us the confidence to raise our full year guidance on both revenue and adjusted EBITDA for 2025 and our improved 2026 outlook. We remain dedicated to delivering growth, profitability expansion and strategic capital allocation and believe that our results to date collectively illustrate our progress and potential as we continue to evolve our business and drive shareholder value.

With that, I'll turn the call back over to Matt for his closing remarks.

Matthew P. Flake
CEO & Chairman of the Board

Thanks, Jonathan. Before we open it up for questions, I'll close with a few final thoughts. In summary, Q3 was another good quarter defined by strong financial results and record third quarter bookings. The record bookings execution was driven by broad-based sales performance with 7 total Tier 1 and enterprise wins. We also shared some exciting developments in our AI journey, showcasing several solutions in development at our Dev Days event that demonstrated how we're using leading-edge AI technologies to empower our customers, their account holders and partners in the months and years to come.

Looking ahead, our record 3Q bookings performance and the strength of our pipeline gives me confidence that we'll close the year strong and enter 2026 positioned for continued subscription revenue growth and an improved profitability outlook.
Thank you. And with that, I'll turn it over to the operator for questions.

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Question and Answer

Operator

[Operator Instructions] And your first question comes from the line of Parker Lane with Stifel.

Jeffrey Parker Lane
Stifel, Nicolaus & Company, Incorporated, Research Division

Congrats on the quarter. Matt, some changes on the management team that you outlined here. I guess, coming off of bookings, a record bookings quarter here for 3Q. Maybe just talk about why now is the right time to make some of these changes to the structure of that organization? And what you expect the biggest changes we'll see in the near term are under the new leadership here?

Matthew P. Flake
CEO & Chairman of the Board

Yes. Thanks, Parker. For us, it's -- yes, you guys live quarter-by-quarter. We didn't just do this overnight. We've been trying to structure the business in a way to align the technical resources where our delivery support, the people that build the product and host the product are aligned because so much of that is connected to the engineering team. And so Hima is a proven commodity for us. We've been really impressed with him. Kirk hired him as a big advocate for him.

And then putting Kirk in a position to do go-to-market and the product side of things, where he has deep experience. He's been a buyer. He's been a seller. He's been on our side as well. So it's just a perfect fit at this time, and we wanted to get it done before the end of the year, so we could put our plans together for '26 and beyond. So it's -- coming off a strong quarter just happened to be what happened. But really excited about these changes, and I think they put us in a position to really accelerate our products, our go-to-market as well as our initiatives around AI.

And I'm sorry, what was the other part of the question?

Jeffrey Parker Lane
Stifel, Nicolaus & Company, Incorporated, Research Division

I think you touched on most of it there, Matt. Maybe just to pick up on AI, you highlighted some of the new development from the Dev Days. Obviously, AI is a huge focus area for every industry. But just wondering, if you look at year-end markets, what sort of appetite there is there, and more importantly, budget there is around AI? How much of a prioritization is this in your end markets? And what are you expecting the timeline to be there for contributions and benefits to your deal cycles as a result of it?

Matthew P. Flake
CEO & Chairman of the Board

Yes. Keep in mind, we've been using AI for fraud and cross-selling and products like that for a while. Our buyers were the most conservative business people in the country, arguably in the world. And so they are leaning in and learning. We're having a lot of conversations around it. We're trying to understand the problems they want to solve from a product's perspective. And so that's how you educate yourself and build the right products. The Dev Days, obviously, there's a lot of activity there. So encouraged by their engagement with us, and we think there's a lot of opportunity there. When it folds into the revenue and the cost side of things, I'm not in a position to share that at this point, but we definitely think there's going to be a lot of opportunity there on both of those lines.

Operator

Your next question comes from the line of Terry Tillman with Truist.

Terrell Frederick Tillman
Truist Securities, Inc., Research Division

Matt, Jonathan, Kirk and Josh, my first question, you actually have -- you beat me to it a little bit. I was going to have a lot to ask about AI. So you had a lot in your prepared remarks, and then, Parker had a good question on it. I guess, maybe another question kind of coming at this AI kind of angle or opportunity is, you talk about a single platform approach and how folks tend to cross-pollinate across commercial, small business and retail. Do you see maybe a quickening of the pace of, hey, we really need to clean up our digital banking front end though if we really want to do this AI stuff the right way? I'm not trying to put words in your mouth, but do

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you see this as potentially helping kind of accelerate some of this kind of brownfield replacement opportunities for digital banking before they actually buy some of these AI tools? And then I had a follow-up.

Matthew P. Flake
CEO & Chairman of the Board

Yes. I think a couple of things to understand about what I think are differentiators in our space, in particular. Everybody has horizontal and vertical software in the trash right now. I would point out some things about our industry in particular. Number one, I think incumbency and trust are both factors that provide meaningful and durable advantages for us. We have hundreds of customers. We have thousands of long-standing integrations to complicated back-office systems that require constant care and feeding.

We have 20 years of compliance frameworks around securing the data that is accumulated on our single platform, as you mentioned, for retail, small business and commercial banking workflows. I think financial institutions need, and are going to require, a trusted partner to help them adopt AI safely and responsibly when you're talking about the buyers we're dealing with.

And from -- and then there's a data and distribution advantage we have. We have 27 million end users, average of 3 accounts per user with probably an average of 7 years of history. That includes posted transactions, balances, payments, behavioral data, demographic data. And we're going to continue to use that data to enhance our customers' end-user experience, back-office operations, fraud prevention, cross-selling capabilities, efficiencies for us.

And then you have a vast partner network that we believe will continue to work with us to distribute their AI solutions focused more on use cases that we will work to integrate into our workflows and complement the digital banking experience. And so that, coupled with the announcement we made today around the structure of this company in a way that it'll empower us to capitalize on the strategic advantages over the coming years. For us, the customers and Q2 team are excited about this opportunity. We just have to execute on our plans, which we have a track record of doing.

So there's a lot of opportunity there. We're using it internally, externally with customers and everything else, and we're seeing real progress in that area. And we don't anticipate to sit on our hands and wait for somebody to come do this. But I do believe the incumbency and the trust aspect and the data and the distribution capabilities are significant tailwinds for us in this race.

Terrell Frederick Tillman
Truist Securities, Inc., Research Division

That's great to hear. And I guess, I don't know if this is for you, Matt or Jonathan. And I'm not usually wanting to start looking at numbers and asking numbers questions on the calls. But it does look like it was a pretty substantial uptick versus the prior year on like RPO. And I know the subscription ARR picked up some, and I know some of this was kind of churn timing from last quarter. Where I'm going with this is we knew second half or we thought second half would be stronger than the first half on just the seasonality of your bookings. But I usually think of 4Q as the big quarter. Is there any tilt that's different potentially this year in 3Q to 4Q bookings?

Matthew P. Flake
CEO & Chairman of the Board

No, we are cautiously optimistic about the fourth quarter. We're focused on getting deals done. We have a lot of activity. I see a lot of good indications, but I don't know anything until it's done, but we are -- the pipeline is strong. We didn't drain it in the third quarter, and we're going to -- we intend to execute on those and continue to build the pipe for '26.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Terry, the only thing I'd add is, as we talked about at the beginning of the year, the mix of first half versus second half was going to -- we predicted would be slanted towards Tier 1 and enterprise in the second half. The third quarter was a great start to the second half in that regard because we did see a really strong performance in that upper tier in that Tier 1 and enterprise segment and saw from a sub's ARR bookings perspective, by far, the strongest quarter of the year as that -- as we expected. And as Matt said, no feeling like we borrowed from the fourth quarter. So I feel good about the opportunity moving forward, but we got to execute on it.

Operator

Your next question comes from the line of Andrew Schmidt with KeyBanc Capital Markets.

Andrew Garth Schmidt
KeyBanc Capital Markets Inc., Research Division

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Guys, good to be back on the call. Great results here. Great to see the sub ARR acceleration on top of a tougher comp. I wanted to ask about just the 2026 sub's ARR growth of 13.5% you outlined. Continue to see good long-term growth trends. But I guess you have to make some assumptions when you're providing that outlook. Obviously, you have good visibility given the recurring revenue base, but there's cross-sells, there is existing user growth and things like that. Maybe you could talk through just some of the assumptions that are in there.

And then also, you commented on the bank M&A environment. Historically, it's been a positive for Q2, and we seem to kind of be in the sweet spot here given the current environment. Maybe talk about whether that's layered into those assumptions or whether that could be incremental?

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Yes. Thanks, Andrew. So, to hit the first part of the question, when we think about sort of the 13.5% for 2026 subscription revenue growth, that's mostly informed by the bookings outcomes year-to-date and the mix of those bookings, which gives us good visibility into 2024. When you think about what we do in the fourth quarter of this year, smaller deals, cross-sell, renewal activity, that can have an impact. But the bulk of it, we have visibility into based on actual bookings that we've obtained so far year-to-date. So we feel really good about that number, have conviction.

And most importantly, the performance in the third quarter gave us the confidence to lift it from what we had predicted and communicated all throughout the year at 13% up to 13.5%. So it has assumptions around ongoing performance in line with what we've done when it comes to the near time to revenue levers, like cross and renewal activity, but there's no sort of incremental impact from the net new stuff that we're experiencing -- expecting significant impact in '26.

From an M&A perspective, that's a little bit different. There, we don't really build that in from the standpoint of upside for our subscription revenue base. We do have some visibility, and we certainly make assumptions around services work tied to M&A. And I think that's informed a little bit in some of the non-subscription line item guidance we gave on the '26 front.

But to the extent that goes more in our favor than it has historically, that would be upside to the plan. But we've seen a pretty strong year from an M&A standpoint. I mean, Matt talked about 2 deals this year, where we won up into the acquirer tech stack and for the combined bank, which is a great sign for us. But overall, M&A activity from a services perspective has been pretty high in 2025. And so we expect that to continue in 2026, but not necessarily to see the same growth we saw year-over-year relative to 2024.

Andrew Garth Schmidt
KeyBanc Capital Markets Inc., Research Division

Perfect. And then if I could -- if I just could ask about just quickly on pricing, it's been a topic of conversation with investors. And I think typically, Q2 has been premium priced just given the value that you bring to clients. But maybe to comment if you're seeing anything different in the environment since it has been a discussion that's come up, not specifically Q2, but just broader in terms of the industry. But any comments there would be helpful.

Matthew P. Flake
CEO & Chairman of the Board

No, there's nothing abnormal. I mean, a lot of people that don't have the feature functionality we have, they use price as a tool to try to win deals. And sometimes banks go for that. We have a lot of discipline around that. We will walk from a deal if it doesn't fit our economic model and hope to pick them up later. But there's no significant change on the pricing side of things from what we've seen from people.

Operator

Your next question comes from the line of Matt VanVliet with Cantor Fitzgerald.

Matthew David VanVliet
Cantor Fitzgerald & Co., Research Division

Curious on -- given your recent success of upselling, cross-selling your existing customers, how should we think about the renewal cohort over the next 5 quarters or so? Any differences in sort of the shape or size of the cohorts coming up for renewal? And within that, is there any outsized opportunities where maybe you're already on retail to sell commercial or commercial to sell retail and things of that nature?

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Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Yes. Thanks, Matt. I'll take that. I mean, to your last point, yes, we have lots of those opportunities, and that certainly make up some of the larger, what we call internally, cross-sales significant deals that are in the pipeline. But when it comes to the makeup of the '26 renewal cohort, we did -- we talked about this earlier in the year. But when you look at the performance on renewals in '23 and 2024 combined and look at the composition of that cohort and compare it to the '25-'26 cohort, it really is very, very similar, both in terms of number of opportunities and the mix within them. So we feel really good. It's not -- and it's not as though the renewal performance so far in 2025 has borrowed from '26 or anything like that. So we feel really good for the fourth quarter of 2025 and throughout '26 that the opportunity set in front of us, both in terms of number of deals and the size and shape of them, are comparable to what we've done in recent periods.

Matthew David VanVliet
Cantor Fitzgerald & Co., Research Division

Great. And then, as you look at the opportunity for Innovation Studio, not needing to build every little agent or AI widget out there by leveraging partners, seems like a big opportunity. And maybe as banks are a little more willing to accept AI technology is sort of where we're going, should we think about Innovation Studio maybe even further accelerating here now that you have at least one product in virtually all your customers? And how should we think about the overall revenue contribution in '26 versus still being a couple of years away from real materiality?

Matthew P. Flake
CEO & Chairman of the Board

Kirk, why don't you take the Innovation Studio product question, and then, Jonathan can take over. Go ahead.

Kirk L. Coleman
President

Yes. From an Innovation Studio perspective, really 2 important points in there. One is that if we sort of think about our existing partner ecosystem and the new partners we're bringing to the ecosystem, it continues to be really important for them to have a partner like us who has great technology, great distribution, but also kind of like this very strong technical backbone on which to build their solutions to because you can have these features and functions that these fintechs deliver. But if you don't have all the data, all the APIs, all the integrations that we do, you really can't get as far with them. So that continues to be really important.

If we think about it from an AI perspective, what we're seeing is those partners are really kind of continuing to come to Q2 to co-develop and distribute their AI solutions. And that's not just our existing fintech ecosystem, but it's also what our customers are building for themselves and also new players that you might see in the market like the services companies and others that want to build kind of specialized AI agents that they can distribute into the financial services.

Again, all of that is really important for our Innovation Studio because if you think about the legacy financial services infrastructure, if you don't have a partner like us, it's really hard to scale any kind of solution into that environment. So that's where we see a lot of strength currently.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

And what I'll add up from a revenue growth perspective, '24-'25, we've seen phenomenal revenue growth from the Innovation Studio ecosystem. And you're right, we are seeing some use cases that are pretty exciting in terms of the adopted fintech partners and the entire ecosystem all thinking about AI in terms of their own point solutions and then us getting the benefit of that as there's adoption inside the platform. So we're excited about it. We think '26 will be another great year of growth from an Innovation Studio revenue perspective. And as a reminder, like that is very high-margin revenue. We're only recognizing it on a net basis. So it's a valuable revenue stream to us, and we are building a go-to-market apparatus and investing in the go-to-market team to try and capture that growth opportunity that you're asking about, Matt.

Operator

Your next question comes from the line of Ella Smith with JPMorgan.

Eleanor Osgoode Smith
JPMorgan Chase & Co, Research Division

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So first, I was hoping to ask about seasonal trends. Are there any seasonal trends to note when it comes to cross-sell from existing customers? And how long does it usually take cross-sell commitments to hit your revenue line?

Matthew P. Flake
CEO & Chairman of the Board

From a seasonality perspective, yes, the fourth quarter is usually our biggest cross-sell opportunity. It's the end of the year, people trying to fill out their budgets. I was really happy with the third quarter. Some of that was from our Connect conference that built up and the excitement from seeing the products. And then the fourth quarter should be as strong as cross-sell opportunity.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Yes. And from a time-to-revenue perspective, unlike net new, these can go to revenue much, much faster. It just varies depending on the product. And so some of the stuff can get live really quick, especially when you're talking about cross-selling, let's say, an Innovation Studio partner that's already in production to certain products that maybe there is a, call it, 3- to 6-month timeline on the outside, in some cases, if it's not sort of a cross-sell of the digital banking component like retail to commercial or vice versa. So if it's an ancillary product, the timelines are faster.

Eleanor Osgoode Smith
JPMorgan Chase & Co, Research Division

That's very clear. And for my follow-up, can you speak to the appetite of existing and prospective customers to reinvest in technology? Is it changing given it's a somewhat lower interest rate environment?

Matthew P. Flake
CEO & Chairman of the Board

The demand environment has been strong, and it remains strong. I think interest rates, there's still uncertainty about what they're going to do. I think from a customer perspective, whether it's a bank or a credit union, they don't want to be caught in the situation they were in, in the 2012 to 2022, which is they were doing the loans, but they didn't have the operating accounts. So they learned their lesson, and they're trying to get the best digital banking, retail, small business, commercial solutions so that they can get the operating accounts when the lending environment comes back. And so they want to have the best product, and that's why we continue to win in that space, and I think we're going to continue to. So demand is strong, and I anticipate it continuing to be strong even as rates go down, assuming they will.

Operator

Your next question comes from the line of Cris Kennedy with William Blair.

Cristopher David Kennedy
William Blair & Company L.L.C., Research Division

Just wanted to follow up on the gross margin outlook for next year. Can you just talk about some of the levers that you have to get to that 60% target?

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Yes. For sure, Chris. So the single biggest lever that we will see driving that upside in 2026 is the completion of our cloud migration project on the digital banking side. And so we'll be completing that here at the end of '25, very early in 2026. And so as we exit the data centers, you see that depreciation roll off, the very clear cost savings coming off.

And then, as you think about operating in the environment that we're in from a cloud perspective, there's just so much opportunity for learning that environment and operating with more elasticity, more understanding of how to be efficient in that new world. And so we feel really good about the guidance we've given. But there's also all the other things that go into that in terms of revenue mix, AI efficiencies, all the things we're doing across support and delivery to become more efficient that are all accruing into that gross margin line.

Operator

Your next question comes from the line of Alex Sklar with Raymond James.

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Jessica Wang
Raymond James & Associates, Inc., Research Division

This is Jessica on for Alex. So sort of touching on what you've been saying about the strength in your risk and fraud solutions and your cross-sell, how should we be thinking about the contribution of risk and fraud to -- as a percentage of bookings year-to-date relative to previous years?

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

We've never discreetly given projections around risk and fraud because so much of that solution is embedded within digital banking, but we can say that the growth of that business exceeds that of most of the other product lines that we have. And so you are seeing a greater mix in 2025 than we have historically in terms of the contribution from the fraud tech solutions. And I can say, as we think about the plans for 2026, we see a demand environment that suggests that will continue.

Jessica Wang
Raymond James & Associates, Inc., Research Division

Got it. And also, thinking about -- so we've been hearing some concerns in the end market about credit risk over the last couple of months. I think earnings have been turning up better than feared. But can you provide some color on what you're seeing from the health of your customer base? And any changes in demand patterns in terms of your solutions that may be are more focused on the credit side?

Matthew P. Flake
CEO & Chairman of the Board

Kirk, why don't you take that?

Kirk L. Coleman
President

Yes. On the credit -- so if you sort of look broadly, and we -- again, we pull all the call reports on all of our customers. So we watch this really closely. The banks are really well reserved right now. I think we would start to start there, and that's -- if you look back kind of like even on a 10-year basis. So what we see is, although there's been a couple of banks that have had to report some losses here recently, if you kind of look more broad-based, even in those banks, they were well reserved to be able to handle those losses that they reported.

And so right now, credit quality is actually holding up pretty well. Those credit provisions look like they're in a healthy range. What we see in our PrecisionLender relationship pricing line of business, continues to be very strong in terms of the demand for that product as customers are thinking about how do I reprice relationships as the interest rate environment changes, particularly since there's still a little bit of uncertainty in terms of exactly how that's going to play out and as they're thinking about '26 and what their growth trajectories look like. So don't see any red lights on the credit front yet.

Operator

Your next question comes from the line of Charles Nabhan with Stephens.

Charles Joseph Nabhan
Stephens Inc., Research Division

Congrats on the results. A couple of quarters ago, you gave some real good metrics around the cross-sell opportunity between retail and treasury management. And I wanted to revisit that to get a sense for how much runway or wood there is to chop within the customer base in terms of cross-selling those 2 products. Also, I wanted to touch on whether you're seeing more uptake of both commercial and retail solutions on your newer deals.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Yes. Thanks, Chuck. Yes. No, that's a metric we track closely. It's a huge -- you call it TAM or SAM opportunity inside our customer base. When you think about cross-sale of significance, what we call it internally, we still have, call it, in a customer -- Tier 1 customer base, so financial institutions over $5 billion in assets. Only 10% of them have all 3 of retail digital banking, commercial digital

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banking and PrecisionLender or relationship pricing as we call it now. And so that is a huge cross-sell opportunity. And that dovetails well into your second point.

We still see a good mix of deals that start with commercial, go to retail. We had a great one like that this quarter, and we see that all the time. But you also have some really good. We had a great net new win that went for the full platform. And so it just -- it depends, and both of those were Tier 1 institutions. So it just depends on the strategy and the timing and the budget of the financial institution. But we feel really good about that. That's why we win a lot. That's a big differentiator for us. And again, from a cross-sell perspective, that continues to be a huge opportunity given how few of our Tier 1 institutions have all those different products.

Charles Joseph Nabhan
Stephens Inc., Research Division

Got it. And as a follow-up, I wanted to talk about your product roadmap and get a sense for how you balance M&A, partnership and organic growth as well as what specific products or areas you might look to as a means of either enhancing your existing functionality or broadening your TAM?

Matthew P. Flake
CEO & Chairman of the Board

Yes. I mean, I think the platform, we look at it and say, on the retail side, we want to make it more personalized for users as they log in and they can have things that are relevant to what their day looks like. From a business perspective, we want to continue to -- we want to add that functionality as well. Plus we want to add deeper commercial functionality that allows people -- the banks to go help there -- to go acquire larger businesses in their region.

Fraud, obviously, we're investing heavily in that. Innovation Studio gives us a lot of scale in a lot of different products. And then, also the ability for us to cross-sell and market products. And then you have AI tied to all of this, whether it's operating efficiency for the bank, agentic AI to help people understand what they need to do. So there's all of these products that we have. We have a core modernization strategy with Helix. There's a lot of different things that we're doing that are going to expand our TAM and kind of grow with our customers as they try to get into new areas and sign new customers and gather more deposits. So strategically, we are really well positioned.

Kirk, if you have anything to add, feel free to add. I don't know if I broadly covered it.

Kirk L. Coleman
President

No, I think you broadly covered it. I mean, again, what we see from our customers, and we've had 3 really great customer events over the last 45 days, and they reinforced this in addition to our Customer Advisory Board, but they're really looking to us to help guide them through this current stage of innovation. We brought them through digital, we brought them through mobile, we brought them through cloud. We're going to bring them now into AI. And so having that trusted partnership and really being very interactive with us in terms of the feedback that they give us and the feedback we give them in terms of what the roadmap should look like is a really powerful kind of flywheel for us.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

And Chuck, to the first part of your question around build versus buy versus partner, I mean, we think about that all the time. It's an equation where we want to be able to exercise all of those different levers. And obviously, we're building products, and the Innovation Studio ecosystem along with some of our long-standing partnerships pre-Innovation Studio, we have a very robust partner strategy.

And then when it comes to buying, I think it's obviously a part of our long-term strategy and one we've exercised in the past. But the bar has been raised for what it would take for why we need to own an asset and how we think about valuing the asset and what the financial criteria of those businesses would need to be. So all 3 of them are relevant, and Matt and Kirk covered the areas where we would be interested, and that would be the same in the context of M&A.

Operator

Your next question comes from the line of Dan Perlin with RBC Capital Markets.

Daniel Rock Perlin
RBC Capital Markets, Research Division

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I just wanted to touch base on kind of the macro, kind of the state of what's been happening here as of late in that there's a bit of a dislocation, I think, happening with one of the large core providers. They're going to go through a lot of, I would say, change over the next couple of years in terms of their core consolidation. And I know we're not specifically talking everything on your business. But I'm just wondering how much kind of the derivative fallout from that could create some really interesting RFP opportunities for you guys over the next couple of years. And just how would you frame that in that context?

Matthew P. Flake
CEO & Chairman of the Board

Yes. Historically, as I've seen core consolidation happen over the last 25-plus years, it generates opportunities for us. So when a bank is forced to -- or credit union is forced to switch off of the general ledger they're running on, it pushes them to go evaluate all their technology and what they want to do because it's such a disruptive thing for them. So I -- RFP volume, I looked at it before, is similar to what it was last year right now, but this stuff is just kind of hitting the market now. So it's something to watch. Obviously, we're paying attention to it.

For us, we know all the prospects in banks and credit unions. We're calling on them all the time, marketing to them and keeping our name in front of them. So when they do decide to take a look, hopefully, we get called. That's the objective. So other vendors have different challenges. We've all had challenges at different times. And I don't -- I expect those to get fixed. And so we can't rest on our laurels and think some of that stuff is going to be a problem. And so we're going to continue to attack the market we're going after and use our product and our customer experience and our culture as a differentiator.

Daniel Rock Perlin
RBC Capital Markets, Research Division

Yes. No, that's great. Just a quick follow-up. On the '26 guide, if I'm just looking at the numbers, and they may differ a little bit, but like it looks like the incremental margin on EBITDA somewhere in the high 40s, low 50s versus kind of in the 60s kind of where you are maybe going to land this year. Again, maybe there's a little bit of squishiness in the numbers. But net-net, it looks like it's coming down a little bit. Is that because there's like this investment opportunity cycle that you're going into, especially given the fact that you've got this migration on the gross margin side, and it does feel like there's plenty of other opportunities for leverage? So I'm just wondering what's maybe a little bit more embedded in that.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Dan, let me make sure I'm getting your question right. Are you referring to Q4 EBITDA?

Daniel Rock Perlin
RBC Capital Markets, Research Division

No, '26 guide EBITDA, 250 basis point margin expansion year-on-year. Just the incremental margin on that would suggest it's probably closer to 50 versus maybe 60 that you're going to land on in 2025.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

Yes. I got to make sure I'm following you. When we look at our 2024 to 2026 financial framework, one of the metrics we talked about was EBITDA margin expansion. And what we talked about there was the 3-year average, '24 to '26 would see 360 basis points of improvement on average. With 2024 in the bag, and 2025, the guide we just provided, both well over 500 basis points of expansion each of those years, the implied 2026 EBITDA margin expansion before the color we gave today was quite low. It was sub-100 basis points in terms of the implied '26 margin expansion. In providing that 250 basis points of expansion, I think what we're trying to show is we actually expect more operating leverage in 2026 than what those numbers implied. So hopefully, that helps. I just -- I didn't reconcile that to the 40 to 50 number you were talking about.

Daniel Rock Perlin
RBC Capital Markets, Research Division

Yes. No, that -- believe me, I'm not knocking on the 250 basis points. That's a great number. I was just referring to the incremental margin associated with that embedded for '26 versus '25, but we can have that in our follow-up call. Thank you.

Jonathan A. Price
CFO and Executive VP of Strategy & Emerging Businesses

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Okay.

Operator
Thank you. There are no further questions at this time. This concludes today's call. Thank you all for attending, and you may now disconnect.

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