23-Feb-2022

NetApp, Inc. (NTAP)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon, ladies and gentlemen. Welcome to the NetApp Third Quarter Fiscal Year 2022 Earnings 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 would now like to turn the call over to Kris Newton, Vice President, Investor Relations.

Kris Newton

Vice President-Investor Relations, NetApp, Inc.

Thank you for joining us. With me today are our CEO, George Kurian; and CFO, Mike Berry. This call is being webcast live and will be available for replay on our website at netapp.com.

During today's call, we will make forward-looking statements and projections with respect to our financial outlook and future prospects, such as our guidance for fourth quarter and fiscal year 2022, our expectations regarding future revenue, profitability and shareholder returns, the value we bring to customers, our ability to drive continued growth in both our hybrid cloud and public cloud segments, and our ability to manage through the current supply chain environment, all of which involve risk and uncertainty.

We disclaim any obligation to update our forward-looking statements and projections. Actual results may differ materially for a variety of reasons, including macroeconomic and market conditions, such as the continuing impact and uneven recovery of the COVID-19 pandemic, including the resulting supply chain disruptions; and the IT capital spending environment; as well as our ability to gain share in the storage market, grow our cloud business and generate greater cash flow.

Please also refer to the documents we file from time to time with the SEC and available on our website, specifically our most recent Forms 10-Q and 10-K including in the Management's Discussion and Analysis of Financial Condition and Results of Operations and Risk Factors section. During the call, all financial measures presented will be non-GAAP unless otherwise indicated. Reconciliations of GAAP to non-GAAP estimates are posted on our website.

I'll now turn the call over to George.

George Kurian

Chief Executive Officer & Director, NetApp, Inc.

Thanks, Kris. Good afternoon, and welcome, everyone, to our Q3 FY 2022 earnings call.

We delivered another outstanding quarter, building on the momentum we've had in recent periods. Demand for our solutions is strong and powered by the alignment of our differentiated technology portfolio with customer priorities. In Q3, our focused execution delivered double-digit revenue growth led by the impressive performance of our Public Cloud services and all-flash array businesses; record high gross margin dollars, operating income and earnings per share. NetApp plays a critical role in helping customers achieve their business and cloud transformation goals.

I am pleased that our differentiation here continues to receive third-party validation by industry leaders, independent analysts and existing and new customers. We were recognized by Amazon Web Services for our achievements as an AWS Partner. NetApp was named the 2021 AWS Independent Software Vendor Design Partner of the Year – US for the jointly-engineered and natively-integrated Amazon FSx for NetApp ONTAP service.

Additionally, GigaOm called out NetApp as the only vendor with a multi-cloud strategy and execution that translates to a continuous data management plane across clouds and locations, a comprehensive enterprise-grade feature set and flexible deployment options. We were listed as a leader in three GigaOm Radar Reports, Cloud File Systems, Primary Storage for Large Enterprises, and Enterprise Scale-Out File Systems. Not only are we a leader in each category, we are the only vendor to lead in all three. This recognition spotlights the value we bring to our customers on their cloud and digital transformation journeys.

Customers are also endorsing our value, creating strong demand for solutions in both our Hybrid Cloud and Public Cloud segments. Growth in our Hybrid Cloud segment was driven by continued strength in object storage and all-flash arrays. Our all-flash array business hit another milestone in Q3, with a record high annualized run rate of $3.2 billion, an increase of 23% year-over-year.

All-flash array penetration of our installed base ticked up another point to 31% of installed base systems, giving us substantial headroom to continue to help existing and new customers modernize their storage environments with cloud-connected flash arrays. We further enhanced our position with the introduction of the AFF A900, which delivers unified support for file, block, and object protocols, built-in data protection with cutting-edge anti-ransomware capabilities, and the high performance and resiliency required to support the most critical business workloads.

Public Cloud ARR grew to $469 million, an increase of 98% year-over-year, including the benefit from the CloudCheckr acquisition which closed early in Q3. Public Cloud dollar-based net revenue retention rate remains healthy at 169%, as customers increased their usage of our Public Cloud services and adopt new products. The expanded market reach from our cloud partners and the broadening participation of our field sales organization has delivered outstanding performance in our Public Cloud segment this year, which puts us well ahead of our plan to achieve $1 billion in ARR in fiscal year 2025.

We, uniquely, have fully integrated services with all the major public cloud providers. I am pleased with the level of engagement from our cloud partners and with the performance of our cloud storage services. Azure NetApp Files again grew ahead of plan; Cloud Volumes Service for Google Cloud is ramping nicely; and while still very early days, we are seeing lots of proofs of concept and activity with AWS, FSx for NetApp ONTAP.

Our differentiated CloudOps Portfolio for multi-cloud infrastructure management is also growing well, led by Spot and Cloud insight. It is expanding our addressable market, and opening opportunities with new buyers at existing customers and with new customers, as we help them reduce the cost and complexity of managing their rapidly growing cloud environments.

We are delivering innovation at cloud speed and enhancing our solutions to address the needs of cloud natives and born-in-the-cloud applications. We've made Cloud Backup Kubernetes aware and broadened Spot Ocean with automated cloud infrastructure and application management for Apache Spark and Ocean CD, enabling faster deployment of Kubernetes applications with end-to-end visibility and management.

As I mentioned earlier, we closed the CloudCheckr acquisition early in Q3. CloudCheckr complements the FinOps capabilities of Spot with the multi-cloud reports, analytics and governance needed to plan, manage and optimize cloud costs to ensure organizations get the most out of their cloud investment.

We continue the rapid pace of organic and inorganic innovation with today's announcement of the acquisition of Fylamynt. Fylamynt extends our leadership in cloud operations. Adding Fylamynt's cloud automation technology to the Spot platform will make it easy for customers to integrate Spot solutions with their existing tools, processes and infrastructure code. This will accelerate their ability to take advantage of Spot's suite of capabilities for understanding and optimizing their cloud infrastructure. I'm excited to welcome the Fylamynt team to NetApp.

As I've said many times, our strategy to help customers deal with the challenges of managing data and applications in hybrid multi-cloud environments is helping us expand our business by winning new customers and displacing the competition.

A global third-party logistics company chose FSx for NetApp ONTAP to host data migrated from Nutanix systems in its data centers. They chose NetApp-based cloud services for our resiliency, cost efficiency and multi-protocol support. This win marks a new logo for us and has already created additional opportunity for Cloud Manager and Cloud Insights.

Another new customer win came from a multinational energy infrastructure company, who chose Cloud Volumes ONTAP in Azure to migrate workloads away from on-premises Dell systems. They are now considering replacing expired Dell systems with on-premises NetApp systems to make it easier to move data across environments in the future.

We had a first-time win at an international government agency with Spot Eco to optimize its multimillion-dollar cloud spend. This win becomes a lighthouse reference account for us which we can leverage to reach into other related agencies.

In summary, our strong Q3 results underscore our unique position in solving organization's most significant challenges in both cloud-native and traditional applications, on-premises and in hybrid multi-cloud environments.

First, we help customers simplify and modernize existing data centers and deploy traditional applications quickly and confidently. Second, we help customers adopt modern application architectures like Kubernetes and microservices for new workloads and deploy data-rich applications like machine and deep learning. And third, we help customers optimize cost, performance, availability and security for applications and associated infrastructure across multiple clouds.

The complexities created by rapid data growth, multi-cloud management and the adoption of next-gen technologies creates a sizable opportunity for us. With focused execution, I am confident in our ability to capture that opportunity and deliver continued growth.

We're holding an Investor Day on March 22, where we'll talk more about our growth opportunity and our plans to drive shareholder value. You can register at investors.netapp.com. If you have any questions, please reach out to the IR team.

Before I turn the call over to Mike to walk you through the numbers, I want to take a moment to welcome Harv Bhela to NetApp as our Chief Product Officer. Harv brings with him more than 25 years of experience building industry-defining software categories and cloud services. I also want to thank Brad Anderson for his leadership and wish him well in his retirement.

With that, I'll hand it over to Mike.

Michael J. Berry

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

Thank you, George. Good afternoon, everyone, and thank you for joining us. As a reminder, I'll be referring to non-GAAP numbers unless otherwise noted.

Before we go through the financial details, I think it would be valuable to walk you through the key themes for today's discussion. Number one, Q3 was another strong quarter, with all-time company highs in gross profit dollars, operating income and EPS as our business model continues to show significant operating leverage as we grow our operating profitability and margins.

Number two, our cloud business had another outstanding quarter. We clearly are solidly ahead of our original plan to hit our $1 billion ARR target in fiscal 2025. Number three, we are prioritizing meeting as much customer demand as possible as we navigate near-term component shortages and expect revenue to continue to be constrained in Q4. And number four, we are increasing our full-year guidance for revenue, EPS and Public Cloud ARR, driven by the outperformance in Q3 and a very healthy demand backdrop for Q4.

Now to the details. In fiscal Q3, we delivered strong revenue, gross margin and operating leverage across the entire business. Outstanding execution by the NetApp team yielded Q3 billings of $1.76 billion, up 10% year-over-year. Revenue came in at $1.61 billion, also up 10% year-over-year. Our solid Q3 results were driven by continued strong demand across both our Hybrid Cloud and Public Cloud segments.

Hybrid Cloud segment revenue of $1.5 billion was up 6% year-over-year. Within Hybrid Cloud, we delivered product revenue growth for the fourth consecutive quarter and expect this momentum to continue into Q4 and throughout fiscal 2023. Product revenue of $846 million increased 9% year-over-year. Consistent with the trends we've seen over the last two quarters, software product revenue of $507 million increased 18% year-over-year, driven by the ongoing mix shift towards our all-flash portfolio. Total Q3 recurring support revenue of $586 million increased 3% year-over-year.

As George highlighted, our all-flash revenue run rate, which includes both product and support revenue, eclipsed $3.2 billion for the first time in the company's history, and was up 23% year-over-year.

Public Cloud ARR exited Q3 at $469 million, up 98% year-over-year and 21% sequentially driven by strong growth in Azure NetApp Files, Spot and Cloud Insights, with CloudCheckr contributing $35 million in ARR. Organic Public Cloud ARR, excluding CloudCheckr was $434 million in Q3, up 83% year-over-year. Public Cloud revenue recognized in the quarter was $110 million, up 100% year-over-year and 26% sequentially. The growing scale of our Public Cloud portfolio continues to positively impact the overall growth profile of NetApp, delivering 4 of the 10 points in revenue growth.

Recurring Support and Public Cloud revenue of $696 million was up 11% year-over-year, constituting 43% of total revenue. When combined, software product revenue, recurring Support and Public Cloud revenue totaled $1.2 billion, another company high, and increased 14% year-over-year, representing 75% of total revenue, up from 72% in Q3 2021. We ended Q3 with $4 billion in deferred revenue, an increase of 4% year-over-year. Q3 marks the 16th consecutive quarter of year-over-year deferred revenue growth, which is the best leading indicator for continued recurring revenue growth.

Total gross margin was 67%, reflecting the value of our software and Public Cloud portfolio. Total Hybrid Cloud gross margin was also 67% in Q3. Within our Hybrid Cloud segment, product gross margin was 52%, while our growing recurring support business continues to be very profitable, with gross margin of 92%.

Public Cloud gross margin of 71% was accretive to the overall corporate average. As we highlighted last quarter, we expect Public Cloud gross margins to continue to trend towards our long-term goal of 75% to 80%, as an increasing percentage of our Public Cloud business will be built on software solutions. The introduction of FSx for ONTAP with AWS, and the addition of CloudCheckr to the Spot portfolio, both of which are software offerings, support our long-term margin goal.

Q3 highlighted the tremendous leverage in our operating model, with operating margin of 25%, an all-time company high. EPS of $1.44 was up 31% year-over-year and also represented a new quarterly record for the company. Cash flow from operations was $260 million and free cash flow was $199 million. During Q3, we repurchased $125 million in stock and paid out $111 million in cash dividends. In total, we returned $236 million to shareholders, representing 119% of free cash flow. We closed Q3 with $4.2 billion in cash and short-term investments.

As many companies have highlighted during this earnings season, the dynamic supply chain situation continues to cause disruptions across the technology ecosystem. These headwinds were further exacerbated by Omicron. In addition to a worsening freight and expedite environment, we also experienced component supplier decommits beginning in the second half of Q3, which required us to purchase components in the open market at significant premiums.

We were faced with the short-term decision of supporting the robust customer demand versus optimizing near-term product margin. NetApp has consistently focused on being a great long-term strategic partner to our loyal customer base, especially throughout the last two years of COVID. Consistent with this philosophy, we made this strategic decision to prioritize meeting customer demand with the trade-off being lower product margins in the short-term.

To be clear, the pricing and availability of our core HDD and SSD components are stable and are not a contributor to the near-term headwinds.

With these supply chain headwinds as a backdrop, I want to highlight two critical takeaways. Number one, we believe these cost headwinds are temporary in nature; and number two, we expect that Q4 will be the trough for product margins. As you all know, the timing of getting completely through these supply chain challenges remains fluid, but we do expect cost improvements in the coming quarters as the supply headwinds begin to ease throughout the first half of fiscal 2023. We also expect our recent price increases to help further stabilize product margins in the coming quarters.

As the supply base for components and airline cargo normalize, we are confident that product margin will return to its structural level in the mid-50s, particularly as our mix continues to trend towards all-flash. We do anticipate these supply chain challenges to impact our product revenue and product gross margins in Q4. The supply chain headwinds and our ongoing actions to mitigate them have been factored into our Q4 and updated full-year guidance. We expect Q4 net revenues to range between $1.635 billion and $1.735 billion, which, at the midpoint, implies an 8% increase year-over-year.

We anticipate consolidated gross margin in Q4 to be approximately 64%. The near-term margin headwind is being driven by an incremental $50 million to $60 million of premiums we expect to incur in open market component purchases.

Consistent with our philosophy and culture, we actively prioritize being a great strategic partner to our loyal customers, many of which have been with us for over 25 years, and feel great about the discipline and execution the NetApp team has displayed in managing through the current supply situation.

We expect operating margin to be approximately 22% in Q4, which would have been closer to 25% without the recent supplier decommits. Assumed in this guidance are Q4 operating expenses of $705 million to $715 million, driven by continued investment in revenue-generating activities, including expanding our Public Cloud portfolio and investments in both our Cloud and customer success sales teams.

We anticipate earnings per share for Q4 to range between $1.21 and $1.31 per share. Assumed in our Q4 guidance is our expectation that other income and expense will be a negative $15 million, and our tax rate will be approximately 18%. Our Q4 guidance implies revenue growth of approximately 10% year-over-year for fiscal 2022.

We also have growing confidence in our expanding Public Cloud opportunity, driven by enhanced go-to-market activities, deeper and broader cloud partnerships and continued product innovation. As a result, we are raising the guidance on our Public Cloud ARR with a new range of $525 million to $545 million exiting fiscal 2022.

Please note that Fylamynt is a tech and talent acquisition and will not contribute any ARR in Q4.

The implied forecast for total gross margin is approximately 67% for the full year. Our disciplined management of the business, despite the backdrop of supply cost headwinds, has allowed us to reaffirm our full-year operating margin guidance of 23% to 24%. We are raising our fiscal 2022 EPS guidance. We now expect EPS to range between $5.07 and $5.17, representing 26% year-over-year growth at the midpoint.

In closing, I want to thank the entire NetApp team for the outstanding execution and delivering strong Q3 results. We will continue to be disciplined and long-term minded as we manage through the temporary supply challenges to meet as much customer demand as possible. Given the current environment, George and I are incredibly proud that the team stayed focused on our strategic priorities and have collectively leaned into executing against a tremendous growth opportunity we see over the next three to five years.

As George mentioned, we plan to host an Investor Day on March 22nd, where we will further discuss the long-term growth potential and value drivers for our shareholders, customers and partners.

I'll now hand the call back to Kris to open the call for Q&A. Kris?

Kris Newton

Vice President-Investor Relations, NetApp, Inc.

Thanks, Mike. Let's open the call for questions. Operator, let's begin the Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Karl Ackerman with Cowen. You may proceed with your question.

Karl Ackerman
Analyst, Cowen and Company, LLC

Q

Yes. Thank you. First question for Mike, if I may. You spoke about how revenue is constrained by component shortages in your fiscal Q4, but I wanted to better understand how that may be impacting your deferred revenue growth, which, you know, has moderated to 4% growth. And so, I was hoping you could describe in a little bit more detail why that may have slowed? And how we should think about the trajectory on a go-forward basis?

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Sure. So, hey, thanks for the question, Karl. So there's two parts of that. So the first thing is, when revenue is constrained and we're not able to ship or invoice, it does not go into deferred revenue. So, it does not go on the balance sheet until it's actually invoiced. So, if we're not able to ship, it does not go on the balance sheet. On deferred revenue, this is a super-important question, I'm going to tie it also to support revenue. When you look at the year-over-year growth for the last seven quarters of total deferred revenue and total support revenue, that has averaged somewhere between, call it, 4% to 6% when you take into account the impact of FX.

So, to be more specific, in Q3 and Q4 of last year, Q1 of this year, we had a benefit of FX of 2 to 3 percentage points. This quarter is actually a headwind of 1 percentage point. So, when you normalize deferred revenue and support revenue, and those two are going to go almost hand-in-hand for the FX impact, you're going to get between 4%, 5% or 6% on an annual basis for all of those. So, hopefully, that answers the question.

Again, if we don't ship, it doesn't go into deferred, and then deferred and support also have been impacted by FX and they would largely move together. Thanks for the question.

Karl Ackerman
Analyst, Cowen and Company, LLC

Q

Thank you. I'll hop back in queue.

Operator: Thank you. Our next question comes from Meta Marshall with Morgan Stanley. You may proceed with your question.

Meta A. Marshall
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks. Just on the supply chain impact, I wondered if you could give any sense of type of product that was impacted more. And maybe just a split between what is kind of what you would call freight versus underlying inputs kind of difference in the headwind that you're seeing, and whether it's kind of giving you more visibility as you look into kind of the next fiscal year, or whether you're seeing kind of order activity pick up as customers try to assure availability? Thanks.

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

First of all, with regard to the large items in our bill of materials, meaning processors, DRAM, hard drive, solid-state storage, we have a very well-managed supply chain and have seen continued support from our leading suppliers. Most of our storage media are multi-sourced, as you would expect, and we have had really good engagement from them.

I think the places where we have seen supply decommits have been mostly in analog semiconductors. These are low volume – low value components that are used across a lot of our product families for things like voltage stabilization and other kinds of analog functions in those systems. So, they are broad-based across our systems portfolio, and which is why we've had to resort to, in some cases, open market purchases to offset constrained supply or supplier decommits that we saw in the middle of Q3.

With regard to the logistics, as you all know, cargo airfreight has been the major source of distribution of both parts and finished products, and airfreight was impacted by Omicron. We're hopeful that we can see a steady recovery as we head into fiscal year 2023 of both parts availability and logistics constraints. And I can certainly share with you the multistep action plan that we have taken, that includes engineering programs, that includes strong supplier engagement, that includes pricing uplifts and discount management, as well as close customer engagement to get us through this process.

Meta A. Marshall
Analyst, Morgan Stanley & Co. LLC
Q

Great. Thank you.

Operator: Thank you. Our next question comes from Mehdi Hosseini with SIG. You may proceed with your question.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP
Q

Yes. Thank you. Mike – I got two questions. First one is for Mike. You talked about April to mark the trough in operating margin. Does that mean despite seasonal trend into Q1 July quarter, the mix will help you and we should see a margin expansion? And then on – just a quick follow-on on all-flash array, how should I think about the mix of all-flash array between on-prem or enterprise customers versus the cloud? And I'm assuming that the cloud would be considered new type of customers for your all-flash array. Thank you.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

So, hey, Mehdi, it's Mike. So, if I – I just want to replay back your question and is your question, the lower operating margin in Q4, which was driven almost entirely by the premiums, and what was the question on the mix going into the July quarter?

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP
Q

Yes. I'm assuming that July would follow some sort of a seasonal trend revenues down, but you would benefit from the mix so that your operating margins would rebound despite lower revenues.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Yeah. So, we haven't guided fiscal 2023 yet. We'll talk about that on the next call. What we would tell you is that we wouldn't expect any change in our seasonality from Q4 to Q1. That's been relatively consistent. The one thing I'd ask you to think about as well going into Q1, and both George and I talked about it is, the growth in Cloud ARR is starting to have a much bigger impact positively on revenue growth, as well as gross margins, which goes to OpInc. So, that would be the one area I would ask you to consider as you do your models for next year and again, we'll guide Q1 on the Q4 call.

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

A

With regard to...

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

Great. And is...

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

A

Go ahead, Mehdi.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

No, I was just going to repeat the question, diversification of all-flash array customers.

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

A

Yeah. With regard to our customer footprint, we are winning with multiple elements of our portfolio. All-flash arrays continue to be well ahead of market growth rates which is a clear indication that we are gaining share, and we are doing that by both winning new workloads in existing customers, as well as new customers.

Our Cloud portfolio, as I mentioned with an example on our call, gives us strength not only in net new to NetApp customers on the Public Cloud, but also an opportunity to displace their previous suppliers in their data centers as they harmonize their cloud environment with their data center environment and our CloudOps portfolio, Spot, Cloud Insights, CloudCheckr have been a source of great new customer additions.

Mehdi Hosseini
Analyst, Susquehanna Financial Group LLLP

Q

Thank you.

Operator: Thank you. Our next question comes from Wamsi Mohan with Bank of America. You may proceed with your question.

Wamsi Mohan
Analyst, Bank of America Merrill Lynch

Q

Yes. Thank you. George, I was wondering about if you could talk about the confidence in Q4 margins being a trough. What times are you seeing that is making you think that specifically? And it appears that you're not baking in headwinds from NAND and HDDs and you called out good supplier relationships there. But it seems as though some of these are running into some issues as well and if you could comment on – if those had – if those start to become headwinds, is it right to understand that that's not contemplated to create incremental margin pressure? And I have a follow-up.

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

A

Okay. Let me take that in two parts. Let me first talk about the NAND, SSD market and then talk about the rest of the supply base, if that's all right?

Wamsi Mohan
Analyst, Bank of America Merrill Lynch

Q

Sure.

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

A

On the – you know, on the NAND side, we obviously have strong supplier relationships across the memory industry and are clearly multisource for all elements of our supply portfolio and SSDs. With regard to the recent incident impacting one of the members of that industry ecosystem, they, as you know, are not our leading supplier for SSDs. And so, we feel good about the work that we've done on our SSD base.

There may be some increases in prices in SSDs, but our engineering and manufacturing team has done a super job, and we expect that for the go-forward, the total storage media cost will be flat year-on-year. So we feel good about that, offsetting certain elements of the supply base with other elements of the supply base.

With regard to the broader – why do we believe product gross margins are a trough in Q4? Listen, there's been a lot of work that we have undertaken to deal with the supply constraints. Clearly, we have most of the large volume items and the high dollar items in our supply base are well managed, and we do not see them impacted by the supply constraints that we have seen so far.

There are certain elements of our supply base that we are dealing with, with decommits in the quarter that has required us to be in the open market and we have engineering qualifications going on for all of the major elements to create alternate sources of supply or to engineer our way around those supply constraints. And some of those engineering solutions have reached the market and will come to market over the course of the first half of fiscal year 2023.

The second – the third element is pricing and discount management. As you know, we have communicated previously that we did raise prices in the fall, and we have recently also communicated another impending price increase that takes effect this month. Those two price increases will have the primary impact later in Q4 and going through, for the most part, the benefit will be seen in fiscal year 2023. And those are all the mechanisms that cause us to feel confident that while we have been dealing with a constrained supply base, we have put in place a lot of controls to allow us to feel better about the path forward.

Wamsi Mohan
Analyst, Bank of America Merrill Lynch

Q

Okay. That's really helpful. And if I could, Mike, just to go back on your seasonality from fiscal 4Q to fiscal 1Q comment, if I understood this right, you're taking actions in paying open market prices to mitigate the revenue impact. So, are you able to – but you also noted that you do have some revenue impact in fiscal Q4 and you're – if we take George's comments here about sort of the supply chain normalization happening as you head into fiscal 2023, then why would we not see a better-than-normal seasonality in fiscal 1Q 2023 if fiscal 4Q is constrained? Thank you.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

Yeah. So, hey, thanks for the question, Wamsi. So, we do – going into Q1 after Q4, assuming Q4 plays out as we expect, that really all depends on the availability of supply and specific supply. And hey, mix matters here a lot. George talked about the components affecting a lot of the products across our portfolio. So, as it sits today and as we look into Q1, we would expect to see some of that flow into fiscal 2023. When that's going to hit, really depends on where we are from a supply chain perspective and specific components. And again, we'll update you on the Q4 call in terms of Q1.

And certainly, the backdrop is, hey, we feel really good about the demand environment. Timing of those are really dependent on the supply chain situation, Wamsi.

Wamsi Mohan
Analyst, Bank of America Merrill Lynch
Q

Okay. Thank you so much.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

You bet.

Operator: Thank you. Our next question comes from Aaron Rakers of Wells Fargo. You may proceed with your question.

Aaron Rakers
Analyst, Wells Fargo Securities LLC
Q

Yeah. Thanks for taking the question, guys. I have two as well, if I can. Just building on kind of Wamsi's question there. I guess the simple question for me is that you talk about the confidence in returning to a mid-50% product gross margin. Obviously, you're working through some things and you've outlined kind of your expectations on storage media costs being flat, but, with all of that said, do I think – should I think that gross margin on the product line returns to mid-50s in fiscal 2023? Is it second half of fiscal 2023? Any kind of framing of how you're thinking about the longevity of the pressures on that product gross margin would be helpful.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

Hey, Aaron, it's Mike. So, thanks for the question. So, hey, this is super important. So, just as a context, as you look at fiscal 2023, just a couple of things for you folks to think about. We really think we executed well on the things that we can control in Q3. And we've raised guidance and revenue ARR and EPS, largely due to the great work of the team and we have multiple new highs. We will expect to continue to execute well going into fiscal 2023.

This is, as we sit today, we're not guiding Q3, but what we would say is, hey, let's do a replay of what we have said, and I think this will help you, which is, product revenue has grown for four straight quarters. We expect that to continue into next year. We've talked about the supply chain issues. We expect to moderate as we go through the first half of fiscal 2023. So we would hope and expect that we would get back to that mid-50s during the second half of next year. And that's really driven by the three things George talked about: The improving supply chain situation; freight and expedite; and the impact of the price increase. So, as you look at next year, yes, we would expect to get back sometime in the second half of the year. Hopefully, that helps you with your modeling. Again, we're not giving guidance for Q3, just as we sit today, but hopefully, that helps a lot, Aaron.

Aaron Rakers
Analyst, Wells Fargo Securities LLC
Q

Yes, that's very helpful. And then just as a quick follow-up, you know, you talk about the Public Cloud business, and I know that you mentioned that Google, in particular, was ramping. Could you just give us maybe a bit more context of where we're at as far as the progression of maybe both Google and Amazon at this point? And when those – you know, how we should think about those really kicking into that Public Cloud revenue?

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

I think we're pleased with all of our partnerships. Azure NetApp Files was the really strong performer this quarter as it has been for several quarters now, which demonstrates both our ability and knowledge of how to scale a hyperscaler relationship and the enormous strength and leverage that gives us once it's scaled.

I would say the earliest of the three is Amazon FSx for NetApp ONTAP. We announced it in September, and we are very, very pleased with the level of trials and early activity. They have frankly, surpassed our expectations, but it's early in the going and so, it takes time to translate those trials into paid customers and to expand the relationships across the FSx. So, I would say, we're excited, but we've got a long – lot of work to do, and we know where – what that work is. And so, you should expect, broadly speaking, I see FSx about 18 months behind where we saw ANF with Microsoft Azure.

Google is in between. Google has – we have seen several big customer successes with Google, and we are working to expand the range of workloads and the range of use cases with them across the portfolio.

Aaron Rakers
Analyst, Wells Fargo Securities LLC
Q

Thank you.

Operator: Thank you. Our next question comes from Samik Chatterjee with JPMorgan. You may proceed with your question.

Samik Chatterjee
Analyst, JPMorgan Securities LLC
Q

Hi. Thanks for taking my question. I had a quick couple of questions on the Public Cloud as well and just following up on Aaron's question. I think this first one, if you can help me understand if I look at your ARR – Public Cloud ARR, you did have a increase of about $80 million or so, which looks to be an acceleration sequentially compared to how you've done in recent quarters. How much of that is maybe attributable to CloudCheckr? And excluding that, it does still look like an acceleration, so, if you can get us – give us some more insight into how much of that is driven by some of the newer partnerships, versus it does sound like more of the growth coming from partnerships that you initiated earlier? That would be great. And then I have a quick follow-up on Public Cloud ARR as well.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Sure. So, this is Mike. I'll take the first part. So, we finished Cloud ARR at $469 million, as you referenced 98% growth. In that number CloudCheckr represented about $35 million of ARR. So, the "organic" business, about $434 million, that was a year-over-year growth of about 83% versus 80% in Q2 and 89% in Q1. So, really nice growth on the organic business. And as we called out, that was really driven by Azure NetApp Files, Cloud Insights and Spot.

Samik Chatterjee
Analyst, JPMorgan Securities LLC

Q

George, any – sorry, any color on what's driving the acceleration here? How much of that is coming from the earlier partnerships with Azure versus the newer partnerships with AWS?

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

A

As Mike mentioned, the new partnerships are not material contributors yet. The – we are excited about the potential, but you should see that potential realize over the next few years. I think that in the past quarter, the vast majority of the acceleration comes from both new customer additions as well as when you see a really strong dollar-based net retention rate, it shows that once a customer uses one of these cloud portfolios, they expand their use quite substantially. So, I think that's where the vast majority of the progress has been.

Samik Chatterjee
Analyst, JPMorgan Securities LLC

Q

Okay. Good. Thank you.

Operator: Thank you. Our next question comes from Simon Leopold with Raymond James. You may proceed with your question.

Simon Leopold
Analyst, Raymond James & Associates, Inc.

Q

Thanks for taking the question. I don't think you've talked about your other growth rates. And I just wanted to see if you could maybe help us get a better understanding of how your customers are behaving, given that we had a sense that in IT space, many customers, given the lengthened – lengthening of lead times and the supply chain constraints, are putting in orders earlier. I want to confirm if you're seeing that and what kind of order growth rates you're experiencing. Thank you.

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

A

Listen, we don't see any unusual behavior. We have close relationships with our customers, clearly, we are monitoring, given the supply chain situation, a very, very tight inspection of our order backlog and our order pipeline. We see healthy broad-based demand but no sense of shadow demand or multiple purchases to – in our pipeline. So, we feel good about the sort of the real demand in the business, and we're doing as much as we can to meet it. Demand, as Mike has said, is outpacing supply.

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

Thank you.

Operator: Thank you. Our next question comes from Rod Hall with Goldman Sachs. You may proceed with your question.

Rod Hall
Analyst, Goldman Sachs & Co. LLC
Q

Yeah. Thanks for fitting me in. I wanted to start off with the price increases. We've seen other people in this general category of products, increasing prices by around 10%. I wonder if you guys could maybe quantify the ballpark of those price increases. And maybe comment a little bit on the stickiness of that, too. There's a difference of opinion as to whether these are going to be around to stay and will people flex prices back down as underlying costs go back down as they do. So, just wanted a comment on that, if I could get it.

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

Listen, I won't give you a specific number. I'll just say, your read of the industry and our participation in it are – is in the target range, right? So, I will just say, we monitor the behavior of the industry and the cost of our supply, and we take appropriate action. We've taken two actions as we mentioned earlier, one in the fall and the second one in February, and we should see the benefits of those play out over time.

We have to give our customers the benefit of those orders that are already in flight or quotes that are in-flight, you have to honor them to be a good partner to customers. But over the course of Q4 and certainly heading into the new fiscal year, you should see the benefits of that come into the business. With regard to the likely duration and so on, listen, we always trade off being a good partner to customers with the need to maintain margins in our business. It's too early for me to comment. We will continue to monitor the situation, and if we make changes, we will let you know.

Rod Hall
Analyst, Goldman Sachs & Co. LLC
Q

Okay. And then I had a quick follow-up and that is on – the Public Cloud services, we were wondering, is all of that regionally accounted for in the Americas, or, do you spread it across the regions? And then I guess more generally, after you answer that one, just comment maybe on the strength of the Americas. What's driving that? It was pretty strong this quarter.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

Yeah. So, I'll answer to the first question as the large majority of the PCS business is generated in the Americas, to the extent that there is international business that flows through entities internationally, we would certainly report it that way. The strong results in the Americas, as you mentioned, they did have a very strong quarter. That's where we saw a lot of the strong order growth come in. So, the Americas had a good quarter, both in the Hybrid Cloud and the Public Cloud segments, Rod.

Rod Hall
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Great. Thanks, Mike.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Thank you.

Operator: Thank you. Our next question comes from Steven Fox with Fox Advisors. You may proceed with your question.

Steven B. Fox
Analyst, Fox Advisors LLC

Q

Hi. Good afternoon. Just first of all, just a clarification on some of the comments you made about the quarter just closed. Are you saying that unmet demand was entirely related to supply chain? Or was there also a further acceleration in orders? And then I had a follow-up.

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

A

Demand – as we said, demand is outpacing supply. We've been aggressive to meet demand wherever we could and I will just say, our team executed really well. I think that we'll just be transparent. Demand has outpaced supply both in Q3 and we expect in Q4.

Steven B. Fox
Analyst, Fox Advisors LLC

Q

Okay. That's helpful. And then, George, it seems like the M&A that you've done on the Public Cloud side is starting to have a compounding effect on your growth rates. Is there any way to sort of think about how that sort of changes the view for longer-term growth in Public Cloud, given that when you first set some of these targets, you didn't have some of the capabilities you have now? And sort of how that fact layers into growth going forward? Thanks.

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

A

I think, first of all, listen, we know we are clearly ahead of our $1 billion ARR target. We will communicate the long-term targets and our perspectives on the cloud business at our Investor Day, right? So, I am really excited about the portfolio we've built. We started with cloud storage, we have natively integrated cloud storage with the world's leading cloud providers, and you are seeing the acceleration of that business. We also expanded our cloud portfolio with a strong position in cloud infrastructure management with Spot, Cloud Insights, CloudCheckr and now Fylamynt helping the entire portfolio get easily adopted by customers.

And so, I really do feel like we have built two strong beachheads in markets that are expanding to our overall TAM and are demonstrating the ability for us to get new customers and cross-sell and upsell them a lot of different things. So, I'm really excited about our portfolio. We continue to be disciplined acquirers and manage shareholder returns, both with investing for the long-term growth of our business, while returning a significant amount of free cash flow to shareholders.

Steven B. Fox
Analyst, Fox Advisors LLC

Q

Great. That's helpful. Thank you.

Operator: Thank you. Our next question comes from Jason Ader with William Blair. You may proceed with your question.

Jason Ader
Analyst, William Blair & Co. LLC

Q

Yes. Thank you. So, George, I understand that the supply is – sorry, the demand is outpacing the supply, but how would you characterize the demand environment right now versus, say, the last few quarters, especially for your hybrid solutions, in light of what some people have talked about with some pent-up demand impact in 2021?

And then just as a quick follow-up, I know you guys are not guiding for FY 2023 revenue, but Mike, any early thoughts on kind of puts and takes in terms of helping us thinking about the model for revenue in 2023?

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

A

Listen, I think we continue to see steady broad-based demand, right? It's very solid. It's across a lot of different industries, a lot of different verticals, and they are for use cases that are headline news in the industry, digital transformation, cloud enablement, unstructured data analytics, artificial intelligence, ransomware protection. I mean, these are all well-known use cases with broad secular demand.

I did not believe that there was a V-shaped recovery to be honest. I think IT departments are mature buying centers, and they buy steadily over time. I think the year-on-year compares in some cases, were exacerbated by the fact that during COVID, you saw the opposite pattern for many companies. We had a good business pattern even during COVID. So, I continue to remain optimistic.

Our team has executed excellently. We have gained share in every category that we have played in, and our Hybrid Cloud business has two strong growth engines in object storage and all-flash.

Jason Ader
Analyst, William Blair & Co. LLC

Q

And Mike...

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

And then, hey, Jason, on your question – I'm sorry, did you want to add something?

Jason Ader
Analyst, William Blair & Co. LLC

Q

No, go for it. Yes, go for it.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Okay. Great. So I'll go back over what basically Aaron's question, so we're exiting – when you look at the different revenue components, four straight quarters of growth in product, we've guided for the fifth in Q4, and we expect that to continue in 2023. On a year-to-date basis, product is up about 11%. Support, we've talked about, when you normalize for FX, hey, the last seven quarters, it's been a 4%, 5%, 6% grower. And again, look hard at deferred revenue, especially short-term deferred because more than 90% of support revenue in a quarter comes off the balance sheet.

The Cloud ARR, again, we'll update you in March, but you can do your own forecast there. As I talked about in my script, hey, Cloud contributed 4 of the 10 percentage points of growth in the quarter, so it's really starting to have a meaningful impact. And then, hey, nice results in Professional Services, but it's pretty small. So, those would be the puts and takes going into next year. The one thing to keep in mind is that's largely organic. We'll continue to obviously be disciplined acquirers, but we do look to expand our cloud portfolio next year as well.

Jason Ader
Analyst, William Blair & Co. LLC

Q

Thanks very much. Good luck.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Thank you.

Operator: Thank you. Our next question comes from Nik Todorov with Longbow Research. You may proceed with your question.

Nikolay Todorov
Analyst, Longbow Research LLC

Q

Yes. Thanks and good afternoon, everyone. A question on – regarding – given all the constraints and the price increases you guys talked about, are you seeing any changes in customer behavior in relation to whether they prefer hardware versus cloud solution? Or do you see any increase in appetite from fully managed solutions like your Cloud services or maybe Keystone?

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

A

We feel good about the ability to serve customers in all of the ways that you talked about, absolutely on target. I think we've seen – while we haven't seen any sort of radical shift in behavior, the long-term trends around cloud and the use of as-a-service models broadly defined, continue to be playing out for us, our cloud portfolio continues to be really, really strong and we are able to help customers deploy workloads very quickly on public cloud environments, if they aren't able to build and deploy an environment in their data center.

Keystone also had a good quarter. It's early in the going, but we continue to see more and more vertical industry wins, more and more new customer wins and also wins across our geographic base, just like you would expect us to be focused on when managing an early business. So I feel good about both parts of the business. And then, of course, our differentiated product portfolio, as we said, we're focused on growing all-flash and object storage. We have the best operating system in the market for hybrid flash and that had a good quarter. So, good execution across the board.

Nikolay Todorov
Analyst, Longbow Research LLC

Q

Got it. Thanks guys. Good luck.

Operator: Thank you. Our next question comes from Shannon Cross of Cross Research. You may proceed with your question.

Shannon Cross
Analyst, Cross Research

Q

Thank you very much. Just two for me. You guided $705 million to $716 million, I think it was for OpEx last quarter and came in about $683 million. I'm just curious how you're thinking about OpEx and your ability to sort of toggle it, if gross margin remains under pressure? And then if you can just talk a bit about Asia since it was about 12% of revenue, which seemed low, was there anything specific to pressure that? Thank you.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Sure. So, Shannon, it's Mike. On OpEx, yes, we did come in a little bit below guidance. That was really driven by timing of program spend and quite frankly, we had baked in being able to hire more folks than we were able to. So, that were – those were the two big drivers.

From Q3 to Q4, we've talked about it, hey, we want to make sure that we're investing in the areas that drive growth. So, the increase is driven by cloud, both in sales and in product. There is some program spend that we didn't spend in Q3 that will flow into Q4 and then there's always timing around things like commissions, so that's Q4. And it's a great question on toggling OpEx. I mean, again, our view is this is temporary. It's going to work its way through to 2023. Therefore, we don't want to do anything that hamstrings the growth in the business. If something changes during 2023, we'll certainly take a look at it, but that's not our stance today.

The Asia revenue drop that you saw is really driven by two things, largely supply chain, and us not being able to deliver. So, that was mostly supply-chain related, versus, we were able to deliver more in the other geos, which is why you saw that year-over-year drop in revenue.

Shannon Cross
Analyst, Cross Research

Q

Great. Thank you.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Thank you.

Operator: Thank you. Our next question comes from Jim Suva with Citigroup. You may proceed with your question.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you. I just have one question. It's probably for George, or maybe Mike. But, you've been very ethical, loyal and true to your customers who placed orders and agreeing to the terms and contracts and commitments. When you hear these decommitments, what's the action or reaction to NetApp then strategically? Do you find alternative providers long term or do you – those who contracted with you who broke their promises come back and give you some concessions down the road? Or do you just kind of diverse or break the bridge and move on without them?

I'm just kind of curious because you've taken the high road and it seems like some of your suppliers have really put you in an awkward situation.

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

A

Listen, I think these are all the conversations that we have with our supply base. We have good long-term suppliers that support the vast majority of our [ph] BAM (01:01:17) and that we manage directly. There are other components that are integrated into sub-assemblies in our overall systems, that sometimes are – have been a part of the challenge here.

There's sort of multiple discussions there, right? I think clearly, we want to understand the reasons for such a decommit. We want to understand where we are in sort of the ability for the customer – for the supplier to meet our demand profile. And then there are ways that we have worked really hard in engineering to continue to build diversity of supply across our entire bill of materials, and in the cases where we don't feel like we can rely on a supplier to give us access to other suppliers. And so you'll see us continuing to work that over the next several quarters to make sure that we have all the levers at our disposal to meet demand.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you. Thank you so much, George.

Operator: Thank you. Our next question comes from Ananda Baruah with Loop Capital. You may proceed with your question.

Ananda Baruah
Analyst, Loop Capital Markets LLC

Q

Yeah. Hey, guys. Thanks for taking the question. Yeah. Just a quick one for me. George, how would you describe in hybrid environments where your sweet spot is today for object storage and all-flash arrays? And do you think that changes over time as you add to the portfolio?

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

A

In all-flash arrays, clearly, we are the strongest vendor in the mid-range systems and mid-range is displacing traditional high-end systems. So, we are in more and more and more customers winning the really high end of the market as well, so, really strong, broad-based distribution of our portfolio. Our hybrid flash systems have done really well in the entry market. If you look at the entry price bands growth rates, those are much more hybrid flash businesses than all-flash business. And so, the combination of those two give us the ability to cover a broad range of use cases with the right form factor.

With regard to object storage, it's another extension of our unstructured data portfolio. The unstructured data started out in files for the most part and increasingly, as the scale of those repositories have grown, customers have started to use object technology to allow for management and ease of administration. Our solutions have been really, really strong. I think we're focused on that market, we have a really good cost-effective, highly scalable, centrally managed object reposit – you know, solution and even in the object world, we have unique integrations with the Public Cloud that allows us to build a truly hybrid object environment, combining some parts of the environment being in customers' data centers, and some parts being in true Public Cloud under one policy framework.

Ananda Baruah
Analyst, Loop Capital Markets LLC
Q

That's super-helpful. I appreciate it. Thanks.

Operator: Thank you. Our next question comes from Amit Daryanani with Evercore. You may proceed with your question.

Amit Daryanani
Analyst, Evercore Group LLC
Q

Thanks for squeezing me in. I apologize if this has been asked already. The first one I had was on the Cloud ARR side. I think you talked about the gross margins being 71% better than corporate averages. Is there a way to think about at what point do we cross over and start to see operating margins in that business, that are in line to corporate averages potentially?

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

Yeah. So, Amit, this is Mike. So, we go down in the segment reporting to gross margin, at this point, we don't have any plans to go down to operating margin. We'll continue to look at that, but we're going to report segment reporting revenue down to gross margin.

Amit Daryanani
Analyst, Evercore Group LLC
Q

Fair enough. And then, you know, on these component issues that you are – I think you and everyone has been going through these challenges now, as I think about maybe the April quarter headwinds, right, and you've talked about the gross margin issues, is there a way to think about how much of that is freight logistics versus component issues? And then is there any revenues you left on the table in April that you would call out or quantify for us?

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.
A

So, the majority of the headwinds are from components versus freight. Freight and logistics are there, but the components are a bigger piece of that and then we won't quantify what that was from a revenue perspective. What we'd say is that's all baked into the Q4 and full-year guidance that we gave.

Amit Daryanani
Analyst, Evercore Group LLC
Q

I guess, Mike, [indiscernible] (01:06:14) we should have conviction that we could pick up whatever revenue is left on the table in the July quarter as you are requalifying some of these products and these bottlenecks alleviate, right?

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Yes. So there was a previous question on that. What we'd say is, to the extent that we have supply available and we're able to deliver those, and they could flow into Q1, we're not guiding Q1 yet. We'll do that at the end of Q4. But that is almost entirely dependent on the supply chain situation and mix matters here, it's super-important in terms of what is the mix and what are the components.

Amit Daryanani
Analyst, Evercore Group LLC

Q

Fair enough. Thank you very much.

Michael J. Berry
Chief Financial Officer & Executive Vice President, NetApp, Inc.

A

Thank you.

Operator: Thank you. Our last question comes from Louis Miscioscia with Daiwa. You may proceed with your question.

Louis Miscioscia
Analyst, Daiwa Capital Markets America, Inc.

Q

Okay. So, I've got four demand questions and two OpEx ones. So – but joking aside, when you look at what happened in calendar 2018 with a big hardware refresh cycle, I know you talked multiple times about demand is outpacing supply. But, just curious, because some of my CIO checks suggest that there is a replacement cycle coming on, maybe more in the back half of this year?

And then on top of that, some of my CIO checks also suggests that with some IT workers getting back to the office or just people getting back to the office, that's also some of the growth drivers. So, I know you did talk about a couple before, George, but maybe if you could extrapolate, if some of these are also contributing to hopefully a good demand year for you all this calendar year.

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

A

Yes. Listen, I think you hit the points quite accurately. I think we see the improvement in the overall sort of return to work and the impact from Omicron sort of easing through the course of the year, all things remaining the same and we think that demand continues to be really solid, steady and broad based. And so, we're excited about the year ahead.

We're certainly not guiding next fiscal. We'll guide it when we guide it. But, as I said in my remarks, we feel very, very good about the demand picture, and we're working hard to meet it with as much supply as we can get.

Louis Miscioscia
Analyst, Daiwa Capital Markets America, Inc.

Q

Okay. Thanks. Good luck on the New Year.

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

A

Thank you.

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

As we wrap up, I want to leave you with three call-outs, the sizable and enduring trends of cloud and data-driven digital transformation, where we at NetApp play a critical role in helping customers achieve their goals are driving broad-based customer demand for our products and services.

Our embrace of cloud has expanded our addressable market. The real opportunity is still in front of us. And thanks to our strong Public Cloud Services performance, we are well ahead of our plan to achieve $1 billion in ARR in fiscal year 2025.

Our focused execution and effective management of temporary supply chain headwind enable us to capture our expanding opportunity and deliver operating leverage as we grow our operating profitability and margins.

Thank you and I hope to see you at our Investor Day next month, where we will talk more about our long-term growth and value drivers.

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