

Full Reviewed Transcription

Temenos Group

Q1 2021 Results Conference Call and Live Webcast

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COMPANY REPRESENTATIVES

Max Chuard, Chief Executive Officer

Takis Spiliopoulos, Chief Financial Officer

PRESENTATION

Operator

Ladies and Gentlemen, welcome to the Q1 2021 Results Conference Call and Live Webcast. I am Sandra, the Chorus Call operator. I would like to remind you that all participants will be in listen-only mode and the conference is being recorded. The presentation will be followed by a Q&A session. You can register for questions at any time by pressing * and 1 on your telephone. For operator assistance, please press * and 0. The conference must not be recorded for publication or broadcast.

At this time, it's my pleasure to hand over to Mr. Max Chuard, CEO. Please go ahead, Sir.

Max Chuard

Thank you, operator. Good afternoon and thank you for joining today's call. I hope you've been able to access our results presentation on our website. As usual, I will start with some comments on our Q1 performance and then, I will hand over to Takis for an overview of the financials before giving some concluding remarks.

Starting on Slide 7, it was a great quarter and a strong start to the year. Banks are facing significant pressure in the end markets, with new competitors and changing demands from the customers. And an increasing number of those banks are pushing ahead with IT transformation projects after the disruption of 2020. We had very strong growth in both our SaaS and license businesses in the quarter. And SaaS ACV, in particular, was up 130%. The ACV growth was a combination of new customer signings and volume growth in existing customers. The SaaS revenue growth reflects the strong ACV we booked in the second half of last year, flowing through into the P&L this quarter.

Overall, total software licensing was up 26%, and our EBIT margin expanded 5 percentage points, demonstrating the strong operating leverage of our business model. We introduced total bookings as a new KPI this year, to reflect the increasing contribution from SaaS in our business and to enable you to track the overall growth in our business.

The growth in total bookings this quarter of 105% clearly demonstrate that banks are returning to spend on the IT platforms to address the structural pressures they are facing. In fact, total booking in Q1 2021 exceeded that of Q1 2019, which was our highest quarter ever. Lastly, we had a very strong cash quarter, both operating and free cash, which reflects the strong growth in recurring revenues.

Moving to Slide 8, our SaaS ACV was up 130% this quarter to reach 12 million Dollars. This was a combination of new logo wins and volume growth within some of our existing clients. Some of our existing clients have seen incredible growth in demand for the product and services. And the scalable consumption model is one of the key attraction of our SaaS offering and we clearly benefit from this.

From a regional perspective, the U.S. was the largest contribution to SaaS ACV this quarter, followed by Europe. Looking at the SaaS ACV pipeline for the rest of 2021, the majority of this is driven by demand for Transact. However, a significant portion is also coming from Infinity where we are seeing strong traction among new and existing customers.

On Slide 9, you'll see that our plans fall into 1 of 3 main groups in terms of size and buying behaviors which explain why our SaaS growth is largely incremental to our business. Large banks prefer predominantly on-premise license model, with some selective use of SaaS and cloud, in particular for peripheral or digital operations. Most large banks will run the software directly themselves, either on-premise or in the cloud.

Mid to lower tiers banks are also largely on-premise, renovating by lines of business and we do see increasing use of cloud and SaaS in this segment. For SaaS, Temenos Cloud operation runs the software. And challenger banks and fintech's are almost entirely SaaS for the operation. These banks will not have bought a license on-premise and so the demand for SaaS is incremental to our growth.

Turning to Slide 10, we had a great growth in total bookings, which reflected the strong demand environment in Q1 for both Transact and Infinity. Total bookings reached 120 million Dollars, which was up 105% on Q1 2020 and was also ahead, as I said, on Q1 2019. The growth in total bookings was driven in particular by very strong growth in SaaS, as well as, strong growth in licenses. We also saw an increase in average tenure this quarter compared to last year. This growth demonstrates the mission critical nature of our software. We are signing long term multi-year contracts, and this growth in backlogs is increasing our revenue visibility over the coming years.

Our backlog was at 1.8 billion Dollars at the end of 2020. And today, it is around 3 times our annual product revenue. Our total booking underpins our guidance for this year, as well as, our target to reach 1 billion Dollars of total bookings by 2025.

On Slide 11, I'll give an overview of our sales performance in the quarter. The sales environment improved through the quarter, continuing the trend we saw from Q4 2020. And we had a very good quarter in the U.S. in particular, which was the largest contributor to total software licensing driven by growth in our SaaS and license business.

We also had a strong performance in Europe, as the region continued to recover and we see increasing levers of demand for both license and SaaS. Tier 1 and Tier 2 banks contributed 37% of total software licensing up from 19... 18% in Q1 2020, as small large banks pushed ahead with the strategic IT renovations. And sales to the installed base remained strong contributing 74% of total software licensing. We had 10 new client wins and our service teams and implementation partners made very good progress with 28 implementation go-lives in Q1. Lastly our pipeline continued to build through the quarter, which underpins our confidence in the outlook for the year.

Moving to Slide 12, we announced 2 strategic partnerships earlier this year. The first was with salesforce where we are combining all of Salesforce CRM capabilities with a broad set of transaction capabilities provided by Temenos Infinity. The second was a strategic agreement with DXC to offer the bank's clients a progressive digital transformation path. I'm pleased to say that both of these partnerships are making good progress. With Salesforce the teams are working on integration of the 2 platforms with a plan to launch in Q3 this year. And we've seen strong interest from Salesforce clients in participating in early adopters program. And with DXC, with our early stage discussion and workshops ongoing with a number of potential targets, DXC has a very large customer base of U.S. and international banks running legacy core banking systems, and so there is a lot of potential here.

Now turning to Slide 13, I'd like to give an update on our U.S. business. The U.S. was our largest contributor to total software licensing in Q1 and had strong growth in both license and SaaS. We signed several new U.S. logos, as we continue to increase our brand awareness and footprint in the market.

As we mentioned in February, our Tier 1 U.S. bank went live in Q1 with Transact, which is a great domestic reference for us. We also expanded our SaaS reference customer base in the quarter, for example, Varo, the first consumer fintech making history for having received a banking license in the U.S. and PayPal who are running the Buy Now Pay Later product across multiple geographies including the U.S. on Transact. The U.S. continues to be the largest contributor to our global ACV pipelines for 2021, and we are investing in our sales and marketing to ensure we can capture future demand and drive growth in our business going forward.

Finally turning to Slide 14, as we highlighted at our Capital Markets Day, we are operating in a huge market, a 63 billion market, with well over 70% of the spend still done in-house. This gives us a very large run rate for growth in the medium and long term.

Banks are continuing to face significant structural pressures across digital, regulatory, cost and competition. The growth in demand for digital services through the pandemic was massive and it's forcing banks to be considered how the service, the customers and whether the IT system are fit for purpose. Demand for our products and technology is clearly accelerating in particular for SaaS and this is driving our pipeline growth. And the acceleration in SaaS is largely incremental to our future growth.

We are very focused on maintaining our market leadership position. We do this through our commitment to innovation and R&D investment which is the highest in the industry and the breadth of functionality and localization we can offer.

I'm particularly pleased with the growth in total bookings this quarter which is driving growth in backlog and increasing our visibility not just for 2021, but in the medium term as well. The next 2 slides are from our February Capital Markets Day and give additional color on the structural pressure banks are facing and our competitive positioning.

I will now hand over to Takis to talk through the numbers for the quarter.

Takis Spiliopoulos

Thank you, Max. On Slide 18, I'd like to give you an overview of the financial performance in Q1 2021. All figures are in constant currency unless otherwise stated. We had a great quarter across all our main KPIs reflecting the sustained improvement in our end market continuing from Q4 2020 also into the first months of 2021.

Looking at the P&L first, SaaS revenues were up 22%, driven by the strong ACV bookings in the second half of last year and total software licensing had strong growth of 26% as an increasing number of banks continue to pursue strategic transformations. These growth numbers were achieved despite considerable headwinds from HCL as we had communicated in February. I will talk in more detail about the HCL headwinds on growth rates in a minute.

As we had expected maintenance returned to growth of 3% in the quarter and total revenue was up 7%.

Our EBIT grew 31% in Q1 2021 and our reported EBIT margin reached 27.2%, up 430 basis points and even up 500 basis points on a constant currency basis. I'm particularly pleased that we delivered another strong cash performance and continued the trend from previous quarters.

Operating cash flow was up 25% and free cash flow grew 28%. We ended the quarter with DSOs at 107 days, down 4 days sequentially which also helped to drive cash performance. Our net debt at the end of Q1 2021 was 864 million and leverage remained flat at 2.1 times despite having executed 89 million of the share buyback program, thanks to our strong free cash flow generation and some tailwind from the U.S. Dollar appreciation versus year end. We will resume the share buyback as of tomorrow.

Moving to Slide 19, I will run you through some key figures for the quarter. As I mentioned the strong ACV bookings in particular in Q3 2020 drove SaaS revenue growth of 22%. Licenses also returned to growth of 28% in the quarter. Maintenance recovered as expected having reached a trough in Q4 2020 growing 3% in the quarter in line with previous indications. For Q2 2021, we still expect maintenance to grow 2% to 3% with subsequent acceleration in H2 2021 towards the 4% to 5% growth rate and vision for the full year, so unchanged versus previous communication.

I'm very pleased with the level of growth achieved in Q1 2021 despite considerable headwinds from HCL on our SaaS and total software licensing growth rates. Beyond 2021, the strong license growth forecast for this year will again lead to maintenance growth acceleration in 2022 and beyond.

Service revenues in Q1 2021 were slightly up sequentially but declined 9% year-on-year reflecting the delayed impact from lower license signings in 2020. I expect service revenues to be broadly flat in Q2 2021 with subsequent acceleration to drive services growth of about 4% for the full year.

Looking at the cost base our operating costs were flat year-on-year. However, we do expect costs to grow over the coming quarters as we continue to hire in R&D and sales and see some increase in travel and accrue greater variable costs.

Moving to Slide 20, we have provided the impact in queue 2021 of the Kony non-banking clients moving off from the Temenos P&L to HCL in the quarter. As a reminder, we signed a deal with HCL in Q2 2020, where they bought a license and maintenance contract, and the right to sell the Kony multi-experience development platform for non-banking services globally. As part of this, non-banking customers from Kony are migrating to HCL with the largest impact in the first couple of quarters of this year.

This created a substantial 9 percentage points headwind on SaaS revenue growth this quarter, 8 percentage points headwind on total software licensing, 2 percentage point headwind on revenues, and 16 percentage points headwind on EBIT growth.

Overall, we expect the impact from HCL to be stronger in H1 2021 than in H2 2021. Therefore, SaaS growth in Q2 2021 will be similar to Q1 2021. The strong ACV performance in the recent quarters will then become more visible in the SaaS growth acceleration in Q3 and Q4 to deliver the unchanged 2021 growth target of 30%.

On Slide 21, we show like-for-like revenues and costs adjusting for the impact of M&A and FX. As a reminder, we closed the acquisition of Kony at the end of Q3 2019. So Q1 2021 figures are all organic, and therefore in line with our constant currency growth rates, so no reason to repeat them at this point. In terms of FX, the stronger Euro had a positive impact on revenues, but the stronger Swiss and British pound had a negative impact on costs. Taking into account, all currency movements and hedging, FX had a small negative impact of about 1 million in the quarter.

Turning to Slide 22; net profit grew 28% in the quarter and in line with EBIT, while EPS grew 29%. Our tax rate was 15.6% for the quarter and we continue to guide for 2021 tax rate at 16% to 18%.

Moving to Slide 23, our DSOs reached 107 days at the end of Q1 2021 down 4 days sequentially and 2 days lower versus one year ago. With improving balance sheet quality at banks, we still see no issues in our clients' ability to pay, and also see no requests for revised payment terms. We still expect DSOs to be below 105 days by year-end. Beyond 2021, we expect DSOs to continue on their downward slope towards 85 days by 2025, driven by continued improvement in DSOs linked to licenses and services, and an increasing contribution from SaaS in the P&L, which typically has DSOs more in line with maintenance.

On Slide 24, our Q1 2021 LTM cash conversion was 110% well above our target of converting at least 100% of IFRS EBITDA into operating cash. We expect our cash conversion to be at least 100% for 2021, driven by strong growth in recurring revenue. We have already seen strong growth in ARR this quarter and expect this to continue going forward.

On Slide 25, we show the key changes to the group liquidity since the end of the year. We generated 75 million of operating cash flow in Q1 2021. The other main movement was the share buyback of 89 million.

Our cash position on balance sheet at the end of the quarter was 66 million with our net leverage reaching 2.1 times. We expect our net leverage to remain at comparable levels at year-end 2021 accounting for the share buyback and the free cash flow generation.

Now, turning to Slide 26, we had strong growth in ARR of 7% with limited attrition on maintenance and SaaS linked to our core business of Transact and Infinity. HCL remains a considerable headwind as we have the Kony non-banking customers moving to HCL from Temenos in particular in the first half of this year. I'm pleased with our ARR growth in the face of this headwind.

We also had strong growth in deferred revenue, up 28% which reflects good levels of collection on maintenance, as well as, the increasing contribution from SaaS in our P&L mix. This drove strong free cash flow generation of 46 million, up 28% year-on-year. We remain disciplined around our CAPEX spend. I would note that our net capitalized development costs for the quarter was 5.4 million down from 6.2 million in Q4 2020. We expect net capital light development for 2021 to be at/or below the prior year level assuming no further M&A.

Now moving to Slide 27, I wanted to quickly remind you of the KPIs that we introduced in February with our Q4 results and the Capital Markets Day. We introduced 2 new KPIs to help you monitor the progress we are making. These are first target for total bookings, which includes the fair value of license, committed maintenance and SaaS. This will give you an indication of how the total new business generated is growing and should make the acceleration of our business through SaaS visible.

We are now also guiding on annual recurring revenues, ARR, which we consider best practice to demonstrate the growth trajectory of our recurring revenue streams. ARR is defined as all committed revenue across SaaS and maintenance and will include new customers cross and up-sell and any attrition. Please note that we have put slides in the appendix with tables showing SaaS ACV, ARR, total bookings and free cash flow by quarter to help you track these numbers.

On Slide 28, I'm pleased to reconfirm our guidance for 2021. As always, the guidance is on a non-IFRS basis and in constant currencies. You can find the FX rate assumptions in the appendix. We are guiding for SaaS ACV growth of 40% to 50%, which is largely incremental.

For ARR, we guide for 10% to 15% growth, driven by committed SaaS revenue from the ACV we have booked and the reacceleration in our maintenance growth rates during the year.

We expect to grow total software licensing by 14% to 18% as licenses returned to growth this year and as we have seen in Q1 2021, and driven by the sustained growth in SaaS.

Total revenue growth is forecast at 8% to 10% as we digest the somewhat slower growth of maintenance and services in 2021, both of which we expect to accelerate throughout the year and in 2022 and beyond. As a reminder from 2021, we will be excluding the costs of share based payments and related social charges from our non-IFRS presented financials, i.e. the IFRS 2 costs.

We have provided a full reconciliation for our 2021 EBIT guidance under both the new and old definition, as well as, IFRS 2 costs for both 2020 and 2021 for reconciliation purposes. We are guiding for EBIT growth of 12% to 14% to U.S. Dollars 362 million to 369 million, implying an EBIT margin expansion of 130 basis points from 35.9% to 37.2%. We have maintained our target of converting over 100% of EBITDA into operating cash and expect DSOs to be below 105 days by year-end 2021. We expect a tax rate of 16% to 18% for 2021 and our net leverage to be at comparable levels by the end of the year.

On Slide 29, I'd like to reconfirm also our 2025 targets, which we presented at our Capital Markets Day in February. These targets are organic growth rates per annum. We expect total software licensing to grow 15% to 20% as we see banks committing to strategic IT spend for digital transformation, driven by competitive pressures and structural changes to their end markets. SaaS will clearly grow significantly faster at around 30% plus and licenses are expected to grow at 10% plus per annum. This will drive total revenue growth of 10% to 15% per annum.

We expect to expand the EBIT margin to around 41% by 2025, driven by strong growth in license and maintenance, improving our SaaS gross margin and leveraging R&D and G&A. I would note we still expect to grow R&D on an absolute basis by around 7% to 8% per annum to enable us to invest in our SaaS and cloud capabilities, AI and technology in particular. With demand clearly returning post 2020, we expect total bookings to grow 17% to 22% per annum, increasing our backlog and providing revenue visibility with ARR to grow at least 15%. ARR in particular will drive free cash flow growth of at least 15% per annum to reach more than 600 million by 2025.

Now, next on Slide 30, this is a slide we showed last quarter, but I wanted to give a quick run through of our non-IFRS EBIT and margin expansion in 2021. Our EBIT growth will be driven in particular by our growth in recurring revenue, as well as, licenses, whilst continuing to invest in R&D and sales and marketing, and with greater variable cost accrual compared to 2020. As such, we expect to deliver an EBIT margin expansion of around 130 basis points in 2021.

As previously mentioned, we are now excluding IFRS 2 costs from our EBIT margin targets. We have also provided the respective bridge under the previous definition in the appendix.

Finally, on Slide 31, I'd like to give you a quick update on the share buyback. As a reminder, we launched a share buyback of up to 200 million in February. So far, we have completed 89 million of this, and the buyback will resume as of tomorrow.

With that, I hand back to Max.

Max Chuard

Thanks, Takis. Turning to Slide 33, I'd like to invite you all to join us at TCF Online on the 26th and 27th of May. This is our annual global client forum, and a great opportunity to see new product releases, listen to our clients and engage with our product and management teams. And you can register using the link below or on our website.

Finally on Slide 34, in conclusion, we had a great start to 2021 across all our KPIs. We had very strong growth in SaaS with signings with new clients, and volume growth in existing clients. And the growth in ACV from 2020 is now reflecting in our SaaS revenue growth as well. We also had strong license growth in the quarter.

The growth in total booking was outstanding, reflecting the mission-critical nature of our product and the strength of our sales force and our clients' relationships. And this growth was broad based across both new and existing customers, and both license and SaaS. It give us great confidence in delivering on our 2021 guidance.

Our business model of selling packaged upgradable software, with a single code base on-premise of SaaS, enable us to grow revenues and expand our EBIT margin as well as we saw in Q1. And our strong cash collection and increasing SaaS contribution is driving our operating and free cash flow this quarter, and our growth in deferred revenues give us increased visibility. To maintain our leadership position in our market, we continue to invest in our business, in particular, in R&D and sales to drive our future growth.

With that, operator, I'd like to open the call for Q&A.

QUESTION & ANSWER

Operator

We will now begin question and answer session. Anyone who wishes to ask a question or make a comment may press * and 1 on their touchtone telephone. You will hear a tone to confirm that you've entered the queue. If you wish to remove yourself from the question queue, you may press * and 2. Participants are requested to use only handsets while asking a question. Anyone who has a question may press * and 1 at this time.

The first question comes from James Goodman from Barclays. Please go ahead.

James Goodman

Good evening. Thank you. Maybe I could start just on the U.S., it sounds like you are very satisfied with the performance there. It's very important clearly for the medium-term growth prospects. Maybe you could just talk us through a bit the competitive dynamics in the wins that you had across licensing and SaaS you know, particularly on the licensing side were they displacing competitors, or who... maybe who are you up against regularly in the deals? How does the U.S. look in the pipeline, is it as strong relatively as it was this quarter?

And then I had a couple of questions, just a bit more clarity on the SaaS metrics development. Just trying to understand that better, please. The first of those was just looking at the SaaS revenue, sequentially more than year-on-year, was up a couple of million just under? And... But I was more expecting a full quarter of the Q3 bumper signings that we saw. So can you just help us with how much of the Q3 or Q4 ACV is yet showing up in the quarter, and how much is still to come? And why we wouldn't... shouldn't expect, I guess, a decent sequential increase into Q2 given the run rate of ACV?

And secondly, on SaaS on the ARR, if I just look at the run rate at the quarter, I guess, times 4, it's a bit ahead perhaps of the reported ARR that you've given again with the ACV that you signed I might have expected a reported ARR to be higher. So can you sell-through that sort of FX or phasing or Kony just to understand that metric? Thank you.

Max Chuard

Hi, James. Let me start with the U.S. And let me start with the pipeline, which... yes, Q1 was very strong in the U.S., but I have to say also the activity that was developed during the quarter is... has been very, very encouraging.

So I'm very pleased with the development that we are seeing in the U.S. both on the SaaS and on the license side. And as I had mentioned in February, we also see some larger, more strategic project coming to market in the U.S. So there is really I would say increased activity overall in the U.S. both for the more traditional license side, but as well on the SaaS. And as you know, it's now a few years we've made significant investment to ensure that we are well-positioned in that market. If I look at SaaS, I would say our technology, our modern cloud-native technology is really making a major difference in that market. As I mentioned, we start to have some amazing references as well in that respect, I mentioned Varo, I mentioned PayPal. But we've got all like Grasshoppers and other. We've got globally more than 60 challenge banks using our solutions. So we are very well-placed in that respect.

On the more traditional side of the competition when we are facing the incumbent vendors like FIS and Pfizer, which I would say would be the main 2. I think you know, we've... over the years we've been able to build more and more references, more size, more credibility in the U.S., which is really starting to play and to resonate very well in the market. We mentioned the Tier 1 bank that went live on Transact in Q1. So there is more and more for us to be successful and really to leverage the main differentiator, which is our technology, the advanced technology, the ability to deliver projects very effectively and very cost effectively. And now that we are slowly overcoming the fact that we are new, the fact that now we've got more and more references, more credibility, I think we are able to position the solution better. At the same time as you know, we've announced 2 strategic partnerships in the... globally, but clearly there is a U.S. angle with both DXC and Salesforce that also supports the generation of activity in that market.

Takis Spiliopoulos

Hi, James, let me take the 2 SaaS questions. So clearly, this is why we have been flagging the impact from HCL, which is quite material probably around 2 million to 3 million on a quarter. And if you look at the ACV numbers, we should... with usually 3 to 4 months delay, the ACV growth will then flow into the SaaS revenue line. So clearly, this was the one from Q1, sorry, from Q3 was offset now in Q1. The one from Q4, we will see largely offset also for Q2. But then the way we see HCL, because we know the expiration dates you will see then a material step-up starting in Q3, when you would see the 3 million, 4 million sequential improvement you would expect.

So this is just masked by what is flowing off from our P&L from the Kony nonbanking customers, yes, substantial impact in H1 and much less in H2. So this is why we gave that kind of, transparency. So yes, sequentially I think from Q1 to Q2, you should see a slightly higher SaaS growth, but probably around the same growth rates on a year-on-year basis.

On ARR a similar impact, but much smaller. The 7% we have shown here will probably have been around 8%, if you exclude the impact of HCL, again on the full year it's also... it's more about 2% impact on ARR, but this is included in our 10% to 15% ARR guidance we have for the full year. So, yes, we give the full transparency.

On attrition, we have not seen any change, talking about the attrition on the banking business, same for maintenance and SaaS. It's around the usual 3% 4% per annum. We haven't seen any change on this one. So this is clearly all driven by the HCL impact.

James Goodman

Yes. Much appreciated. Thank you.

Operator

The next question comes from Chandra Sriraman from Stifel. Please, go ahead.

Chandra Sriraman

Yes. Hi. Thanks for taking my question. Hi, Max. Hi, Takis, congrats on a strong start to the year. Just a few questions from my side. The implementation go-lives are picking up. I was just wondering, in terms of feedback for remote implementation, is that becoming the norm? I'm just wondering if the new set of lockdowns have an impact on deal signatures that you see?

My second question, just coming back to cannibalization. The ACV step-up you saw in Q3, that has remained quite strong in Q4 and Q1. Can you just comment on cannibalization? Are you seeing anything or you're able to forecast these cloud deals better now? And maybe the last one, would you be able to comment on cloud gross margins, or is that a more annual thing. Thanks.

Max Chuard

Hi, Chandra. Let me take the first question. We don't see from the fact that there are still restrictions as a concern to close deals. So if you want the fact that we've been able to deliver the last 12 months very successfully projects remotely, 100% remotely. Clearly, that has overcome any concern that some customers had, for instance, potentially in Q2 2020 or even in Q3 2020. So that I think we've been able to overcome.

Now, regarding the future of those implementations. Today, the majority... I mean, most... all of it is done remotely.

Probably as things were to normalize, when the lockdowns will be lifted, we probably will see an hybrid model, where there will be clearly much more use of remote and cloud technology as well. But I think there will be also a little bit of physical presence.

Clearly, our sales front, we are gearing up to be able to deliver all the projects remotely, because that's one thing that we've been pushing and driving for a very long period of time. And I think with COVID, we were able to get a long way. Probably once things will go back to normality, we will see a little bit of an hybrid model. But I think some of the learnings we got during COVID will be there too for the long term.

Takis Spiliopoulos

Yes. Hi, Chandra. On cannibalization, we have not seen any in this quarter. We have not changed or not see any changes to the pipeline, both on the license and ACV side, i.e., deals flipping over. So I think, ultimately, our guidance is based on what we have guided for the long term that you could see 1% to 1.5% of the growth being cannibalized, but clearly, nothing seen in Q1 at this point. Also on the SaaS ACV growth, yes, there has been a couple of strong quarters. Now, if you keep in mind there are 2 growth angles for SaaS ACV, one is you acquire new clients. So this is the incremental part, new fintech's, new challenger banks coming to us. But you also grow with the success of your existing client base. So this is more volume-driven.

And the third element we have seen overall in our ACV business, also some deals becoming larger in terms of the size. Now, it's clearly going to be still volatile. I think we feel comfortable with our ACV growth rate for this year having had a good start; it's clearly something we take for us.

Now on the cloud gross margin, what we have guided for is still valid, hasn't changed in the last 2 months. Clearly, we've put in a lot of effort in the automation part. So, that's... that will start to come through in this year. Also the volume-driven operating leverage will come through. Let's say we feel comfortable with the way the gross margin is evolving throughout the year. And clearly, there has been an improvement in Q1, but we will not provide on a quarterly basis what the number is. But for the full year, clearly as we highlighted, we want to make a considerable step forward, i.e. front-end load the gross margin improvement we have forecasted until 2025.

Chandra Sriraman

Great. Thank you.

Operator

The next question comes from Laurent Daure from Kepler Cheuvreux. Please go ahead.

Laurent Daure

Yes, thank you. Good evening, Gentlemen. I have 2 questions on my side. Coming back to the comments you made on competition, I was wondering how often in your pipeline do you face in fact an internal solution, I'm referring for example to the SEB decision to work with Google? So, any granularity on that would be useful.

And my second question is more for Takis, it's back on the HCL headwind, but more for the following years. Where will we stand in terms of revenues to be missed kind of by the end of the year? Thank you.

Max Chuard

Hi Laurent. Listen, on the... how often do we see an internal solution in a process. It used to be the case in the past where most of the times we had an internal solution on that. I would say that over the years, this has mainly disappeared, not totally, but I would say we see less and less the bank coming with their own system as a credible option. I think the bank understands that there is a need to change and understand that putting more money into the legacy will not address the issue.

So, we see less although still it happens sometimes. I'm not saying that we don't see at all, but really at a lesser degree compared to what we had in the past. So, when we compete, it is against traditional vendors, as we've mentioned, or against when it's for SaaS against some cloud... new cloud vendors that have emerged the last let's say 3 to 5 years. And the way we... why we win and the way we win most of the cases is because we can compete very effectively with very modern technology, cloud native, but also to reach an angle, we cover... we've got our customers in one of 5 countries. So, we understand the localization of in every of those countries. But at the same time, and this is what differentiates I would say compared to the new vendors is the fact that we've got 27 years of deep banking expertise. So, we combine both... the best of both worlds and that's why we are very strong from a competitive point of view.

Takis Spiliopoulos

And Laurent, I'll take the question on HCL. So, as we had pointed out in previous discussions, the Kony non-banking customers were mostly on one to 2-year contracts. Now, we signed the contract in June 2020, which means by Q2 2022 all will be gone.

Now, there is obviously an overweight in this year which means for next year, you will have let's say very limited headwind on SaaS and licenses and overall total software licenses. So, I would say maximum 1% to 2%.

Laurent Daure

And in terms of their payment what is left to be cashed in from HCL?

Takis Spiliopoulos

Yes. As we said, this is a multiyear deal, 7 years, which means we collect the annual payment in Q2 of this year, same as we did last year, the initial one in Q2 2020. So then we'll have another, basically, 4 years or 5 years going forward with the annual payment in every Q2 of the year.

So going forward, if you already look at 2022, there will be probably a net impact which is almost zero. And beyond 2022, so 2023 and beyond, you will have, let's say, 1, 2 percentage points positive impact on your license line from this HCL payment.

Laurent Daure

Okay. This is very clear. Thank you, Takis.

Operator

The next question comes from Andreas Müller from Zürcher Kantonalbank. Please, go ahead.

Andreas Müller

Yes. Good evening, Gentlemen. Thanks for taking my questions. Takis mentioned already that the average deal size went up also particularly in the competitive deals. Do you see that as a trend going forward as well? And on what fact do you attribute that in general?

Takis Spiliopoulos

I think, hi, Andreas. I think it's probably premature to call something a trend. Keep in mind, Q1 is still the smallest quarter of the year. So any individual deal can have an impact on the average deal size, be it on the license side or be it on the SaaS side. So I would not read anything into that. Clearly, our ambition as we always said on the license side is to do more with Tier 1 banks. This is the same also on the SaaS side. If you are successful in winning new customers and they're successful, these trends do move the average deal size up. They buy more volume, they buy more accounts and so on. So, I guess, that was probably one of the main drivers, as we did quite a bit of business with existing customers in Q1.

Andreas Müller

Okay. And on the competitive deals, the new clients, I mean, there, at least according to my calculation also on the deal size was even larger in Q1 than pre-COVID level. You say, okay, and you attribute this to a very small quarter, but on the competitive deals nothing has changed there or nothing to interpret, is that right?

Takis Spiliopoulos

No, we would not call any trend change that... neither on the competitive deals, nor on the existing deals. I mean, clearly, with more and more product you can sell, there is... hopefully, we can drive our clients to buy more. So this could be a factor in the long term. But we don't see any change to average deal sizes, you know which we would need to call out.

Andreas Müller

Okay. Thanks. And as a last question on the share-based comp, I mean, that still guided to 20 million. Now you have already made 6 million. And can you again explain the assumption between the 20 million? That's basically if you hit the targets, or is that something we shouldn't attribute to that?

Takis Spiliopoulos

Yes, there is a number... there are a number of assumptions underlying these IFRS 2 charges. Keep in mind, there are always free long-term incentive plans running in parallel. So it's not just for one year. So this is clearly a factor. This is the estimate at the beginning of the year. We still believe the 20 million is the right number. It's not a linear... it's not a linear approach. So I think, in terms of modeling, I would take 3 times 4 million, 4.5 million for the next 3 quarters. So it's still unchanged, 20 million for the full year.

Andreas Müller

Okay. Thank you very much.

Operator

The next question comes from Hannes Leitner from UBS. Please, go ahead.

Hannes Leitner

Yes. Thank you for letting me on. I have also a couple of questions. Just a brief follow-up on the HCL. Could you help us understand, if you get any revenues if HCL signs with a new customer in that non-core business? So, is there any potential SaaS revenue stream coming from there?

And then you presented the average contract lengths. Maybe you can comment, where it's surprisingly quite a short-lived license and maintenance contract again for 3.6 years. We would have thought that should be slightly longer.

And then, in terms of your SaaS revenues, could you maybe decompose a little bit where the different buckets are? It feels a little bit with again the low average contract lengths of 3.9 years, it seems that this is more on the front office compared to core banking. And on that note, you mentioned at the Capital Markets Day that there... the core banking customers you have they are less likely to move. So with only 10 customer wins in Q1, it seems you have quite a lot... a difficult position to win competitive deals. Maybe you can comment there what you see there? Thank you.

Takis Spiliopoulos

Okay. Let me take those first. So, the one you mentioned at the beginning, no, there is no royalty or any revenue flying to us, if HCL signs new customers on their software, or what they have developed, there is no flow through to us. So we don't benefit anything. So the HCL is... the HCL partnership, if you want this is just one way when the customers are moving to them at the contract expiry and the one-time payment per annum we get there.

Now on the contract length, if you keep in mind, let me explain this in a bit more detail. Our standard contracts on initial signing are for a 5 year maintenance commitment, if we look at licenses. Now, when an existing client buys more licenses, more modules, or more seats, this is usually added to the master agreement i.e. with incremental maintenance. If this is within the first 5 years, the incremental maintenance will have a tenure which is equal to the balance of the 5 years remaining, okay? So after 2 years, its 3 years left. After 3 years, its 2 years left. So this is one driver of the average tenure.

Now after 5 years, most clients move to one year rolling maintenance contracts i.e. the incremental license and maintenance would also therefore... also have a tenure of one year. So if you put this all together the 3.6, we have shown is the average tenure across all contracts. So yes, if you have more new logos, more new wins, clearly that pushes up the average tenure.

On the SaaS contract length, now we have seen and it's the same approach there, on the SaaS, what we always said is between 3 and 5 years. Clearly, Infinity seems to have as a trend usually more towards 3 to 4 years, while Transact is 4 to 5 years. Clearly, we had now more Transact in Q1. That's why the average tenure was higher than last year.

Now again, I would not read into those numbers too much from our first quarter. Clearly, it has... it has had a positive impact on bookings that we increased the tenure. And clearly, this is a trend we're going to see for the rest of the year, it's going to be very good, but I think we stay conservative in our approach to what we take as a forecast.

Hannes Leitner

Thank you. And then just a brief one, on the housekeeping question. In your Annual Report, you had a share-based compensation of 6 million in the cash flow statement. So the delta is some social charges. Can you give us that number because to reconcile it then to the previous year, because there you reported the 39 million? So just to understand the moving parts here. Thank you.

Takis Spiliopoulos

Yes, we'll follow up on the detailed split.

Hannes Leitner

Thank you.

Operator

The next question comes from Stacy Pollard from JPMorgan. Please go ahead.

Stacy Pollard

Hi. Thanks very much. 2 questions from my side. First of all partnerships, DXC and Salesforce. Can you comment a bit more to their contribution to the Group in Q1 or perhaps expectations on a yearly basis? And then do you plan to do more strategic partnerships along these lines? Second question, just thinking about net leverage, what kind of leverage would you stretch to for M&A? And does the current M&A pipeline... well, basically what does the current M&A pipeline look like for you now?

Max Chuard

Hi, Stacy. Listen, we just announced the DXC and Salesforce partnerships. So clearly, no contribution in Q1 from either of them. And as I said, there is significant activity, workshops taking place. But probably the impact on 2021 would be rather limited. However, I said there is a lot and it's very exciting.

On the Salesforce side, the plan is to be able to launch it in Q3. So hopefully, we will see some impact from that, but it's really going to be towards the end of the year. So I will say limited for 2021.

Now clearly, the fact that Temenos is open from a technology point of view, works with any partner and that the fact that we are 100% committed to the banking segment, it brings lots of opportunities for us to collaborate and to partner with other companies. And I think that could be... we could see more of those partnerships in the future. Clearly, we are very focused on making those successful. And if we can see that there are other partnerships that can leverage and give us access to the market faster and be a win-win between them and us, I think it's something that we will clearly consider.

Takis Spiliopoulos

Hi, Stacy, let me take the leverage questions. I mean, clearly, we have ample ammunition left despite the buyback. However, one of the reasons why we did the buyback was clearly seeing our shares as undervalued, but at the same time seeing M&A opportunities at very, very high levels in terms of valuations, which did not make sense for us.

Now the pipeline we still got on the M&A front and we have not seen anything, which would make us jump up and down and execute let's put it this way. So if nothing happens on the M&A front, we'll be towards the same level of leverage by the end of the year. How far or how far above can we go, you have seen with Kony we went above 3 times. If necessary clearly, we have covenants in place, which allow... which allow for that or more but this has no priority right now or this year.

Stacy Pollard

Okay, useful. Thanks.

Operator

The last question for today's call comes from Michael Foeth from Vontobel. Please go ahead.

Michael Foeth

Yes, good evening, Gentlemen. Just 2 follow-up questions. On the U.S., you mentioned that your investments are starting to resonate. I was wondering if you can comment on how your deal win rate has developed in the U.S. today versus maybe 2 to 3 years ago. And how does it compare with your win rates that you're seeing in Europe?

And the second question would be on SaaS, somehow looking at your ACV numbers, which are very strong; the SaaS guidance of 30% growth seems sort of conservative. So is it correct to assume that you're very confident with that 30% growth number for 2021? Thank you.

Max Chuard

Hi, Michael. On the U.S. deal win rates, let me say that what is very exciting in the U.S, clearly, we started in the U.S. doing a lot with Infinity. I mean, that's through different acquisitions that we've done. And what has really improved, clearly Infinity continues to progress. But if I focus now more on Transact, which was really I have to say where we've seen a significant improvement on our win rates would be on the Transact side, and I will say both on the SaaS and on the license. So I think that's very encouraging. And I think also the U.S. is really a market where there is really increased activity and Transact now is very well placed and had something... I mentioned PayPal, what we are doing for them is just amazing and the volume and the ability to scale and to support them. And all of that is on Transact. And so we've got more and more of those success stories to tell in the U.S. So I'm very pleased with the increased win rate that we've got in the U.S. on Transact.

Takis Spiliopoulos

Hi Michael. Let me take the ACV question. So it is correct that we have seen this strong ACV growth as I explained before to James not yet flowing through. However, we are confident that having the visibility on HCL when the contract expires that this... we have seen the worst. If you look at the full year guidance of 30%, it incorporates 5 percentage points of headwind on... just from HCL. So I think the underlying 35% probably shows the picture in a much better way.

Now assuming there is no change in attrition or anything and we keep delivering on the ACV, because what you deliver on Q1 and Q2 ACV is then basically locked-in for the year, we feel confident with that number. But also beyond I think it's worth pointing out if we deliver the 40% to 50% ACV growth for this year, this will drive a 30% plus growth also for 2022 and beyond.

Michael Foeth

Okay. Very clear. Thank you.

Max Chuard

Thank you, everyone. And as I said, I hope you'll be able to join us on TCF online, and I'm sure we'll be talking very soon. Thank you. Bye.

Operator

Ladies and Gentlemen the Conference is now over. Thank you for choosing Chorus Call and thank you for participating in the Conference. You may now disconnect your lines. Good-bye.

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