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Q2 Holdings, Inc. (QTWO)

Q1 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Julianne, and I'll be your conference operator today. At this time, I would like to welcome everyone to the Q2 Holdings' First Quarter 2022 Financial Results Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there'll be a question-and-answer session. [Operator Instructions] Thank you.

I'd now like to turn the call over to Josh Yankovich, Investor Relations. Sir, please begin.

Josh Yankovich

Head-Investor Relations, Q2 Holdings, Inc.

Thank you, operator. Good morning, everyone, and thank you for joining us for our first quarter 2022 conference call. With me on the call today are Matt Flake, our CEO; David Mehok, our CFO; and Jonathan Price, our Executive Vice President of Emerging Businesses, Corporate and Business Development.

This call contains forward-looking statements that are subject to significant risks and uncertainties, including with respect to our expectations for the future operating and financial performance of Q2 Holdings. Actual results may differ materially from those contemplated by these forward-looking statements, and we can give no assurance that such expectations for 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 to be filed this week and subsequent filings, and the press release distributed yesterday afternoon 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 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 may be found on the Investor Relations section of our website and in our Form 8-K filed with the SEC yesterday afternoon.

Let me now turn the call over to Matt.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Thanks, Josh. I'll start today's call by sharing our first quarter results and highlights from across the business. I'll then hand it over to Jonathan to provide more insights into our emerging businesses. David will then discuss our financial results in more detail.

In the first quarter, we generated non-GAAP revenue of \$134.3 million, up 15% year-over-year and 1% sequentially. We also added over 500,000 users to our digital banking platform during the quarter, resulting in a year-over-year increase of 8%. That brings us to approximately 19.7 million total registered users.

Our Q1 results exemplified many encouraging themes. First, we saw a solid execution across our sales teams. We signed two enterprise deals with our loan pricing solutions, as well as four Tier 1 deals across banking and lending. We're pleased with the breadth of deals we continue to win, both in the diversity of institutions choosing Q2 and the variety of products being selected across those deals.

Our Emerging Businesses also had a strong first quarter. Q2 Innovation Studio was cited as a key differentiator in the vast majority of our net new digital banking wins, and we continued to see rapid adoption from our customers and a growing partner ecosystem.

And with Helix, our banking-as-a-service solution, we continued to win new deals across a broad range of verticals, and we launched an exciting new program with NYDIG, a leading Bitcoin provider, all of which Jonathan will discuss in more detail shortly. Our product innovation also continues to be recognized by leading industry analysts. This quarter, IDC named Q2 a leader in their IDC MarketScape for North American Digital Banking Customer Experience Platforms, referencing the Innovation Studio as a key driver of our ranking.

While we were pleased with our sales performance from the quarter, we believe this type of third party acknowledgment supports our vision and product strategy in the new frontier in financial services and highlights the hard work of our talented product and engineering teams. With these themes in mind, I'd like to walk through our sales wins for the quarter in more detail.

We had another strong quarter in the Enterprise and Tier 1 segments with our lending solutions. This is the second quarter in a row with the multiple net new enterprise wins, further exemplifying that the demand environment in the Enterprise segment has improved and we're succeeding in converting demand into new customers. One of our enterprise deals in the quarter was with a top 10 US bank. This bank sees our loan pricing

tools as a valuable way to enable their commercial bankers with actionable, in-the-moment insights, enhance the efficiency and experience of their staff, and help them better serve their clients.

Our technology's ability to seamlessly integrate with other critical systems like their CRM solution was a key reason we won the deal. And the strength and size of our customer base is a significant value to our lending customers and prospects because these solutions use loan data from across our customers to make real-time recommendations to commercial lenders. The more data they have, the more effective the pricing engine becomes. And as we said in the past, we have demonstrated an ability to expand our enterprise loan pricing relationships over time. With some of our largest enterprise customers, we've more than doubled the contracted average recurring revenue in the first two years.

So, while landing these enterprise accounts is significant, we believe each one represents a substantial expansion opportunity beyond the initial booking. We now have roughly half of North American banks over \$100 billion in assets using Q2, including the five largest Canadian banks which are all using our loan pricing capabilities in some capacity.

Another one of our Tier 1 deals from the quarter was the cross-sell of our loan origination solution to an existing Tier 1 digital banking customer. This is just another example of the importance of our strategic relationships with our customers, which puts us in a favorable position to cross-sell and do other areas of the business. And having recently shifted to an enterprise selling motion in which our sales force is enabled to sell virtually the entire Q2 portfolio, we expect to see more of this expansion activity over time.

We also continue to add Tier 1 customers on the digital banking side, signing three net new Tier 1 banks in the quarter. Complementing those Tier 1 wins, we also had a solid quarter in the Tier 2 and 3 segments. Our broad-based success underscores an emerging trend in our digital banking business over the past few quarters. We're signing a wide variety of progressive financial institutions from across the market. Tier 1 through Tier 3 banks and credit unions, retail and commercial that are looking to upgrade to a premium digital banking platform as part of a widespread technology refresh accelerated by the pandemic.

To give a better sense of the kinds of financial institutions choosing Q2 digital banking platform, I'd like to share a few specific wins from the quarter. One of the Tier 1 deals we signed was a roughly \$10 billion financial institution with a progressive growth strategy centered around their strong fintech partnership business. This is a great example of a bank that's heavily invested in using technology to strategically grow their business. They selected Q2 for both retail and commercial digital banking in the quarter. And given how progressive this bank is, I believe this win is a testament to the strength of our single platform architecture, our approach to user experience, and the flexibility we provide through Q2 Innovation Studio.

Our second Tier 1 win was also unique. As we shared in the recent quarters, our customers frequently tend to be on the acquiring side of M&A transactions, which can benefit Q2 as the acquiring institution typically rolls the acquired entity onto their digital banking technology. But during the quarter, we actually had a Tier 1 win emerged from a scenario where an existing customer was acquired by a non-Q2 bank. Rather than the acquiring institution rolling the Q2 customer onto their legacy online banking system, the bank evaluated Q2 and chose to adopt our digital banking platform across the entire combined entity.

Given how atypical it is for an acquiring institution to adopt the technology of the acquired bank, I'm really proud of this win. Rather than choosing the path of least resistance and keeping their legacy system, the bank made a strategic, long-term investment in our solutions, a strong endorsement of Q2's platform.

We also had success in the Tier 2 and Tier 3 segments as we continue to see customers include more Q2 products at the time of their digital banking decision. In fact, the largest digital banking deal from the quarter from a bookings perspective came from a Tier 2 institution that adopted not only digital banking, but also our onboarding, fraud management, and marketing intelligence solutions.

Finally, we just crossed the one year anniversary of our ClickSWITCH acquisition, and the sales performance has been impressive on multiple levels. We've attached ClickSWITCH to a majority of net new digital banking deals over the past year. And we're seeing interest from fintechs, clients who are looking to leverage ClickSWITCH to drive primacy with their customers.

ClickSWITCH has also proven to be a valuable product to help us land new accounts as a stand-alone solution, particularly in the enterprise space. During the first quarter, we signed a top 25 US bank, along with several Tier 1 ClickSWITCH deals, all important relationships that we will look to expand over time.

As the broad mix of deals from the quarter demonstrates, we believe financial institutions are actively looking for opportunities to invest in technology. And one area that we have seen as an increasing priority is modernizing the commercial banking experience.

Yesterday, we announced Q2 Catalyst, a new solution set comprised of our commercial banking and lending capabilities. With Q2 Catalyst, we're positioning ourselves as a single strategic partner to help financial institutions digitize their commercial banking relationship, from winning and onboarding new clients to serving and growing those relationships over time. While the products within Q2 Catalyst like treasury onboarding, loan pricing and corporate digital banking are already established in the market, we believe taking them to market as a combined solution set with unique integration value will be a powerful differentiator for us in commercial banking and lending.

Before I hand the call over to Jonathan to share some updates from our Emerging Businesses, I want to reiterate how pleased we are with the way we started the year. The demand environment has continued to improve. And when you couple that with our robust solution set and broad sales execution across our lines of business, we believe we are still well-positioned for the re-acceleration of revenue growth exiting 2022 and heading into 2023.

Thank you. And with that, I'll hand the call over to Jonathan.

Jonathan Price

Executive Vice President-Emerging Businesses, Corporate & Business Development, Q2 Holdings, Inc.

Thanks, Matt. I'll start with Q2 Innovation Studio where we continue to see growing demand from both a partner and customer perspective. We formally launched the Innovation Studio in June of last year. And as of the end of the first quarter, more than half of our digital banking customers are now using Q2 Innovation Studio in at least one of our programs. And we already have a growing number of customers utilizing every Innovation Studio program, partnering with fintech solutions via our Marketplace programs and building and extending their digital platform with their own resources. This is exciting because we believe that more broadly our financial institutions use Innovation Studio, the closer our relationship becomes and the greater the long-term revenue opportunity.

And Q2 Innovation Studio continues to be a key contributing factor in winning net new digital banking deals. More than 80% of net new digital banking deals in the quarter included Innovation Studio, and those financial institutions specifically resided it as the driver in their decision to choose Q2.

We also grew the total number of partners by 25% in the quarter. This pace of adoption is encouraging and validation that our distribution channel is providing a compelling value proposition to this rapidly growing partner ecosystem, and that financial institutions are seeing the value in working with these solutions to drive rapid innovation for their end users and introduce new revenue opportunities. And we're building out a revenue share ecosystem that customers are just beginning to benefit from. And while we are in the early stages of driving meaningful new economic opportunities for our customers, we believe the ability to create these sources of revenue will strengthen our position as a strategic partner rather than just a vendor.

Moving to Helix. This business also had several key highlights in the quarter. We continue to sign new customers from across a range of different verticals and landed a new deal with one of our largest customers, effectively extending our partnership and growing the economic opportunity associated with this relationship.

We also launched a strategic program with NYDIG, a leading Bitcoin company. As we discussed when we won this deal in the second quarter of 2021, NYDIG is leveraging our Helix platform to power their new payroll offering called Bitcoin Savings Plan, a benefit program offered through US employers. Bitcoin Savings Plan enables employees of participating companies to auto-convert a portion of their paycheck to Bitcoin with no transaction fees. The program is off to an exciting start with employers from a wide range of industries. Given NYDIG's unique go-to-market model in which they partner with employers and the simplicity of the user experience, we're optimistic about the potential of this relationship to grow substantially over time.

And as we've communicated in the past, we consider these program launches important milestones in unlocking the value of Helix client relationships. Our Helix solutions typically have an upfront minimum with significant potential for long-term revenue acceleration related to user growth and adoption following a program launch.

One quarter into 2022, I'm excited about the year ahead for Helix. We're signing new clients and entering new verticals, extending existing relationships and launching major client programs. And with the state of our pipeline and a marketing lift from our recent rebrand, I believe we're entering the remainder of the year with great momentum.

Thank you. And with that, I'd like to pass the call over to David to discuss our financials.

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

Thanks, Jonathan. In the first quarter of 2022, we built on the momentum that began in the second half of last year with strong demand, revenue that exceeded the high end of our guidance, and EBITDA that fell within our guidance range. I'll begin by reviewing our results for the quarter and conclude with updated guidance for the second quarter and full year 2022.

Total non-GAAP revenue for the first quarter was \$134.3 million, an increase of 15% year-over-year and up 1% sequentially. The year-over-year growth for the quarter was driven by an increase in subscription revenue resulting from new customer go-lives and organic user growth. Sequential increase was also driven by new customer go-lives within our digital lending space, as well as an increase in service-based revenue. The over-achievement of revenue relative to guidance was primarily generated by our Helix solutions.

Transactional revenue represented 13% of total revenue for the quarter, down from 14% in the prior year period and consistent with the previous quarter. Transactional revenue dollars in total had a slight sequential decline due to a slowdown in traditional bill pay volume during the quarter.

Annualized recurring revenue or ARR grew to \$594.2 million, up 20% year-over-year and 3% sequentially. Year-over-year and sequential growth was primarily from net new bookings and cross-sales. In addition, the sequential growth in the quarter also benefited from increased usage-based revenue from our Helix solutions, driven by growth in users and transactions. As we previously mentioned, some of our Helix customers have exhibited seasonally larger increases in usage-based revenue related to tax season.

We ended the quarter with approximately \$1.4 billion in backlog, an 8% increase year-over-year, and sequential decline of approximately \$18 million. The year-over-year increase in backlog was largely a result of bookings added through the net new bookings, as well as renewal opportunities with existing customers, both concentrated in the second half of 2021.

As I mentioned in the last quarter's earnings call, Q1 had far fewer in-target renewal opportunities, which impacted our sequential backlog growth. In-target renewal opportunities will remain lower in the second quarter before improving in the second half of the year. As a result of the strong sales performance observed during the quarter, as well as the pipeline for the remainder of the year, we continue to believe we will have strong year-over-year backlog growth for the full year of 2022.

As we previously mentioned, we feel ARR is an important key performance indicator, which provides a barometer for bookings within a given quarter, in addition to reflecting the run rate for our usage-based revenue, which will be important to consider as the revenue mix of our business evolves.

While both ARR and backlog have limitations as forward-looking indicators due to booking seasonality, the timing of renewals, and backlog recognition being limited to contractual commitments, we believe these indicators when viewed in conjunction with our commentary on bookings and new wins, illustrates a more holistic picture of the business demand we're observing and provide support for our long-term financial model.

Gross margin for the first quarter was 51.4%, down from 52.6% in the first quarter of 2021, and down slightly from 51.5% in the previous quarter. The year-over-year decline in gross margin was primarily due to incremental delivery resources associated with several previous strong quarters of net new wins across the business. A sequential decline in gross margin was attributable to an increase in employee-related expenses, including incremental hiring costs and benefits, as well as an increased mix of lower margin pass-through revenue. Over time, we continue to believe that the mix of Helix usage-based revenue will shift towards margin-accretive revenue opportunities.

Total operating expenses for the first quarter were \$65.7 million or 48.9% of revenue compared to \$54.9 million or 46.9% of revenue in the first quarter of 2021 and \$61.5 million or 46.5% of revenue in the fourth quarter of 2021. The year-over-year increase was predominantly driven by increased head count, rising people costs, marketing expenses associated with stadium naming rights, and the expenses associated with our Austin-based facility opened in the second quarter of last year. Sequential increase in operating expenses as a percent of revenue were driven primarily by additional head count, which was concentrated within R&D and sales and marketing. Also, a seasonal ramp in payroll taxes and an increase in hiring cost and benefits.

Adjusted EBITDA was \$8.1 million, down from \$9.9 million in the first quarter of 2021 and \$10.8 million in the previous quarter. In total, we incurred approximately \$1.5 million of expenses in the quarter above our expectations related to benefits and onetime hiring fees, with about 40% of that overage being incurred within the cost of sales and the remaining portion within operating expenses. The increased costs associated with benefits were related to an increase in medical claims which were up significantly, both sequentially and year-over-year.

Hiring fees were predominantly associated with an accelerated pace of hiring for critical resources intended to position the business to drive accelerated growth in the back half of the year and into 2023.

We ended the quarter with cash, cash equivalents, and investments of \$413.7 million, down from \$427.7 million at the end of the fourth quarter. Cash used in operations for the first quarter was \$4.6 million, driven largely by the timing of our annual bonus payout and an incremental payroll run during the quarter, which specifically resulted in approximately an \$8 million incremental impact to cash. In addition, we incurred net capital expenditures of \$3.9 million and generated negative free cash flow in the quarter of \$12.8 million.

Let me wrap up by sharing our second quarter and updated full year guidance. We forecast second quarter non-GAAP revenue in the range of \$139.5 million to \$141 million. We're raising our full year non-GAAP revenue guide to the range of \$577.5 million to \$581.5 million, representing year-over-year growth of 15% to 16%. As we previously mentioned, we believe our year-over-year revenue growth rates exiting 2022 will be higher than those observed in the first half of the year, and we remain confident that we will be positioned for annual revenue growth rate expansion in 2023.

We forecast second quarter adjusted EBITDA of \$7.4 million to \$8.9 million and full-year 2022 adjusted EBITDA of \$41.4 million to \$44.4 million, representing 7% to 8% of non-GAAP revenue for the year. The adjusted EBITDA we are forecasting in the second quarter reflects continued higher costs associated with an increased pace of hiring new employees and a ramp in [ph] G&E (00:22:42). We expect the acceleration of revenue in the second half of 2022 contemplated by our guidance will coincide with margin expansion.

In summary, we had a solid start to the year and believe we position ourselves well to deliver on accelerated revenue growth in the second half of the year and into 2023 with an expanding margin profile.

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

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Thanks, David. In closing, I'm pleased with our performance across the business in the first quarter where we had substantial traction and broad-based execution. We saw ongoing success in the Enterprise space as our loan pricing solutions help us move upmarket and continue to add some of the world's biggest banks to our client roster, which, in turn, produces substantial data that goes back into our solutions, helping financial institutions of all sizes make better, more profitable loans. On the digital banking side, we had a diverse mix of wins, both in landing new customers and expanding existing relationships, highlighted by three Tier 1 net new wins that adopted a broad set of products.

Our Emerging Businesses also had a strong quarter. With Helix, we continued to add customers from various verticals and launched a new program with NYDIG, which we expect to grow substantially over time. And we're beginning to see the flywheel effect with Q2 Innovation Studio. It's attracting world-class fintech partners, helping us win net new deals and driving deeper engagement with our customers.

And while it's still early innings from a revenue perspective, we believe the recent traction demonstrates the long-term opportunity Innovation Studio can bring to our business. We're pleased with our broad-based execution and believe it demonstrates why we're uniquely positioned to facilitate the new frontier in financial services by partnering with leading banks, credit unions, fintechs, and brands.

Thank you. And with that, I'll turn it over to the operator for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Alex Sklar from Raymond James. Please go ahead. Your line is open.

Alexander Sklar

Analyst, Raymond James & Associates, Inc.

Q

Great. Thanks. Matt, you've been moving upmarket for a while now, probably since the time of the IPO, but the Tier 1 and Enterprise activity seemed to accelerate over the past few quarters. I'm curious, are you seeing any changes in terms of what you're displacing in the market and how that compares across your digital banking and lending offerings? Thanks.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Yeah. Thanks, Alex. Yeah. We've continued to have great momentum upmarket, \$5 billion and above, and I think we've got more than 65 digital banking customers of that size, also with more than 40 digital lending customers. I think, to some extent, they put the brakes on harder during the pandemic earlier and then they had to fire it back up in 2021. So, the decision-making in that area has come back to life obviously. I think we've got three straight quarters of enterprise deals with PrecisionLender. Digital banking, obviously a couple straight quarters with Tier 1s.

I think it's more a matter of, as they come out of the pandemic, they are – the importance around digitizing their business is at the top of the list for them right now, and that's where you're seeing this activity. So, our solution set matches up very nicely with what they're trying to do. Our customer base are able to reference off other customers that are similar sizes and shapes to them. And so it's just – there's a network effect that occurs. And the expansion opportunities within these customers is tremendous, whether it's for lending or digital banking. So, it's – , we're hitting on all cylinders in those areas. And I look forward to a big second quarter and the back half of the year. I think you'll probably see digital lending on the Enterprise side have to catch its breath on the Enterprise side. But the back half of the year, that should be a good year for them. So, really encouraged by what we're seeing upmarket.

But also, I'd highlight that we had two Tier 2 deals that were of the size, if not bigger, from an MRR perspective on digital banking than some of the Tier 1s. And I think what's happening is, you have a sales force that's out talking about digital transformation now and not just point solutions. And what that's leading itself to is larger deals at these banks that are below \$5 billion because they can make a bigger decision, [ph] just (00:27:09) focused on the line of business. And I think you'll begin to see that translate upmarket as well. So, we'll see ASPs continue to increase as well.

So, just really solid performance coming out of the pandemic. Obviously, there are some bigger economic issues, but feel really good about where we are in the pipeline and upmarket, as well as in Tier 2 and Tier 3.

Alexander Sklar

Analyst, Raymond James & Associates, Inc.

Q

Got it. That's great color. And just a quick follow-up for David. Based on the 20% ARR growth we've seen over the past two quarters, it sounds like you're kind of expressing comfort in acceleration in the back half of 2022. I'm curious how you feel in terms of comfort level on the acceleration going to 2023.

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

A

Yeah, Alex. We still feel good relative to what we disclosed, both in Investor Day and then repeated again at the start of the year in terms of the acceleration. And one of the things that we've talked about is the size of some of the opportunities that [ph] way (00:28:04) over the last six months, we've won nine Tier 1 opportunities, seven Enterprise opportunities. All that's fantastic, and we're excited to see that manifest in the P&L. But keep in mind, that's going to be late year stuff because it does take longer to implement those solutions. So, we start to see that ramp really occur end of Q3 into Q4, and then that acceleration that we've been talking about in FY 2023.

Alexander Sklar

Analyst, Raymond James & Associates, Inc.

Q

Okay. Great. Thank you, all.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Yeah. Thanks, Alex.

Operator: Our next question comes from Terry Tillman from Truist Securities. Please go ahead. Your line is open.

Q

Oh, great. Morning, everyone. This is [ph] Robert (00:28:40) on for Terry. Thanks for taking the questions. My first one is on Helix. So, at this point, there's been a lot of programs launched, a lot of customers. Any of that stand out or any becoming more material? And can we get an update again on the long-term growth trajectory in banking-as-a-service over the next three to five years? Does this ability changed, improved, or about the same? And then I have one follow-up. Thanks.

Jonathan Price

Executive Vice President-Emerging Businesses, Corporate & Business Development, Q2 Holdings, Inc.

A

Yeah. I can take the first one – this is Jonathan – on Helix. I think we've talked about some of the clients that we've launched. We're a little sensitive about what we share on a name by name basis. But we've seen things like tax season and just the proliferation of multiple accounts held by these end users lead to big opportunities to engage with these users and see them transact with things like debit cards and credit and the like. And so we have multiple clients that we're super excited about what we've seen here in the first and second quarters so far, again, largely driven by events like tax season and other big marketing sprints that they do to try and engage with these users. And often, they're offering meaningful incentives.

And so there's just been a host of names that we're excited about. And obviously, we talked about the one that we just are launching now from a Bitcoin payroll perspective. I think that's a very innovative opportunity with US employers and excited to work on that with the NYDIG team. So, lots of big opportunities. And, David, you can comment too on the growth. What we shared at Investor Day, we believe that this is going to be a highly accretive

business to our overall growth rate as a company. And I think we share sort of north of \$100 million as the long range target leading into 2026, so – [ph] looking forward (00:30:16).

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

Yeah. That's right. [ph] Robert (00:30:18), one of the things that we're looking at is how to model out this business because it is a little bit more unique in terms of the economic models that drive it. But we certainly feel comfortable based upon the transactional volumes that we're seeing associated with these, because remember, there's lower required minimums that occur with these. So, that means lower recurring revenue, but [audio gap] (00:30:38) especially start to ramp pretty quickly. And we're modeling that out. Feel really good about how we're positioned for that accelerated growth. And as Jonathan said, it's going to be an accretive growth rate over the next 40 years to our overall business.

That's great. Appreciate the color. And then just had one quick follow-up on Catalyst. How meaningful could Catalyst end up being? And could that move the needle in more Tier 2 or Tier 3 growth or too early to tell at this point? Thanks.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah. Thanks for the question. We are obviously extremely excited about Q2 Catalyst. It's a unique offering that offers the ability for our customers to work, to digitize the business process of both pricing a relationship, pricing Treasury services, and then helping sell the customer on the technology with tailored demos, and then onboarding the customer which is a real delay and a real challenge when you sign somebody up to become a new borrower or depositor at your bank, and then helping him open the business account through digital acquisition or SMB loan origination, moving to – then ultimately comes out how do you serve the customer with unified digital banking platform on both the lending and the digital banking side. And then growing that relationship, which is so important to these banks and credit unions that are focusing on commercial business side of things.

So, it doesn't have a – it's not specific to a tier. You could be a Tier 1, a Tier 2, a Tier 3 financial institution. But Q2 Catalyst for us is highly differentiated. I got reports yesterday from several folks that were out talking with large Tier 1 customers that said they want this as soon as they can get their hands on it. So, it's a game changer for us in the marketplace. There's a lot of work from the product teams that have gone on to it. And if you think about it, it's a culmination of a lot of the assets that we've built and then also acquired over the last three to four years with PrecisionLender, Cloud Lending, digital banking grow.

And so we're really excited about it. I think it's going to be a real game changer for us, and I'm really proud of the work that's come out of this. And I think no matter what bank or credit union you are, this fulfills our mission of how do we help our customers build their business and strengthen their communities. So, we're excited about it.

That's excellent. Thanks so much.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Thanks. Appreciate it, [ph] Robert (00:32:53).

A

Operator: Our next question comes from Andrew Schmidt from Citibank. Please go ahead. Your line is open.

Andrew G. Schmidt

Analyst, Citigroup Global Markets, Inc.

Hey, guys. Thanks for taking my questions, and great to see the continued step-up in demand. On that point, I was hoping you'd talk maybe a little bit about your conversation with the financial institutions. Obviously, there's a few puts and takes in terms of just health this year. Obviously, more geopolitical uncertainty. Interest rates going up, maybe a positive. But obviously, the impact on mortgage volumes. Just curious overall what you're hearing from FIs from a health perspective as a starting point. Thanks a lot.

Q

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah. Thanks, Andrew. They are – to kind of your point, interest rates are going up. It hasn't really hit the consumer or the small business – or the business lending out there. Obviously, mortgage is taking a hit. But they are – the trade-off is, is what's going to happen with the economy, and I'm not going to opine on that. But if you think about our solution set, our PrecisionLender tool, I talked to a president of a really large bank here in Texas, and he told me that 40% of the lenders at the bank have never written a loan in a rising rate environment. You need a tool to help you price a loan in that situation. And that's where PrecisionLender comes into play.

A

The volumes that we're seeing on digital, I think we've had more than 1 billion logins on our digital application in the first quarter. So, the amount of volume that these systems are seeing is unprecedented, and we're at the center of those transactions. And if you think about a tough economic environment, if that is what is ahead, digital is going to make them more efficient, it's going to drive profitability, allow them to serve their customers in ways that they may not be able to do it with people.

So, we are at the center of this right now, and the opportunity and the conversations I'm having with people is they want products like Q2 Catalyst. They want products like PrecisionLender to simplify their life. ClickSWITCH, allowing people to move an account and bring their direct deposit with them. All these things are top of mind, and our solution set lines really well with what the customers need. And then obviously, Jonathan talked about the momentum on the Helix side of the business. So, who knows what's going to happen? But I think we're going to be in a really good position on either side of that trade.

Andrew G. Schmidt

Analyst, Citigroup Global Markets, Inc.

Thanks for that, Matt. That's a great point about loan pricing solutions. Thank you for that. In terms of just the cost and the inflationary environment, David, I think you called out a few impacts in the quarter, hiring fees, benefits, etcetera. Looks like you're able to largely offset that for the year. Maybe talk about just what the offsets are. And then, obviously, this is still a moving target, but ability to manage potential ongoing cost inflation and retention and things like that. Thanks a lot.

Q

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

A

Yeah. Sure, Andrew. And the way that I categorize this is sort of those that we know and those that we don't know. And for those that we know, we're fairly confident that we're going to continue to see increased hiring costs coming into Q2 and Q3. We factored that into our guidance, not only for the quarter, but for the full year. And that's something that's – we're actually feeling good about in terms of our ability to hire and get resources ramps because we do have a lot of these larger opportunities going live later in the year.

Then there's sort of the unknowns. The unknowns would be things like benefits. We did see a spike in Q1. And one of the things that we've done in our guidance and for our full year modeling is, we've taken up the – what we do is we forecast that in a per employee per month basis. And we've taken it up above what we had in the original forecast, above last year, but it's still slightly below Q1. And, again, this is just trying to use the data that we have on our disposal to forecast the best of our ability.

And then there's going to be things that were – we think we know like T&E. We expect that to ramp up based upon the opening up that we've seen post-Omicron. We saw a ramp-up in travel in March. We expect just continue to see that in Q2 and then going forward for the rest of the year. So, all of those things are incorporated.

And then to your point, we're always working on areas of efficiency to try to offset that, and that's across the organization. And those were some things that we're executing on, and we feel really good about the offsetting measures that we have in place to allow us to deliver the full year EBITDA that we provide in the guidance.

Andrew G. Schmidt

Analyst, Citigroup Global Markets, Inc.

Got it. Thank you very much, David. Appreciate the comments.

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

Thanks, Andrew.

Operator: Our next question comes from Parker Lane from Stifel. Please go ahead. Your line is open.

Jeffrey Parker Lane

Analyst, Stifel, Nicolaus & Co., Inc.

Yeah. Hi. Thanks for taking the question, and congrats on the quarter. Just wanted to sort of circle back on sales efficiency in particular. What impact has the launch of Q2 Catalyst and the ability of the whole team to sell the expensive portfolio had on sales efficiency recently? And how does that scale over the next few years as more and more of the team goes out with the full bag?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah. So, I don't have a lot of reports. We launched Q2 Catalyst yesterday. But we have been talking about it with customers. Any product we roll out, we spend a lot of time with customers. And I think we landed on this in partnership with our customers in trying to solve the problems that they're facing, whether it's onboarding, whether it's – winning the deal initially, onboarding it, or serving and growing with them. So – but I think it's going to have a tremendous impact and lift in the deals that are out there right now, it's going to help us close them, and then generating more lead up, more opportunities in the pipe will be great. From a deal efficiency perspective, whether it's win rates or whether it's deal counts in the pipeline, whether it's – everything is trending in the right direction for us.

And the sales, the enterprise selling motion that we launched really puts us in this position where we're able to go back to existing customers. I talked earlier about the more than 100 – whatever. We have 105 digital banking/digital lending customers, and then we have another 70-plus that are above \$5 billion in assets that have the various products. Our ability to go back into those accounts with hunters and expand our product offerings is going to continue to fuel the growth of this business for a long time.

And then on the net new side, our products, the surface area, the digital transformation that we're pitching to people with proof points around how we can do it is differentiated. As I mentioned earlier, you're beginning to see that show up in the Tier 2 and Tier 3 segment by having reps that go out and talk about all the products. Let's talk about how you want to digitize lending, let's talk about how you want to digitize onboarding, how you want to digitize digital banking. All those things are where we're having a broader conversation, compete favorably against point solutions, and are broadening our ASPs and opportunities out there. So, continue to invest in that group and train them and get them up to speed. But they're doing a lot of work and a lot of heavy lifting, and we're very optimistic about the pipe as we look forward.

Jeffrey Parker Lane

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Got it. Makes sense. And then from an inflation perspective, I know last quarter you sort of called out a potential slowdown there because of the strong bookings in the back half of the year. Is that playing out here in real-time? And how is that being impacted by sort of the macro backdrop and current labor condition?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Yeah. Parker, I think you're talking about the – in the fourth quarter, we had fewer go-lives. I think you're going to begin to see a pickup in go-lives in the back half of the year from the – we had five quarterly pandemic bookings, and then we started to pick it up late third quarter last year. And obviously, the momentum in the pipe has continued all the way through the first quarter. So, maybe there's a little miscommunication there, but we're – we had put 500,000 end users on digital banking, so a lot of growth in digital lending. Obviously, Helix is up to 12 million accounts or something. So, everything is coming together. It's just a matter of having – the rats got to work through the snake from the five quarterly pandemic bookings, as you guys are well aware. In the back half of this year, we should see the momentum that we see that carries us into 2023.

Jeffrey Parker Lane

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Got it. Thanks for the feedback.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Thanks, Parker.

Operator: Our next question comes from Pete Heckmann from D.A. Davidson. Please go ahead. Your line is open.

Peter J. Heckmann

Analyst, D.A. Davidson & Co.

Q

Hey. Good morning. One quick one on transactional revenue. Can you give us a little bit more idea in terms of the breakdown there? Traditional bank [ph] aggregated (00:41:31) bill pay versus some of the maybe different types of transactional revenue, whether that be Biller Direct or some of the things coming from Helix and kind of how those growth rates differ between the two?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Yeah. Hey, Pete. Yeah. The majority of the transaction was still bill pay. Bill pay did decline year-over-year, which is why you saw it remain at 13%. Then you have other drivers in Jonathan's business that are hitting that from a transactional standpoint, and then there's actually some pass-through transactional revenue that's hitting the services and other line item as well.

So, when you see suppressed margins in that space, which you do in the filing, that's the biggest driver there, is that all – the pass-through transactional revenue that we're talking about, that does sit in other in the services, another line in the filing.

Peter J. Heckmann

Analyst, D.A. Davidson & Co.

Q

Okay. All right. And then just in terms of the bank M&A, I think you've given some updates in the past. But in terms of the M&A that has happened over the past 18 months, that you did indicate the one surprise of picking up an acquired customer – or picking up the [ph] acquirer (00:42:40). But on average, yeah, would you say you still feel like you're coming out on top in most of these mergers?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Yeah. I mean, just the Q1 numbers, I don't – David, I don't know if you have them in the script, and I can't remember – it was 2020 or 2021, we were on the acquiring side.

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

A

That's right.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

So, you're still talking numbers of – our customers are the ones that are doing the M&A. And I think we had – this is directionally correct – about 116 acquisitions in 2021 and 104, we were the acquirer or the MOE – or a part of the MOE. So, that momentum continue into Q1, which is I think 2020 or 2021, we were the acquirer or the MOE in it. So, just a testament to the client roster we have and their approach towards growth and how they're going to compete in this environment. So, we certainly hope that trend continues, and I don't know any reason why it wouldn't.

Peter J. Heckmann

Analyst, D.A. Davidson & Co.

Q

Great. Good to hear. Thanks.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Thanks, Pete. Have a great day.

A

Operator: Our next question comes from Joe Vruwink from Baird. Please go ahead. Your line is open.

Joseph Vruwink

Analyst, Robert W. Baird & Co., Inc.

Great. Good morning, everyone. And maybe wanted to go back to commercial solutions broadly, obviously talking about Catalyst a lot on the call. But can you talk about just the broader investment environment? It's always a priority for banks, but it does seem, just based on what we hear, to be getting more of a renewed focus in investment plans looking into FY 2023. Are you kind of seeing that show up in your pipeline? And if it does play out that way, how does Q2 stand up from a competitive sense?

Q

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah. I don't know, just take away from retail or the Helix business. But obviously those are things that we're investing in, and we compete favorably in those environments. On the retail side as well, a lot of really interesting things on that technology. But from a business perspective, we're seeing whether it's a credit union that is looking to get into business lending, operating accounts. Commercial banks obviously have – it's been their focus for a long time. And they have seen the power of using – digitizing the commercial experience. They've just not have the solutions to compete with the PNC, Bank of America, Wells, Chase, and Citi.

A

And so what we're doing is bringing a solution that's even broader than what they offer from a pricing perspective to a onboarding and then unifying an experience. It's not just retail, small business, commercial, ACH, wires, and tax payments. It's everything. It's the relationship. It's the tools they use to onboard these customers. And then we're beginning to see the power of Innovation Studio by incorporating products like Autobooks into the solutions, which is like an accounting software packaged for our customers.

And so the breadth of our offering, the modern technology that sits on a consistent experience across a mobile phone, a tablet, or a desktop; the fact that they can include retail digital banking with that, so they have a single platform to support with one set of logins, one set of integrations to the back end, one system to administer, one system to upgrade; all of those things are tailwinds for us as you see an environment where people are moving to digitize the experience with the customer, drive meaningful – use the data to drive meaningful solutions, security solutions, or even products for these customers. We're in a very unique position with the decisions we've made and the investments we've made in that technology to differentiate ourself against the competition. And I think you're going to begin to see that translate into the momentum we've talked about in the back half of 2022 and beyond.

Joseph Vruwink

Analyst, Robert W. Baird & Co., Inc.

Okay. That's great. And then, again, not to put you on the spot with a macro outlook, but clearly, a concern out there, particularly with the regional banks that were maybe due for a bit of economic slowing. I guess does that square with some of the things you're now bringing up? The fact that maybe Tier 2, Tier 3 is more slower to come back. They're now coming back now. And when they come back, they're transacting with Q2 in a really sizable way. Is that any indication or leading indicator of maybe what is expected into next year?

Q

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Let me just clear up that real quick. So, the Tier 1s were the ones that came off-line the fastest, and then it took them the longest to get back on. So, \$5 billion and above larger institution, they said in 2020, when the pandemic hit, we are going to stop. And then, it took them a while to get the engine fired back up. This is commentary from many quarters ago. The Tier 2, Tier 3 shut down at the same time, but they came back to life faster just because they're small organizations and they can get approval faster on those.

So, the Tier 1 opportunities are what have been opening up for us on the digital banking and the digital lending side because of those conditions I talked about: the increased rate – the rising rate environment, the lack of experience in that area, the importance of digitizing the digital banking experience – the digital experiences for commercial customers and consumers. So, I'm prognosticating on the macro environment is something that I'm proud – that I have no business doing. But I think the point I was making earlier is, even if it is a tough economy, digitizing the experience is how you're going to get efficiency out of your business. And so that's where the demand environment continues to pick up.

And also, the proven set of solutions that we have, the amount of volume, almost 20 million users on this application, and those users are actually probably more than 1 million, maybe 2 million businesses are on that application. So, I think you're going to continue to see a move towards – at the pace that we have, digitizing the banking experience.

I think if you – and this is me pontificating on my own views here, but I think one of the things that the market got wrong with Q2 was, they thought we were a pandemic trade. I actually think we're a reopening trade. Our customers had to go focus on taking care of the in-client, making sure that their customers were healthy and doing everything they could, but they saw the power of digital while they were off or they saw the weaknesses in the digital banking products that they had. And as the economy picked back up and it reopened, that's when our pipeline started to pick up, Q3 of 2021, Q4 of 2021. And then you see the momentum in Q1.

So, the reopening trade is really where we are, and we're going to see more momentum in that area, and I'm really encouraged by the activity, the pipeline being up, the deal count up, the activity being up. So, that's where we sit today and we think whether it's retail, small business, commercial, lending, deposit side, onboarding, acquisition, data, we're uniquely positioned to continue to capitalize on the market and the opportunity in front of us.

Joseph Vruwink

Analyst, Robert W. Baird & Co., Inc.

Q

Okay. Thanks for the clarification, Matt. I'll leave it there.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Thanks, Joe.

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

A

Thanks, Joe.

Operator: Our next question comes from Matt van Vliet from BTIG. Please go ahead. Your line is open.

Matthew David van Vliet

Analyst, BTIG LLC

Hey. Good morning, guys. Thanks for taking the question. Matt, you might have touched on a little bit of this, but maybe I'll – we'll get Jonathan to also pontificate around it. But as you look at sort of what you've built out between the Innovation Studio and kind of the more inclusive Helix Group there, are – especially on the Helix side, is this something you can go back to some of these enterprise banking customers that you've gotten in some lending relationships with and talk to them about launching some newer products, some digital-only interfaces, things of that nature. So, can you kind of take this whole pre-built platform to those guys? Are they doing some of that stuff internally and this really is more of an [indiscernible] (00:50:20) fintech type of singular focus?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah, Matt. I'll have – this is why I have Jonathan in the call with me. So, Jonathan, why don't you talk about that?

Jonathan Price

Executive Vice President-Emerging Businesses, Corporate & Business Development, Q2 Holdings, Inc.

Yeah. No. I think it's a very timely point because we are starting to see more and more and have conversations more frequently with our existing digital banking clients around that concept of a digital-only initiative. We think it is an interesting opportunity, and we certainly think that there's a lot of awareness right now of the strategic value of a cloud-based core and the cost advantages and the speed advantages that that brings to the FI to think about differently, if they want to launch a digital-only initiative at a target demographic quickly and cost effectively, as I mentioned. So, it is definitely something we're looking at.

Historically, that use case has been challenged by just the banks' ability to understand the differentiation between the traditional cores and what these cloud-based next-gen cores allow for from a banking functionality perspective. So, we're working through that now, but we do think it's actually going to open up a new market for us as we head in probably more towards the back half of this year and into 2023. But it's a good question because it's coming up now in a way that it wasn't 6, 12 months ago.

Matthew David van Vliet

Analyst, BTIG LLC

All right. Great. And then, Matt, you mentioned two of the large banks in Canada, but curious in terms of the international markets, maybe outside of the US and Canada. How are the lending solutions being sold there? How are they being presented? What's the traction been like? And are the buying patterns or decisions or overall kind of outlook any different than what you're seeing from some of the larger North American-based customers looking at those products as well? Thanks.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah. Matt, so on Canada, just to clarify, the top five banks all use our pricing tool in some form or fashion. So, we've done really well in Canada. We've seen Europe open up with a little bit of a hiccup based on what was going on with the war. Asia is picking back up again. Australia, I think they just raised rates again this morning or would have been this afternoon. So, you'll see the similar dynamics that we've talked about there. But we also have our finance customers over there.

The opportunity for us internationally from a pricing perspective comes from these large global banks that are going to begin to use these tools globally and spread the product, so it's an expansion opportunity within PrecisionLender and even Cloud Lending to some extent. So, we are hopeful that you'll see the international business pick up in the back half of this year. We've been pretty consistent with – I would say, patient with that space, and we'll continue to invest in that group. We have a great team in Europe. We have a great team in Australia that we're investing in. We were able to get the team out on the road to see them in Australia.

A couple weeks ago or a month or so ago, the team is fired up, and I think we're really focused on what we're doing. So, I think the – we have contemplated all of this into our guidance in 2022 and when we talk about 2023. So, it should be nothing but upside for us as we move forward with our solutions in Europe and Asia.

Matthew David van Vliet

Analyst, BTIG LLC

All right. Great. Thank you. Very helpful.

Q

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Thanks, Matt.

A

David Mehok

Chief Financial Officer, Q2 Holdings, Inc.

Thanks, Matt.

A

Operator: Our next question comes from James Faucette from Morgan Stanley. Please go ahead. Your line is open.

Q

Hi. Thanks for taking my question. It's [ph] Michael (00:53:45) on for James. I just wanted to quickly touch on some of the earlier comments that were made related to the conversations that you've been having with various FIs. So, I guess just in general, like, who is most likely to lean in in this environment? Are you seeing – or is there any notable takeaway in terms of bank and credit union size in terms of customer acquisition or who's sort of trying to re-engineer their tech stack, etcetera?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Yeah. I mean, [ph] Michael (00:54:17), I would say that if you look at what we – our solutions and who we've got and kind of a law of attraction that occurs within this business, and we've talked about it through the M&A numbers, is you look at a management team or an ownership group of a bank or a credit union – obviously, on a management team of a credit union, it's a group of folks who want to focus on growing the business both through organic growth within the customer base, and that means build using more products and digitizing it, and then also expanding through winning new deals in the marketplace, whether it's through commercial customers or retail customers. We've had a lot of success in launching programs with our customers to help them either gather deposits or to help them pick up new loan opportunities.

A

At the center of it is data where we have all of the data where there's behavioral data that occurs on the devices, transactional data that we use through the system to help our customers determine that. And so it's usually financial institutions that are viewing this as, they have no interest in selling, they're going to grow by organic growth within our customer base, they're going to win new deals in the marketplace, and they're probably going to go through M&A.

So, those are the people that we end up winning the most of, which is where you want to be. And I think what that translates to is, you're going to see a lot of our customers that are \$1 billion to \$5 billion become \$5 billion to \$10 billion banks in the next two to three years. You're going to see \$5 billion to \$10 billion banks become \$10 billion to \$20 billion banks. And that's the cadence that we've seen honestly over the last eight years of this business, but in particular since we went public in 2014.

So, we lean towards people that want to use technology as a weapon and not as a shield, and that's how we win the deals. And we're going to continue to approach those customers because we think they're the long-term winners in this marketplace.

Q

Very helpful. And then, Jonathan, I think last quarter, you mentioned the number of net new deals citing Innovation Studio as a differentiator. It was closer to 30% from memory, and it seems to have really inflected here to upwards of 80%. So, I guess, can you just quickly dig into the biggest factors that are driving that inflection? It seems to be a pretty big differentiator in some of your RFP activity.

Jonathan Price

Executive Vice President-Emerging Businesses, Corporate & Business Development, Q2 Holdings, Inc.

A

Yeah. I mean, we're just seeing it more than ever as a differentiating factor in these net new conversations with digital banking prospects. I mean, when you think about how it broadens the aperture of what our application can provide for both consumers and small businesses, it really does bring more value out of the gates. And when you're talking through that at the sales cycle and now with this enterprise selling motion that Matt talked about, we can really embed that value prop into the messaging from the beginning. And, again, it's wide. Like, when you think about the ability to bring small business applications that go beyond just what the bank is offering or what Q2 builds with our digital banking platform and really changes and helps run the small business, the value proposition is just deeper. And so we're seeing that become a conversation throughout these deals, and, yeah, north of 80% of the deals in this quarter cited that and took down the Innovation Studio as part of that deal, and cited it, as I said, as a differentiating factor that led to their decision.

So, I think it's a multitude of factors, and they're seeing what we really do expose the API docs and everything to everyone upfront. Everyone can see the menu of applications, the models that we're looking at, how self-service it is, and it's adding a lot of value to these discussions. So, whether 80% is the right barometer or not, that's certainly a high number and we'd love to see that continue. But we definitely think it's going to have an impact moving forward on our ability to win that new deals. But also, when we talked about how we grew the partner ecosystem by 25% in the quarter and over 50% of our bank's customers, existing customers, are now using at least one program, we expect this also to be very impactful to the existing customer base. So, that's the big opportunity for us as well.

Q

Very helpful. Thanks, everyone.

A

Thanks, [ph] Michael (00:58:16). I think we have time for one more.

Operator: Our last question will come from Charles Nabhan from Stephens. Please go ahead. Your line is open.

Charles Nabhan

Analyst, Stephens, Inc.

Q

Hi. Good morning, and thank you for taking my question. Wanted to get your comments on – some further comments on your implementation capabilities. Specifically, you've made some investments in the past year, and you obviously have a ramp-up in go-lives coming up. But just curious where you think you stand in terms of those investments, given the demand you're expecting over the next couple of years.

And secondly, given the uptick in go-lives expected in the second half of the year, could we anticipate a higher concentration in professional services revenue as a headwind to margins?

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Hi, Charles. I guess I'll take each one of those independently. So, yes, we did invest in implementation resources as we started to book some of those opportunities in the second half of last year, and that's continued to ramp. As we've been talking about throughout the morning, this morning, we've got a strong pipeline, not to mention the fact that we had a strong Q1. So, all of that leads to more implementations, not only the end of this year, but now into 2023. So, that is continuing to be a primary area of focus for us, and we're doing a great job of utilizing our resources currently and then adding new resources to make sure that we're hitting on-time deliveries for our customers.

In terms of the go-lives, over the course of the second half of the year, the way that we – the way that the revenue model works is, you're deferring all of the services costs that we're incurring during the course of that time, or most of them. I shouldn't say all, but most of them. And then once we go live, we end up starting to recognize that over the life of the deal. So, it includes the services costs, as well as the licensing costs. So, I would not anticipate you see an inordinate amount of implementation costs relative to the license fees. However, we also talked about Premier Services as being a larger mix of the business in our Investor Day back in December. That is something that you are starting to see in Q1 and continuously for the rest of the year. That's a very sticky business for us and one that we feel is very strategically important for our customer base.

Charles Nabhan

Analyst, Stephens, Inc.

Q

Got it. I appreciate the color. Thank you.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

A

Sure, Charles.

Operator: We have no further questions. I'd like to turn the call back over to the presenters for any closing remarks.

Matthew P. Flake

President, Chief Executive Officer & Director, Q2 Holdings, Inc.

Thank you, operator, and thank you, everybody, for attending today. We're obviously encouraged by what we've seen over the last couple quarters and are very optimistic about the back half of this year. Thanks, everybody, for attending, and we will talk to you for the rest of the quarter till we go quiet. Have a great day.

Operator: This concludes today's conference call. Thank you for your participation. You may now disconnect.

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