

SolarWinds, Inc.
Form 10-Q
August 02, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the quarterly period ended June 30, 2013

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the transition period from _____ to _____

Commission File Number: 001-34358

SOLARWINDS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)
3711 S. MoPac Expressway
Building Two
Austin, Texas 78746
(512) 682.9300

73-1559348
(I.R.S. Employer
Identification No.)

(Address and telephone number of principal executive offices)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

On July 30, 2013, 75,413,380 shares of common stock, par value \$0.001 per share, were outstanding.

SOLARWINDS, INC.

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Safe Harbor Cautionary Statement

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and the Private Securities Litigation Reform Act of 1995. Such statements may be signified by terms such as “anticipates,” “believes,” “continues,” “estimates,” “expects,” “intends,” “targets,” “may,” “could,” “should,” “will,” “would” or similar expressions and the negatives of those terms. In this report, forward-looking statements include statements regarding our financial projections, future financial performance and plans and objectives for future operations including, without limitation, the following:

Our expectation to grow our business by focusing on initiatives such as increasing our presence in several key geographic markets including Asia-Pacific, Latin America, Europe, Middle East and Africa by expanding our product portfolio, localizing marketing material, and establishing new relationships with distributors and resellers, expanding our web presence, brand awareness and improving our communication with prospects and our current customer base both domestically and internationally, acquisitions of products that will expand our network management and systems and application management offerings or potential acquisitions of products in new markets and international expansion company-wide at lower cost locations to drive our competitive advantage;

Our expectation to continue to pursue acquisitions that will enable us to enter new markets, or new segments of our existing markets, by bringing new product offerings to market more quickly than we can develop them;

Our belief that the acquisition of N-able will allow us to leverage the opportunity associated with rapidly growing adoption of the cloud and SaaS-based services among SMBs by enhancing our remote monitoring and management offerings and adding MSP service automation to the broad range of management challenges that we address for the IT industry;

Our belief that we can bring the key features of our operating model to the N-able business and help drive revenue growth in the remote monitoring and management market;

Our expectation to continue to generate solid growth while delivering strong operating income and to increase our cash flows from operating activities with our disciplined approach to investing in our business combined with our large market opportunity;

The premise that we will be able to deliver ongoing value to our customers and maintain a long-term financial relationship with the users of our IT management products;

Our expectation that our revenue growth will be approximately 20-22% for the full year of 2013;

Our expectation that core product transaction volume growth will be the primary driver of our new license growth;

Our expectation that our Non-GAAP operating margin will be approximately 49% for the full year of 2013;

Our belief that IT-related trends and the limitations of existing offerings present a significant market opportunity for our products;

Our expectation that our revenue will continue to grow as we capitalize on IT-related trends and other market opportunities through acquisitions and development;

Our objective of targeting total new sales growth of 20% for our existing license and subscription products and new product offerings over the next three to five years;

Our belief that there is a substantial opportunity for additional sales of our software in the Europe, Middle East and Africa, or EMEA, region, the Asian-Pacific region, and the Latin American region, and our intention to increase our sales, marketing and support operations in these regions;

Our belief that although difficult economic conditions in certain geographic regions may adversely affect the sales of our products, such conditions also could offer us an opportunity to market and sell our products to mid-size businesses and enterprise customers at compelling prices compared to the prices of some competing products;

Our expectation that the U.S. federal government will continue to be a significant market opportunity and our belief that the ease of deployment, power and scalability of our products gives us a competitive advantage to sell to various agencies and departments of the U.S. federal government;

Our expectation that we will continue to experience inconsistency in the buying pattern of the U.S. federal government for larger transactions with our products;

Our belief that many of our larger transactions with the U.S. federal government, both new licenses and maintenance renewals, are dependent on specific projects that may not be continued at the same scale in the future due to budgetary

cuts or other reasons, and the reduction or cancellation of specific projects such as these could result in our sales to the U.S. government growing less rapidly than expected or even decreasing;

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• Our expectation that maintenance revenue will continue to increase in absolute dollars in future periods;

• Our expectation that our cost of revenue will increase in absolute dollars and fluctuate as a percentage of revenue as we acquire additional companies or technologies and as we increase our headcount to support new customers and product offerings;

• Our expectation that we will incur approximately \$16.0 to \$17.0 million of incremental expenses for the remainder of the year as a result of the N-able acquisition;

• Our expectation that our operating expenses will continue to increase in absolute dollars as we make long-term investments in our business both domestically and internationally;

• The possibility that our operating expenses in future periods may increase in absolute dollars and fluctuate as a percentage of revenue as we acquire additional companies or technologies and integrate the businesses;

• Our intention to continue to grant equity awards to our current executives and employees and those who join us in the future through acquisitions or otherwise, which will result in additional stock-based compensation expense;

• Our expectation that we will continue to hire sales personnel in the United States and in our international sales offices to drive new license sales growth;

• Our expectation to continue to invest in our websites, online user community site and marketing programs to drive customer downloads and support our new product launches;

• Our expectation that the continued expansion of our research and development centers in the Czech Republic and India will continue to result in an increase in facilities and personnel costs;

• Our expectation that we will continue to invest in our research and development activities by hiring engineers in our international locations, which will allow us to continue our research and development growth strategy internationally;

• Our expectation that we will incur higher administrative costs in future periods as our business continues to grow both organically and through acquisitions;

• Our expectation that our international income, as a percentage of total income, will increase and that such increase should result in a corresponding decline in our effective income tax rate;

• Our continued investment in the sales and marketing efforts that drive our revenue growth;

• Our expectation that our international cash and cash equivalents will continue to increase as a percentage of our consolidated cash and cash equivalents;

• Our intention that the earnings generated by our international operations will be invested indefinitely in those operations and our expectation that we will not repatriate those earnings to our domestic operations;

• Our estimation that our capital expenditures for the remaining six months of 2013 will be approximately \$3.0 million, primarily related to purchases of equipment and software in our Austin and Czech Republic locations to support their continued growth;

• Our expectation that repurchases of our common stock under our share repurchase program will occur over the next 12 months although the exact timing of repurchases and number of shares of common stock to be purchased will depend upon market conditions and other factors;

• Our expectation that our share repurchase program will be funded using our cash on hand and cash generated from operations;

• Our belief that our existing cash and cash equivalents and our cash flows from operating activities will be sufficient to fund our operations and our commitments for capital expenditures for at least the next 12 months; and

• Our expectation that the lease for our future corporate headquarters in Austin, Texas will commence in the second quarter of 2014 and our plans with respect to either terminating our existing lease through a settlement with our landlord or subleasing all or part of our existing corporate headquarters to a third party for the remaining lease term through May 2016.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially and adversely different from any future results, performance or achievements expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those summarized under Risk Factors and Management's Discussion and Analysis of Financial Condition and Results of Operations in our annual report on Form 10-K for the year ended December 31, 2012 and our quarterly reports on Forms 10-Q and other documents we file with the

Securities and Exchange Commission ("SEC"). Given these risks and uncertainties, you should not place undue reliance on these forward-looking statements. Also, forward-

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looking statements represent our management's beliefs and assumptions only as of the date of this quarterly report on Form 10-Q. Except as required by law, we assume no obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially and adversely from those anticipated in these forward-looking statements, even if new information becomes available in the future.

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PART I: FINANCIAL INFORMATION

Item 1. Financial Statements

SolarWinds, Inc.

Condensed Consolidated Balance Sheets

(In thousands, except share and per share information)

(Unaudited)

	June 30, 2013	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	\$148,894	\$179,702
Short-term investments	27,028	49,276
Accounts receivable, net of allowances of \$336 and \$271 as of June 30, 2013 and December 31, 2012, respectively	35,754	32,506
Income tax receivable	907	142
Deferred taxes	2,242	1,712
Prepaid and other current assets	3,675	3,322
Total current assets	218,500	266,660
Property and equipment, net	8,916	8,342
Long-term investments	20,351	12,823
Deferred taxes	1,951	338
Goodwill	252,342	158,601
Intangible assets and other, net	91,393	70,631
Total assets	\$593,453	\$517,395
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$4,203	\$4,050
Accrued liabilities	11,486	14,226
Accrued earnout	—	121
Income taxes payable	1,443	4,037
Current portion of deferred revenue	108,015	97,672
Total current liabilities	125,147	120,106
Long-term liabilities:		
Deferred revenue, net of current portion	6,472	5,084
Non-current deferred taxes	3,396	483
Other long-term liabilities	12,648	8,908
Total liabilities	147,663	134,581
Commitments and contingencies (Note 8)		
Stockholders' equity:		
Common stock, \$0.001 par value: 123,000,000 shares authorized and 75,328,950 and 74,633,412 shares issued and outstanding as of June 30, 2013 and December 31, 2012, respectively	75	75
Additional paid-in capital	247,944	229,277
Accumulated other comprehensive loss	(2,632)	(1,145)
Accumulated earnings	200,403	154,607
Total stockholders' equity	445,790	382,814
Total liabilities and stockholders' equity	\$593,453	\$517,395

The accompanying notes are an integral part of these condensed consolidated financial statements.

SolarWinds, Inc.

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Condensed Consolidated Statements of Income
(In thousands, except per share information)
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2013	2012	2013	2012
Revenue:				
License	\$31,131	\$29,454	\$61,856	\$56,911
Maintenance and other	45,373			