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Smartsheet, Inc. (SMAR)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the Smartsheet Third Quarter Fiscal Year 2022 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. [Operator instructions] As a reminder, this conference call is being recorded. I would now like to introduce your host for today's conference, Aaron Turner, Head of Investor Relations. Thank you. Please go ahead.

Aaron Turner

Head-Investor Relations & Treasury, Smartsheet, Inc.

Thank you, Blue. Good afternoon and welcome everyone to Smartsheet's third quarter of fiscal year 2022 earnings call. We will be discussing the results announced in our press release issued after the market close today. With me today are Smartsheet's CEO, Mark Mader; and our CFO, Pete Godbole.

Today's call is being webcast and will also be available for replay on our Investor Relations website at investors.smartsheet.com. There is a slide presentation that accompanies Pete's prepared remarks, which can be viewed in the Events section of our Investor Relations website.

During this call, we will make forward-looking statements within the meaning of the federal securities laws. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends. These forward-looking statements are subject to a number of risks and other factors

including but not limited to those described in our SEC filings available on our Investor Relations website and on the SEC website at www.sec.gov.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, our actual results may differ materially and adversely. All forward-looking statements made during this call are based on information available to us as of today and we do not assume any obligation to update these statements as a result of new information or future events except as required by law.

In addition to the US GAAP financials, we will discuss certain non-GAAP financial measures. A reconciliation to the most directly comparable US GAAP measures is available on the presentation that accompanies this call, which can also be found on our Investor Relations website.

With that, let me turn the call over to Mark.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

Thank you, Aaron, and good afternoon, everyone. Welcome to our third quarter earnings call for fiscal year 2022. Today, I'd like to focus on three key areas: our strong Q3 results which saw an acceleration of our revenue and billings; our continuing momentum in both enterprise and SMB; and how Smartsheet is driving innovation in more departments across more industries than ever.

While Pete will give you the details, I do want to highlight a few standout areas of Q3 performance. Smartsheet revenue for the quarter grew 46% year-over-year to \$145 million, and billings grew 50% year-over-year on an adjusted basis to \$162 million. We also exited the quarter with more than 9.5 million Smartsheet users, and in October we set a Smartsheet record for licenses bought by new customers in a month. Overall, we increased our ARR 10% quarter-over-quarter. Our reacceleration, our aggressive investment posture, and our new high watermarks and pipeline and large deal volume make me more bullish than ever on the prospects of the company.

As many of you know, Smartsheet is a cloud-based platform for dynamic work that empowers employees and teams to transform how they work. Through a combination of a no-code platform, a global community, and a broad service offering, customers unlock business value by transforming projects, programs and processes at scale. Rather than being just a task-oriented tool, Smartsheet can scale from a simple project used by a five-person firm to an enterprise SaaS platform that enables work across critical business systems at the largest companies in the world. That extensibility is a huge factor, driving the momentum we are experiencing in this emerging global work management market.

That momentum often gets started when a specific team or department – let's say, performance marketing deploy Smartsheet to streamline campaign management. As work is shared with other departments via Smartsheet, those departments begin to understand the value of the platform and viral growth occurs. This low-friction method of trusted growth occurs across companies and is amplified by Smartsheet's work from anywhere accessibility.

As customers graduate from basic productivity use cases to transforming operational workflows, we see rapid uptake and acceptance across more departments. For example, in Q3, we had wins within marketing departments at companies like USA TODAY, United Airlines, and Turner Broadcasting; HR departments at companies like Sonos, Avalara, and University of Southern California; in sales departments at Robert Half and Juniper Networks; in legal departments at [ph] Kerros (04:47), NetApp, and Ambev; in operations at Estée Lauder

and Piedmont Healthcare; and at government entities including the U.S. Department of Agriculture, the U.S. Department of Health & Human Services, and the FAA.

A couple of use cases I'd like to call out. We saw expansion at Hewlett Packard Enterprise and Aruba, an HPE company, where the marketing and sales departments are tracking events and consolidating input gathered from various sheets, Smartsheet forms and update requests into a global calendar used by field sales and executives.

And at Autodesk, the legal department is using Smartsheet Salesforce Connector to [ph] pull in (05:22) deal data to track negotiation points, fallbacks used, and security issues. With Smartsheet, Autodesk reduces the manual effort related to inputting their deals, which allows managers to track and report on recurring issues, monitor team bandwidth, and improve strategic decision making. This continued momentum in the enterprise where we build deep relationships with customers at more senior levels is driving bigger deals and positioning Smartsheet as the preferred choice for work management across the enterprise.

All of which ties back to our bookings for the quarter. Q3 saw both a new quarterly record of 203 deals of more than \$50,000 and a new quarterly record of 77 deals of more than \$100,000, up 92% and 114% respectively year-over-year.

And this is recurring while we invest in high potential markets like Europe, Asia Pac, and the federal government. Smartsheet Regions, our regional Smartsheet offering, is now available in the EU and enables customers to establish plans with their content hosted in Germany.

On the federal government front, we continue to make progress scaling this long-term, highly sticky opportunity. While government is small percentage of our total ARR, the ARR growth rate coming from the government entities grew in excess of 125% year-over-year in Q3 with a significant ramp in logos landed.

Beyond the numbers, I'd like to talk for a minute about our Smartsheet innovations that are driving customer uptake. Our investments in WorkApps no-code solutions and content management are paying off. With the pace of innovation quickening on WorkApps, configuration and distribution, the table is setting up nicely for WorkApps to become a major driver in shaping how people interact with Smartsheet.

More than 50,000 WorkApps have been created to-date, providing evidence that strong demand exists within – for creating composite solutions across the company Smartsheet deployment while also helping them maximize yield from existing cloud investments such as Microsoft 365 and Google Workspace.

Content creation and collaborative review is also going mainstream. With nearly a quarter of a million PDFs, images and videos proofed within Smartsheet in the quarter, new muscle is being developed around how people enroll others in content review. With the integration between Smartsheet and Brandfolder deepening, new and existing customers choosing Smartsheet for digital asset management have a more flexible and powerful way to securely store, customize and share assets.

Our platform and differentiated capabilities allow us to attach to a variety of workflows, placing us in the upper right of the Leaders quadrant for both the G2 Project and Portfolio Management and Digital Asset Management grids. And customers consistently score Smartsheet highly in the CWM and PPM markets. In fact, in those categories, we have the most five star reviews in Gartner Peer Insights compared to all other vendors.

The combination of providing simplicity at the end user level and flexible capabilities to manage programs at scale, plus security and governance controls required by enterprise IT is what sets Smartsheet apart. In PPM, we

bring a modern approach that connects bottoms-up project and process management with portfolio level views that give senior leaders organization-wide visibility to define standards, manage resources, and align on priorities. Smartsheet's ability to integrate equally well with both current and legacy systems of record gives our enterprise customers the ability to use the Smartsheet platform both wide and deep across their organizations.

In the digital asset management space, we've unified two market leading solutions, Brandfolder DAM and Smartsheet CWM. By creating one platform for marketers and creatives, shared visibility is achieved and teams are positioned to respond quickly to asset performance.

Our digital content lifecycle and asset management capabilities enable Smartsheet customers like McLaren Racing to accelerate content workflows for planning, creation and distribution using that single platform. For example, McLaren Racing's partners and fans will now be able to easily locate, access, and share content from race days. Photographers and videographers on the racetrack can uphold their content directly into Brandfolder and McLaren – for the McLaren team to approve and distribute in real time.

In Q2, we launched Smartsheet Advance, a new tiered way for customers to unlock the full potential of Smartsheet at scale. At the entry tier, Advance Silver enables businesses to orchestrate sophisticated programs, projects, and processes at scale using premium capabilities like Control Center. Advance Gold has the ability to connect Smartsheet solutions to other systems of record via Data Shuttle and Bridge as well as connectors to platforms and tools like Salesforce and Jira. At the top tier, Advance Platinum adds capabilities for organizations that desire additional levels of compliance, governance and advance policy management.

With Smartsheet Advance now in the market for two quarters, we have seen that our packaging approach that enables customers of any size to benefit is hitting the mark. One notable customer win was with USA TODAY where the marketing team's executive leadership was charged with solving challenges of cutting inefficiencies, eliminating budget overrun, and reducing employee turnover in order to scale their events business. Smartsheet Advance will support the phased implementation of multiple solutions, beginning with Control Center, Data Shuttle, and the Salesforce Connector.

But Advance is more than a mechanism for expansion. 46 Advance deals in the quarter were sold to new customers of Smartsheet. The offering helps accelerate discussions with those who want to start big and start now. [ph] Sansone Group (10:59) was able to hit the ground running with Advance Silver, migrating workloads from legacy tools into an end-to-end project and portfolio management solution. From project intake to execution to executive reporting, [ph] Sansone Group (11:11) uses Smartsheet Control Center to ensure that construction projects are deployed with consistency, and key information is automatically surfaced to executive leadership of this rapidly expanding business.

Advance is resonating with customers of all sizes, not just enterprise customers, with 51 of the Advance deals coming from organizations with 200 employees or fewer. One of those customers, [ph] Sofos Consulting (11:34), is using Advance to standardize their professional services offerings around client onboarding, project management and service requests. The centralization and visibility of key information has allowed the executive team to have true insight into client projects, in particular on resource allocation and capacity. Overall, this was a very successful quarter with 160 Advance deals closed.

Before I pass the mic to Pete, I'd like to touch on the leadership appointments we announced a few weeks ago. The promotion of three senior executives, Jolene Marshall, Stephen Branstetter, and Andrew Bennett to C-level roles, brings deep institutional knowledge and proven innovation into central roles for our next phase of growth. Each of these decisions is grounded in our commitment to empower anyone to drive meaningful change and

further positions us to provide clear ownership, drive operational excellence, capture the market opportunity and best serve our stakeholders.

Additionally, as previously announced, Chief Product and Strategy Officer, Gene Farrell; and Chief Legal Officer, Paul Porrini, will be departing Smartsheet. Gene and Paul have been with Smartsheet since before the IPO and contributed to our growth from a \$100 million company to an over \$0.5 billion ARR category leader.

I'm very grateful to Gene and Paul for helping position the company well for our future success. Smartsheet veteran of three years, Praerit Garg, has assumed joint leadership of the product and engineering team at Smartsheet. I very much look forward to writing Smartsheet's next chapter with Praerit and the rest of the team.

And on the topic of team, I'm proud of the recognition we have received for our strong company culture, including being named a Best-Led Company by Inc. Magazine, being named the Best Place to Work in Australia by WRK+, and earning seven Comparably Awards in 2021.

The momentum we're seeing in so many areas as demonstrated by acceleration in revenue and billings, driven by the best bookings performance in the company's history motivates our entire Smartsheet team.

I look forward to talking with you in Q&A. But for now, I'm going to turn it over to Pete. Pete?

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

Thank you, Mark, and good afternoon, everyone. As Mark mentioned, Q3 was a great start to the second half of the year, continuing our momentum of crisp execution against the backdrop of an improving global economy. Our Q3 outperformance relative to our guidance was a function of strong execution by our sales team, significant enterprise expansions, another record number of larger deals, and continued success of our Advance offering, which is resonating with companies of all sizes.

I will now go through our financial results for Q3. Unless otherwise stated, all references to our expenses and operating results are on a non-GAAP basis, and a reconcile to our GAAP results in the earnings release and presentation that was posted before the call.

Getting into the numbers now, third quarter revenue came in at \$144.6 million, up 46% year-over-year. Subscription revenue was \$132.6 million, representing year-over-year growth of 46%. Services revenue was \$12 million, representing year-over-year growth of 50%.

Turning to billings. Third quarter billings came in strong at \$161.6 million, representing year-over-year growth of 44%. As you'll recall, in September of last year, we acquired Brandfolder. As a part of the acquisition accounting, we recorded onetime billings of \$4.7 million associated with the acquired deferred revenue from Brandfolder's balance sheet. After adjusting for this \$4.7 million, our year-over-year billings growth rate in Q3 is 50%. Approximately 91% of our subscription billings were annual, with 5% monthly. Quarterly, semiannual and multiyear billings represented approximately 4% of the total.

Moving on to our reported metrics. The number of customers with ARR over \$50,000 grew 56% year-over-year to 2,078. The number of customers with ARR over \$100,000 grew 72% year-over-year to 868. Both of these ARR customer segments experienced the largest sequential net additions in our company's history. These customer segments now represent 53% and 38% respectively of total ARR. The percentage of our ARR coming from customers with ARR over \$5,000 is now 85%.

Next, our domain average ACV grew 37% year-over-year to \$6,368. We ended the quarter with a dollar-based net retention rate of 131%, a 3 percentage point improvement from Q2.

Q3 was the first quarter to incorporate Brandfolder, which was a headwind of less than 1%. The full churn rate dropped further and is now below 5%. Over the course of this fiscal year, we've experienced large incremental improvements in our dollar-based net retention rate as we've replaced quarters negatively impacted by COVID with more normalized quarters.

In Q4, we will complete the lapping of our COVID impacted quarters from fiscal year 2021. Now, that we will be lapping more normalized quarters, we expect our dollar-based net retention rate to stabilize around the 130% level.

Now, turning back to the financials. Our total gross margin was 82%. Our Q3 subscription gross margin was 88%. We expect our gross margin for fiscal year 2022 to be between 81% and 82%. Overall operating loss in the quarter was negative \$2.7 million or 2% of revenue, an improvement from 15% of revenue a year ago. This margin improvement was a function of scale across our sales and marketings and R&D lines inherent in our model. Free cash flow was negative \$6.3 million, which overachieved against our guidance due to strong collections and the timing of a legal settlement, payment of which is now expected to occur in Q4.

Now, let me move on to guidance. For the fourth quarter of fiscal year 2022, we expect revenue to be in the range of \$151 million to \$152 million, billings to be in the range of \$204 million to \$205 million, non-GAAP operating loss to be in the range of \$20 million to \$18 million, and non-GAAP net loss per share to be between \$0.16 and \$0.14 based on weighted average shares outstanding of 126.5 million. Our net free cash flow is expected to be in the range of negative \$6 million to negative \$4 million.

Given our strong Q3 results and continued momentum in our business, we are raising our full fiscal year 2022 revenue and billings guidance. We now expect our revenue to be in the range of \$544 million to \$545 million, representing growth of 41%. Billings are expected to be in the range of \$641 million to \$642 million, representing growth of 42%. We expect non-GAAP operating loss to be in the range of \$40 million to \$38 million and non-GAAP net loss per share to be between \$0.32 and \$0.30 for the year based on approximately 125 million weighted average shares outstanding. Our free cash flow margin in fiscal year 2022 is expected to be negative 4%. We also expect the success we've experienced this year to continue for the foreseeable future. As such, we are providing initial billings for year-over-year growth guidance of 37% to 40% for fiscal year 2023.

To conclude, we were pleased with the quarter in several fronts, the acceleration in revenue and billings, the success of Advance with the opportunity for it to be a significant future driver, and the net expansion rate that has crossed 130%. We see an enormous opportunity in front of us, and we will continue to invest behind this signal.

Now, let me turn it back to the operator for questions. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from the line of Brent Thill from Jefferies. Your line is now open.

Brent Thill

Analyst, Jefferies LLC

Q

Good afternoon. Mark, you called out record net new client wins. I'm curious if you could just drill in, give us a little more color, what you're seeing in – effectively, if you can talk a little bit about where you're seeing that. Are you seeing that the enterprise, SMB, international – just give us a little more color on that, that would be great.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. You bet, Brent. I think part of it was in the last two quarters we really have had an opportunity to balance our investment across a couple of investment areas; one being at the very high end sort of capable Advance Platinum served the most, I guess, [ph] a sort of (21:40) companies in terms of their policy management and enterprise. On the other end of the spectrum, it's the antithesis of that. It's like how can you get someone who's passing by to check out your product and have it resonate with them and have them take a step forward.

And in Q3, we refactored our entry level plan called Pro plan. And what we found was that by removing some of the restrictions on things like sheet capacities and limits, it gave people a lot more freedom to get started and gain confidence, and that has started to play out. So, the month of October was the highest new license total we've had in the company's history. And that was really exciting for the team. We take a lot of pride in our ability to expand and I think there's equal excitement internally now about landing.

Brent Thill

Analyst, Jefferies LLC

Q

And maybe a quick follow-up for Pete just when you think about Mark's comments about net new coming in stronger. Are you adjusting your quota-carrying capacity differently as you look at this, or are you – you're acting in quicker rate, are you effectively trying to get the current reps just more productive?

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

A

We're not adjusting our quota capacity. We've already leaned in heavily as a part of our investment posture. We think that serves us well to take care of the incremental demand whether it comes from enterprise expansions or it comes from these new customer additions and new license addition.

Operator: Your next question comes from the line of Mark Murphy from JPMorgan. Your line is now open.

Mark R. Murphy

Analyst, JPMorgan Securities LLC

Q

Yes. Thank you very much. Congrats on a fantastic result. So Mark, I believe Smartsheet is several years ahead of the field in terms of the FedRAMP certifications. And I noticed the Federal News Network was highlighting Smartsheet for the rest of the agencies. Can you talk to us about the traction there or – does it feel like you're

running the table with those massive contracts? And, I guess, I'm wondering, is it helping to support this pretty robust billings guidance that you're giving us for the out year.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

I really related more to the early years of Smartsheet, where we were planting many seeds. So, I referenced the logo growth. And when you land at an agency – I mean, I'd love to be able to say, Mark, we're closing huge seven-figure contracts at every agency, we're not. But we're planting a ton of seeds. We're getting a sense for what the agencies want. We're adjusting our R&D to support that. And I do expect in out years, as we talk about this being a highly sticky category, once you're in, we think – and what we're observing is that the growth within those agencies absolutely exists. But I would really liken this too that the earlier phase of Smartsheet we were really planting, and then we shift into growth, and then sort of hyper growth in out years.

Mark R. Murphy

Analyst, JPMorgan Securities LLC

Q

Yeah. I see it. Okay. And Pete, I was curious about the Advance version of the product. Which specific elements of that package do you think are resonating the strongest? And, is this something – can we see that manifesting somehow in the financials? I mean, obviously, there's a lot of strength. But I guess I'm wondering how that manifests. Is it helping – your churn is extremely low now. Your retention is strong. Is it coming through in the health of the billings numbers that we're seeing?

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

I'll take this one. When we introduce new product and innovation, you always hope that each of them are going to be a home run. And when they're actually in market and you see what the customer uptake is, then you really get to see it play out. And one of the things that we introduced in the spring through Advance was this product called Data Shuttle. And Data Shuttle is a mechanism that allows people to take datasets from any source and to bring this into Smartsheet and then shuttle them back out once they've done processing on them within Smartsheet. That is the fastest growing offering we've had at the company in its history.

Now, is it ratable? No, it's not charged on a ratable basis, however, it is a component which is a capability – a premium capability that people are really latching on to. Those are the types of home runs you need within a portfolio to get attached. And one of the – how that connects to loss rate is that when somebody has a durable, repeatable process on your platform, they tend to stay. So, the more people we can get exposed to these things, the better.

The second one I would point to is relatively new one. We just turned on for our enterprise customers, which is a Snowflake-powered analysis capability within the product that allows people to do things like time series reporting. You know, the old adage, he or she holds the keys to the kingdom also hold time series. And it's – when I look at – in the matter of months and a half, more than 50% of the enterprise customers have utilized that capability. And thank you Snowflake for putting us in a position to deliver that to our customers, but those are the kinds of things you look for in the portfolio that really, I think, help drive the strength. And I think give us confidence for the out year. I mean, there are multiple things that give us confidence for the out year, but those are two things that have really landed.

Mark R. Murphy

Analyst, JPMorgan Securities LLC

Q

All right. Very helpful. Thank you, Mark.

Operator: Your next question comes from the line of Scott Berg from Needham. Your line is now open.

John David Godin

Analyst, Needham & Company

Q

Hey, guys. This is John Godin on for Scott Berg. Thanks for taking my questions. First, I'm just kind of curious, how's your conversations around some of the more transformational deals been evolving? You're starting to see this type of broader demand earlier in the sales cycle and maybe are you increasingly seeing the end users start to push that upwards at a more rapid rate than previously? Thank you.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. We are seeing the continued bottoms-up approach work very well, and I think the better you can present your offerings and get them to discover them utilize and promote them, the better.

I think there's another part of the approach though which is quite opposite to that, which is helping somebody understand how your innovations will drive value realization after which you have the right to monetize. And that is not always in the bottoms-up motion. So when I think about how we're going to some of these large brands and doing discovery sessions with them to help them understand how to unlock value more on a strategic level, that is quite useful as well.

So I think this – it is a hybrid approach, how do you let discovery occur and self-directed growth to occur combined with more of that consultative approach, which really plays out well in those scaled environments. And we refer to that spectrum as the customer journey, right? And endpoint – and end users can have a different journey expectation than maybe an executive.

John David Godin

Analyst, Needham & Company

Q

Great. Thank you. And then Pete, just quickly on gross margins. It looks like you've raised the level of expectation from, I think, 79% to 81% to 81% to 82% for the year. Is there anything specific to call out there on the gross margin line? Thank you.

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

A

No. I think the reason we raised the margin by the amount you mentioned is because we've only got one quarter to go and we've seen the trend of how we've sort of worked on gross margin and maintained and raised that. That's really the way we set the table for you, folks.

Operator: Your next question comes from the line of Alex Zukin from Wolfe Research. Your line is now open.

Allan Verkhovski

Analyst, Wolfe Research LLC

Q

Hey there. This is Allan Verkhovski on for Alex Zukin. Thanks for taking the question. You touched earlier on all the new management changes of the company. And while we certainly see this going on as company scale, can

you just go a little bit more in depth in terms of what you're most excited about with the new members on the team, what could be done differently or better? And then I have got one follow-up.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. I think when you look at change and opportunity, I often look at what – how you apply risk to change. And one of the things I'm very grateful for is that of the new appointments, we have existing institutional knowledge, we have existing culture alignment, which allows you to really move forward swiftly and with great confidence. And one of the things that we're trying to achieve is how you accelerate decision making. So, as I look at the unification of marketing with Andrew as our CMO looking after the demands and the brand, the product marketing and other elements that constitute marketing, we have a much, much faster decision flow than we had prior where we had elements of marketing existing within three different parts of our business.

When I look at Praerit taking on engineering and I look at the ability to have a unified product and engineering person help be the arbiter in the moment, that lets us make faster engineering decisions.

When I look at Jolene taking on things like procurement and risk and working with our CSO, I look at the scope of legal also expanding.

So, the neat thing about having institutional knowledge brought into that SLT is that, from a ramp standpoint, you get to bypass that in many cases. And when I look at having, what, 2,600 roughly people on the roster now, it's also an amazing thing to be able to point to someone growing their career within the business. So, I think it's a really, really neat composite there.

And I think on the Stephen front, on the COO, Stephen as our SVP of Ops just prior to getting the appointment of COO, he's been running the rhythm of the business. And he is – as we look at really formalizing our approach to expanding international, I really look forward to Stephen taking that institutional knowledge and applying it in our new markets.

Allan Verkhovski

Analyst, Wolfe Research LLC

Q

Got it. That's really helpful. Thank you for that. And lastly as a quick follow-up. So you mentioned those really strong statistics about new licenses and the strength that you saw overall in October. Can you just kind of touch on what you saw on a monthly basis in that demand environment kind of through November? I mean – we went through – went through, through Q3, through November, how are you seeing people approach their expansions in Smartsheet as they think about the remote work environment and plans for next year? Thanks.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. I think the neat thing about seeing strength is that when you see strength, you want to invest more behind it. So, as we look at improvements to how people land and how they procure and how they expand, it just causes you to want to put more both engineering and go-to-market dollars behind it. So, as we paired the launch of our new Pro plan, we absolutely flexed in terms of making sure it was in front of more people.

And when we think about our marketing investments heading into next year, we look at top of funnel, we look at mid-funnel, and we look at bottom of the funnel. And we're really ramping in each of those areas.

As I think about the rest of the year and heading into next year, I think the awareness of mainline individuals within lines of business being able to serve themselves and derive great value like that is hitting mainstream now. So, it's less about evangelizing a new concept that nobody understands and more about getting people aware of your solution on the concept that is really gaining steam. I actually assign more to that than I do the notion of hybrid work or working remotely.

Allan Verkhovski

Analyst, Wolfe Research LLC

Q

Got it. Thanks for that color and congrats again on a really strong quarter.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Thank you.

Operator: Your next question comes from the line of Arjun Bhatia from William Blair. Your line is now open.

Arjun Bhatia

Analyst, William Blair & Co. LLC

Q

Yes. Thank you, and I'll add my congrats on a great quarter. I think you mentioned that you're expecting net retention to stabilize around the 130% range going forward. Obviously, a very strong net retention rate. Can you give us a sense for what's actually – what the primary drivers are behind that? Is it uptake of events or are you still seeing customers – just user growth – core user growth that's driving that as Smartsheet proliferates within the existing customers?

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

A

So, Arjun – this is Pete. I think if you looked at the quick-down of the net dollar retention rate, we're seeing strength across all verticals, first of all. It's coming all across every word vertical, every customer segment. And what we're seeing is expansions in large enterprise are going up and churn is coming down. So that's the way this thing is getting built out and we're seeing that reflected in the numbers that show up as the 131%

Arjun Bhatia

Analyst, William Blair & Co. LLC

Q

Okay. Understood. And also, Advance, seems like there's a lot of good momentum there. Mark, you pointed out – or you provided a handful of stats that point to the diverse kind of uptake we're seeing across the base. I'm curious, is there a difference you're seeing yet in the size of a deal that includes Advance versus one that doesn't, because I would assume that those customers are a little bit more sophisticated, I'd say, in their usage of Smartsheet. So curious what you're seeing in terms of deal size.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. Of our top 10 deals in the quarter, 6 of them did have Advance elements to them. The really promising stat that I love from the earnings call was the fact that we had many new customers buying Advance. So when I think about someone being prepared to take on more, in the past we often talked about maybe \$1,500 to \$3,000, let me just dip my toe in and get a couple licenses. They are now having more substantive discussions on how can we start a little bit bigger and a little bit faster.

And the neat thing about Advance is that it's simplifying the conversation. I think in past calls we talked about the – do you look at a menu with 32 items on it or do you want to look at a menu with 4 items on it. The four-item menu is much easier to traverse. And I do expect continued strength on the new lands as well. And again, those are happening in an assisted motion, those are less to self-directed. But, we have hundreds of quota-carrying reps now who are in a position to have that discussion. So, yeah, I think it's really setting up nicely.

Arjun Bhatia

Analyst, William Blair & Co. LLC

Q

Wonderful. That's great to hear. Thank you and congrats again.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Thanks.

Operator: Your next question comes from the line of Terry Tillman from Truist. Your line is now open.

Joseph Meares

Analyst, Truist Securities, Inc.

Q

Hey, everyone. This is Joe Meares on for Terry. Thanks for taking the question. Just wondering if there's any recent customer reaction on the new platform announcements that you guys made at the ENGAGE event, including the Customer Managed Encryption Keys, Enterprise Plan Manager and the Data Retention Controls that you guys announced?

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. I would say the reaction in many cases is congratulations, you may now proceed. And I say that a bit jokingly, but if you don't have some of these things and it's a hard requirement, you don't get to pass go, but you stop. And I love the fact that we now have the right to proceed. We think we can deliver a ton of value to customers. And getting boxed out on one of those, I'll call it, a technicality; it's an important technicality, that is like the worst thing to experience as a SaaS provider. You've worked so hard to build, build, build and you want to do that next big expand and you get stuck.

So, I just – those three that you mentioned are just great examples of things that are very important to some people and now we have a chance to really get past that nicely. And once you get into that scenario where, like Enterprise Plan Manager, it's less about a new discrete feature function for the end user, it's about making the administrator's life easier, and let them sort of operate in a more confident manner. And that's worth a lot once you get into those big accounts.

Joseph Meares

Analyst, Truist Securities, Inc.

Q

That's really helpful. Thanks. And then just as a follow-up just to kind of double click on the promotions stuff. Related to Andrew Bennett's promotion to CMO, what does that mean for commercial sales and demand generation areas? Are there any new leaders emerging there or any other changes related to go-to-market or field sales?

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

Yeah. Part of the unification I spoke to in a prior answer was about aligning that demand gen, the brand, the product marketing under one leader. So, Andrew, who previously owned demand gen in his combination commercial sales and demand gen brings that over with him to the sales org. We are also looking at elements within our SDR function and keeping those aligned. So, you really have a very tight top, mid, lower funnel grouping now. And as it relates to our worldwide field operations on the sales side, very strong layers in the UK, Australia, East/West US, and they're working directly with our CRO right now.

Joseph Meares

Analyst, Truist Securities, Inc.

Q

Thanks so much. Appreciate it.

Operator: Your next question comes from the line of Steve Enders from KeyBanc. Your line is now open.

Steve Enders

Analyst, KeyBanc Capital Markets, Inc.

Q

Hi. Great. Thanks for taking the questions. I guess just wanted to touch on the billings outlook that you are providing for next year. And I guess what kind of really gives you the confidence to go at this number? I mean, are those things you've already seen that are booked on – that are booked or is this about pipeline or the faster close rates you're seeing with Advance? I guess, what are some of the factors that are in there contributing to the outlook here?

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

A

So – this is Pete – when I look at the confidence that we've seen in the last few quarters, we see – we're very bullish in fiscal year 2023, and we've seen this bullishness come in both the expansions we've seen at the enterprise level, as well as the number of customers and new licenses we're adding. You've seen momentum in our, what I call, Advance sales and when you couple that with our ability to add in higher sales capacity, we see that as a natural extension of the plays we've run this year. So, we're seeing that play through in the guide we've provided to you for next year between 37% and 40%.

Steve Enders

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. Got you. Appreciate the color there. I guess just as we think about the newer marketing use cases that you've been – you're calling out with Brandfolder and some of those capabilities, I guess what have kind of been the differentiating factors as you go and close some of those marketing use cases with customers now?

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

A

We've seen customers appreciate being able to engage with one provider. And it's not just do they provide the capability sort of independently, but how do they work together. And when I think about the deepening of Brandfolder and Smartsheet coming together, it's about how do things like proofing in Smartsheet parlay into brand distribution via Brandfolder, how can we understand the cost of our campaign development and the performance of an asset in Brandfolder. These are all things that are starting to be realized now. And that's the yield you get.

Right after an acquisition is done, right, you have two basically independent products. And then, to what degree can you bring those two together? And as we head into next year and we look at our hundreds of quota-carrying reps, they're going to be in such a better position to talk about a unified DAM and CWM product versus last year that – again, it's another one of those things that gives us great confidence heading into next year.

And I would say, in this – with this persona type – the marketing persona type, I would say they're maybe even a little bit more particular about things working well and – and, again, as we – one of the reasons why we're investing so much in the integration of these two.

Steve Enders

Analyst, KeyBanc Capital Markets, Inc.

Okay. Perfect. Appreciate the color there and thanks for taking the questions.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

Yeah.

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

No problem.

Operator: Your next question comes from the line of Keith Bachman from BMO. Your line is now open.

Keith Bachman

Analyst, BMO Capital Markets Corp.

Yes. Thank you very much for taking the question. Also, very impressed – very impressed with guidance you're – given on the billings. I wanted to focus on two parts of that if I could and then I was going to follow with just a quick clarification.

In terms of – just a philosophical, you've guided the kind of 130% on the net retention rate. And so, therefore, if we look at 37% or 40% kind of billings growth, I assume that we should just philosophically think about kind of 30% from existing customers and the 7% to 10% from new logos, so to speak. And I just want to see if that's how philosophical we could approach it.

And then the other question, if you could just describe a little bit on WorkApps. Where is that really generating new activity and where do you think that's – where is that most specifically showing up in terms of – is that mostly new customers in the retention rate? Is it new? Just help us understand a little bit how WorkApps is driving competitive differentiation. Thanks. And then I just wanted to ask a quick follow-up to – clarification afterwards.

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

So Keith, I'll take the first part of your question and then I'll let Mark answer the WorkApps part of your question. So, as we described the stabilization of 130%, you should think of it as being – here's the rough numbers that I would build my models on. And then as you think about the additional pieces that comes from essentially new business in other spots which we've sort of talked about, that is an accurate way to think about it. Mark?

Keith Bachman

Analyst, BMO Capital Markets Corp.

Okay. Fair enough.

Q

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

On the WorkApps side today, WorkApps is something that is available to our enterprise customers. And so, I would say the companies who are more fluent with our product have deployed it are now using WorkApps to come up with these more curated ways to enroll people in the product, distributed either internally or externally. And we do hold that option card to be able to say, as WorkApps becomes better and better, and we have ways to introduce it to other plans, maybe even a trial user, we will fully pursue that. But right now it is really more for the existing customers, those enterprise customers to drive significant value. But we're actively thinking about the role it can play based on the resonance it's had.

A

Keith Bachman

Analyst, BMO Capital Markets Corp.

Okay. So, it sounds like more of an upsell help today than – particularly in the enterprise. Okay. Terrific. Just – and just you know...

Q

[indiscernible] (43:56)

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

Yeah. And I think one thing – sorry. One thing I would add, though, is it's difficult to factor how the presence of something influences someone's initial decision, right? So, even if you don't experience in your trial or is a Pro plan user and you know it exists, it may still play a role.

A

Keith Bachman

Analyst, BMO Capital Markets Corp.

Yeah. Fair enough, fair enough. Okay. All the demand metrics are just very sound, and the guidance is quite impressive. So, the one thing that I want to ask, though, is a clarification. The free cash flow guidance is a little lower than I thought. You mentioned the tax or a payment – a onetime payment in there. Could you just clarify what is the payment and how much for the Q4 free cash flow guide?

Q

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

Yeah. It's a onetime payment of \$10 million as a part of a legal settlement, which we had previously disclosed. Unrelated to our ongoing business, it's just the cash part of the settlement, if you will.

A

Keith Bachman

Analyst, BMO Capital Markets Corp.

Okay. Perfect. Many thanks.

Q

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

Thank you.

A

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

You're welcome.

A

Operator: Your next question comes the line of George Iwanyc from Oppenheimer. Your line is now open.

George Iwanyc

Analyst, Oppenheimer & Co., Inc.

Thank you for taking that question. Mark, maybe if you can share some color on Smartsheet Regions and now that you launched that, how your international momentum is built after you launched that in a new market?

Q

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

Yeah. Much similar to the conversation we had about some of those enterprise capabilities like the managed encrypted keys and such. Regions is similar. If someone has a requirement for you to host their data in a country you don't have it, then you move on to another option. So, I love the fact that we have the option card that we can present, and we have – there are examples of people in the first week that we had it available, elected to deploy their Smartsheet environment in that area.

A

I think as quarters go on, we'll have a really good sense for what the economic impact is, how we decide to go into other regions and how quickly. But it's really – really proud of the team for having gotten it ready ahead of schedule and in market and activated.

Again, I think the ability for the – both the initial customer experience, that person who's considering Pro or Business or the Enterprise, it actually is relevant to both populations. So, I think both our insight team and our large enterprise team will be beneficiaries of this.

George Iwanyc

Analyst, Oppenheimer & Co., Inc.

Following up, maybe broadly speaking on the competitive landscape, with the new customer momentum, is that typically a greenfield opportunity? Are you seeing those as competitive bid situations? And as you expand, are you displacing, are you seeing natural growth?

Q

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

So, we see it as still – I think this market is so fascinating because I think it is one of the most diversified TAMs in SaaS. And what I mean by that is you have tens, if not hundreds of thousands of buyers of these solutions. You don't have one person in IT. You don't have one CFO. You don't have one head of people ops who's buying an HRIS system. You have people in business units making decisions. That results in many, many buying decisions happening in an uncontested way where an individual is considering it for their business unit, their team, or their division.

A

And so, how I describe the new environment, very lightly contested, people graduating from the way they've done work overtime. In accounts of significance, you do start looking across other divisions, other teams, and seeing other tools use and such. So, the importance of having diversity in your user base, critical.

And when we look at some of our biggest accounts and we see like 60 nodes of Smartsheet across six divisions, we – I would actually prefer that hand over being super deep in one division. So, I think that diversity does create a lot of greenfield for a lot of companies. And then, just make darn sure you don't become known as, oh, they are a pure fill-in-the-blank-division type company. You really want to – we believe you really want to be able to spread.

George Iwanyc

Analyst, Oppenheimer & Co., Inc.

Thank you.

Q

Operator: Your next question comes from the line of Tyler Radke from Citi. Your line is now open.

Q

Good evening. This is [ph] Boyoung Kim (48:14) on for Tyler Radke. Thank you for taking my question. And I wanted to build on an earlier question about what's giving you the confidence to initiate 2023 billings growth outlook and better understand what's driving the strength this year as well. We could break it down into use cases. To what extent do you see greater demand for use cases within the CWM category versus a traditional PPM category? Is there any use cases that you'd call out that's done particularly well since you updated last quarter guidance, that would be helpful? And then, I have a quick follow-up. Thanks.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

Yeah. On the PPM front, I would say people are growing less satisfied with the old approach. And the old approach would be, give me a planning tool and then I'll execute it in some other way. They're looking for a more unified environment. So, this notion of totally disconnected – I'm going to plan and allocate capital in one area and then just sort of have my team get it done in another way. That is feeling quite antiquated.

And I think that, again, the market is getting more deeply familiar with the modern way of doing it, which is what we're really driving. So, even though we do experience, as we talked about, legal departments, HR department, sales department, service department, a really – the bow wave of a lot of demand remains centered on the project and process and program orientation, and then it vectors from there. So, it's interesting that you highlight the PPM realm because it's still a very, very common theme of someone's initial buying criteria and decision.

Q

Great. And then I want to touch on the USA TODAY example. I think you talked about how their use case revolved around scaling the events business. So with that, are there any macro level talent that you're seeing from factors such as return of events and conferences, anything that you'd call out on a broader level there? Thank you.

Mark Patrick Mader

President, Chief Executive Officer & Director, Smartsheet, Inc.

I would say our revenue is so distributed. I wouldn't call out one specific sub-segment or sub-use case as a material contributor, I would say that there's growing evidence that people have figured out how to operate in a model, which is hybrid. And so, when we look at how people are executing events, people are doing them still

A

virtually, that we are starting to see people execute events in-person as well, as well as in that hybrid mode. And I think that will – I think people – again, their confidence is growing in that. But people are not sitting still. They're making decisions.

Operator: Your last question comes from the line of Andrew DeGasperi from Berenberg. Your line is now open.

Q

Hi. This is [indiscernible] (51:05) on for Andrew. Thanks for taking my question. So, last quarter you touched on the increase in partner deals especially with partners that has like specific expertise in specific areas like healthcare and manufacturing. Just wondering how you're seeing [indiscernible] (51:19) go-to-market with partners continue this quarter. Are these partnerships growing and how are they impacting the ACV?

Pete Godbole

Chief Financial Officer & Corporate Treasurer, Smartsheet, Inc.

A

So, we were really pleased with the performance with, what I call, partner collaborated bookings. They represented a key part of how we close deals. The way this works is whether we have the expertise or partners have the expertise, we work collaboratively with them. Some of these are focused on individual verticals like manufacturing, et cetera. And we've seen that this works really well because they are with us as we sell to the customer a solution that works for the customer.

In terms of numbers, the partner collaborative bookings represented what I call low-teens of our business and really strong year-on-year growth. So, we're pretty proud of how this played out with our partner channel.

Q

Thanks. That's helpful.

Operator: There are no further questions at this time. I would now like to turn the conference back over to Aaron Turner.

Aaron Turner

Head-Investor Relations & Treasury, Smartsheet, Inc.

Great. Thank you. And thanks everyone for joining us today and we will see you out in the road and talk to you next quarter.

Operator: This concludes today's conference call. Thank you for participating and have a wonderful day. You may all disconnect.

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