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DocuSign, Inc.

Second Quarter Fiscal Year 2022 Earnings Conference Call

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen. Thank you for joining DocuSign's Second Quarter Fiscal Year '22 Earnings Conference Call.

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As a reminder, this call is being recorded and will be available for replay from the Investor Relations section of the website following the call.

I will now pass the call over to Annie Leschin, Head of Investor Relations. Please go ahead.

Annie Leschin

Thank you, Operator. Good afternoon, everyone. Welcome to DocuSign's Second Quarter Fiscal Year '22 Earnings Conference Call.

On the call today, we have DocuSign's CEO, Dan Springer, and CFO, Cynthia Gaylor.

The press release announcing our second quarter results was issued earlier today and is posted on our Investor Relations website

Before we get started, I'd like everyone to know that we plan to participate virtually in a few upcoming events. These include: Wolf's Inaugural TMT Conference on September 8; Citi's 2021 Global Technology Conference on September 13; Piper Sandler's Global Technology Conference on September 13; and Jefferies Software Conference on September 14. You can find more information about these events in the press releases section on our Investor Relations website. As other events come up, we'll make additional announcements.

Now, let me remind everyone that some of our statements on today's call are forward-looking. We believe our assumptions and expectations related to these forward-looking statements are reasonable, but they are subject to known and unknown risks and uncertainties that may cause our actual results or performance to be materially different. In particular, our expectations regarding the effects of the evolving COVID-19 pandemic on our business, including the potential effects of the pandemic on our customers' businesses and the pace of digital transformation, are based on our best estimates at this time and are, therefore, subject to change. Please read and consider the risk factors in our filings with the SEC together with the content of this call. Any forward-looking statements are based on our assumptions and expectations to date, and, except as required by law, we assume no obligation to update these statements in light of future events or new information.

During this call, we will present GAAP and non-GAAP financial measures. Non-GAAP financial measures exclude stock-based compensation expense, employer payroll tax on employee stock transactions, amortization of acquired intangible assets, amortization of debt discount and issuance costs from our notes, acquisition-related expenses, fair value adjustments to strategic investments, impairment of lease related assets, and, as applicable, other special items. In addition, we provide non-GAAP weighted average share count and information regarding free cash flows and billings. These non-GAAP measures are not intended to be considered in isolation from, a substitute for, or superior to, our GAAP results. We encourage you to consider all measures when analyzing our performance. For information regarding our non-GAAP financial information, the most directly comparable GAAP measures and a quantitative reconciliation of those figures, please refer to today's press release, which can be found, again, on our website at investor.docusign.com.

Now, I'd now like to turn the call over to Dan. Dan?

Dan Springer

Thanks, Annie. Good afternoon, everyone, and welcome to our Second Quarter Earnings Call for Fiscal 2022.

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Today, I'd like to focus my comments on three key areas: our strong Q2 results; how companies are increasingly digitizing their agreement processes; and how we're cementing DocuSign as a critical pillar of the anywhere economy.

Jumping straight into our second quarter financials. DocuSign's strong performance continued as we delivered a balance of growth and profitability at scale. Revenue grew 50% year-over-year to $512 million, and billings grew 47% year-over-year to $595 million. Our international business continued its strong growth, up 71% year-over-year. We expanded our customer base beyond the 1 million mark, including the addition of 13,000 new direct customers, and some very significant CLM wins with large customers. Finally, we continue to see a strong expansion and upsell motion for eSignature and the broader Agreement Cloud suite, driving our dollar net retention of 124%.

Overall, I am proud of how our team has continued to stay in front of the evolving COVID business environment. We are helping organizations of all sizes, leverage the power of the agreement cloud to digitize the foundation of doing business, the agreement process. Not only do customers see DocuSign as a vital part of their response to COVID, many have also seen a better way of doing business from anywhere and we believe that will become their new normal. One of our customers, Stacy Johansen, who's the President of Downeast Insurance, told us that when COVID hit and they had to close their physical doors, DocuSign saved them. In her own words, and I quote, "If it weren't for the ability to get an electronic signature, we wouldn't have written half of the new business we did last year." Having succeeded beyond expectations by fully embracing digital tools, Downeast resolved to do business this way from here on.

Another example is one of Canada's largest automotive dealers. In response to COVID, the company adopted DocuSign eSignature and DocuSign Payments to support remote sales and service. The program was so successful, it spawned a larger initiative to offer digital transactions across their entire dealer network. As one company executive put it, "DocuSign has become part of facilitating the full breadth of remote experiences."

These are just a few examples of what we're seeing again and again. Being able to do business and operate from anywhere is what people now expect. Plus, it saves time, money, and trees.

To cement DocuSign's position as a critical pillar of the anywhere economy, we are executing on three core themes as a business. The first is to stay focused on customer success. We are helping our customers and partners to shift their perspective from reactive to proactive, and enacting enterprise-wide programs to automate and digitize their end-to-end agreement processes.

Let me highlight just a couple of examples.

One of our largest U.S. state government customers saw a substantial increase in the thousands of employees accessing their systems remotely. We were able to scale our eSignature solution to allow the HR and the administration teams to handle the increased load. In addition, the agency rolled out DocuSign's CLM to simplify three complex workflows, resulting in 97% of all contracts being completed in significantly less time. And we're not helping state agencies. Today, DocuSign served the majority of the cabinet agencies in the U.S. Federal sector.

In the private sector, one of the world's largest media and entertainment companies has been a longstanding DocuSign user, and has digitized over 400 paper-based workflows with us, growing adoption by 100% year-over-year. Now the company has deployed in multiple use cases and has seen a multimillion dollar return on their investment in the DocuSign Agreement Cloud.

The second theme is giving our customers an agreement cloud platform they can grow into. That means offering the most comprehensive set of applications and integrations available for the agreement process. They can start with eSignature and then expand into other areas, like contract lifecycle management, and

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into specialized solutions in verticals, like mortgage and life sciences. With every DocuSign Agreement Cloud released, we keep adding to our capabilities and differentiating our platform.

Let me note some of our latest highlights.

For eSignature, we debuted new ID verification capabilities to allow both automatic and manual identity review by senders. it's now also possible for an identity check to be done once and then remain valid until the envelope is complete, dramatically improving the experience for sender and signer alike.

We've improved the embedding and management of our Clickwrap solution, and one of our largest retail customers recently completed more than 1 million transactions using DocuSign Click.

We introduced a new integration and add-in for Splunk, bringing the security insights provided by DocuSign Monitor into one of the most popular enterprise monitoring tools.

We continue to grow the number of notarized transactions completed on our platform. Today, DocuSign Notary supports the most online notaries in 18 U.S. states, with more coming in the future.

Turning to CLM. Two key areas stand out for me. The first is our continued buildout of buy side CLM capabilities. We have released Obligation Management, which is huge, and a connector for our key partner Ariba. This add to other buy side connectors shipped earlier this year.

The second CLM highlight is our enhancement of AI-based search and reporting capabilities, within the offering we call CLM+. It features automatic contract term extraction and allows for searching of agreements, not only by keyword, but also by AI-driven concepts, such as renewal dates within the next 90 days. This saves a huge amount of time and manual effort.

And then, there's the trust and security enhancements to the DocuSign platform. We continue to bring enhanced security features to our product suite, with solutions like DocuSign Monitor, which I mentioned earlier. We are also deepening our trust and security relationship with our customers. For example, we recently held a number of CISO summits, and we are collaborating closely across our customer base in trust and security topics, where there's tremendous demand.

Together, these advancements in our products move us closer to a unified platform of record for agreements and agreement processes.

Finally, the third theme is our international business. This remains a highlight for us, as our teams outside the U.S. contributed more revenue in Q2 than in any other quarter to date. The key drivers for EMEA, LatAm and APJ mirror those that we've seen here in the U.S. And by way of example, one of Europe's fastest-growing enterprise-focused startups, Celonis, saw a dramatic increase in the volume of contracts that needed to be generated, reviewed and processed, a workflow that had been largely manual to date. But by implementing DocuSign’s CLM, the company addressed these inefficiencies, saving the legal team countless hours, and delivering contracts 80% faster than before. Further expansion is already planned into the procurement and HR teams.

In APJ, one of our largest financial services customers, the Commonwealth Bank of Australia, expanded its number of use cases, and saw a substantial increase in transaction volumes. One team saw a 175% increase in documents processed through DocuSign, and another noted a 17 day faster time to revenue. The customer's now embarking on an automation project to further integrate and streamline the experience up and downstream.

As these examples indicate, we're pleased with how our international business is accelerating, driven by the same factors of speed, cost efficiency, and user experience that are propelled domestically.

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Okay. Before I hand it over to Cynthia to walk through the financials, I want to mention another factor that has always been central to DocuSign - our environmental impact. Our eSignature solution alone has replaced billions of pieces of paper, along with significant amounts of the waste, water, carbon and wood that are required to make and transport that paper.

In addition, to help fight global warming, DocuSign is also committed to achieving carbon neutrality by 2022. As part of this effort, we have launched an ESG portion of our website and have organized a multi-functional team to coordinate our overall sustainability strategy. We will continue to help our customers realize their ESG goals, while we work to be a positive example in the running of our own business.

I'm incredibly pleased with DocuSign's performance in the second quarter. Our team has continued to deliver across the board and has done so with a real focus on customer and partner success.

I look forward to talking to you in the Q&A shortly. For now, over to Cynthia.

Cynthia Gaylor

Thanks, Dan, and good afternoon, everyone.

Q2 was another solid quarter as we outperformed on both the top and bottom lines. We crossed the half billion dollar marketing revenue for the first time this quarter, and once again, we demonstrated our ability to balance growth and profitability with solid operating results and strong cash flows.

Total revenue increased 50% year-over-year to $512 million. Subscription revenue grew 52% year-over-year to $493 million, thanks to strong customer demand, early renewals and upsells, driven by accelerated consumption from our expanding install base.

Our international business had another outstanding performance, with strength across the board, led by EMEA. In total, our international revenue grew 71% year-over-year to almost $114 million, representing a record 22% of total revenue.

Billings grew 47% year-over-year to $595 million, as we continue to see strong early renewals and expansion of existing customers.

Total customers crossed the one million mark, with more than 65,000 new customers added in the quarter. This brought our total customer count in Q2 1,053,000 worldwide, an increase of 41%, compared to a year ago. We added 13,000 direct customers, bringing the total to 148,000, an increase of 50% year-over-year. We also saw customers with an annual spend greater than $300,000 grow 37% year-over-year to a total of 714 customers. For the fifth quarter in a row, dollar net retention exceeded the high end of our historical range, coming in at 124%.

Total non-GAAP gross margin for the second quarter was 82%, compared with 78% a year ago, while subscription gross margin was 85%, compared with 83% a year ago.

Our strong revenue growth, again, outpaced spending this quarter. Non-GAAP operating margin was 19%, or nearly $100 million, compared with 10%, or $34 million, in the second quarter of last year. Investing for top line growth remains a high priority for us in the second half of the year, including increasing sales capacity and marketing programs, innovating our products scaling our back office systems and processes. We see the tight talent market as an opportunity to up-level and develop our people internally while adding complementary skills as we drive the next phase of growth.

Non-GAAP net income for Q2 was $98 million, compared with $35 million in the second quarter of last year.

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We ended the quarter with 6,551 employees, an increase of 31% over last year.

Our cash flow remained robust in Q2. Operating cash flow came in at $178 million, or 35% margin, due to continued top line outperformance. This compares with $118 million, or 35%, in the same quarter a year ago. Free cash flow reached $162 million, or 32% margin, in the quarter, compared to $100 million, or 29%, in the prior year.

We exited Q2 with $887 million in cash, cash equivalents, restricted cash and investments.

Now, let me turn to guidance.

Clearly, the last year and a half had been exceptional in nearly every way for DocuSign. In the last six quarters we had scaled our business nearly twofold, more than double our operating profitability, nearly doubled our customer counts, and reached our highest dollar net retention levels yet. Any way you look at it, this is impressive growth at scale.

Halfway through fiscal 2022, we had seen customers renewing earlier in the year as they've used more envelopes and their purchases catch up with consumption levels. While we do not expect to maintain the peak levels of growth seen at the height of the pandemic, our value proposition is strong. Regardless of whether people go back to the office, we don't see them going back to pen and paper.

Turning to the numbers. For the third quarter and fiscal year '22, we anticipate total revenue of $526 million to $532 million in Q3, or growth of 37% to 39% year-over-year, and $2.078 billion to $2.088 billion for fiscal '22, or growth of 43% to 44% year-over-year. Of this, we expect subscription revenue of $505 million to $511 million in Q3, or growth of 38% to 39% year-over-year, and $1.995 billion to $2.005 billion for fiscal '22, or growth of 44% to 45% year-over-year.

For billings, we expect $585 million to $597 million in Q3, or growth of 33% to 36% year-over-year, and $2.409 billion to $2.429 billion for fiscal '22, or growth of 40% to 41% year-over-year.

We expect non-GAAP gross margin to be 79% to 81% for both Q3 and fiscal '22. We expect non-GAAP operating margin to be 17% to 19% for Q3 and 16% to 18% for fiscal '22.

We expect to see a de minimis amount of interest and other income. And we expect a tax provision of approximately $6 million to $9 million for fiscal '22.

We expect fully diluted weighted average shares outstanding of 205 million to 210 million for both Q3 and fiscal '22.

In closing, we ended the first half of the year in a strong financial position. We are focused on investing for future growth, scaling our business and cementing DocuSign as a critical pillar of the anywhere economy. We would like to thank our customers and especially our DocuSign team for their partnership and hard work and helping us deliver another successful quarter. We look forward to continuing to execute in the second half of the year.

Thanks again for joining us today. We will now open up the call for Q&A. Operator?

Operator

Thank you. We will now be conducting a question-and-answer session. One moment, please, while we poll for questions.

Thank you. Our first question comes from Bhavan Suri with William Blair. Please proceed with your question..

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Bhavan Suri

Thank you. Can you guys hear me okay?

Dan Springer

Yes, can hear you fine.

Bhavan Suri

Great. Congrats and solid quarter, especially that NDRR (phon) number. That was fantastic. It's rare to see a company at scale improving NDRR, usually it trends down. So congrats on that. I have one question. It's really a big fundamental question. It's not about a quarter or even about a year, but it's not data. And we've talked about this a lot. As you think about the long term, we've talked about how you will leverage the mass amounts of contract data you have access to. You've talked about Seal, we've talked about remote notary, we've talked about a bunch of things. But I'd love for you to talk about, again, not a quarter or even 12 months, but 24 or 36, even three to five years, how are you going to monetize that data? How does that data drive stickiness but also monetization of platform? I'd love to just talk through that process. Thank you.

Dan Springer

Yes. So, really interesting topic and one we think a lot about. Let me break it into two pieces, what I think we will do and what I think we won't do, particularly in that timeframe you just described. What we are going to do is leveraging the existing data and the reporting and analytics tools we have as well as the increasing focus on artificial intelligence to go deeper to leverage that data to help our customers run their business better. And I gave an example in the prepared remarks about how folks have been able to learn more about their business and be able to search against their agreements that they've done in the past to understand how they could quickly find information to, again, help them to improve the performance of what they do. We think we have a huge investment opportunity there, which we're going to aggressively invest in. The Seal Software was a great example of an acquisition we did to enhance, in this case, our artificial intelligence, engineering skill set, but I think you're going to see us doing a lot more in the data science world to make our products more able to help customers run their business better.

Second thing is, we can mine that information to help us drive more customer success. So we can take a look at how people are using our products, how they're not using our products, which use cases they're not availing themselves of. When they have incomplete segments of agreements because certain parts of the company might not being as responsive as others and help them really pinpoint and run their business better and help them figure out ways to grow more with DocuSign because of that.

So that's probably the—to give you a couple of flavors of things we're excited about.

One of the things that a lot of people ask about is, would we be able to figure out a way to leverage all the agreements across our different customers, to offer different kinds of services to people. We're super sensitive about that. At this point in time, we are a B2B software company. Our job is to serve our customers. Taking their data for some other purpose is not on our road map in any way. I agree that there's sort of a lucrative sounding opportunity there, but at this point when we talk to our customers they say, "We'd like to use our data ourselves, thank you very much. I'd like you to make the good living you do of helping us be successful with our business, not sort of extract that information to use in another way."

I would tell you, the one exception to that is, when you think about the way we train our models, particularly around things like artificial intelligence, the fact that we have lots of customers, over a million

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customers now, we had a 13,000 new direct customers alone in this last quarter, we're going to get more and more people using our model that is going to allow us to do better learning on those models, which will of course be a benefit across all of our customer set. But to the specific data, we're not going to take our customers' data and use it for other purposes.

Bhavan Suri

No, I think it's helpful, and again, I'm going to stick to the same question but push back a little bit. I totally agree with you that you'd want to cross data and take someone else's data and share with someone else, especially across the same competitive customers. But I guess my question is, help us think through, Dan, how you're monetizing it? I concur others have had data for a long time and they're always talking about benchmarking data and selling benchmarks back to customers whenever they have expenses, whatever we can show you is the best for that buck. Help us understand how that AI it drives stickiness but monetization I think is interesting. And not again, today, but over time, how should we think about where DocuSign ends up benefiting from a revenue and earnings perspective from that?

Dan Springer

Yes. Well, I think there's a couple of things, and going off again on that first what we are going to do, the first bucket I talked about, let me give you a couple of examples of how we're seeing that play out. But to be clear, the bulk of it is not about us monetizing that data, sort of back to those customers, but just allowing them to be more effective. And we just have a really strong point of view here that if we drive customer success and we increase the quality of the ROI they get, it's only good for our business. It just drives further adoption of the core business we have. So our thinking isn't about a new sort of set of service offerings, but enhancing what we already do with the Agreement Cloud so people would want to put more with us.

Now, one of the benefits it allows us to expand our footprint, I think, related to your question is, when someone realizes that they should have all of their agreements in our repository in a sort of a CLM solution at DocuSign, that means they're going to go out to all of the other parts of the company that haven't yet adopted our eSignature, as an example, and say we really want to consolidate and get all that information into one repository. We believe that is the way we win with data by showing people that when they integrate across their Agreement Cloud with DocuSign that the information we can extract across their agreement and help them across their business, understand how to operate it more effectively and more efficiently, that's where the payout comes to them and then in turn it comes to us because they grow with us.

So that's really the core of how we think about it as opposed to a new set of offerings where we might leverage that data to effectively sell back to them.

Bhavan Suri

I appreciate it. Congrats and thanks for the candor. I really appreciate that. (Multiple speakers). Thank you.

Operator

Thank you. Our next question comes from Sterling Auty with JPMorgan. Please proceed with your question.

Sterling Auty

Yes. Thanks. Hi guys. I just have one question as well, and it's really regarding one of Cynthia's comments about not having sustainable growth at the peak levels of the pandemic, which no one

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expects. But this week in particular, we've seen a number of high growth companies highlighted by Zoom starting to show that post-pandemic deceleration. My question is, how should investors think about the pace of moderation in your growth as we move forward, especially in light of the high growth that you're showing on the international front?

Cynthia Gaylor

Sure. Thanks for taking questions, Sterling. So, I think we've been talking about it in the last several quarters, right, that we wouldn't expect our growth to maintain at the peak levels that we saw kind of during the height of the pandemic. Now that's not to say that we still won't have very strong growth and solid growth. We had a very strong first half of the year and we're guiding a strong second half. So I think one of the beauties of our model is it is a subscription-based model and so these things tend to be gradual but we did see peak levels of growth at scale during the height of the pandemic and we wouldn't expect that to continue. So it's very consistent. I don't think there's anything really different in kind of what we're seeing now versus what we were seeing before and saying before in terms of our growth rates.

Sterling Auty

Understood. Thank you.

Operator

Thank you. Our next question comes from Brad Sills with Bank of America. Please proceed with your question.

Brad Sills

Great. Thanks guys, and congratulations on a real nice quarter. I wanted to ask on the Agreement Cloud, obviously you've seen some early traction there. Congratulations on that. I know there's a lot of hard work on the product side and you cited some of the deliverables there. My question is, where are customers starting here? is it typically with insights, or analyzer? Are they already running eSignature? Or is it CLM that they typically start with as a repository for terms and conditions and then they go into analyzer? What is the typical path look like for kind of the entry in the Agreement Cloud? Thank you.

Dan Springer

Yes, absolutely, Brad. So the first answer is sort of implied in your question. I'm going to make sure I'm absolutely clear about it. The tip of the spear for us is eSignature. So the vast, vast, vast majority of our customers start with signature, and for the simple reason that until you've figured out a way to digitize your agreement and capture them in an online fashion, it's really hard to do the remaining aspects of the Agreement Cloud. You don't have digital agreement. So clearly, eSignature is where people start.

What we're seeing is the second move tends to be to CLM. It's the construct of once they start thinking about that repository that you referred to in your question, that's where we really see the opportunity for them to start thinking about a full feature Agreement Cloud that they want to build out across their own system of agreements. So CLM is where we see the next move, and that's where we see ourselves, as you've heard me mentioning on the prepared remarks, where we see a lot of traction right now.

One of the things to keep in mind is, last year, when we had the surge in eSignature demand that Cynthia was just referring to at that peak of COVID, we had our customers really pushing us to go signature, signature, signature. Of course, that was natural for us because that's what brought us to this dance, right, but we said we had to sort of slow down some of our focus on the other parts of the Agreement Cloud just to meet customer demand because we are at our core a customer success company and the DocuSign employees rallied to meet that surge in demand. Now, this year, we're starting to see the

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opportunity go back to where we were really two years ago and say now let's focus on CLM, it's that next big opportunity to really expand people into the Agreement Cloud. We think that will be the foundation for most companies in how they really build out the rest of the Agreement Cloud beyond signature.

Brad Sills

That's great. Dan, thank you so much. Maybe just a follow-up on that. What is the effort involved to go from eSignature to CLM? What does the implementation cycle look like? Given that this is a repository, there's data that resides in here. Is there an SI partner community that you've developed here to help with that work? Or is it more seamless? Maybe it's just not that complicated to go from eSignature to CLM? Thank you so much.

Dan Springer

Well, as you guessed, we're working hard to make it as seamless as possible, but let me be absolutely clear that the construct of someone becoming an eSignature customer is very different than becoming a CLM customer. And we've done a fantastic job in our core signature product to build an amazingly easy to use service. And one of the things that's indicative of that, if you look at the fact that we have over 900,000 customers that have come to us through the web and they never had to talk to anyone at DocuSign if they didn't want to. We're a wonderful people to talk to, I hope you understand, but they don't have to. They can sign up online and start using our award winning software.

So, when you get to CLM, you absolutely are going to probably have a statement of work. We'd love it when we get to use one of our SI partners. We do have a fantastic professional services team. But that goal, that organization, that sort of train the trainers, and over time we really want to see that SI ecosystem really will blossom to the point that it's a smaller and smaller part of what we do.

Now, less than 5% of our revenue is services. It's not like it's something that's become a big part of our business. But we really feel the right way to be as ubiquitous as we can is to build a strong network there. And then we believe for the vast majority of customers they will leverage, whether it's our ProServ or if they have a really strong IT team internally and they have available resources, which is fairly unusual, if they have that they can do it themselves, but the hope for outcome is it'll be the SI network and we're excited about that progress. We've been building a super strong ecosystem there and that's a focus for us in the years to come.

Brad Sills

Great to hear. Thanks, Dan.

Operator

Thank you. Our next question comes from Scott Berg with Needham. Please proceed with your question.

John Godin

Hey guys. This is John Godin on for Scott Berg. I appreciate you taking my question. Are you guys seeing anything different as far as trends go over this past quarter as far as the mix of growth coming from higher consumption levels of existing use cases versus adding additional use cases or moving across the different departments?

Dan Springer

So in terms of if we're doing anything different, we're going to be, of course, responsive to our customers. And so, while we do have a fantastic customer success organization that's out there suggesting to our

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customers where their most likely next applications might be and what use cases might make the most sense for them.

The answer is, again, we respond to the needs of their business. From a customer standpoint, I think we're seeing growth across both. We are seeing a lot of people expanding the volumes, I gave some examples in my opening remarks of customers who said, we have a use case, it's working well with DocuSign and we want to do more of that. Commonwealth Bank is a good example of that.

But we also have seen fantastic examples of people expanding the number of use cases. Remember our Land and Expand model is really based upon the fact that we get in, we deliver fantastic ROI to one group in the Company for an initial use case that we land with, and then expand across not only more use cases, but also more departments and other divisions within that company.

And so, I would say from the standpoint there, there's nothing different that I've noticed in the last year than prior years in terms of that mix, I think at the very peak of COVID we probably saw an increase in more use cases, that sort of expansion of more things people were doing over volumes because they just realized they were critical parts of their business they needed to address in the anywhere economy they hadn't done. Today, I think we're probably back to the normal mix of what's increasing the volumes of existing use cases and what's increasing new use cases.

John Godin

Great. Thank you, guys.

Operator

Thank you. Our next question comes from Karl Keirstead with UBS. Please proceed with your question.

Karl Keirstead

Thank you, and congrats on the nice numbers. Cynthia, I'd love it if you could talk a little bit about your margin outlook for the second half. Despite raising your total revenue guide by $50 million, you left your operating margin target of $16 million to $18 million intact and that would require a step-down in the fourth quarter, so maybe you could talk a little bit about what assumptions are driving your second half margin outlook. Thank you.

Cynthia Gaylor

Yes, thank you for the question. So, in terms of margin, we've been performing at the low end of our long-term target margin. And as we said last quarter, we're really looking to make sure we are investing for growth just given the large market opportunity we have and the traction we're seeing in the business.

So, we'll continue to do that, particularly building sales capacity, in our marketing programs and in our product development teams. And we will continue to do that through the back half of the year. Also, remember, as we look into next year, we do look to hire in Q4 and for folks to start in Q4, that will build capacity going into next year and so Q4 tends to have more expense built into it than some of the other quarters.

So that's driving those assumptions, I'd also just remind you from a margin perspective, some of the top-line outperformance we've seen in the first half, certainly shows operating leverage in our business model, right? But we are looking to invest for growth over the long term, and that's what's built into the assumption in the second half in terms of the margin.

Karl Keirstead

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Got it. Okay. And then maybe a follow-up again for you, Cynthia. You mentioned that you had another quarter of good early renewal and expansions. When you look into the guidance you provided for the second half, what are you embedding in terms of a continuation of those early renewal and expansion trends that you saw in Q1 and Q2? Are you expecting that to moderate in the second half?

Cynthia Gaylor

So, the way I would describe it, I think, and we talked about this a lot on last quarter in Q1, we did see a strong early renewal in Q1. I would say that has continued to moderate and was baked into the guidance. As we came into Q2 and similar assumptions are baked into the guidance as we moved to the second half of the year.

But we wouldn't expect to have those peak levels that we were talking about last quarter and the quarter before. But we always will have some early renewals, which are a good thing, because it shows customers are using the product and consuming at higher levels. But we wouldn't expect those peak levels, so our expectation on that is consistent with the guide and it's baked in how we're looking at our consumption trends and then the revenue trends (inaudible) a lot of that.

Karl Keirstead

Got it. That's very clear. Thanks, and congrats again.

Cynthia Gaylor

Thank you.

Operator

Thank you. Our next question comes from Rob Owens with Piper Sandler. Please proceed with your question.

Rob Owens

Great. Thanks for taking my question. Was hoping to drill down a little bit on the international front and the success that you're seeing. I think it is about a year ago where you announced a new President of International and obviously, we've seen acceleration over the last year, so, maybe help us understand where you're seeing success and what the second half is going to look like over the next year. Thanks.

Dan Springer

I think we've been pleased across the board with international. I don't think you've put up numbers in the 70s for growth unless you're having pretty good success across the board. I would say our strongest performance in the quarter was in EMEA, which is our largest geography outside of North America.

But it was, again strong across the board; APJ, LatAm performed well for us. And I think going forward, it's more of the same. I think we've talked a lot about this construct that we had this focused eight in terms of the core countries where we're operating in and I think we want to continue to focus on those eight and I think over the next year or so you're going to see us expanding on that a little bit.

We may end up getting to a place where it's more like nine or ten countries where we see that we have sort of a presence, not just online. We sell to over to 180 countries if you look at our online business, but we really have dedicated people with feet on the ground.

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So, I think that's the way I think about it is the core eight will be big. Europe, I think, is going to continue to be a super exciting opportunity for us. But we're investing aggressively in branding internationally, and we don't have the same well-known reputation outside of the U.S. as we do have in the U.S.

And we're putting—Cynthia referred to the idea of building sales capacity, and a significant portion of that will also go into the international markets. And we are super bullish that we have a big opportunity.

Keep in mind, when you look at that growth, this quarter we hit a record and it's still only 22% of our revenue is coming out of our home country. And so that is a low number for what the opportunity is. So, we have a lot of growth ahead internationally.

Rob Owens

Thanks, Dan.

Operator

As a reminder, we ask participants to limit themselves to one question. Our next question is from Pat Walravens with JMP. Please proceed with your question.

Rob Owens

Oh, great. Thank you. Let me add my congratulations. And I'm assuming that reminder was for me. So (multiple speakers).

Pat Walravens

All right. Hey, Dan, we'll stick on international. I think the eight-cores are North America, Australia, U.K., France, Germany, Japan, Brazil, and Mexico. And so, the largest economy (multiple speakers).

Dan Springer

I just want to say you said North America. I hate to interrupt you, you said North America. U.S. and Canada, our friends in the north are their own independent country despite efforts for people like you to make them the 51st state. So yes, as our Canadian colleagues out there, we absolutely consider them a separate and important part of the focus eight. Go ahead with your question.

Pat Walravens

Okay, so I think the largest economies that are not on that list would be China, India, Italy, and the Middle East, Africa. So, I'd love to hear your thoughts on any of those.

Dan Springer

Yes, so I think the answer with China is obviously it’s incredibly complex. I'll knock that one off first. I think the perspective is we see a huge opportunity obviously with the second-largest economy in the world and the largest population, probably for at least another 10 years before India catches up.

But it's also really complex and fraught with a lot of risks as you know well. We do not have a near-term expansion there. I will tell you a lot of our customers are asking us to figure out more options for what we do.

People can sign in China, of course, but to really deal with the complexity of that market is something we need to do, but I would not put that on a very big short-term piece.

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India is an area where we have done a little bit of work already, and I think we see that as one of the significant opportunities for our future in the next year or two, future big investment and growth.

You talked about Italy; we actually have Italy and Spain about the same perspective in terms of in Europe and thinking about the opportunities for larger countries there. We think that's going to be an area over the next year or so where you will see us do more expansion, looking for ways to put feet on the street there.

And I think that can be attractive. The Netherlands is another area that I would add to that. And you know about the rest of North America, but Mexico is a place where we've actually recently started to hire people already. So, we can get all three of the North American countries into that mix. The Middle East is the last one I believe you mentioned.

We served the Middle East out of our Dublin hub for EMEA. I don't think we have seen as much sort of demand from both the commercial group that sells out of Dublin and the online business we do to suggest that the Middle East would be as fast as some of those other countries. But obviously, it's going to be an area that will be a growth area for us, but it would probably come later than the Italy, Spain, Netherlands, countries I mentioned there.

Pat Walravens

Great, thank you.

Dan Springer

Thank you.

Operator

Thank you. Our next question comes from Kirk Materne with Evercore ISI. Please proceed with your question.

Kirk Materne

Thanks very much and congrats on the quarter. Cynthia, I was wondering if you just talk about the net retention rate as we start to lap the peak demand periods from last year. Just talk about how you feel about the ability to stay up at these rates.

And I was also wondering if the rest of the Agreement Cloud, whether it's SIRAM Analytics, is starting to influence that at all? My guess is not yet but I just wonder if you could just comment on that as well. Thanks.

Cynthia Gaylor

Sure. Yes, we were really pleased with the 124% this quarter, coming off the high of 125% last quarter. So, we would expect going into the back half of the year to stay at or above our historical ranges.

And so, nothing's really changed there. The great thing about that metric is, it does demonstrate our dedication to customer success and making customers successful with our products and as they continue to expand their footprint with DocuSign across products.

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But I would also agree with your statement that the non-eSignature products are contributing a little bit to that number, but aren't the main driver. It's really, as Dan said, signature is the tip of the spear for us and that includes that metric as well.

Kirk Materne

Thank you.

Operator

Thank you. Our next question comes from Tyler Radke with Citigroup. Please proceed with your question.

Tyler Radke

Hi. Good afternoon. Thanks for taking my question. I wanted to ask you about the new customer additions. Clearly, that number has remained pretty healthy this year despite the big numbers that you put up last year, I think it was still multiples of the pre-pandemic number of customers you're putting up. I guess if you could just help us understand, are the use cases that you're landing these customers a lot different than what you saw last year, I guess.

In some ways, investors might ask why would a customer not have signed up for DocuSign last year and are signing up now, are there kind of new regulatory hurdles that they've been able to get over. Just any color you could provide on just kind of the impetus for new customer strength now compared to last year. Thank you.

Dan Springer

For sure, I don't think there's any significant difference in the use cases. We're seeing people start out with, particularly by vertical within a vertical, I think people are starting in the same use cases. To answer the sort of the conundrum which people ask us all the time of, who hasn't started with DocuSign already when you look at those new customer accounts.

Just give you two thoughts to think about it. One is TAM and one is the number of companies. They are obviously highly correlated numbers. But if you think about the signature TAM at 25 billion and growing, and you think about the rest of the Agreement Cloud it's coming close to doubling that TAM. And you look at the fact that, if you take a look at Cynthia's guidance, we're going to do a little over $2 billion of revenue. And we are by far a dramatic market share leader, a clue (phon) with over half the market. The answer is, this is an underpenetrated space.

So, and if you think about the fact that we've got a little over a million customers, we got pretty excited to say we passed a million customers. But I mean, just in the United States alone, there's like 25 million businesses.

So if you think about the global number, many multiples of that. So, the reality is, we are lightly penetrated. This is very early innings in the game, and it's true that if you work in financial services like everyone, all of you on this call, you can't imagine a Company not using DocuSign.

But there are tons of verticals that are—just we're not even scratching the surface and we strongly believe that every Company can and should use DocuSign by the time we get to them. And so, the answer is we're going to be adding a lot of new customers every quarter for years to come.

Tyler Radke

Thank you.

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Operator

Thank you. Our next question comes from Alex Zukin with Wolfe Research. Please proceed with your question.

Alex Zukin

Hey guys, thanks for taking my question. So, Dan, maybe just for you, I want to go back to Sterling's question because I think it's an important one. I think we're all trying to understand the magnitude of deceleration, and if we take a look at the metrics, I just want to hear from you may be a little bit more color about the pipeline, about retention rates, particularly in the SMB category.

And if we look at the guidance, the guidance for billings does look incrementally more conservative than you've had in the past few quarters. So, I just want to understand, is that cautiousness a sign of something that you're seeing in the business or how would you qualify it?

Dan Springer

Yes. Absolutely. I'll let Cynthia talk about the guidance. It's her domain and expertise, but I'll just give you my view. I think it's a pretty strong guide. If you look at the historical rates, the Company has grown. We feel pretty good about it considering that the last time we were giving guidance before the pandemic, our Company was half the size.

So, we've doubled and we're still looking at what I think are a really strong guide, particularly on revenue, but as well on billings. I'll let Cynthia give you her view on that. In terms of your question about what's happened in the marketplace, I mean, we feel good.

We feel like we're seeing a lot of demand. We're happy with the new customer ads, we're happy with the revenue growth. Again, if you'd asked me a couple of years ago how I'd feel about five numbers in front of our growth rate in revenue, I'd feel pretty good.

I don't think there's a perspective we have that the business has some significant slowdown. I do think what Cynthia said and I would reiterate that the peak of COVID that was a big tailwind for us.

And so, for us to do the work, to try to create growth that would look like that long run. I think it would be very, very difficult to be able to deliver that. But I do think we're going to continue to have strong growth rates.

I'll let Cynthia talk specifically to the guide, but from a standpoint of in the marketplace, we're not seeing any differences in churn rates in any meaningful way, we're not seeing—customers very rarely leave us. If we don't do the right job of customer success and adoption, we might have people where we had some dollar churn.

But if you look at the 124% on the net retention, whatever gaps we're having there we're more than making up with, dramatically so, with the upsell and the growth. So, I think our success teams are doing a fantastic job at driving fantastic growth in the base. And then again, the new additions, I think they speak for themselves. We're continuing to add a large number of new customers each quarter.

So, I would not take or look at these financial results and say that it's indicative of any sort of significant slowing in the business. I think the numbers are strong.

So, Cynthia I don't know if you have anything to add on the guidance specifically to Alex's question.

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Cynthia Gaylor

Sure. That was a very comprehensive answer. Maybe just at the edges, I would say on the back half of the year, I mean, our guidance philosophy has been consistent since the Company went public and we guide to what we can see.

And as Dan said, we had a very strong first half, and we're raising guidance in the second half off of considerable scale over the last 12 to 18 months. So, we're feeling good about the business and we're feeling good about the growth rates in the guidance. But we do guide to what we see, not what we—we don't speculate beyond that.

Alex Zukin

Understood. Thank you, guys. Maybe just a quick follow-up. Is it possible to get the RPO metric on the—so that we can kind of have a gauge of the bookings?

Cynthia Gaylor

Yes. That will be in our Q, so that will be publicly available in the Q, but we don't use RPO just given the duration of our contract and the way that's calculated. We don't think that is an indicative number, but when you see it, it will be quite strong and the growth rate year-on-year on that metric is also quite strong.

Alex Zukin

Perfect. Thank you, guys.

Operator

Thank you. Our next question comes from Rishi Jaluria with RBC. Please, proceed with your question.

Rishi Jaluria

Wonderful. Thanks. Thanks so much. Really nice to see continued momentum here. Just one question I wanted to ask maybe about what you're seeing in terms of services, because looking at your guidance, you're expecting a bit of an acceleration on the professional service's line in the back half of the year relative to what we've seen in the first half.

Anything, in particular, is it due to just more CLM and that requiring a little bit more services? I know your services mix is going to remain very, very low, it's always been, and I expect it's going to be that way. But you are expecting this little bit of uptick. So maybe walk us through the assumptions embedded in what you're expecting on the professional services line. Thanks.

Dan Springer

Yes. Just inching to your point. It's not one of the areas we spend a lot of time thinking about because it is such a small portion of our business. But let me tell you this in terms of thinking about services as you think about the comments earlier.

We would love to have less and less of the services that are provided to our customers on our P&L provided by our team. We are a partner first company. We want to invest in building out an SI network that does the vast, vast, vast majority of all the services work for our customers.

One is we think that's what they do, and what we do is build fantastic software. So, we like the idea of that, for the specialization that we have. So, if you do see from time to time, any positive blips in services

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relative to our overall software, it's probably going to be indicative of what you mentioned. Which is if our mix moved more to other parts of the Agreement Cloud, like CLM, where there is going to be more services, there's going to be more statements of work required for implementation, that would be the thing that would drive more services for us. But again, our hope is that over time, we continue to take any of that incremental service opportunity and move that into the SI partner network that we've built so that we create a fantastic opportunity for them to reinvest into the DocuSign Agreement Cloud as a core platform that they want to sell.

Rishi Jaluria

Wonderful. Thank you so much.

Operator

Thank you. Our next question comes from Michael Turin with Wells Fargo Securities. Please proceed with your question.

Michael Turin

Hey, there. Thanks. Good afternoon. Cynthia, going back to the early renewal commentary, is there anything you can provide just remind us how much visibility you have into those underlying dynamics as they're playing through in your customer base?

And does that renewal conversation insert an opportunity at all to just engage more broadly? I'm assuming it does across the Agreement Cloud. And if so, are you changing gearing, have you changed gearing just as part of the investment spend to just help take advantage of that conversation? Thank you.

Cynthia Gaylor

Yes. It's a great question and I think when we're thinking about—through the customers, and the expansion economics if you will, what we've seen is customers sometimes use more than what they've purchased and so we don't charge them overages per se, but we look forward as an opportunity to reengage with the customer, talk to them about how they're using the products and how they could be using them more. But we do use that as a time to have them renew or expand on what they're doing with us.

And so, it's both on the eSignature side as well as the broader Agreement Cloud. But you characterized it quite well in terms of the dynamics that we're seeing. And as we talked about a couple of quarters ago, we did see through the pandemic a high incentive early renewals, and we're not expecting to see those types of peak levels.

But we do you have visibility into customer consumption and how they are using the product, how they're consuming it through the lifecycle of their contracts. So that is something that we track.

But also, sometimes customers will develop new use cases, and we use it as an opportunity to reengage with them on what else we can be doing with them, but also making sure that their contract terms match their consumption levels.

Michael Turin

Great. Thank you.

Operator

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Thank you. Our last question comes from Shelby Seyrafi with FBN Securities. Please proceed with your question.

Shelby Seyrafi

Yes. Thank you very much. Can you elaborate on the increased investments you're going to have in the second half, especially in Q4? And to be clear, are you implicitly guiding for the non-GAAP operating margin to decline in Q4 from Q3 because of the increased investments?

Cynthia Gaylor

So, I think, implicitly, we give a range of guidance on the operating margin, and part of that is dependent on where the revenue comes in, where the top line comes in, and part of it is dependent on the investments that we're making.

And so, I think the takeaway here is we are looking to invest for growth and particularly in our sales and marketing team to help drive top-line growth, and then in our product development areas, as we continue to innovate around the product and maintain our leading position in the market with customers.

I think those are the two main areas. I'd also note, given how the Company has grown at scale, we also have a lot of back-office catch-up that we're doing with systems and processes and things like that. So, we're continuing to make investments in the back-office to make sure we can serve our customers at a scale. So those are the areas of investment.

But as I said, this year, our top-line outperformance has exceeded our ability to spend in quarter, and so we're looking for that to catch up by the time we get to the end of the year because our intention is to invest for growth versus optimize for maximum operating margin.

Shelby Seyrafi

Thanks.

Operator

Thank you. There are no further questions at this time. I would like to turn the floor back over to Management for any closing comments.

Dan Springer

Well, thank you much all for joining us. We look forward to seeing you, albeit, unfortunately, virtually, in the next coming months and then talking to you after Q3. Thanks so much for joining us.

Operator

This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation. Have a wonderful evening.

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