[NUAN] - Nuance Communications, Inc. Q3 2020 Results Conference Call
Wednesday, August 05, 2020, 5:00 PM ET

Officers
Mike Maguire, Head of Investor Relations
Mark Benjamin, Chief Executive Officer
Dan Tempesta, Chief Financial Officer
Diana Nole, Executive Vice President
Rob Dahdah, Chief Revenue Officer

Analysts
Saket Kalia, Barclays
Sanjit Singh, Morgan Stanley
Stephanie Davis, SVB Leerink
Jeff Van Rhee, Craig-Hallum
Daniel Ives, Wedbush
Shaul Eyal, Oppenheimer
Vikram Kesavabhotla, Guggenheim

Presentation

Operator: Good day, and welcome to the Nuance Communications Third Quarter 2020 Earnings Call. [Operator Instructions] Please note, this event is being recorded. Now, I would like to like to turn the conference over to Mike Maguire, Head of Investor Relations. Please go ahead, sir.

Mike Maguire: Good afternoon, and welcome to our Q3 2020 call. I hope everyone is healthy and remaining safe during these times. Joining me today to discuss our Q3 results are CEO, Mark Benjamin; CFO, Dan Tempesta; and Executive Vice President and General Manager of Healthcare, Diana Nole. Additionally, during the Q-and-A portion of the call, we will be joined by Chief Revenue Officer, Rob Dahdah.

Before we begin, I would like to remind everyone that our discussion includes predictions, estimates, expectations and other forward-looking statements. These statements are subject to risks and uncertainty that could cause material differences in our actual results. Please refer to our recent SEC filings for a discussion of these risks. All references to income statement results are non-GAAP unless otherwise stated. As noted in our press release, we have issued prepared remarks in advance of this call, which are available on our IR website. That material is intended to supplement our comments on this call today.

And with that, I'll turn the call over to Mark.

Mark Benjamin: Thanks, Mike, and welcome to Nuance. We're excited to have you on board. And good afternoon everyone, and thank you for joining us. Before we begin, I'd like to take this opportunity to share that my thoughts and those of the entire Nuance community continue to be with those who have been affected by COVID-19. We'd also like to extend our deepest gratitude for all of those who are working tirelessly on the front lines, especially all the doctors, nurses and clinical staff who are helping to care for those in need.

As an executive team, we continue to prioritize the health and safety of our employees, customers and communities, and therefore have maintained our work-from-home guidance for the majority of our global workforce. Overall, we continue to be very pleased with the effectiveness and productivity of our employees in this virtual environment.

In turning to our Q3 performance, I'd like to mention a few highlights before providing deeper context on our results. Despite COVID-19 challenges, we exceeded the high end of our guidance expectations for revenue and EPS. We delivered strong growth in Dragon Medical One and our newer cloud-based solutions in healthcare, which contributed to our continued Healthcare ARR growth. Our enterprise business continues to see solid adoption of our Intelligent Engagement solutions as companies accelerate their digital transformation strategies amidst the pandemic.

In line with our capital allocation principles, we fully repaid the $230 million that was borrowed under our revolver in March 2020. We hired Diana Nole as EVP and General Manager of our Healthcare business, who I will introduce later in the call. And finally, we published our inaugural ESG report highlighting our commitment to upholding high ethical standards, creating value and making a positive and lasting difference for our employees, communities and those we serve.

Digging into our performance a little deeper. I know many of you are interested to hear about the effect COVID-19 has had on our business, so I'd like to provide you with a brief update. As you saw in our prepared remarks, this quarter, we continued to advance our strategic initiatives amidst the pandemic that began to unfold over the past few months. As expected, our Healthcare business felt the effects of a widespread disruption in preventative care services and the deferral of elective procedures as health systems shifted resources to address the critical care of COVID-19 patients. This disruption was partially mitigated as elective procedures rebounded at a faster rate than we previously expected.

Our legacy Healthcare license sales saw a year-over-year decline due to project deferrals, though we did not see as severe an impact as we originally anticipated. And while we did see delays in certain deployment projects such as non-strategic EHR implementations, we have been partnering with hospitals as they learn to adapt, and we have been supporting them as they manage these initiatives remotely. In our enterprise business, we have experienced some COVID impacts, but have largely benefited from increasing trends toward digitalization and AI transformation.

Overall, I could not be prouder of our team for all their hard work and agility in quickly adapting to the new environment in which we're living. The success of our organization through these challenging times is a true testament to the resiliency of both our employees and our business.

We continue to believe that the headwinds associated with the pandemic are short term in nature and that our company is well positioned to capitalize on longer term trends that we are seeing. For example, we are beginning to observe hospitals strategically investing in telehealth and virtual care models, and we believe many of our products fit well within this strategy, which can act as a tailwind for our volumes even while face-to-face patient care volumes are down. Similarly, in our enterprise business, we are seeing an increased interest in our Intelligent Engagement platform as companies look to accelerate their digital transformation strategies as well as in our security and biometric solutions as fraud rates continue to rise in conjunction with the pandemic.

Dan will provide further details on the financial implications of COVID on our business later in the call; however, I do want to be clear that while our strategic solutions continue to show resiliency in the face of the pandemic to date, we do recognize that some of our global customers, particularly in Healthcare, are facing continued pressures directly related to the unpredictable nature of COVID-19. We will continue to support them as they care for our communities and will stand by them during these challenging times.

Taking a closer look at our Healthcare business. I am first and foremost excited to welcome Diana Nole to the team as our new Executive Vice President and General Manager of our Healthcare business. Diana brings more than 15 years of experience leading global healthcare operations, most recently serving as Chief Executive Officer of the Wolters Kluwer Health division, where she oversaw all operations for the $1.3 billion global provider of healthcare information, software solutions and services. Prior to that, she served as President for the Digital Medical Solutions division of Carestream Health, where she oversaw global operations for the $1 billion provider of healthcare equipment, software and services with global development sites. I am confident that her experience leading global teams who are delivering integrated AI solutions for healthcare's most pressing problems will be invaluable in propelling our Healthcare business forward and feel she has already made a positive impact in her first months here in the role.

I am delighted to have Diana on the call with us today. And without further ado, I would like to hand the call over to her to share a few thoughts with all of you. Diana?

Diana Nole: Thank you, Mark. I am truly excited to be part of the team and to be joining at such a transformative time in the company's history. Throughout my conversations in my first few months here, it is clear that everyone shares a fierce passion for helping to solve some of the healthcare industry's most complex challenges and to enhance the trust between physicians, clinical staff and their patients.

When I joined Nuance, I was already familiar with the company's decades long track record of innovating AI-powered speech driven solutions for healthcare providers. But more than that, I was familiar with how these innovations prioritize the doctor-patient relationship that is central to good care and even more essential to a positive patient experience. In fact, as then an outsider looking in, I was always impressed with Nuance's customer brand and loyalty. And now I see it from the inside, and it's even more impressive. I am thrilled to be able to continue to tackle these issues alongside so many talented employees here, and I look forward to advancing our strategic vision of the future of healthcare.

Mark Benjamin: Thank you, Diana. We're very excited to have you with us. From a Q3 performance standpoint, we continue to execute against our strategic healthcare plans of pivoting to the cloud, deepening our international presence and expanding downmarket.

As I mentioned at the beginning of the call, we saw strong growth in our Dragon Medical One solution, up 34% compared to last year. We continue to expand our cloud-based offerings internationally with the launch of DMO in Norway as well as closing our first Dragon Cloud deals in Germany and in Finland.

In our strategic focus of expanding our go-to-market capabilities into community hospitals and ambulatory environments, we're seeing positive traction as well, with new wins during the quarter such as Auburn Community Hospital. Just as a refresher, our international ambulatory and community healthcare initiatives were two of several important growth drivers for our future, and you should see these as delivering in the early innings.

In our diagnostics business, we continue to see solid demand for our cloud-based AI-powered solutions, with new wins from Novant, Methodist Healthcare System of San Antonio, and Lee Health. These deals are the result of our ability to deliver tangible results that are helping radiologists recover from the temporary suspension of non-urgent care through increased productivity, while affording them the ability to work remotely. Additionally, our clients benefit from our add-on solutions such as Follow Up Manager, which sits on top of our PowerScribe One platform and helps save lives while providing a strong return on investment for healthcare systems by tracking failed follow-ups on incidental findings.

The health of our DMO offering combined with these cloud-based radiology solutions and others, such as CDE One, drive persistent strength in our Healthcare ARR metric. While we are still in the early cloud transition with many of these offerings, we believe the traction we have seen to date validates our commitment to creating a highly recurring subscription-based revenue model. With these great results, we are now raising our full year ARR guidance to 24% to 28% growth, up from 13% to 21% that we forecasted just 90 days ago. This new ARR guidance range actually puts us nearly all the way back to our full year pre-COVID guidance. So needless to say, we are quite pleased with our salesforce's results.

We are also excited about the progress we have made through the quarter with our Dragon Ambient eXperience solution, or DAX. Physician burnout and exhaustion are primary concerns for hospitals and have only intensified in these challenging times. DAX eliminates time-consuming documentation and administrative tasks through the latest advancements in AI that support clinical documentation that writes itself. The impact of this offering continues to shine through for users with high physician satisfaction scores and a 20% increase seen in patient throughput due to the significant reductions of clinical documentation time from a physician's day.

Since DAX also allows doctors to leverage the technology for in-person or virtual and telehealth visits, we are also able to maintain exam volumes even when face-to-face encounters are down. Additionally, with our easily implemented solution, physicians can leverage our mobile app on their smartphone or other device and use that to capture patient encounters and clinical notes securely and automatically as part of their patient exams, regardless of type.

Although still in the very early stages, the value proposition of DAX is being commercially recognized, and we have signed several exciting new customers, including WellSpan Health, Boston Children's Hospital, Children's Hospital of Atlanta and Lehigh Valley Health Network. We continue to progress on the expansion of DAX, rolling out offerings for new specialties this quarter, including nephrology and neurology. Just as a reminder, these sales bookings are not yet included in our ARR guidance.

Finally, as you saw last week, we announced that Cerner has selected our virtual assistant platform to reduce the cognitive burden on care teams and improve the patient experience. Building upon the existing integration between our Dragon Medical platform and Cerner Millennium, our customers can now utilize our state-of-the-art virtual assistant technology to navigate and retrieve information from the EHR just using their voice. This allows clinicians to spend more time with their patients and less time on their computers. This was a competitive win for us and a testament to several factors including our deep existing relationship with Cerner, our superior conversational AI and speech and natural language understanding technology, our high-trust certification to ensure sensitive patient data remain secure; and our ability to support deep integration within Cerner's platform. Just on the news from the press release last week, we heard directly from many Cerner-Nuance customers on just how excited they are with this step forward in our partnership.

I'd like to turn now to our Enterprise business, where we saw revenues decline 5% year-over-year as we expected, due largely to timing of licensing and professional service projects that progressed ahead of plan in the first half of the year. Despite some temporary moratoriums on spend and other project deferrals during the quarter, we remain highly confident in the resiliency of the segment and overall demand for our state-of-the-art solutions.

With consumers increasingly seeking digital channels for customer service and online purchases, we experienced strong demand for our Intelligent Engagement products, landing our first sale in Latin America during the quarter with Banco Macro, one of the largest domestically owned banks in Argentina.

As always, this quarter we continue to put our customer needs at the forefront. With contact centers facing a surge in call volumes, our voice-to-agent messaging eliminates hold times by allowing customers to leave a detailed message that is automatically transcribed, understood and routed to agents, resulting in increased customer satisfaction and reduced call volumes in contact centers. We also added new support for organizations to integrate Google Business Messages directly with their customer service platforms, which creates a fully integrated, seamless experience for agents and consumers alike.

Additionally, as organizations continue to experience a notable spike in fraudulent activity with the pandemic, we saw persistent demand in the quarter for Gatekeeper, our cloud-based security and biometrics solution. We take pride in providing our customers with tangible cost savings and added protection, such as what we're doing with National Australia Bank, who is utilizing our

Gatekeeper offering to authenticate more than 120,000 customers within seconds using voiceprints. I am also extremely proud of our team for further enhancing the solution with the innovation of our AI biometrics age detection technology, which enables seniors to receive prioritized customer service and added fraud protection. Customers such as Telefónica are already seeing the benefits of this added layer of security.

Advancements across both our Healthcare and Enterprise solutions continue to gain us market recognition both from customer success stories as well as third-party validation. In fact, we are thrilled to have been recently named a leader in “The Forrester New Wave™: Digital-First Customer Service Solutions” as well as “Top Healthcare AI Innovation Leader” in Frost & Sullivan’s latest analyst report, “The Frost Radar: Artificial Intelligence for Healthcare IT, Global, 2020.”

Before I turn the call over to Dan, I want to take this opportunity to share a few additional corporate highlights from the quarter. By now, I think most of you know that making Nuance the best place it can be, both internally from an employee experience perspective as well as a great company to do business with, continues to be a priority for the executive team, the Nuance Board, and me. To that end, we have taken a number of actions in support of this, including the recent publication of our inaugural Environmental, Social and Governance report. As our first formally published progress report on these initiatives, we believe the document underscores our ongoing commitment to upholding high ethical standards, creating value and making a positive and lasting difference for our employees, communities, and those we serve.

As we look to uphold these high ethical standards, we also know that the more diverse we are as a company, the stronger we are, which is why we continue to value, celebrate, and actively support our differences of race, gender, orientation, thought, creed, and perspectives. This is something I personally feel very strongly about. So I recently signed the CEO Action for Diversity and Inclusion Pledge, which is my commitment to act on and support a more inclusive workplace for our employees, our communities, and society at large. We will continue to devote the necessary time and resources towards this effort to create a just and equitable environment, where all of our employees feel empowered to reach their full potential.

Additionally, and as part of these efforts to create a positive and supportive culture for our employees, we recently conducted our fourth annual employee opinion survey, which is designed to help us understand what it's like to work for Nuance so that we can identify current areas of strength as well as areas where we have the opportunity to improve. I am pleased to share that we had our strongest company-wide participation rate to date, and our results positively increased year-over-year across every single metric. The executive team and I are very pleased with these results as they are a positive indication that we continue to make Nuance a great place to work, which is important as our highly engaged employees are the driving force behind our cutting-edge technology and our ability to deliver superior customer outcomes.

The good work we have done internally is also being recognized externally, and this quarter, we were named one of the “Top 50 Companies to Sell For” by Selling Power, a business magazine focused on sales management solutions that publishes an annual list of the best companies to sell for in the United States. This accolade marks our sixth Employer of Choice award we have received in just 2020, which includes being “Best Places to Work” certified, and receiving accolades such as Best Places to Work for LGBTQ Equality, Best Places to Work in Boston, Best Places to Work for Dads, and Montreal's Top Employers award. We couldn't be prouder of the great strides we have made and we will continue to work hard to build upon the success.

And with that, I'd like to turn the call over to Dan to discuss our financial performance.

Dan Tempesta: Thanks, Mark, and thanks everyone, for joining us today.

First, I want to start off by echoing what Mark said and welcome Diana to the Nuance team. We have already seen the drive and passion from Diana that will help accelerate our momentum, and we are excited to watch her unlock even more value within our Healthcare business. I also want to reiterate Mark's recognition of the great work being done across our company to create a supportive and empowering culture for our employees. These focused efforts are not only creating a more collaborative environment, but are also helping to drive better, faster innovation and more meaningful outcomes for our customers.

And with that in mind, I will now turn to our Q3 results. As Mark mentioned, along with the discussion of our performance, I will also be addressing the ongoing effects that COVID is having on our businesses. And finally, I will conclude by discussing our fiscal year 2020 updated guidance, which we have detailed in our Prepared Remarks document.

Overall, our Q3 results were favorable in comparison to our guidance ranges, with revenues of $338 million and non-GAAP earnings per share of $0.18, both coming in above the high end of our range. Our Healthcare business experienced an organic decline of 13% year-over-year, due primarily to the impact of COVID, while our Strategic Healthcare revenue, which excludes HIM and EHR implementation revenue, declined 5% year-over-year. Our Enterprise business declined 5% year-over-year, primarily due to the timing of our license sales.

Before diving deeper into our results, it is important to take a step back and refresh everyone on where we were as of our last earnings call in May. At that time, we expected the impact of COVID to lead to reduced volume activity, deferred license and cloud purchases and deferred professional services implementations in our Healthcare business. Specifically, with regard to volume activity, during the trough in April, HIM transcription lines and radiology reports were down 50% to 55% from normal volume levels. However, throughout our third quarter, these volumes improved, and we exited the quarter at about 85% of our pre-COVID volume levels for HIM transcription activity and over 90% of pre-COVID volume levels for radiology reports being generated.

We also discussed how hospitals were reprioritizing some projects to address their immediate needs related to the virus. We anticipated that this reprioritization by hospitals could cause near-term pressure on both license and cloud bookings as well as impact our new ARR growth. While this impact was felt throughout the quarter, we did experience better-than-expected license revenues and encouraging results in ARR, which I believe is a testament to both the resiliency of our business models and the critical value that our products deliver. As a result, as Mark mentioned, we are raising our ARR guidance, which I will discuss shortly.

On the services side, we continue to see hospitals defer some electronic health record implementation projects, and we anticipate that this will lead to further pressure on our professional services revenue. It is worth noting that we have and continue to consider EHR implementation services as nonstrategic to our Healthcare business.

Looking through the effects of COVID, we continue to advance our strategic revenue priorities within our Healthcare segment. We had another strong performance in Dragon Medical Cloud revenue, which generated over $70 million in revenue this quarter. Additionally, we experienced growing demand for our new cloud-based solutions, including PowerScribe One, CDE One as well as Dragon Medical One within our international markets. While many of these products are still early in their transition to the cloud, we are excited about the progress seen so far and feel these offerings will continue to drive our topline performance moving forward.

Radiology and Other revenue declined year-over-year due to a combination of factors. First, the COVID impacts previously discussed lead to lower license and professional services revenue. Second, as we often note, this revenue category is subject to fluctuation due to the timing of multiyear term licenses. And finally, we had planned a near-term impact on revenue due to the ongoing migration of our on-premise install base to our new cloud solutions. In particular, during the third quarter we converted a number of term license CDI customers to our new CDE One cloud offering.

For accounting purposes, this conversion from term license to cloud services result in a noncash reduction of $8 million in exchange for ratable and recurring cloud services revenue that will come in as the services are performed. This migration is strategically important, and we will continue to aggressively look for opportunities to convert current term license customers to our cloud offerings as fast as possible. While we experienced an overall 32% decline in Radiology and Other revenue due to these factors, we are pleased with the performance and the solid growth in cloud ARR and cloud revenue in this category.

Turning to the Enterprise business. Revenue declined 5% year-over-year during the quarter, primarily due to the timing of large license revenue and related implementation projects as well as some temporary COVID-related project deferrals. As a reminder, Enterprise revenues remain subject to fluctuation from period to period related to the timing of license activity. Because of these dynamics and, in particular, the strong license revenue we saw in the first half of 2020, we always encourage investors to assess our Enterprise revenue performance on an annual basis. With that said, the license revenue declines in the quarter were partially offset by growth in our Intelligent Engagement offerings, with particular strength from our Live Agent and Virtual Assistant businesses.

Moving on to our balance sheet. As of June 30, we had a cash and marketable securities balance of $313 million. As you will recall, in March, we made the decision to draw $230 million from our revolver out of an abundance of caution to preserve liquidity as the impacts of COVID were just starting to be felt. As we exited the quarter, we had a better understanding of how COVID impacted our business and our liquidity profile. Therefore, we made the decision to pay down the revolver at the end of our third quarter, reducing our interest expense for the remainder of the year. With the paydown, our share repurchase program is no longer suspended, and moving forward, we will continuously evaluate opportunities for share repurchase and debt retirement.

And one final note on the revolver. Today, we also announced a 12-month extension of our revolving credit facility, which will now mature in April of 2022. Our cash flow from operations in the quarter was $32 million, down year-over-year due to COVID impacts on both revenue and billings. While we previously discussed some potential risks regarding our cash flow due to the possible expansion of DSOs as hospitals request extended payment terms, our DSOs for the quarter remained strong at 57 days.

Let's turn now to our updated guidance. First, we reiterate that the basic tenets of our business model laid out during Investor Day still hold true when you look past the virus impacts. More specifically, we continue to expand our market share across our strategic businesses while migrating to the cloud in Healthcare. We remain committed to our most strategic investments in R&D and Sales, all while making responsible capital allocation decisions. Collectively, these advancements are enhancing the business from both a financial and operational perspective. The combination of our strategy and the resiliency of our business models position us well for the mid and long term. In the near term, however, COVID has and will continue to impact the results, although to a lesser extent than previously expected.

Before getting into the numbers, our 2020 guidance framework includes the following assumptions. For volume businesses like HIM and parts of our radiology business, the low-end of our guidance assumes a slight step back in volumes in the event the outbreaks in Florida, Texas, California and other states reverse the positive trends experienced to-date. This cautious approach is a result of the growing expert opinion to slow down or scale back the reopening of certain states and regions. The high end of our guidance assumes a continuation of the improvement trends we saw in Q3.

For our book and ship businesses, we expect project deferrals across both Healthcare and Enterprise to extend into the fourth quarter, and we have assumed performance similar to our experience in the third quarter. For our services business, particularly our EHR implementation services business, we continue to expect near-term pressure on bookings and project timelines. Finally, while we are committed to our strategic priorities and investments in 2020, we continue to operate with reduced discretionary spend, hiring and travel.

Taking these assumptions and decisions into consideration, we are updating our guidance as follows. We are raising our full-year revenue guidance by $25 million at the midpoint to a range of $1.46 billion to $1.48 billion, implying at 3% organic decline year-over-year at the midpoint. This update reflects the better than previously expected impact of COVID. We are narrowing the range of our full year EPS guidance from $0.10 to $0.05, resulting in guidance of $0.78 to $0.83. And we are reinstituting full year cash flow from operations guidance with a range of $235 million to $265 million.

Turning to our segment guidance. We are raising our Healthcare revenue guidance to a range of $901 million to $911 million, up $18 million at the midpoint from our previous guidance. We also would remind investors that we had a significant uplift to Dragon Medical license revenue in the fourth quarter of last year, resulting in a difficult compare to this upcoming fourth quarter. This compare will be evident on the Dragon Medical license and product line.

Our updated Enterprise revenue guidance is $527 million to $535 million, up $5 million at the midpoint from our previous guidance. We are also raising our Healthcare ARR guidance to $370 million to $380 million. This brings our updated midpoint to the low end of our original guidance range prior to the COVID adjustments. As Mark highlighted, this supports the strong results we are seeing from the salesforce related to our cloud offerings. Additional color on our updated guidance can be found in our Prepared Remarks document available on our investor website.

Lastly, before opening the call to questions, I would like to let you know that we will be attending the Oppenheimer Technology, Internet and Communications Conference on August 11 and the Deutsche Bank Leveraged Finance Conference on October 6. These conferences will be held virtually, and we hope to see you there.

With that, I would like to turn the call back over to the operator to take your questions.

Questions and Answers

Operator: And we will now begin the question-and-answer session. [Operator Instructions] And the first question today will come from Saket Kalia with Barclays.

Saket Kalia: Mark, maybe just to start with you. I would love to dig into DAX just a little bit more. Understanding it's early, can you just give some broad brushes about the pipeline there, what the reception has been on pricing? Maybe if Rob Dahdah is in the room, he could comment on that, as well as how you are going to go to market there. Or how are you going to market there versus maybe how you go to market with the rest of Dragon business? Sorry, there is a lot there, but does that make sense?

Mark Benjamin: Yes. Totally. I appreciate the question. Good to hear from you. So for starters, we are super excited about the new logos that we mentioned on today's call. That's just a handful of them. And just to remind you, Saket, as you know because you mentioned it's early days, we only did go to GA with the product in the first calendar quarter sometime in late February as COVID made its way to the shores of the U.S. So obviously, not the best timing to do to make a product launch. But despite all that, I'd say DAX is really performing remarkably well.

Let me start with the technology. I'll get to your go-to-market as well. I mean, the solution itself is the technology is critically important. And by all metrics internally from our teams, R&D teams, the solution is really exceeding even our most aggressive internal expectations as far as performance. So we're super pleased with the solution and its capabilities relative to the AI and ML models. Plus also, we're seeing from the early adopters, Saket, the patient counts and exams that are flowing through have come back, which are really important for the data modeling and really continues to make the solution, I think, quite differentiated and quite effective. So we're doing well there.

And also, and Rob is here, so he'll comment, we have been incredibly surprised in a positive way that with all these distractions taking place in our healthcare market at the provider level, facing COVID and other aspects, we're still seeing a tremendous amount of interest with DAX. We are conducting at great volumes a number of DAX presentations, product demonstrations that are live. And as you saw this quarter, because you follow us closely, this is our first quarter mentioning new wins within DAX, and, again, just a handful of them. So I'd say the go-to-market is really proving to be quite exciting from the market.

As far as what we are doing as far as these early signings, we are taking a very, I think, measured approach to starting these institutions with, say, 10, 20 or 30 docs across a handful of specialties, some of these early specialties that we have talked about, getting them in front of the solution, getting their providers using the solution and seeing how high the ROI can be, and the ROI being measured in many different ways, Saket. So from productivity and patient throughput to physician satisfaction, patient satisfaction, the accuracy of the clinical documentation and note that comes back from the solution. So there's just really many, many measurement points that drive the ROI and we are seeing incredibly strong results with some of these early pilots with these customers. So Rob, maybe you want to add some color on go-to-market?

Rob Dahdah: Yes, yes. Thanks, Mark. Mark covered -- as a former salesman, he covered most of the answer there. But I will say, with the obvious challenges around the current environment, we've been really pleased with the reception around even the pricing which we are delivering to the customers and prospects we have in our pipeline. And it's also given us an ability -- we always had a chance with our product suite to be able to pick up the phone and get a response to any health institution. But this has really helped us solidify the elevation discussions in the C-suite, and we got great reception there. It's a very meaningful opportunity for them to transform how they work with their patients, with their physicians. And so all of that has held true, and if anything, has been firmed up in the current environment. So we are very pleased here early on.

Mark Benjamin: Yes. Saket, the one thing I would add is that these early pilots with these new customers, all of them have very big ambitions with the solutions. So us planting 10, 20, 30 docs, maybe even 50 docs to start with in the early days, the early results and the early feedback from the first physician using the solution to the 30th or 40th is, "This thing is really delivering." And none of these customers are looking just to give this to 20 to 30. It's a much bigger proposition to them over time.

Rob Dahdah: Yes. Absolutely. Not one customer has indicated that their first signup is their last. This is literally a journey, and they're taking the first steps with us.

Saket Kalia: Got it, got it. That's great detail. I really appreciate it. Maybe if I could sneak in a follow up for you here, Dan. Slightly different part of the business, but I guess the question is how are you thinking about the trajectory of the HIM transcription business, perhaps, after COVID? And I understand that thinking about life post-COVID is tough just in general. But I guess do you think that on a normalized basis, we can get back to sort of that typical year-over-year decline that we were seeing before? Or do you think that COVID perhaps impacts that trajectory, again, for HIM transcription specifically long term?

Dan Tempesta: Yes. Saket, thank you. Good question. And of course, it is important in the model. Of course, in this fiscal year 2020, we're going to end the year at a number less than when we entered the year we thought we would be at. So our original guidance is probably going to be somewhere in the neighborhood of $10 million to $15 million less as we exit the year than what we originally started with. So normally, I would say it's a 15% decline and build that into the model next year and the year after, et cetera. Because we're ending at a lower number, I would probably say, maybe for 2021, you should think of it as a 10% to 15% decline, but thereafter, it gets back to that 15% level. So we're really not seeing any permanent changes or differences in that trajectory or in that business, so I think it does get back to a normal trajectory of decline thereafter.

Operator: And the next question will come from Sanjit Singh with Morgan Stanley. Please go ahead.

Sanjit Singh: Congrats to the team on the healthcare ARR raise for the year. We're almost back to what the original guidance was, so extremely impressive in a difficult environment. I actually wanted to follow up on DAX as well. Is there anyway, Mark or Peter, you can frame out the opportunity for in-person DAX on versus telehealth DAX? And what do you see as the bigger opportunity? And what do you see as gaining the earliest market traction? We could start there.

Mark Benjamin: Yes. So Sanjit, I'll start. And Diana's here, and she may have some input. And, of course, Rob's here. But certainly, telemedicine and telehealth and virtual exams have become, I think, quite popular. And DAX is really designed to serve both the in-room patient exam or a virtual exam with the same solution. And we're actually very excited about -- first, we've made DAX app driven. So any of these platforms that providers may use can integrate quite efficiently with DAX. So the physician during the in-room exam versus the virtual exam, I can assure you if they are using it for one, they're going to want to use it for both. So it does become very much quickly a way of life that's hard to go back to the old way, if you will, of doing something.

Sanjit, the other thing I would say regarding telemedicine or telehealth in general is the value proposition of DAX coupled with the productivity models that make telemedicine capable, meaning the telemedicine appointment is for the non-acute, non-emergent interaction between a physician and patient. So anything that is administrative, such as the heavy burden of clinical documentation that DAX alleviates is actually, you could argue, is an even much higher value proposition for that type of model. So we happen to believe that while it could accelerate and it could expand the use of DAX, we think it just as a heavy value proposition relative to either model for, in some ways, the same reason, but for some enhanced reasons.

So Diana, I'm not sure if you have anything to add.

Diana Nole: Yes. Mark, I would just reinforce my observation. I have talked with some customers so far. And, first of all, they say, telehealth is here to stay, and they are wanting to talk about what the platforms are. And so to your point, my experience has always been they want to use the same platform, whether it's an in-office or in telehealth. So we will be well positioned for that, and so I think that's one good thing for us. We are also a platform that is always very agnostic to the interface that we have, and so we always build our solutions to work with all of the various types of solutions that may be considered in terms of the video application of it. But it's really the backend embedded nature of our solution into the EHR that I think is what differentiates us in terms of being selected by the physician and the provider.

Sanjit Singh: That's super-helpful. And as a follow up, when we were talking to some of these early DAX customers, we definitely got that feedback on increased patient throughput, frankly much larger than 20% that you guys are mentioning in some of these specialties that we talked to. In terms of just how DAX is going to evolve, there are some pieces that still have some human intervention in it. What do think -- in terms of just the automation road map, is there any way to think about the timeline for when DAX even gets more automated, particularly between the summary -- the transcription of the conversation or the summary of the conversation and the turnaround for the doctor? How are you thinking about that piece?

Mark Benjamin: Yes. So it's the right question, Sanjit. So for starters, just understanding that the doctor or the physician themselves, they actually get a highly accurate clinical note from DAX. And whether there is an element that's automated or there's an element also runs through our quality review check which they all do, the accuracy in the note is really what the physician receives on day one of using DAX. So that's, I think, important to know. So it's not as if they are getting a lower quality note as the automation rates ramp. It really is a high quality note. And I think as you have done some very good market checks, the accuracy of the note is -- and we've heard from many of them that it's actually better than their own note. So that's, I think, important to have as a baseline.

But certainly, as the specialties roll, the automation, like the learning models, started to improve the automation rates. And then, much like we saw with Dragon Medical One, is that over time -- and certainly, the technological advances around neural nets and other things have helped close the gap in many ways. And we have incredible amounts of data to help model this. And now, we are collecting incredibly richer conversational data with our DAX solution.

So over time, hence the specialty rollout, like as an example, on ortho or ENT or some of our earlier specialties, the notes or automation rates are much higher. And that was kind of what I was intimating at the beginning. The technology is really showing even our own internal measurements with great promise. And over time, that will happen. But to be clear, there will always be a quality review process. We're talking about people's lives. And ultimately, no matter what, the physician or the provider has to sign off on the clinical note, but very encouraging from a technological capability and kind of as we ramp up the automation rates. And then again, it will go by specialty.

Operator: And the next question will come from Stephanie Davis with SVB.

Stephanie Davis: Congrats on the quarter. So we are seeing faster-than-expected recovery across the hospital space, which has had some beneficial effects to the hospital-facing health IT vendors. So beyond your Healthcare ARR, is there anything to call out about the pickup in traction there? And as a follow-up to that, what sort of timeline do these conversations have to translate into wins now that hospitals are considering buying again?

Rob Dahdah: Yes. Hi, Stephanie. This is Rob Dahdah. Thanks for the question. So definitely the right observation. We are able to have -- actually, I feel like because of the nature of our solutions, we were able to have discussions even in the darker hours of COVID because we just were critical to their success. And so I think it's definitely been good for us in terms of having more of those conversations and some of the other solutions that we have that maybe were more extended. But I think overall, it's definitely, as you saw in the numbers, reflected, been positive for us.

The DAX conversations are happening with greater frequency, so we don't have any tempering or dampening of that pipeline. And I think we're seeing more and more of an ROI from what we deliver, helping them as they think about how they're going to climb out of this because revenue is going to be very important to them. So overall, I think, as we said all along, we were very well positioned before this. And if anything, the nature of this crisis has really put us in a very good position going forward.

Mark Benjamin: Yes. Hey, Stephanie, this is Mark. So maybe I'll just add a little. So again, a number of our initiatives that you're aware of, conversions to the cloud in radiology, our international expansion, those are also -- we've seen a faster recovery, if you will, relative to go-to-market, relative to sales activity, relative to pipeline and actual deals, hence the ARR raise. I guess all those contribute to the improvement in ARR. And as an example, Europe's been -- they had the COVID effect sooner than us, and they therefore -- they've either learned to contain it, manage it or live with it, you choose. And so we're seeing some strength there. We're seeing that also with radiology.

So I think as Rob mentioned, the importance of ROI, the pressure now on the economics within the system, the provider systems, which were never great to begin, with and certainly now the most challenged they have ever been, the solutions have to have meaningful ROI. Fortunately, none of it requires capital, none of our solutions require any CapEx or any cost upfront, and they are higher ROI. So as I tell Rob, the fish just jumped in the back of the boat. Right, Rob?

Rob Dahdah: Yes. Piece of cake.

Stephanie Davis: Rob, just got to keep closing those deals. Mark, one other question on Cerner and your collaboration there. What sort of share economics should we think about for that? And does this mean that Rob is going to be able to leverage the power of the Cerner salesforce? Or is it something that could only be enabled if the hospital is an existing joint client?

Mark Benjamin: Okay, so I'll answer that, I think, in two parts, if you don't mind. So starting with the baseline of the Cerner-Nuance relationship. We've enjoyed a multi-decade relationship with Cerner. And our go-to-market and our product integrations, you could say, essentially, at the core level with DMO and Cerner have been, I think, something that both companies are quite proud of and the results are obvious. And the go-to-market approach has been a mutual go-to-market approach. We co-sell. They resell some. We play point on others.

So it's really been a very, I think, successful relationship with Cerner and that will continue. And in our announcement -- so that's the first part that I'd respond with. The recent announcement, which is super exciting for us, is Cerner was looking to expand their solution set on top of their EHR with a virtual assistant. And they were looking for the most competitive solution in the market. They wanted, in their view, what they could build their platform around and their virtual assistant skills around. And ultimately, any VA could sit on top of Cerner and sit on top of or integrate with Dragon Medical One.

So we, like anyone else, wanted to win the business. We love the relationship. We have, I think, nearly 80%, if not exactly 80%, overlap of Cerner customers using Nuance solutions. And we were excited to get the call and to get to the win and now allow them along with our capability with the VA to go to their customers that are -- whether there are DMO customers or not, again, we have high market share with them, now have a Nuance-created VA for Cerner to go to their customer base with. So it was a win we were thrilled with.

Operator: And your next question will come from Jeff Van Rhee with Craig-Hallum. Please go ahead.

Jeff Van Rhee: I will try to sneak a couple in here. Maybe just, Dan, starting with the radiology. I know you've talked about the migration paths and I believe the migration math on term to cloud was one to 1.5 times revenue uplift. And apologies, I kind of jumped in midstream here. But it sounded like you are calling out some headwind from that migration. And as I remember the math, it was a one to 1.5 uplift. Have you changed your outlook there?

Dan Tempesta: No. Not at all. If you are making a migration in the middle of a term license, so let's say you have a five-year term license and under the revenue rules, you take all the revenue upfront. If you change in, say, year three, you have to have an adjustment to some of that remaining payment still left on the term license that you took as drop-down, but you are going to enjoy -- so it's like a noncash adjustment. You are going enjoy all of that in that one to 1.5 times uplift in cloud services once we turn it on. So this is a really -- this is validating exactly what we talked about at Investor Day, and we are going to do more of it.

Jeff Van Rhee: Got it. Got it, fair enough. And then, I guess back to DAX for just a quick second. It sounds like great progress. Obviously, I think it's a game-changing product for the industry. If you take your Dragon users from in cloud, call it 500,000 to 600,000, I know you are rolling out DAX specialties fairly quickly here. When you to look out 12, 24 months, what percent of that's -- maybe you use 600,000 Dragon users. What percent of those will have an available DAX solution that's relevant to them?

Mark Benjamin: Well, I think if we -- Jeff, and you know the product quite well, so I realize you are pretty fluent at this point. I think the specialties will ultimately drive the SAM, if you will, the addressable market that we could have Rob actually go pitch DAX to and win. And what we are seeing with, essentially, every one of the names we've mentioned today and others is that these are multi-disciplined, multi-specialty hospital systems. And they're ultimately going to start with a few specialties and expand so we released, as we said in previous quarters, we are expanding to specialties every quarter, one to two to three per quarter. The team always likes when I use a number like that because it puts pressure on the R&D teams. But I think ultimately, the addressable market for us is to cover all the ambulatory specialties, which would largely cover the numbers you're using, the 500,000 to 600,000 physicians that use some Dragon solution today.

Jeff Van Rhee: Yes. Got it, helpful. Maybe just one last. Shifting gears, I want to touch for a second on Enterprise. Obviously, you've got the bifurcated businesses with voice and digital channels. I'm just curious, as the year has progressed, how have the pipes in those respective segments of Enterprise progressed, the both digital channels contrasted with voice channels, and specifically as to how you've seen the pipe progress through the year?

Mark Benjamin: Yes. I'll comment, and maybe Dan or Rob will comment on anything. But I think as we've laid out, as we laid out on Investor Day, our growth is really coming from the Intelligent Engagement category, which includes digital and our voice bio, or security bio business. And in the quarter, we actually had very good strength in our Virtual Agent, Live Agent or LAVA solutions, as well as others within the Intelligent Engagement platform. So we're seeing it exactly play out as we expected, including the numbers and including, hard compare, this quarter versus last year's Q3. So we're very pleased. We moved the year range up in the Enterprise business, essentially, to the higher end of even the original side of things. And I think Rob will cover pipeline, and Dan will add any color as well.

Rob Dahdah: Yes. Thanks, Mark, and thanks for the question. The pipe continues to progress. I think we have an opportunity across the whole spectrum, really. And as we mentioned even on the Healthcare side, it holds true for Enterprise. The solutions we offer now, which were always relevant are even more so in the current environment. And so we feel like we're in a very good position across the spectrum to be able to address these needs for our customers.

Dan Tempesta: Yes. I think that, Jeff, the only thing I'd add is if you think about our model and what we laid out on Investor Day, we're tracking really well. We said this year we would probably be 55% in the voice IVR space, and then 45% of that business would be the Intelligent Engagement. And that's lining up really nicely. And the bookings pipeline that we see come in is definitely trending towards that Intelligent Engagement category. So that helps us grow to that 55% in that three-year timeframe that we talked about. So feeling good about it.

Operator: And our next question will come from Daniel Ives with Wedbush.

Daniel Ives: So for Rob and Mark, just in terms of hiring, especially sales on the healthcare side, could you just talk about that in terms of activities just given the pipeline? Is that something that's just continued to step up, given the opportunities?

Mark Benjamin: Yes. Thanks, Dan. Absolutely. Obviously, early on, we were super-cautious as we were on the front side of this. But as we see our opportunities, we've always had support throughout it because we saw the growth. And it's really only possible with the investment that we've had in not only the systems, but the people. And so, yes, we're hiring. We're, of course, being selective. We think there's great talent available, fortunately or unfortunately for where they're coming from, but fortunately for us. So we're stepping up our hiring. And it's across the business, and it's not just a domestic thing. We have opportunities, especially as we grow internationally, to continue to grow our group out there. So we've been moving forward as planned.

Daniel Ives: And then, for both of you, and then, obviously, Dan can chime in too. In terms of just when you start to think about just a larger deal, in terms of just the size of deals in the pipeline that are larger, more hospital standardization deals across the board, especially in the next-gen cloud platform, is that something where you're starting to see a discernible trend in terms of just the scale and scope of deals?

Mark Benjamin: Well, the scale in terms of the size of the deals, we're fortunate. It's not a go, no-go where they have to big bang everything all at once and write a check. We have the opportunity to flex with the conditions and have something to offer pretty much every system we talk to and every customer, even on the Enterprise side. So you don't need to go all in. And I think that's really served us well because we've been able to have meaningful discussions, begin implementations, sign deals.

I think the number of deals, if anything, is increasing. So we have opportunities as we expand it into the mid-market, as we expand it overseas, as we take on these great partners like Microsoft. We have opportunities to get in a number of places that we weren't before. So I'd say the scope, the scale, in terms of volume has definitely increased. And that's where we're really excited.

Daniel Ives: Great. And Mark, does Rob wears three-piece suits on June calls too? Thanks.

Mark Benjamin: Yes. Rob has stolen the show here. And yes, his fashion today -- I think it's the first time he has put on a suit in couple of months. So he is pretty happy.

Rob Dahdah: Feels pretty good.

Operator: And our next question will come from Shaul Eyal with Oppenheimer.

Shaul Eyal: I actually want to start with the topic of public cloud providers within the healthcare arena. Clearly great partnership with Microsoft, but Google and Amazon, as we all know, not staying put. Nuance, without a doubt, is a trusted partner for the past couple of decades now. But wonder if there's any change going on. And, maybe, how's Diana thinking about this subject?

Diana Nole: Well, with two months under my belt, I would just tell you, I probably rely more on the 15 years of experience I've had in healthcare. And I think what has always attracted me to Nuance is, and what you will find, is the keys to success in healthcare is, one, you have to have the relationships with the providers. We have a very large install base. It's very satisfied. I think the other thing is we have a proven track record of working within the workflow of what the physician wants, which is the EHR. They demand it, and so you have to have these deep relationships with the EHR vendors like what we do. That's not to be undervalued.

And then, I think the other thing is we just have a tremendous amount of expertise in terms of the field that we play in. The massive amounts of data that we have and the ability that we have continued to leverage that for enhancements in our conversational AI, I think those are our competitive moats that we'll continue to rely on to be successful against any type of competitor.

Mark Benjamin: Yes. This is Mark, Shaul. So I think she answered it perfectly. It's almost as if she has been here for at least three months. But I would say -- the one thing that I would even repeat is the fact that we are a vertical software company that's highly specialized within domains. And healthcare is probably one of the most challenged as far as this deep domain expertise, meaning it's probably the hardest thing. Healthcare data is highly protected, and our experience from years and years, and the data that we have, and the trust that we have built with our customers that allows us to create market-leading solutions that make their operations better is really a differentiator. And it's not just a small differentiation. And the relationships are critical too because trust matters, but I would say being a domain expert as we are is really, I think, the big difference, too.

Operator: And our next question will come from Vikram Kesavabhotla with Guggenheim.

Vikram Kesavabhotla: I wanted to ask about some of the newer initiatives within healthcare, particularly with international ambulatory and community hospitals. And if you can just give us some more color on the feedback from those channels specifically and how you are thinking about the pace of adoption there, that would be helpful.

Rob Dahdah: Yes. So this is Rob. Thanks for the question. I'll start with it. Obviously, we're really excited. We set out to specifically and deliberately grow into those areas. And early on, you have a lot of -- there's a lot of promise, and you do all the research, and then you go strike out and you have to see what you get. And so far we've been really pleased. Obviously, we always operated internationally on prem and now, it's still relatively new, but we've been able to go and have a cloud base or clouds stood up in some of the key markets that we wanted to get to. We've hired our teams out there, and now we already have a key win in every one of those markets. So we'll say very early days, and certainly we'll get better as we go. But we are pleased in the international space.

On the midmarket community hospital space, that was really new area for us. We were totally opportunistic there prior. Again, we set out with a very specific plan. We have a team stood up there, and the early results have been very pleasing. And we're happy not only in a very difficult environment, but we can see the other side of this. And we know we're going to be able to bring value to our customers there. Our story is very well received, so it's all very promising here in those areas.

Vikram Kesavabhotla: Okay, great. And maybe just a quick follow up on DAX. It sounds like you're seeing some encouraging traction here in the early stages. But curious if you can just talk about how we should be thinking about the timelines of the contribution from DAX in your financial results, and in particular, if we should be thinking about this as a driver in fiscal '21 or further beyond that. Any color there would be helpful.

Dan Tempesta: Hey, Vikram. It's Dan. We have been really consistent on this that at this point, we are not commenting on the financial impacts. Although, we're trying to give color in this quarter and next quarter about what we are seeing. We will in November when we roll out the year for 2021. We're definitely going to talk more about the revenue impacts, the ARR impacts, those were excluded at this point, as well as maybe some broader economics on the model. But at this point, we're still gearing up to go to market. We're still getting experience, and we'll continue to give that level of color. But we'll do financials later.

Operator: And this will conclude our question-and-answer session. I would like to turn the conference back over to Mark Benjamin for any closing remarks.

Mark Benjamin: All right. I just want to thank everyone for joining us today and wish you and your families safety during these interesting times. So thank you.

Operator: And the conference has now concluded.