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DocuSign, Inc.

First Quarter Fiscal Year 2023 Earnings Conference Call

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Karl Keirstead, *UBS*

Pat Walravens, *JMP Securities*

Jake Roberge, *William Blair*

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen. Thank you for joining DocuSign's First Quarter Fiscal Year 2023 Earnings Conference Call.

At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session.

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 Roger Martin, Vice President of Finance. Please go ahead.

Roger Martin

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Thank you, Operator. Good afternoon, and welcome to the DocuSign Q1 2023 Earnings Call.

I'm Roger Martin, DocuSign's VP of Finance. Joining me on the call today are DocuSign's CEO, Dan Springer, and our CFO, Cynthia Gaylor.

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

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 pace of digital transformation and factors affecting customer demand, including as a result of the pandemic, 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 contents 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 expenses, 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 counts and information regarding free cash flow 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 these figures, please refer to today's earnings press release, which can be found on our website at investor.docusign.com.

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

Dan Springer

Thanks, Roger. Good afternoon, everyone, and thanks for joining our Q1 earnings call today.

I want to begin by highlighting some of the quarter's results and then go into some important announcements we made around building a scalable organization and enhancing our DocuSign Agreement Cloud suite of products.

DocuSign has begun the year delivering solid results. First quarter revenue was $589 million, representing 25% growth year-over-year. International revenue grew 43% year-over-year, making up 25% of total revenue, versus 21% in Q1 of last year. Our billings grew 16% in the quarter and we delivered dollar net retention of 114%, which is within our historical range. Lastly, we added nearly 67,000 new customers in Q1, an increase of 25% year-over-year, bringing our total to 1.24 million paying customers around the world.

These results have required our team's unwavering commitment and flexibility as we are adapting our go-to-market strategy for the post-pandemic world. Our results also highlight our continued momentum in the digital transformation of agreement workflows for businesses across the globe. While we are experiencing many of the macro-challenges that our peer companies are seeing with inflationary concerns, a volatile workforce environment and general global instability, we are ramping our execution and go-to-market capabilities, as well as strengthening our Leadership Team for the growth opportunities ahead. The

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dynamic macro-environment only highlights the need for digital investments, like DocuSign, and we will continue to partner with our customers to advance their digital transformation journeys.

We're confident in our strategy and path to becoming a $5 billion revenue company. DocuSign continues to be the clear market leader in the electronic signature space, and we are excited about our progress in defining the broader Agreement Cloud category, as well. Our dedication to innovation and our investments in attracting high-caliber talent position us to build upon our leading market share. Our plan to scale is well underway and we are encouraged by the early traction we are seeing, though the level of growth in certain areas is lower than our prior expectations.

Let me share some of the specifics with you.

In Q1, we made further progress in strengthening the foundation for our next phase of growth, building for scale and tackling the go-to-market challenges we've seen in recent quarters as we transition from the height of the pandemic.

Last quarter, I shared that we would be bringing in a world-class Sales and Success leader, and I'm very pleased to note that we made an important hire with Steve Shute as our new President of Worldwide Field Operations.

Also, as I mentioned last quarter, we onboarded a number of outstanding sales leaders in our North American Commercial and SMB segments, who now have been in their seats for a quarter.

Finally, we just hired a new North American Enterprise Team leader, rounding out our initiative to scale our go-to-market leadership. This seasoned team has hit the ground running, focused on recruiting, training and enablement, and with a laser-focus on driving DocuSign to $5 billion in revenue, and beyond.

We also bolstered our team in other key areas. We just announced the appointment of Inhi Cho Suh from IBM, who will transition from being a DocuSign Board member to becoming President of Product and Technology, where she will be instrumental in accelerating innovation within our Agreement Cloud; Jim Shaughnessy, as Chief Legal Officer, previously in that role at Workday; and Jennifer Christie as Chief People Officer, formally the CHRO of Twitter.

In light of these key hires, and with the team we now have in place, we are focused on a second half growth plan that allows us to be successful despite some of the current macro-headwinds, and gives us the foundation for sustainable and predictable growth going into Fiscal Year '24.

I want to now turn to some noteworthy product call-outs.

The big announcement in Q1 was our launch of CLM Essentials, a new addition to our expanding family of Contract Lifecycle Management products. It's a streamlined CLM solution focused on faster time to value and is built specifically for growing organizations to centralize and automate the creating, negotiating and secure storage of their contracts. Essentials also allows customers to easily accelerate contract work and the quote-to-cash process via deep integration with Salesforce, and as our customers' needs grow, there's a seamless upgrade path to our full CLM or CLM+ products.

The other big area of innovation last quarter was in e-signature, where we continue to release a steady pace of features to further simplify and secure signature workflows. Our latest ID verification feature enables signers to verify their identity via trusted financial institutions, like Bank of America, Chase and Wells Fargo. This is a great example of how we're continuing our steady pace of innovation where it counts and leading our category as the name in e-signature, and that lead is reflected in our customer metrics. For example, we grew our customers with a greater than $300,000 ACV by 32% from a year ago. As our successes during the quarter demonstrate, we continue to see both growth and leadership in e-signature, as well as progress across the rest of the Agreement Cloud suite.

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Whether the customers are Fortune 500 or digital SMBs, in our high-growth international markets, like Germany or here in the U.S., we see the same land-and-expand opportunities. The lands tend to start with e-signature, but the expansions are quite varied. Let me share a couple of brief examples.

One of the largest multinational payments corporations, who has been a customer for over a decade, has steadily and significantly expanded their use of e-signature over the last few quarters. Last quarter, the company deployed a new remote work request system with e-signature to their over 60,000 global employees. This is in line with their flexible work-from-home policy, which predates the pandemic. Additionally, this customer recently opened new employee health clinics within each of their main U.S. office locations, where they have turned to DocuSign for a streamlined process when using forms within the clinic operations.

In Q1, we also saw the continued trend of deeper Agreement Cloud adoption. For example, one of the world's largest and most prestigious global consulting firms made the jump from being a long-time e-signature customer to implementing CLM+ globally. With this move, they can now build and execute standardized end-to-end agreement processes, have a centralized document repository with comprehensive metadata, and leverage our AI to identify risk levels in previously executed, as well as in-flight, agreements.

So, to summarize, we posted a solid first quarter for Fiscal Year 2023, we are beginning to see benefits from the optimizations we are making in our go-to-market motions post-pandemic and from our new scaled Sales and Success leadership. While we continue to invest in our employee base to capitalize on the considerable opportunities ahead, we are moderating the tempo of our hiring plans to appropriately balance growth and profitability. We have a $50 billion TAM, we have confidence in our business strategy and, importantly, the outstanding team we have in place.

As we work to build momentum amidst macro-headwinds, we're seeing a steady stream of wins and increased interest from our partner ecosystem to build deeper relationships. Just this week, we announced that we are expanding our global strategic partnership with Microsoft to accelerate what we call Anywhere Work and reinforce DocuSign Agreement Cloud as a preferred solution within the Microsoft AppSource. We have a deep relationship with Microsoft, who's been a longstanding customer and a partner of DocuSign. We expect to continue to broaden these ties and deliver a number of new integrations and capabilities across Microsoft's business solutions, including Office, Dynamics and the Power Platform applications.

So, we have a vast market, the industry-leading product portfolio and a growing world-class team that is focused on driving both growth and margin expansion with disciplined and operational excellence. Our plan to reignite enviable growth is underway and progressing. With these objectives plainly in sight, I'm as optimistic about the future as I've ever been.

With that, I'd like to hand it over to Cynthia to walk through our results and outlook in greater detail. Cynthia?

Cynthia Gaylor

Great, thanks, Dan, and good afternoon, everyone.

Overall, we delivered a solid Q1, as we continue to focus on execution and delivering on our long-term strategy amid a more challenging macro-environment. We made steady progress towards our operating and financial goals, added customers at a healthy pace and expanded our international footprint.

Let me review some key highlights within our Q1 results.

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Total revenue increased 25% year-over-year to $589 million and subscription revenue grew 26% year-over-year to $569 million.

Our international revenue continued to outpace our domestic growth, with a 43% year-over-year increase to reach $144 million in the first quarter and contributing 25% to total revenue. While the strengthening U.S. dollar caused some FX headwinds during the quarter, the impact to our results was not material.

Customer growth remained strong, reflected in approximately 67,000 new customers in the quarter, bringing our total install base to nearly 1.24 million customers worldwide at the end of Q1, a 25% increase, compared to a year ago. This includes 12,000 additional direct customers, bringing our total direct customer base to 182,000, a 34% increase year-over-year. We saw customers with an annual spend greater than $300,000 grow 32% year-over-year to a total 886 customers. We achieved 114% dollar net retention for the quarter, which is within our historic range of 112% to 119%. While we have added customers at a steady tempo and they continue to expand their usage of DocuSign, they are expanding at a slower rate relative to their peak levels.

Total non-GAAP gross margin for the first quarter was 81%, in line with last year, while subscription gross margin was 84%, compared with 85% a year ago.

Q1 non-GAAP operating profit reached $102 million, compared with $93 million last year. Non-GAAP operating margin was 17%, compared to 20% last year.

Non-GAAP net income for Q1 was $77 million, compared with $92 million in the first quarter of last year.

In light of consistent non-GAAP profits for the prior three years, as of Q1 Fiscal ’23, we are including a non-GAAP tax rate in our non-GAAP net income calculation. For Fiscal 2023, we are using a projected long-term non-GAAP tax rate of 20%, which reflects currently available information, as well as other factors and assumptions.

We ended the quarter with 7,642 employees, a 26% increase, compared to last year.

We exited Q1 with over $1 billion in cash, cash equivalents, restricted cash and investments.

Both operating cash flow and free cash flow reached all-time highs in Q1, with strong cash collections, building on our strong Q4 finish. Operating cash flow in the first quarter grew 45% year-over-year to $196 million, or a 33% margin. This compares with $136 million, or 29%, in the same quarter a year ago. Free cash flow came in at $175 million, or a 30% margin, in the quarter, compared to $123 million, or 26%, in the prior year, an increase of 42% over last year.

We recently moved to accelerate our infrastructure migration to the cloud as we continue to scale our business and drive efficiency. This move will have minimal in-year financial impact and, over time, will shift our model away from capital-intensive physical data centers to a more flexible and sustainable model at scale.

Now, let me turn to guidance.

As we’ve indicated, we are confident in our long-term opportunity and in our ability to add new customers and power their digital transformation across the Agreement Cloud with DocuSign. However, we are not immune to the macro-challenges with our customers and peer space. As Dan discussed, we are focused on that which is within our control, innovation across our product portfolio and improving our go-to-market execution. While we have made considerable progress bringing in leaders with significant experience at scale, it’s important to recognize that meaningful traction and better visibility will take multiple quarters.

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We have operating leverage in our business model and are committed to balancing growth with profitability, while also exercising expense discipline. We remain on track to reach our long-term target operating margins. We will continue to make thoughtful and disciplined investments across the Company with a particular focus on our highest priorities, which will drive our growth and success over time. Specifically, in Fiscal ’23, we are moderating our expenses and managing our hiring plans at a more measured pace, appropriately aligning our investments with the current climate and our growth. These elements have been incorporated in the current outlook.

For the second quarter and Fiscal Year ’23, we anticipate total revenue of $600 million to $604 million in Q2, or growth of 17% to 18% year-over-year, and $2.47 billion to $2.482 billion for Fiscal ’23, or growth of 17% to 18% year-over-year. Of this, we expect subscription revenue of $583 million to $587 million in Q2, or growth of 18% to 19% year-over-year, and $2.394 billion to $2.406 billion for Fiscal ’23, or growth of 18% year-over-year.

For billings, we expect $599 million to $609 million in Q2, or growth of 1% to 2% year-over-year, and $2.521 billion to $2.541 billion for Fiscal ’23, or growth of 7% to 8% year-over-year.

We expect non-GAAP gross margin to be 79% to 81% for both Q2 and Fiscal ’23. We expect non-GAAP operating margin to be 16% to 18% for Q2 and Fiscal ’23.

We expect to see a de minimis amount of interest and other income, and we also expect a tax provision of approximately $7 million to $11 million for Fiscal ’23.

We expect fully diluted weighted average shares outstanding of 205 million to 210 million for both Q2 and Fiscal ’23.

In closing, while we are pleased with our Q1 performance, we also acknowledge the work ahead to re-accelerate our growth. The market opportunity is compelling. We have the leading product portfolio and an unwavering focus on driving sustainable growth at scale. We are in a strong position to execute on our go-to-market strategy that will deliver on our commitments to our customers, while helping them transform their businesses across the Agreement Cloud. We are taking the necessary steps and we are confident and energized by the plan we have in place. We’re focused on execution and on balancing growth with profitability as we partner with customers to transform how agreements are prepared, signed, acted upon and managed around the world.

Thank you for joining us today.

With that, we will now open it up for questions. 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 Josh Baer with Morgan Stanley. Please proceed with your question.

Josh Baer

Great, thank you, I appreciate the question. I wanted to get a better sense kind of just between macro and normalization post-COVID as far as demand and competition, just like what might be impacting the revised outlook. I guess, first, on competition, I was wondering if you’ve picked up any change in win rates or any change in the need to discount pricing. Then, related to macro and COVID normalization, was hoping you could characterize the pipeline. Is it healthy and deals are getting pushed because of

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macro, or is it a weaker pipeline just given the gap in demand as demand normalizes post the pandemic? Thank you.

Dan Springer

So, a couple different questions in there. Let me start with your first piece and try to disaggregate, if you will, sort of global macro-economic versus the post-pandemic impact to DocuSign. It's very difficult, as you would imagine, on sort of a deal-by-deal basis, to do that disaggregation. I think we believe the larger impact for us is coming off the sort of very aggressive buying that we had during COVID, but we also do see, and as we talk to other peer software companies, they're sort of reiterating, particularly in Europe, that there may be some impact there. So, it's very difficult to really quantitatively disaggregate it, but I would say the most substantial piece is coming off the COVID high as opposed to the macro-economic component.

In terms of the competitive set, Cynthia and I do an assessment before every single earnings call, we sit down with our Competitive Team and our Pricing Team, and we have not seen anything substantial that changes. Things are a little bit different in different markets, but, in general, we're not seeing any change from a standpoint of thinking about win rates, thinking about the average price that we are achieving. I'm talking primarily of e-signature here, because it's the largest piece of our business, substantially. But, that's sort of the core analysis that we dive into.

From the standpoint of pipeline, I'd say a couple things. I would say that we have had a reasonable amount of churn and change in our field organization. Some of that is absolutely attributable to the so-called Great Resignation. I think it's consistent with what we're seeing in other software companies. We, traditionally, had very, very low attrition in our Company, a single-digit impact the last couple years, and we're now sort of more at industry averages, we think. So, that's been a big change for us. I think one of the challenges when you have turnover in the field, it's tougher to build pipeline, right? If you think about most of our revenue in any given period, it doesn't come from the newco—and as Cynthia articulated, very strong newco again, which I think is a good testimony to the strength of our business and the value proposition and the strength of our brand—it's really more in the upsell, and that is where our field, the CMSs, our AEs need to be out with our customers and saying, "Hey, great, you've gotten good ROI from your first sort of use case of DocuSign, but expand into the next one." What we're seeing is, with that change in the team, not as much focus has been on building pipeline, and I would say that would be a factor in the change in guidance for billings, as Cynthia articulated.

Hopefully, that got each of your questions covered.

Josh Baer

Yes, thanks for the answers. I'll leave it there, since that was three questions already. Thanks.

Operator

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

Brad Sills

Oh, great. Thanks for taking my questions, guys. I wanted to ask about some of the execution challenges that you kind of outlined earlier in the call. I think three quarters ago, when you embarked on this refocus on expansion activity, you outlined some steps being taken there and some changes in leadership. We're now two to three quarters into that and it looks like this effort is turning out to be a bit more material than perhaps you thought initially. I guess my question is what are some of the learnings as you pivoted back

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towards expansion, and what's already working, and do you feel like you have the leadership in place now with these changes to be able to continue on that path to kind of refocus on that expansion activity?

Dan Springer

First off, I would agree with the assessment that initially probably underestimated, I underestimated sort of the impact in the post-COVID sort of demand acceleration and maybe how dramatic that was. Clearly, we saw the business growth rate practically doubled and we doubled the size of the Company in sort of like six or seven quarters. So, it wasn't that we were not aware of the dramatic economics of it, I think we just didn't understand what portion of that would be things like one-time use cases or an acceleration where people bought in a more fulsome way, so that the removal of that very, very strong tailwind, effectively, felt like a headwind. So, I think that's absolutely a fair articulation of my misunderstanding of how dramatic that was.

The second piece. I think, while we talked about the need to sort of enhance and augment the leadership we had for both the scale we've now achieved, as well as for the new model going forward, it wasn't really until more recently, in the last quarter or so, that we, in fact, started to bring in the new sales leadership and go-to-market leadership that we talked about earlier on the call. So, I'd still say it's fairly early days for most of those leaders. The North American Commercial and SMB leaders are just probably about a quarter in. Of course, Steve is just a number of weeks in, and the Enterprise leader hasn't even—we just hired, hasn't begun yet. So, I would say it's still fairly early in the tenure of that augmented leadership.

Lastly, I would say, I think, in terms of lessons learned, it is that the core thing that DocuSign had always done sort of pre-pandemic, about really driving customer success, being an organization that's focused on driving adoption and consumption of what people have purchased, are the core things we need to do. As I mentioned in the last question, we did have reasonable Q1 turnover in our field, which means that we are now onboarding at a higher rate the number of people we need to fill those spots to drive growth, which makes it—a lot of activity has to be spent on the onboarding and enablement of those folks in sort of the DocuSign way, and that, I think, is probably the biggest single contributor to why it's going to take longer than we would have initially said to get back to the enviable growth rates we'd like to see.

Brad Sills

Thanks for that, Dan, and one more, if I may, please. I think you alluded to some early signs of perhaps a slowdown in Europe, in particular. If you could just articulate a little bit on what you're seeing in the different regions, North America, Europe, Asia, with regard to demand, just given all the moving parts of the macro. Thanks again.

Dan Springer

Sure. Well, I would tell you, overall, international has continued to take share, right, and now up to 25%, so we're quite pleased with the relative growth rate of international, and Europe is substantially the largest piece there, but I would say, sort of as you move further east across Europe, we've seen probably some stalled and delayed deals, where people said, "We're not sure what's happening to our economy and we want to be maybe a little bit more prudent." So, that's where we would probably see the places where sort of the unrest has hit us the most, because of the war in Ukraine, and I think the German economy is probably, you know, the substantial economy that's going to be most impacted across Western Europe. I wouldn't say we've seen anything from the global unrest in other regions, like LATAM or APJ, but in terms of the global macro, I don't think we have an ability to really give you huge insight, other than saying we just generally see across the board, from all regions, a sense that companies are thinking about inflation, they're thinking about a potential looming recession, and maybe being more cautious on their buying behavior.

Brad Sills

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Thanks so much, Dan.

Operator

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

Karl Keirstead

Thank you. Cynthia, I think everybody just wants to stress test the back half billings guidance, just to arrive at a viewpoint as to how conservative it is. I think your second half billings guidance implies $1.31 billion, or call it roughly $650 million in billings per quarter, 3Q and 4Q. I'd just like to ask you what assumptions you're baking into that guidance, what you're assuming in terms of the continuation of the customer hesitation that Dan just flagged, what you're assuming in terms of sales productivity improvements in the third and fourth quarter, just so that we can get an understanding of how conservative it is. I'd appreciate any color. Thanks.

Cynthia Gaylor

Yes, thanks for the question. Our guidance philosophy hasn't changed. We guide to what we see and the visibility we have, and we don't have the level of visibility that we would like. However, I would say the philosophy, you know, it bakes into the risks and opportunities we're seeing in the business, and so some of the things that Dan touched upon, in terms of bringing in new leaders, ramping up the field teams, looking at customer demand and use cases, and product opportunities within the customers, and then the macro-environment that we're seeing, that is baked into our current outlook in the back half of the year.

Karl Keirstead

Okay, thank you, Cynthia.

Operator

Thank you. Our next question is from Pat Walravens with JMP Securities. Please proceed with your question.

Pat Walravens

Oh, great, thank you. If I may, I'll do one for each of you.

Dan, why are so many of the reps quitting? I'm sure you've analyzed that. What are sort of the top two reason?

Then, Cynthia, if you have 7% to 8% billings growth this year, doesn't that suggest that you would have sort of 7% to 8% revenue growth next year?

Dan Springer

I'll go in the order you put them out there, Pat. I'd say there are two things. One—and I do think the most substantial component for us, and pretty much everyone I talk to in the software world—is this construct that equity values are clearly down pretty much across the board for the reassessment of multiples, and people lived through some tough years in COVID and they're tired, and people want a change, and I think the concept that we see a lot of people who have been DocuSigners, the people that have that have been longer term DocuSigners said, "I love the culture, I love the place, I just want a change, I'm tired," and it

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was a tough. There was a lot of hard work in the two years with the big growth, but then it's also difficult to feel like, hey, the opportunity is not what it felt like it used to be. So, that's probably those conversations.

We also had a significant number of people that we added during those two years of the very dramatic COVID growth and they kind of knew only one DocuSign, which was, quite frankly, achieving the sales success was a heck a lot of easier than it had been previously, and definitely a lot easier than it is now, and for some of those folks, they said, "You know, the market is telling me that I can get guaranteed compensation some place else, and since I'm no longer brand new at DocuSign, I don't have that opportunity," and so from a compensation standpoint, they said, "I think I'd be better off trying some place new," particularly that a lot of the start-ups, up until at least recently, have been saying, "Hey, we'll guarantee your first year of compensation.

So, I think those are probably the two biggest drivers that we see for why people would say in the field, "I want to try a different sales role."

Cynthia Gaylor

Then, the question on the back half of the year, we're not …

Pat Walravens

No, not the back half of the year, not the back half of the year. Sorry if I wasn't clear. If it 7% to 8% billings growth for all of Fiscal '23, doesn't that mean Fiscal '24 revenue growth is going to be something like 7% to 8%?

Cynthia Gaylor

We're not guiding to next year at this point. I mean, as Dan said, we have new leaders in place, we're ramping the go-to-market. We are guiding for this year to what we're seeing, Pat, and so I think it wouldn't be prudent for us to go beyond this year. We're very encouraged by the steps we've taken. We're very focused on what's in our control. Whether that's the innovation, the go-to-market piece, as we've talked about, bringing on new team members, kind of prioritizing the investments, those are the things we're focused on, along with, and importantly, making customers successful on the platform, so that they can continue to grow and expand with us, right, and so those are the things we're really focused on. We'll have more to say as we move through the back half of the year, but we're certainly facing headwinds across a few of those different dimensions.

Pat Walravens

Okay, I just figured we might as well get the bad news out now. Isn't that kind of the mechanics of how the business works?

Cynthia Gaylor

Yes, I wouldn't say that's the mechanics. I mean, we're—every day of every quarter, we're looking to make the right investments to grow the top line across the go-to-market, and so our guide is reflected on what we're seeing in the business, and as I said, as we move through the back half of the year, we're currently anticipating some headwinds, relative to what we saw 90 days ago, as we've looked at how the markets have developed and the go-to-market changes that we're making are going to take a little bit longer to actually see in the financial results.

Pat Walravens

Okay, all right, thank you.

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Operator

Thank you. Our next question comes from Jake Roberge with William Blair. Please proceed with your question.

Jake Roberge

Hey, thanks for taking my questions. I'm wondering if you could just touch on how the CLM solution's been tracking. I know you've talked about some exciting new product launches, but is that solution seeing the same cross-sell headwinds that signature is experiencing right now, or are you starting to see some better growth in that segment of the business?

Dan Springer

Yes, CLM, thanks for asking, was a bright spot in Q1. We were over 100% of our goal for what we wanted to see in terms of growth there. As you may recall, CLM had, before the pandemic, started to look like it was really picking up, and then across that entire space of other CLM providers. During the pandemic, it got much tougher, as people sort of tried to focus on those shorter term ROI wins that you see in something like signature, right, which really took off during the pandemic, and some of those longer cycle deals in CLM, where it takes more implementation time and you need to have some sort of systems integration work as sort of a requirement to execute on installing that software, now we're seeing that there's a lot of enthusiasm for that. I would tell you, a particularly bright spot, is we just launched CLM Essentials and we already have dozens of wins there, with people that are saying, "This is a way that says we democratize CLM." So, we're quite bullish on the momentum that's building there.

Jake Roberge

Great, and then just thinking about international again, it sounds like EMEA, Eastern Europe might be a little softer, but just curious how—you launched in Mexico three or four quarters, has that geography been tracking as expected, and when we think about the moderation of some of the sales investments you're talking about, will that mainly be international or will you be moderating investments in the States?

Dan Springer

The first piece in terms of international, yes, I think your assessment of the impact from global instability, Eastern Europe would be the area, for obvious reasons, that would be most impacted, and so then as you move—we don't have a significant business in—we have no direct business in the Ukraine or in Russia, and a very small amount of business we've had through our digital, we sort of stopped taking a lot of customers in Russia as part of our support for Ukraine, so that it's not meaningful in any way, but as you move further into Europe, I suppose we'd say that's probably the most likely impact for that to happen.

In terms of other markets, like Mexico, and Mexico is very, very early for us, of course, which has a small number of employees there, so it wouldn't have any sort of meaningful impact, even in the overall international business, in the short run, so I probably wouldn't look to that for an insight there.

I'm sorry, and then the last piece—I apologize. You had one last …

Jake Roberge

Yes, just in terms of the—you were talking about moderating some of your investments, and so will that be primarily international?

Dan Springer

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Yes, yes, absolutely. No, I think the answer is international will probably have less impact, quite frankly. We see that as continuing to grow and take share, as has been our plan to grow faster internationally.

I think when you think about the moderation of hirings, there's two things to think about.

One, we are committed to deliver on the profitability goals that we've set forward, and if we're going to have any reduction in the top line growth, then we want to make sure we're being thoughtful about the spending level, and of course our largest spending item is headcount. We're not doing layoffs, we're not reducing our workforce. We're just tapering the growth rate and the number of hires that we will make. The vast majority of those would be in North America.

The other thing that I would say to that point, one of the challenges we talked about earlier, with the fact that there'd been heightened attrition, which may be starting to—again, particularly, as the start-up community starts pulling back a little, we may see that get a little bit easier, but our concern was that the amount of new people we were hiring to try to drive that growth rate, it was just very difficult to onboard them successfully into the Company. So, the other aspect in moderating the hiring, again, primarily in North America, is to ensure that we can make DocuSigners and bring them on and make them successful for the long term growth of the Company.

So, that's how I think about those factors.

Jake Roberge

Great, thanks for taking my questions.

Operator

Thank you. Our next question is from Tyler Radke with Citi. Please proceed with your question.

Tyler Radke

Thank you. Cynthia, you talked about some lower visibility in your guidance and I'm curious what you're assuming for renewal rates and net retention. I know that in the past you've talked about kind of under-estimating the one-time use cases. Are you expecting that churn picks up just as there's maybe more one-time use cases on the platform, and how should we just think about the assumptions on net revenue retention rate relative to your historical range for the back half?

Cynthia Gaylor

Sure, sure, yes. We've reported 114%, which is within the historic range. For Q2, we're expecting it to be around the low end of the historic range. Remember, dollar net retention is more of a lagging indicator than a leading indicator, given how the measurement is taken off of last year and the cord is snapped on customers who were customers last year and how they expanded over time, so that metric does include churn, and as you noted, it does factors in—if there were one-time use cases, it would be factored into that metric. We're not guiding to the year, but I can tell you, as we usually give color on one quarter out, that we are anticipating it to be around the low end of that historic range of 112% to 119%.

Tyler Radke

Okay, thank you. Dan, you talked about some of the go-to-market changes just as you're looking to re-accelerate growth, and obviously, you know, it sounds like you still believe in the $5 billion target at some point, so I guess, just how long do you think—how many quarters will it take to kind of drive that growth

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back to a level that you're targeting, and where do you kind of aspire the post-pandemic growth rate to be for DocuSign?

Dan Springer

We don't have sort of a long-term growth rate that we've ever sort of put out or published as a perspective. I would tell you this, from the core part of your first question, is that we've provided guidance today that says, hey, this is probably a longer term set of changes to work those through the field than we initially thought, but if you take a look at sort of the growth in absolute dollars, we want to see that picking up in the second half. We want to see getting impact from the changes that we're making quickly. I think it would be probably not prudent to say we have a specific date where we think we're kind of there, but rather just say we're going to be making progress, and as we continue to come out of the kind of post-pandemic impact that we talked about and the second half will start to lap those quarters where we're post the most dramatic impact that we had, from a tailwind standpoint, I think you'll start to see us getting more and more excited about the growth coming back.

Tyler Radke

Thank you.

Operator

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

Alex Zukin

Yes, hey, just two for me. I guess I'm having a little bit of trouble understanding. It sounds like most of the issues, Dan, that you guys are talking about are still, to prior points, execution-driven, rather than macro-oriented, but then, I guess, just in the guidance, I think everybody would appreciate a little bit more clarity. Are you assuming sales cycles lengthen, are you assuming—particularly, in the U.S., are you assuming that your retention rate goes down or your churn increases, or that small business, the digital portion goes down? I think we all appreciate that today most companies are talking about Europe, but there's definitely companies that are talking about domestic deals pushing and seeing domestic impact?

Then, as a follow-up, you talked about the moderating hiring, but you reaffirmed your margin targets for the year, so where are we going to—like, is there a playbook for a more volatile macro that you're anticipating and planning for from a margin perspective and where—if you think about the free cash flow, which a lot of investors focus on for your stock, where is kind of the bottom end of that that you'd be comfortable with for the year?

Cynthia Gaylor

Let me take some of the guide ones first, and maybe Dan can chime in. On sales cycle, we haven't necessarily seen an elongated sales cycle. I think the biggest factor that we've talked about in the prepared remarks was really around the expansion rate and that customers—which, Alex, as you know, customers, we have a land-and-expand model, a customer starts small, they expand over time. That expansion rate and rate of expansion is coming off of the peak levels, and so there are smaller expansions, and that is a big driver of some of the metrics, whether it's on the growth rates, and then on that dollar net retention, the expansion is—the customers are expanding at a smaller rate, or slower rate. So, we're focused on things like making sure that we're talking to the field and enabling customers around different use cases, different products, feature functionalities, selling into different departments, as well as landing new customers, and our new customer rate continues to be strong in terms of our net adds, so we're quite pleased with that metric.

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I think when you think about kind of that back half of the year, we're not guiding on a dollar net retention, but it's fair to say that it is reflected in some of the growth rates, and in Q2, we would expect it to be around the bottom end of that historical range, and then, hopefully, when we get to next quarter, we'll have better visibility and we'll be able to tell you what it looks like more specifically, but that's kind of where we're at now on that.

Dan, maybe you want to talk about the other point.

Dan Springer

Yes. Well, just two other pieces. One, I'd just make a finer point on what Cynthia talked about in terms of the deals. You asked a question around thinking about our field and execution. One of the things, I think, early on, when we did not see the growth we wanted to see, we sort of looked at that and said to our field, "Hey, why are we not achieving it?" and I think initially put a lot of focus on the fact that, "Hey, we need to sort of sell more." Again, most of the dollars that come in come from the growth of our existing business, not the newco. Newco, we haven't seen a dramatic change, but we've seen continuously very strong numbers there. But, if we look deeper into it, from an execution standpoint, we're doing the same number of deals, it's not that we're not getting deals done.

To your macro question, whether it's Europe or North America, we're not seeing that customers are saying, "I don't want to transact with DocuSign." They're saying, "I bought a lot in the last couple of years and I'm going to have smaller deal sizes now," and we did not forecast—we thought about the book of business and said we initially assumed we would grow at the same percentage we had grown before off that book of business, which was now twice as big as it was before the pandemic, and a lot of customers said, "I'm not going to grow at twice the rate, in a dollar standpoint, the same rate that I was growing with you before," and we probably had unreasonable expectations of what the field could deliver on that. But, again, this is a deal size as opposed to deals pushing or customers leaving. We're just getting smaller incremental growth because we're, one, off a larger base, and, two, people had so fulsomely bought during the pandemic time with us.

Then, just to your margin question, we're actually saying we're holding our margin, so we're saying despite seeing some macro or broader headwinds, that other people are also, as you said, commenting on, other software companies are commenting on, we believe we have a really strong model and we can continue to deliver those margins, and that's with operating income. If you take a look at it from a free cash flow, we had an unbelievably strong quarter in free cash flow, and we expect we're going to continue to have a strong cash generation business, because we have a really attractive business model at DocuSign.

Alex Zukin

Got it. Maybe just following up on that answer, from an expansion perspective, is it still to the extent that you have those expand deals that you're in the pipeline contemplating and they're just not occurring, they're taking longer to get done, or these customers are literally saying, "We have what we need for an indefinite period of time," and now, in order to make up for that, you need to land double the volume of new deals?

Dan Springer

So, a couple thoughts. Across the 1.24 million customers, or even 180-odd thousand direct customers, there's no simple answer, because we have quite a range of customers, of course, but if I try to think through it on average, it's dramatically more people saying, "I only need a little bit more, as opposed to a lot more, which I needed last year," as opposed to people saying, "I'm pushing," or "deals are taking

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longer to close." We haven't sort of seen anything significant on that dimension. It is people saying," I've got a lot, I love it, I want more, but just not the same percentage increases I wanted before."

Alex Zukin

Got it. Thank you, guys.

Operator

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

Rishi Jaluria

Hey, Dan and Cynthia, and thanks for taking my questions. I got two here.

One, I want to really understand the mechanics of the Q2 billings guidance, right? Because, if we look at it, not only is it optically really disappointing at 1% year-over-year, but you're talking about effectively adding zero dollars in deferred revenue from Q1 to Q2. I guess, what assumptions are baked into that? I don't think I've ever seen that historically happen in your business from a Q1 to Q2, where you're adding zero dollars of net new DR. Was there like some pull-forward business from Q2 that landed in Q1, or what's going on in that guidance? Maybe you can just help us better understand that, and then I've got a follow-up.

Cynthia Gaylor

It's a good observation. Yes, it's unusual for a Q1 to Q2, but we have had other quarters that I would characterize as flattish quarter-on-quarter. I understand it's unusual for a Q1 to Q2. However, remember with billings, there are timing of when deals fall in or out of the quarter. Q1, net/net, came out pretty much where we were expecting, but there were definitely puts and takes that fell in the quarter versus what fell out of the quarter and the impact on Q2. I understand your point, but I would just remind you that billings can fluctuate quarter to quarter. We do look at the trailing four-quarter averages on those growth rates. As we said, we also look at kind of first half, second half. So, you can kind of look at first half, second half growth rates and what that implies, as well. But, understand the question, but I'd just remind you about timing of deals, particularly when it comes to billings, and that's why we tend to look at averages there.

Rishi Jaluria

Okay, Cynthia, point taken, I get it, but unless there was an actual pull-forward of business from Q2 to Q1—the Q2 billings is a guidance you're giving us, right, it's not a number that actually happened and we can say things moved around. I guess I'm still struggling to understand that, but I'll leave that alone.

I want to turn to geographies. International growth slowed down. That, itself, is disappointing. But, then, if I look at the U.S. side of the business, that grew 0.6% sequentially from Q4 to Q1, and yet you're talking about being underpenetrated in the market opportunity. Is this just the one-time use cases churning off, or what's leading that, because we're effectively on the edge of U.S. revenue starting to decline sequentially, right, we're not that far away from that, especially because revenue is a lagging indicator, and macro is only going to get worse from here, right, not better? Just help me understand what's going on and how I should be reading that number. Thank you.

Dan Springer

Let me take the first piece and you can add on, Cynthia.

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Yes, I think the answer is—I don't want to give you the sense that one-time use cases is substantially the driver, but I would say it's an absolutely significant contributor. We gave some examples, that we talked about before, around we had some very large deals around some of the government loans, the PPE loans that occurred, and our biggest sort of growth in the prior year was in Q1, the PPE loans, so we knew that was going to come to an end, obviously, this quarter, and that was quite substantial. I would say that other—particularly where interest rates are right now, other loans, which is financial services is a big vertical for us, and as interest rates go up, we would expect that people would do fewer loans in a higher interest rate environment, particularly on the mortgage side. So, I think our expectation is that sort of a phenomenon from that macro issue that you're describing.

But, for us, the one-time truly disappearing use case, I think is smaller than the broader component of, hey, we really grew quickly over those two years and we've pulled forward a significant amount of demand, where customers—it wasn't so much DocuSign pushing, but customers saying, "Hey, we really want to buy in a more fulsome way." Those pieces, I think, in aggregate, are bigger than the actual one-time use cases, but one-time use cases in Q1 and Q2, we would say those would be meaningful drivers, as well.

Rishi Jaluria

Okay, got it. Thank you.

Operator

Thank you. Our next questions is from Shebly Seyrafi with FBN Securities. Please proceed with your question.

Shebly Seyrafi

Thank you very much. Can you describe what areas in field sales needed most improvement and what actions do you think Steve Shute is going to undertake accordingly?

Dan Springer

Well, again, I look at as trying to augment the capabilities that we had there. I'd say there's a couple things. One was we just got to a different scale level than we had been and we had strong—many, many years of strong growth, but at a much smaller business, and then, again, we doubled over sort of six or seven quarters, and I think we needed to enhance the overall sales leadership that we had, and that is probably around some of the discipline, around forecasting and planning, is probably the single biggest area.

In terms of the actual execution in the field, which we have talked about, I do believe that we had a challenge, where we brought in a lot of people in a very hectic environment of growth and did not have the opportunity to enable them for the post-pandemic, because they were only here during the pandemic onset and it was easier in that period of time. So, it's not that all of a sudden our field became incapable, but we did bring in a lot of people who hadn't worked in a more traditional environment for buying DocuSign, and I think that's the core piece that he's focused on now, is enabling the current force on the DocuSign way, and it is that core land-and-expand model that we talk about, sort of where we're back to the basics, and I think Steve's going to do a fantastic job of working with the new sales leadership we brought in to augment the talent we already had in stronger delivery there.

Operator

Thank you. There are no further questions at this time. I'd like to turn the floor back over to Dan Springer for any closing comments.

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Dan Springer

Thank you very much. As we said, just in summary, we are pleased with the Q1 delivery that we had, but we're really focused and locked in on what we need to do to continue to deliver strong profitability and reigniting the growth that we talked so much about on the call today. We look forward to having the opportunity to speak with you all soon. Thank you very much for joining us.

Operator

This concludes today's conference, you may disconnect your lines at this time. Thank you for your participation.

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