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NetApp, Inc. (NTAP)

Q1 2019 Earnings Call

CORPORATE PARTICIPANTS

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

OTHER PARTICIPANTS

Rod Hall
Analyst, Goldman Sachs & Co. LLC

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Srini Nandury
Analyst, Summit Insights Group

Kathryn Lynn Huberty
Analyst, Morgan Stanley & Co. LLC

Aaron Rakers
Analyst, Wells Fargo Securities LLC

Timothy Patrick Long
Analyst, BMO Capital Markets (United States)

Sherri A. Scribner
Analyst, Deutsche Bank Securities, Inc.

Andrew James Nowinski
Analyst, Piper Jaffray & Co.

Louis Miscioscia
Analyst, Daiwa Capital Markets America, Inc.

George Iwanyc
Analyst, Oppenheimer & Co., Inc.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Ananda Baruah
Analyst, Loop Capital Markets LLC

Nehal Sushil Chokshi
Analyst, Maxim Group LLC

Simon M. Leopold
Analyst, Raymond James & Associates, Inc.

Irvin Liu
Analyst, RBC Capital Markets LLC

Nikolay Todorov
Analyst, Longbow Research LLC

Eric Martinuzzi
Analyst, Lake Street Capital Markets LLC

Robert Cihra
Analyst, Guggenheim Securities LLC

Erik Suppiger
Analyst, JMP Securities LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon, ladies and gentlemen. Welcome to NetApp's First Quarter Fiscal Year 2019 Financial Results Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will be given at that time.

I will now turn the call over to Kris Newton, Vice President of Corporate Communications and Investor Relations. Ms. Newton you may begin.

Kris Newton

Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

Thank you for joining us on our Q1 fiscal year 2019 earnings call. With me today are our CEO, George Kurian; and CFO, Ron Pasek. This call is being webcast live and will be available for replay on our website at netapp.com.

In Q1, we adopted the new accounting standard, ASC 606. Our historical financial results have been restated to conform to the new accounting revenue recognition rules. Reconciliations of our previously reported GAAP results to the restated ASC 606 GAAP results, as well as our ASC 606 GAAP to non-GAAP results for fiscal 2017 and 2018 by quarter, are included in our Q1 earnings release, which is posted on our website, along with our financial tables and guidance, a historical supplemental data table and the non-GAAP to GAAP reconciliation.

As a reminder, during today's call, we will make forward-looking statements and projections with respect to our financial outlook and future projections, such as our guidance for the second quarter and full fiscal year 2019, our expectations regarding future revenue, profitability, cash flow and shareholder returns, and our ability to grow and expand our opportunities, all of which involve risk and uncertainty. We disclaim any obligation to update our forward-looking statements and projections.

Actual results may differ materially from our statements and projections for a variety of reasons, including global, political, macroeconomic and market conditions, and our ability to expand our total available market, introduce and deliver new and differentiated products and services without disruption, manage our gross profit margins, capitalize on our market position and cloud strategy, maintain execution and continue our capital allocation strategy.

Please also refer to the documents we file from time to time with the SEC and available on our website, specifically, our most recent Form 10-K for fiscal year 2018 and our current reports on Form 8-K. During the call, all financial measures presented will be non-GAAP and ASC 606, unless otherwise indicated.

I'll now turn the call over to George.

George Kurian

President, Chief Executive Officer & Director, NetApp, Inc.

Thanks, Kris. Welcome, everyone. Thank you for joining us today. We delivered a very strong first quarter and are starting fiscal year 2019 in a stronger position than we've been in for years. Revenue, gross margin, operating margin and earnings per share were all above our guidance. This performance reflects our success with customers who increasingly view us as a critical strategic partner for their data-driven digital transformation.

Enterprises see the value of our Data Fabric strategy and are signaling strong confidence in NetApp by making long-term investment in our software IP to enable the Data Fabric across their entire enterprise.

The world is being transformed by digital technology. To succeed in this data-driven economy and radically improve business performance, customers need real-time insights and secure access to their data, regardless of where it resides. The NetApp Data Fabric empowers our customers to do so, while taking advantage of capabilities in the cloud across multiple hyperscalers, operate with hyperscaler cloud-like infrastructure, and modernize traditional IT with flash and connections to the cloud. These capabilities underpin the biggest market transitions as customers shift to cloud, new forms of converged infrastructure, and flash. And we continue to expand our opportunity by innovating with the Data Fabric, broadening its reach by delivering the next-generation of flash empowered SAN and integration with the hyperscalers, as well as increasing its value with new applications and services such as artificial intelligence, machine learning and analytics.

We continue to deliver software differentiated innovation and maintain strong momentum across our key priority areas: all-flash arrays, new forms of converged infrastructure and cloud data services, which represents the biggest opportunities for NetApp to grow and reset the landscape of our industry.

The market transition to flash, which is still in the early stages, creates enormous new opportunity for us as we consolidate and displace competitors' legacy equipment, gain share in new workload deployments and upgrade our installed base with our cloud connected all-flash solutions.

At the start of Q1, we expanded our all-flash array innovation leadership with the introduction of the AFF A800, designed for high performance in cloud to power artificial intelligence and data-intensive applications like machine learning. The AFF A800 supports the industry's first end-to-end NVMe architecture, combining NVMe solid state drives with NVMe over Fibre Channels to deliver lightning fast response times. Based on the new SPC-1 benchmark results performed under real world conditions with deduplication and compression enabled, the AFF A800 is the top performing enterprise all-flash array among the industry's leading storage providers.

With the latest version of ONTAP, which we shipped during the quarter, we continue to expand our SAN technology leadership by delivering NVMe over Fibre Channel capability as a non-disruptive software upgrade on current generation AFF platforms. NVMe over Fibre gives customers the performance of server attached storage with all the benefits of shared network storage.

Our leadership in this area allows us to further expand our opportunity by displacing direct attached storage over time. In Q1, our all-flash array business, inclusive of All Flash FAS, EF and SolidFire products and services grew 50% year-over-year to an annualized net revenue run rate of $2.2 billion. Validating the innovation leadership and momentum of this part of our business, Gartner, again, recognized NetApp as a Leader in its Magic Quadrant for Solid-State Arrays.

Another way we are expanding our opportunity is through participation in the rapidly growing area of artificial intelligence. Earlier this month, we announced ONTAP AI, a solution combining NVIDIA DGX supercomputers and the AFF A800 to create a seamless data pipeline across edge, core and cloud for deep learning deployment. The unique scope and reach of the Data Fabric enables customers to lay down the right foundation to collect and bring together all their distributed data, and then, apply artificial intelligence and machine learning techniques to it. By helping customers unify all of their data for AI, we empower them to deliver better business outcomes. Enterprises are choosing our converged and hyper-converged solutions to build out their private clouds because they are simple, standardized and rapidly deployed.

FlexPod continues to be a platform for customer innovation and investment protection. In the first quarter, we announced new FlexPod solutions to simplify the delivery of cloud infrastructure and deliver focused industry-specific applications. With NetApp HCI, customers are able to accelerate digital transformation by developing a next generation cloud architected infrastructure that manages data and services as one integrated resource, supporting both public and private clouds.

A European-based financial services firm chose NetApp HCI to be the foundation for its private cloud. Our ability to provide a future proof platform to host current workloads and support future multi-cloud requirements enabled us to win against Nutanix. With cloud-like simplicity, NetApp HCI offers enterprises the ability to run multiple applications with predictable performance, as well as scale, compute and storage resources independently to avoid costly and inefficient overprovisioning, capabilities that the first generation HCI vendors cannot match.

Our Cloud Data Services partnerships with Microsoft, Amazon and Google are unique to the industry and are game changing for NetApp's long-term opportunity. Not only are we able to participate in enterprise workloads that are moved to the cloud, we can address born in the cloud workloads and customers. And our entire portfolio is made stronger by being cloud connected.

Five years of delivering ONTAP as software in the hyperscaler marketplaces has given us a unique understanding of the requirements in the cloud. We have identified how to deliver high performance, highly scalable cloud data services with a robust feature set and support for protocols that cloud does not natively provide. Because of deleveraging our R&D, we have been able to bring hundreds of engineers to bear on this problem without negatively impacting innovation in other areas of our business or expanding our OpEx stack.

Only NetApp has partnerships with all the leading hyperscalers and a complete cloud data services strategy for customers. In July, Microsoft announced the public preview of Azure NetApp Files, an Azure native service powered by NetApp technology, enabling enterprises to overcome the challenge of deploying file-based workloads to the cloud. Also in July, we announced expanded availability for NetApp Cloud Volumes for Google Cloud Platform to help customers deploy workloads such as DevOps, video rendering, databases and commercial high performance computing.

In Q4, we began onboarding customers with NetApp Cloud Volumes for AWS. To bring to life why a customer would choose NetApp in the cloud, I'll share with you two examples, one that is a cloud-only solution, and the other, a customer of our on-premises solutions expanding into the cloud.

The first is a large genomic information company that chose NetApp Cloud Volumes for AWS and plans to go live with NetApp services in other clouds. They selected us because our high performance, shared storage service enabled them to gain dramatic improvements in processing and complete analysis that they could never finish before, all while lowering their compute costs. They are recommending that their customers, pharmaceutical companies and hospitals, adopt Cloud Volumes. With Cloud Volumes, they offer consistent performance and advanced functionality while allowing their customers freedom of choice on the cloud.

The second example is a global fashion brand taking its first steps into the cloud. Because of our multiyear relationship with the customer, we were able to help them understand the value of our Cloud Data Services, while reducing their sense of risk. In addition to the purchase of SaaS Backup services from NetApp, they expanded their footprint of on-premises all-flash arrays.

Fiscal 2019 is a foundational year for the SaaS part of our business. And I'm pleased to report that based on Q1, our annualized monthly recurring Cloud Data Services revenue is approximately $20 million. We are transforming our business to reflect the way customers want to consume our technology. The world is steadily moving from being compute-centric to data-centric and customer consumption patterns are shifting from data center equipment to hybrid cloud services. Our competitors are struggling to adapt to the new cloud era and continue to fall behind.

With demonstrated leadership and key market transitions, we are reshaping our industry. We will share more industry-changing news with you at our Insight conference this October. Our results are evidence that we have the right strategy and are driving success with focused innovation and relentless execution.

As we continue to grow and transform, we will maintain our focus on efficiency and shareholder value. At our last Analyst Day, we laid out a compelling long term model and capital allocation plan. And as you can see by our strong Q1 results and capital returns, we are on track to deliver against this plan. I am honored, excited, and humbled by the opportunity ahead. I want to thank the entire NetApp team and our partner ecosystem for all they do to help drive our success.

With that, I'll now turn the call over to Ron to walk through our Q1 financial performance and go-forward expectations. Ron?

Ronald J. Pasek

Executive Vice President & Chief Financial Officer, NetApp, Inc.

Thanks, George. Good afternoon, everyone, and thank you for joining us. As a reminder, we adopted the new revenue recognition rules, ASC 606, this quarter. Our historical financial results have been restated to conform to the new accounting rules. Reconciliations of our previously reported GAAP results to the restated ASC 606 GAAP results, as well as our ASC 606 GAAP to non GAAP results for fiscal 2017 and 2018 by quarter are included in our Q1 earnings release. As a reminder, I'll be referring to non-GAAP results unless otherwise noted.

Our Q1 results reflect the increasing strategic importance of NetApp to our customers as they undertake digital transformations and embrace multi-cloud architectures. We expect continued progress throughout fiscal 2019 toward the long term business model we laid out at our Analyst Day.

Before discussing guidance, I'll provide detail on our performance for the first quarter. Net revenues of $1.47 billion grew 12% year-over-year driven by product revenue of $875 million, which increased 20% year-over-year. Product revenue came in higher than expected reflecting the continued strength of our all-flash array business as well as roughly $60 million from strategic enterprise agreements which we did not include in the Q1 guidance.

Enterprise License Agreements or ELAs are enterprise-wide deals where NetApp is a key strategic partner in implementing the customers' broader digital transformation. From a revenue recognition perspective, the new ASC 606 standard requires the software product component of ELAs to be recognized upfront. Under the old ASC 605 standard, these software licensing agreements were recognized ratably across the life of the deal, typically three years.

The increase in ELAs reflects our strategic presence within large global accounts and their strong confidence in the value of the NetApp Data Fabric. While a clear positive for our business momentum, the structure of these ELAs coupled with the upfront revenue recognition makes their financial impact lumpy and difficult to predict. We did, however, include about $30 million of revenue from ELAs in the guide for Q1.

Moving forward, we will continue to take a conservative approach in predicting the timing and size of these strategic deals. As such, we will not be including ELAs in our guidance for Q2 nor the remainder of fiscal 2019.

Moving down the P&L, software maintenance revenues of $229 million increased 3% year-over-year, reflecting traction of our Cloud Data Services portfolio and continued growth in our installed base. Hardware maintenance and other services revenues of $370 million were flat year-over-year.

As a reminder, we said that the combination of software and hardware maintenance revenues should not be a headwind in fiscal 2019. Gross margin was 66%, above the high end of our guidance range. Product gross margin of 56% increased six points year-over-year reflecting the benefit from the software portion of the ELAs and continued sales force discipline.

Excluding ELAs, product margin was approximately 51%, up 1.5 points year-on-year. Hardware maintenance and other services gross margin was up two points year-on-year due to the benefits from ongoing transformation efforts.

Operating expenses of $650 million were in line with our expectations. We remain committed to strong OpEx discipline and expect operating expenses for fiscal 2019 to be roughly flat year-over-year. Operating margin of 22% was above our guided range. We had a strong start to the capital allocation plan we announced at our Analyst Day.

During the quarter, we repurchased 6.7 million shares at an average price of $74.37 per share for a total of $500 million. Weighted average diluted shares outstanding were 269 million, down 4 million sequentially and 9 million year-over-year. EPS of $1.04 was up 75% year-over-year, predominantly driven by the healthy growth in product revenues and expansion in product gross margin.

We closed Q1 with $4.8 billion in cash and short term investments. Similar to Q4, we again saw healthy growth in deferred and financed unearned services revenue, which increased 4% year-over-year. During the quarter, we paid out $105 million in cash dividends. Our fiscal Q2 cash dividend of $0.40 per share is payable on October 24.

As highlighted at our Analyst Day, we remained committed to increasing our dividend over time. Our cash conversion cycle of negative 20 days improved 28 days year-over-year, reflecting a 23-day increase in days payable outstanding and an 8-day decrease in days inventory outstanding, partially offset by a 1-day increase in DSO. DSO decreased by 20 days sequentially from Q4.

We had another outstanding quarter of cash generation with cash flow from operations of $326 million, an increase of 30% year-over-year. We generated strong free cash flow of $262 million in the quarter, which represented 18% of net revenues and as an increase of 22% year-over-year.

Now onto guidance. To clarify, we remain confident in our mid-single digit fiscal 2019 revenue growth forecast before any benefit from Q1 ELAs or any additional ELAs we may realize throughout the year. In addition, we are raising our guidance for fiscal 2019 margins and EPS to reflect the better than expected Q1 results. Gross margin guidance increases to 63% to 64%, up from 63%. And operating margin guidance increases to approximately 22%, up from 20% to 21%.

In fiscal 2019, we are now committed to delivering EPS growth in the mid-20s versus the original guidance of greater than 15%. Our fiscal 2019 effective tax rate of approximately 18% remains unchanged. We expect to continue to generate meaningful free cash flow in the range of 19% and 21% of revenues enabling our disciplined approach to investing in growth as well as our continued commitment of returning significant capital to shareholders. We also remain confident in our long term three-year growth forecast for revenue and profitability.

Now onto Q2. As a reminder, Q2 guidance excludes any benefit from ELAs. We expect net revenues to range between $1.45 billion and $1.55 billion, which at the midpoint imply a 6% increase year-over-year including more than 0.5 point of currency headwinds. We expect Q2 consolidated gross margin to range between 63% and 64%. We expect fiscal Q2 operating margin to range between 20% and 21%. We expect earnings per share for the second quarter to range between $0.94 and $1 per share.

In summary, I am confident regarding our growth opportunities especially as it relates to our compelling cloud strategy. Additionally, I'm very pleased with the disciplined execution of our team. We are well-positioned to continue to deliver on the commitments we've made to our shareholders, partners, and customers.

With that, I'll hand it back to Kris to open the call for Q&A. Kris?

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

We'll now open the call for Q&A. [Operator Instructions] Thanks for your cooperation. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Rod Hall with Goldman Sachs.

Rod Hall
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. Hi, guys. Thanks for the question. I guess I wanted to dig into the product gross margins which are quite stronger than we expected them to be and see if you guys could tease out maybe what some of the moving parts there were. So in other words was NAND price declines, did that help the margins, are there mix effects going on, just maybe give us a little more color on what drove those strong margins? Thanks.

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

So Rod, I think it's a couple of things. Obviously, it was the benefit of the ELAs this quarter. That was about two points when you do the bridge year-over-year. We also had a little bit of favorable FX and we had a little higher software mix this quarter. The NAND pricing definitely did help a little bit but it gets offset when you have to take the hit to reval. So there might have been some benefit initially but then you have to write the inventory down as the standard decreases.

Rod Hall
Analyst, Goldman Sachs & Co. LLC

Q

[ph] And could you just (24:14) say on that front are you passing NAND pricing through pretty much or what's your thinking on that as we go on through the rest of the year?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

Our intent will be to eventually pass on the price decreases, yes.

Rod Hall
Analyst, Goldman Sachs & Co. LLC

Q

Great. Okay. I appreciate it.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thanks, Rod. Next question?

Operator: Thank you. Our next question comes from Mehdi Hosseini with SIG.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

Yes. Thanks for taking my question. Just when you look into January and April quarter of next year, and I'm not asking for any guide. I just want to see what your views are in terms of the continued upgrade that is going on within your enterprise customers. This has proven to be a multiyear upgrade cycle. And I want to see how much – how do you see this upgrade cycle sustaining beyond the October quarter that you just guided to? Thank you.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

We see that enterprise IT spending, as you have noted, is benefiting primarily from the strength of the global economic outlook. IT spending we've always believed is correlated with economic outlook. Within that, we benefit from a few different specific situations relative to our business. From a portfolio technology perspective, we have shifted our investment and our portfolio and consequently our revenue mix into high growth areas of the market. We see that we can benefit uniquely when customers spend either on the public cloud or on-premises unlike competitors that we have that remain only on-premises.

And finally, as businesses become more data-intensive and build more data-intensive environments like machine learning, high performance storage and data services are benefiting from spending intentions. So we think that this will continue for a period of time. I think at the macro level, I see spending will be correlated to economic growth. So as economic growth slows down, I think it will impact IT spending in aggregate.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Mehdi. Next question?

Operator: Thank you. Our next question comes from Srini Nandury with Summit Insight (sic) [Insights] (26:38) Group.

Srini Nandury
Analyst, Summit Insights Group

Q

All right. Thank you for taking my question. On the AFA sales, can you give us some color what percentage of your installed base has already moved to the new AFA? And then can you also give some color in terms of competition and unit pricing in general? Thank you.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

AFAs are now 14% of our installed base so it still remains a small percentage of the installed base. As we said, we have continued to gain share in the market and outpace the overall market. This is the 15th consecutive quarter of market outperformance and reflects the strength of our offering. Relative to competition, I think we see the broad mix that's available in the market, Dell, HP, Pure, and Nutanix are the most common ones. I think we have a really good competitive position against all of them both because of the capabilities of our specific solutions as well as the unique benefit we bring by allowing customers to deploy our solutions on the public cloud or in their data center something that we call the Data Fabric. So our win rate has been strong and we're excited to expand the range of competitive situations we engage in.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Srini. Next question?

Operator: Thank you. Our next question comes from Katy Huberty with Morgan Stanley.

Kathryn Lynn Huberty
Analyst, Morgan Stanley & Co. LLC

Q

Thank you. Good afternoon. Just a quick clarification and then a question. On the clarification, I believe the prior EPS guidance of 15%-plus reflected no assumption around share repurchase, just curious whether the mid-20% EPS guidance does include buyback or not. And then secondly, can you just give us some guardrails around what you expect in terms of range of potential outcomes for ELAs in future quarters? Will there be quarters with zero ELA revenue and then quarters like July where it could be $50 million to $100 million? What's sort of the range of outcomes as we think about modeling that through in the next couple of quarters?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

Sure. Katy. To answer the first part of your question, we assumed the guide for EPS assumes no further share repurchase. So it's just what we've done in Q1 and the benefit of that from a diluted share comp perspective.

Secondly, with respect to ELAs, it's really difficult to predict when it will happen. And to your point, yes, there will be quarters when they will be zero which is precisely why I said I would not guide them. Even when you think you might get one, it's hard to predict and the timing is very difficult. And they're so large that if you include it and you miss it, it would be a big miss. I'm trying to think of – was there one other part?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

This is why I think, as we've laid out the plan for the year, we are reconfirming that our revenue outlook is mid-single digits without ELAs. ELAs would be additive to the revenue baseline that we have established. And so you should think about it we're essentially guiding upward for the rest of the year.

Kathryn Lynn Huberty
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Understood. Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Katy. Next question?

Operator: Thank you. Our next question comes from Aaron Rakers with Wells Fargo.

Aaron Rakers
Analyst, Wells Fargo Securities LLC

Q

Yeah. Thank you and thanks for taking the question. Yeah. I wanted to ask about the HCI product. I think one of the pieces of the story has been the strong growth that you've been able to report quarter-after-quarter in your flash business. I'm curious as we think about HCI and the competitive landscape against Nutanix and others, is that an incremental revenue stream that we could look at over the next couple of quarters that starts to get broken out? And is there any framing or any kind of qualitative or quantitative commentary you can provide of how big that business is today? Thank you.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

With regard to whether we will breakout HCI or not, we'll provide you that clarity when we do it. At this point, HCI is a part of our product revenue. We have seen a broader number of competitive engagements. And we are winning our share, right? So we feel very confident about the value proposition that we bring to the market. We see that it's a meaningful expansion of the total addressable market that we serve. And we are going to continue to stay focused on innovation and customer expansion. We've had good competitive wins against all the leading competitors in that category. And it reflects the architectural difference that we bring to enterprise-grade hyper-converged. And so we'll give you more details. Come to NetApp Insight. We have some really exciting product announcements at NetApp Insight. And you will see how we build NetApp HCI into our compelling Data Fabric story there. So look forward to it.

Aaron Rakers
Analyst, Wells Fargo Securities LLC

Q

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Aaron. Next question?

Operator: Our next question comes from Tim Long with BMO Capital Markets.

Timothy Patrick Long
Analyst, BMO Capital Markets (United States)

Q

Thank you. Just one and a follow-up, if I could. First on the Cloud Data Services, thanks for providing the run rate there. I think the thinking – the logic was this could add something like 100 basis points of growth this year. Could you talk a little bit – would have to ramp from these levels, could you talk a little bit about the pipeline and how quickly you think this business could ramp?

And then second, just some clarification on the ELAs. I get the difficulty to predict. But could you talk a little bit about the other benefits whether it's increasing installed base, more equipment sales that are ancillary benefits of these larger strategic deals that you're signing? Thank you.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

Let me just start with the Cloud Data Services business outlook. As we said, we are off to a good start. We're excited about the value we bring to customers. We talked about both cloud native customers we've never served, as well as expanding our footprint with both – with enterprise customers we've served in the past. And both of those opportunities are in front of us.

With regard to the availability of our offerings, as we said, we are generally available with AWS. We are in private preview with Microsoft and we are in pre-beta with Google. So we are in an early stage of customer trials. All of these offerings should be generally, commercially available this quarter. So you'll see much broader availability of those offerings this quarter. And the pipeline's healthy. We are excited at what we see going forward in terms of the use cases, DevOps, analytics, as well as database-as-a-service on the public cloud.

With regard to the ELAs, let me just say that I've been involved in these transactions. As Ron mentioned, they are strategic relationships with the largest customers in the world where they standardize on our software across a broad part of their enterprise. It is a validation of the strategic value of our NetApp Data Fabric that customers are buying into a broad footprint standardizing on the Data Fabric. But as Ron mentioned, these are complex transactions where they can shift between CapEx and an ELA and a variety of different structures within the ELA.

One of the things that you see with this year's ELA form is that our operating system is now a standard part of the ELA which is an indication that our Data Fabric now becomes seated in a very large footprint in the biggest customers in the world. And so we are excited. We think this is bullish for NetApp. And Ron can tell you more about how we think about it specifically in terms of the financial aspect of our business.

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

Yeah. I think it is a validation of our technology. It's something that we're really happy about. They are long-term commitments and agreements with these customers. And just to give you a little perspective, they've really grown when we started adding the OS portion into the ELA offering. Last year, when we did the restatement in FY 2018 for ASC 606, the full year was only $20 million in ELAs. So growing now to at least $90 million just in Q1, you can see it's a big uptick, so very, very important. It will make our results from time to time within the year a little lumpy. So you could see a little more volatility in gross margin but over the long term, really no effect.

Timothy Patrick Long
Analyst, BMO Capital Markets (United States)

Q

Thank you.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

It also doesn't change the fundamental seasonality of our business, right?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

Right.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

I think it just reflects the nature of transactions that are lumpy and hard to predict. But it doesn't change the fundamental seasonality of our business.

Timothy Patrick Long
Analyst, BMO Capital Markets (United States)

Q

Okay. Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

All right. Thank you, Tim. Next question?

Operator: Our next question comes from Sherri Scribner with Deutsche Bank.

Sherri A. Scribner
Analyst, Deutsche Bank Securities, Inc.

Q

Hi. Thank you. Just thinking about the gross margin guidance for the full year, it seems pretty low considering how high margins were this quarter. I understand the ELAs helped significantly in the quarter. But how should we think about margins rolling through as we move through the year?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

So what I did, Sherri, was I kept the same guide we had previously and gave at Analyst Day for the year and simply added the benefit of the Q1 overachievement. Nothing else has fundamentally changed to George's earlier point. The underlying seasonality is still the same.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

I think one thing to note, Sherri, is that our product revenue is growing much strong – much faster than service revenue. So if you model it on a year-on-year compare, the mix continues to favor product which is at a lower gross margin than services, right? And so we continue to push towards the long-term commitments that we have made around product gross margins in the 55% range. We're making progress, but it's the mix of product and services that are affecting the full year gross margin picture.

Sherri A. Scribner
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thanks, Sherri. Next question?

Operator: Our next question comes from Andrew Nowinski with Piper Jaffray.

Andrew James Nowinski
Analyst, Piper Jaffray & Co.

Q

Great. Thank you and nice quarter tonight. I just wanted to get more color on your AFA growth rate. So you're the only vendor shipping an end-to-end NVMe solution right now and you're the only vendor that separated your hardware from software enabling customers to support hybrid cloud environment. And you also have the HCI option. So I'm wondering is the acceleration in your AFA growth rate from just – more from just existing NetApp customers that converted to all-flash this quarter? Or is that the additional offerings like HCI and the cloud services that you have, did that alter your win rate versus vendors like Pure Storage and EMC that don't have those offering or all of them to accelerate your new customer growth?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

I think if you look at the installed base penetration of AFAs, they're at 14%, which is a small number. This represents the fact that the majority of our wins are in new workloads at existing customers or net new customers. The strength of our hybrid cloud story is a major part of our value proposition because, simply speaking, we allow customers to do what no one else can. You can start to build a high-performance machine learning environment in the public cloud and when you're comfortable with doing so, you can move it on-premises with your data completely intact and secure or conversely, you can build a secure data lake in your own data center and give your data scientists public cloud workspaces that are compliant with GDPR regulations.

So we have a really unique value proposition in the marketplace. With end-to-end NVMe, we are also able to attack – direct attach server workloads because we offer the same performance of server connected storage with all the benefits of shared network storage, efficiency, single point of management, better fault tolerance and so on. And so that's an additive part of the market that we are able to go after.

And then with the broadening of our portfolio across flash, converged, hyper-converged and cloud, we are now able to address a full platform of customers' use cases. And the strategic ELAs that customers are signing with us is simply the reflection of the elevation of our value proposition with them. And so we are excited at what that means in terms of the traction of the Data Fabric, not only with the hyperscalers but now with our largest customers in turn.

Andrew James Nowinski
Analyst, Piper Jaffray & Co.

Q

Great. Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thanks, Andy. Next question?

Operator: Our next question is from Lou Miscioscia with Daiwa Capital Markets America.

Louis Miscioscia
Analyst, Daiwa Capital Markets America, Inc.

Q

Yeah. So, thanks for taking my call. So, just two quick questions, the first one is on guidance. I know that you're actually guiding to mid-single digits year-over-year growth. But I guess last quarter, you did also talk about sequential growth. And if I look at my model, if I'm modeling this correctly, if you actually grow sequentially at a normal, let's call it, 5% or 6%, you should actually be at the high end of the range. So maybe you can give us just some puts and takes and thinking as to why from a quarter-to-quarter basis the guidance [ph] isn't (41:12) a bit higher here? And congratulations, obviously, on good numbers.

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

Yeah. So Joe (sic) [Lou] the – as I said earlier, the benefit in Q1, we had a large ELA benefit that blew away the guide we gave for the quarter. The underlying seasonality is still there. As I tried to indicate, the ELAs will make some of the seasonality a little more lumpy. So you're right, sequentially, it is down from Q1 to Q2. However, Q2 guide that we gave is up year-over-year at least 6% with a little bit of currency headwind. So you're going to see a little bit of some anomalies as we go forward. When we have these ELAs, they're going to make things a little bit less predictable.

Louis Miscioscia
Analyst, Daiwa Capital Markets America, Inc.

Q

Okay. Great. Thank you. And in the press release, you did mention StorageGRID twice. I'm just wondering if that product is starting to see traction in the sense that object storage has been a little bit slow to take off and, obviously, you're doing so well in some of the other areas. But it'd be nice to get a little visibility here.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

StorageGRID is now a recognized leader in object storage. We see a range of use cases for StorageGRID either for new object deployments or coupled with the file system as an archival tier using our FabricPool technology. We will provide more details of the applications of StorageGRID at our Insight User Conference. There are some interesting use cases for automotive and some other IoT examples where a highly scalable solution like StorageGRID has really interesting applications. I will tell you more at Insight.

Louis Miscioscia
Analyst, Daiwa Capital Markets America, Inc.

Q

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Lou. Next question?

Operator: Our next question is from George Iwanyc with Oppenheimer.

George Iwanyc
Analyst, Oppenheimer & Co., Inc.

Q

Good. Thank you for taking my question. George, your mature products are doing very well. Can you give us a sense of what's driving the strength there and how sustainable the outlook is?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

So as we've said, the headwinds from mature are – have dissipated. The mature product category used to contain three components, OEM, our legacy 7-Mode Technology and add-on storage driven either by 7-Mode or our clustered storage system in all-flash arrays. OEM has done its – has had a good quarter. It can be lumpy through the course of the year depending on the performance of our OEMs. But we had a strong quarter this quarter. 7-Mode is basically not being sold anymore, so it's no longer relevant to our business. And add-on storage had a strong quarter, reflecting the strength of our all-flash array business.

So, what I would tell you is categorizing mature and strategic as separate items is no longer relevant, right, because a large part of the mature business is now being driven by the strength of our strategic products. And so, I think that a better way to look forward is just to look at the aggregate product revenue, which you can see, is very strong. We don't think that mature is going to be a headwind anymore, and as we said last year, could be also a tailwind to our position this year. And so, we're excited at the start. We think that we should continue to see good progress in the mature bucket.

George Iwanyc
Analyst, Oppenheimer & Co., Inc.

Q

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, George. Next question?

Operator: The next question is from Jim Suva with Citi.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you very much, George. The all-flash array traction you have has been absolutely fantastic. It's, as you know, a very dynamic marketplace where a lot of up and coming companies have claimed victory and going to really disrupt things. Yet, some of the more traditional companies who've been innovating [ph] to kind of (45:16) like yourself have continued to gain share and knock them off, so to speak. Can you talk a little bit about the all-flash array landscape and how you see it? Is there still a lot more new startups innovation? Do you think it's going to be a consolidating market? How should we view it? I assume that large corporations want established companies such as yourself and others. But can you just walk us through about the all-flash array from where you sit as CEO the marketplace you see?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

We see that – first of all, the core value in the all-flash array market is in world-class software that allows customers to deploy a range of media but to drive their business process for advantage, right? And I think we have really good software and I think any other company that wants to compete in that market has to have really good software.

We see that the 3D NAND environment will continue to materially benefit flash over performance drives over the next few years. As we have said consistently, as prices ameliorate for 3D NAND, which we are starting to see clearly, that performance drive, the [ph] 10K (46:30) drive segment will concede to the all-flash array segment. There are future derivatives of flash, capacity flash or things like persistent memory optane DIMM for which we have really good solutions for, and I think we feel that what customers will need is a single way to manage your data across not only all these types of media, but all the places you put data in, which we call the Data Fabric, right?

I think the legacy competitors are in a variety of states of challenge. I think if you look at the large players like EMC or HP, they're still trying to rationalize their lead flash portfolio because none of their products is complete. If you look at players like IBM and Hitachi and Fujitsu and Oracle, they're basically conceded and are no longer in sort of new deployment considerations. They are essentially defending the installed base, and the startups are challenged. They have essentially did fast on product innovation and they don't have the market reach to compete. So, it will be – I see some sense of consolidation coming up in the marketplace and we will benefit from that because we're very well-positioned. It's a matter of keeping your head down and executing and that's what we're doing.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you so much for the details and clarifications.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Jim. Next question?

Operator: Our next question comes from Ananda Baruah with Loop Capital.

Ananda Baruah
Analyst, Loop Capital Markets LLC

Q

Hi, guys. Congrats on the solid results. Hey, if in case I missed it, have you yet begun to see a positive benefit in your all-flash array sales from NAND ASP declines? And then, can you just quickly give us an update as you yet begun to see inside of Cloud Data Services, the Cloud Data Services customers come back to you kind of almost as you – well, [indiscernible] (48:37) come back [indiscernible] (48:39) I look at your hardware products after getting a phase of Cloud Data Services? Thanks.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

On the benefits of NAND price decline, we've seen a little bit. I think you will see the mix shift from hybrid flash to all-flash, right? We have said that as the prices went up, we saw a mix shift towards hybrid disk flash systems. You are starting to see the early reversal of that trend back in the all-flash arrays. And I think over the next few quarters, there's no question that we see all-flash arrays become a bigger part of our mix.

With regard to the CDM buyers, there are customers that have got our Cloud Data Services in one cloud provider that are looking to now expand it to another cloud provider as a multi-cloud strategy. There are also customers that have started out with workloads in the public cloud that are coming back to an on-premises environment as a complement, right? So, we have seen a range of competitive displacements where we start to dialogue with the customer in the public cloud for use cases like DevOps and DR that then come back and buy a complementary production environment in their primary data center.

So we're seeing both, multi cloud as well as on-prem extensions, and we're excited at the prospect of using CDS to drive our overall portfolio.

Ananda Baruah
Analyst, Loop Capital Markets LLC

Q

Do you think that can become material over time that sort of reference pipeline there?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

We've said that CDS itself would – in our long-term guide, we said it would be between$ 400 million to $600 million on an annual recurring run rate by the end of fiscal 2021, right? So that, in and of itself, is a material add to our portfolio. This year, we said it contribute an incremental 100 basis points. I think that in terms of its strategic value to customers, it is reflective of the fact that we are outperforming virtually everybody in virtually every segment we compete in. This idea of a hybrid cloud Data Fabric lifts all of the pieces of our portfolio in competitive situations.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Ananda.

Ananda Baruah
Analyst, Loop Capital Markets LLC

Q

Thanks so much.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Next question, please?

Operator: Next question is from Nehal Chokshi with Maxim Group.

Nehal Sushil Chokshi
Analyst, Maxim Group LLC

Q

Yeah. Thank you and congratulations on great results. That sounds like that was a really massive ELA. Is that fair to say that was the biggest ELA signed in NetApp's history?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

So Nehal, it was actually several. That was more than just one. There were probably a half a dozen in that number, which is why it's difficult to predict.

Nehal Sushil Chokshi
Analyst, Maxim Group LLC

Q

Okay. And what were the products that were included within that ELA, other than the operating system SKU?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

It's standardizing on our operating system and software. It's a broad range of offerings. Everything in our portfolio could be bought against that ELA as part of consumption of capacity. So, these are strategic agreements to standardize on our Data Fabric. You typically recognize the software component upfront and there's a commitment to buying forward capacity and customers consume that capacity over time. So, it's – we're excited. These agreements help lift all the elements of our portfolio going forward.

Nehal Sushil Chokshi
Analyst, Maxim Group LLC

Q

And that $20 million in run rate of Cloud Data Services, what percent of that came from the ELAs?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

None.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

All right. Thank you, Nehal.

Nehal Sushil Chokshi
Analyst, Maxim Group LLC

Q

Okay. Great.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Next question?

Operator: Thank you. Our next question comes from Simon Leopold with Raymond James.

Simon M. Leopold
Analyst, Raymond James & Associates, Inc.

Q

Great. I first wanted to follow-up on the ELA contribution effort. Just to clarify, was that a significant portion of the reason mature products were up 15% year-over-year? You've talked a little bit about that but just want to see if the ELA was a contributor to that. And then, in terms of the bigger trending question, I wanted to see how you thought about the use cases for NVMe. And one of your competitors talked about a much broader set and claims that most of your market has very narrow use cases. Can you talk about the opportunities and applications that you see for NVMe? Thank you.

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

So, none of the ELAs are immature. There's really only two things immature, which is add-on business and OEM. So, all of the ELAs are in strategic.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

With regard to NVMe, it's essentially a broad range of use cases where the customer wants really fast, meaning, very low latency for their applications. The most common ones are high performance databases. It could be, for example, where somebody wants to go to a shared storage array rather than using a solution like an Exadata or a Database Appliance, right? And so, that's where we see the early opportunities to position the solution.

Simon M. Leopold
Analyst, Raymond James & Associates, Inc.

Q

And does that include the artificial intelligence that you were talking about? Is that sort of a classic use case?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

It could be a service that's applied to a data-intensive environment like a database or an artificial – or a data lake for machine learning. So, those are some of the examples.

Simon M. Leopold
Analyst, Raymond James & Associates, Inc.

Q

Great. Thank you for taking my questions.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Simon. Next question?

Operator: The next question is from Amit Daryanani with RBC Capital Markets.

Irvin Liu
Analyst, RBC Capital Markets LLC

Q

Hi. This is Irvin Liu dialing in for Amit. Now that you're in the October quarter, can you share with us any thoughts on what U.S. federal government budget flush dynamics are going to look like for you, especially given expectations for increased government IT spend in calendar 2018?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

We have modeled a fairly typical year-end budget flush for the public sector, U.S. public sector.

Irvin Liu
Analyst, RBC Capital Markets LLC

Q

Got it. Thanks. And just a quick follow-up then, I have another question about your hardware and software maintenance businesses. You indicated that these businesses shouldn't be a headwind for you in fiscal 2019. Any thoughts on why maintenance shouldn't be a contributor to growth, given recent quarters of product revenue strength and then you also have net new revenue streams such as Cloud Data Services coming online?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.

A

Yeah. Irvin, just to be clear, we indicated it would not be a headwind to growth. So, it should actually be a contributor as the installed base continues to grow. We just don't guide that piece discretely.

Irvin Liu
Analyst, RBC Capital Markets LLC

Q

Got it. Thanks. That's all I had.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

All right. Thank you, Irvin. Next question?

Operator: Our next question is from Joe Wittine with Longbow Research.

Nikolay Todorov
Analyst, Longbow Research LLC

Q

Hi. Thanks for taking the question. This is Nik Todorov on behalf of Joe. From a strategic point of view, do you see the need to have a composable architecture in your portfolio? And how would you juxtapose that architecture with your HCI offering, which, I think, has some similarities in terms of resource scaling?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

Yeah. I think there's a variety of terms. I think the customers want simplicity of their architecture and they want to be able to, at least, in our belief, not be tied into monolithic scaling of compute and storage, right, that the early vendors in HCI had. And so, different people call things differently. Our solution has many of the elements of composable in it. And so, we feel very good about the positioning of our solution. What we have seen with our customer wins is a reflection of the value of that particular aspect of our architecture.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Joe (sic) [Nik].

Nikolay Todorov
Analyst, Longbow Research LLC

Q

Thank you.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you. Next question?

Operator: Our next question comes from Eric Martinuzzi with Lake Street.

Eric Martinuzzi
Analyst, Lake Street Capital Markets LLC
Q

Yeah. I wanted to revisit the buyback. You spent $500 million this quarter on share repurchases. Could you recap there what's the amount and timeline remaining here?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.
A

So, we have $3.5 billion left to go and I'm giving no indication of the timing. As I said at Analyst Day, I'll give you how much we repurchased on calls like this after [indiscernible] (57:51).

Eric Martinuzzi
Analyst, Lake Street Capital Markets LLC
Q

And then, as far as the current share price, is it opportunistic purchases or do you have a [ph] certain (58:00) amount per quarter?

Ronald J. Pasek
Executive Vice President & Chief Financial Officer, NetApp, Inc.
A

We are – we do opportunistic. We don't do any accelerated share repurchase. We tend to take advantage of dislocations.

Eric Martinuzzi
Analyst, Lake Street Capital Markets LLC
Q

Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.
A

Thanks, Eric. Next question?

Operator: Our next question is from Rob Cihra with Guggenheim Partners.

Robert Cihra
Analyst, Guggenheim Securities LLC
Q

Hi. Thanks very much. Just wondering with flash prices starting to decline again, are you seeing – or perhaps what you think your customers are going to do in terms of like elasticity of demand? I mean, do you expect people to buy more capacity now for the same dollar amount or same capacity at a lower price? Just wondering how you maybe expect that to play out. Thanks.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.
A

I think they will clearly shift the mix from hybrid flash systems to all-flash systems. I think that we saw the reverse trend happen as prices went up. So, it's not like people will spend less. They will just spend the project amount and buy more flash as opposed to disk to consume that budget.

Robert Cihra
Analyst, Guggenheim Securities LLC
Q

Okay. But do you think the amount of capacity of flash they buy, does that change or do you think it's their -like are they're looking for a particular capacity of flash or a dollar amount of flash? I'm just curious if that helps or...

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

They're based – at least, based on what we saw last year, we saw people have a dollar amount and then buy the capacity associated with that. So, they would buy x percentage of flash and y percentage of disk. I think that x was smaller last year than it would be this year. And it will be – y will be smaller this year than it was last year. So, we saw what – customers had a project budget and they would spend it and they would optimize the ratio between flash and disk, and we see that going in favor of flash for the next several years now.

Robert Cihra
Analyst, Guggenheim Securities LLC

Q

Great, great. Great answer. Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

Thank you, Rob. Next question?

Operator: Thank you. And our final question comes from Erik Suppiger with JMP Securities.

Erik Suppiger
Analyst, JMP Securities LLC

Q

Yeah. Just staying on the flash pricing theme, can you just comment how much pricing has come down in terms of your sale price and how much you think that could still come down?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

We don't communicate exactly how and when we pass through savings to customers. As I said, we were the first to raise prices in the market and we are not going to be the first to lower prices in the market. We have a differentiated offering and we are looking to maximize the value that we get for our offering. We have done so in the gross margin trajectory, on product gross margin this quarter, and you'll continue to see us stay disciplined on it. I'm not suggesting that we will never lower the price but I'm suggesting that we're not going to be the first to do so. And we monitor the competitive landscape. We monitor what other people are selling and we'll make the right choices at the right time.

Erik Suppiger
Analyst, JMP Securities LLC

Q

Do you reduce pricing when you see others that are discounting more aggressively or what prompts the – you to make the change?

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

A

Every deal can be competitive. We will make the right tradeoffs between whether we see this to be a strategic account that we want to capture with this – whether this is a broad-based market shift. And it's called market and competitive intelligence that we are highly disciplined about. We have a good read on the market. We have a lot of customer interactions that give us that information, right? And so, as I said, we have a clear interest in extracting as much value for our technology as we can and that value is embedded in the performance and the software capabilities of our systems. And so, we'll be judicious about how we pass through savings to customers. Yes, commodity savings, the philosophy has been that we pass it through but we can time how we do that.

Erik Suppiger
Analyst, JMP Securities LLC

Q

Very good. Thank you.

Kris Newton
Vice President-Corporate Communications & Investor Relations, NetApp, Inc.

A

All right. Thank you, Erik. I'll pass it back to George now for some final remarks.

George Kurian
President, Chief Executive Officer & Director, NetApp, Inc.

Thanks, Kris. We delivered a very strong start to the year and introduced substantial innovation across our portfolio, expanding our industry-leading Cloud Data Services and introducing new partnerships, products and solutions to help data-driven organizations thrive. With our compelling Q1 results and expectation for the remainder of the year, we are off to a strong start in delivering against the long-term model we laid out at our Analyst Day last April.

We raised fiscal year 2019 guidance for gross margin, operating margin and earnings per share. We maintained our expectations of mid-single digit revenue growth before any benefit from ELAs, as we continue our strong commitment to shareholder return, evidenced by the $500 million of share repurchases in Q1.

We will introduce more exciting innovation at our Insight User Conference in Las Vegas in October. We will be hosting technology sessions for the investment community with NetApp executives, and we hope to see you there. Thank you very much.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program. You may all disconnect and have a wonderful day.