Docusign, Inc.

Second Quarter Fiscal 2026 Earnings Call

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Jake Roberge, *William Blair*

Josh Baer, *Morgan Stanley*

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Brad Sills, *Bank of America*

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen. Thank you for joining Docusign's Second Quarter Fiscal Year ‘26 Earnings Conference Call.

At this time, all participants are in listen-only mode. After the speaker's 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.

If anyone should require Operator assistance, please press star, zero on your telephone keypad.

I’d now like to pass the call over to Matthew Sonefeldt, Head of Investor Relations. Please go ahead.

Matthew Sonefeldt

Thank you, Operator,

Good afternoon, and welcome to Docusign’s Q2 Fiscal 2026 Earnings Call.

Joining me on today’s call are Docusign’s CEO, Allan Thygesen, and CFO, Blake Grayson. The press release announcing our second quarter fiscal 2026 results was issued earlier today and is posted on our Investor Relations website along with a published version of our prepared remarks.

Before we begin, let me remind everyone that some of our statements on today’s call are forward-looking, including any statements regarding future performance. 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 factors affecting customer demand and adoption are based on our best estimates at this time and are therefore subject to change.

Please read and consider the Risk Factors in our filings with the SEC together with the content of this call. Any forward-looking statements are based on our assumptions and expectations to date, and except as required by law, we assume no obligation to update these statements in light of future events or new information.

During this call we will present GAAP and non-GAAP financial measures. In addition, we provide non-GAAP weighted-average share counts and information regarding free cash flows and billings. These non-GAAP measures are not intended to be considered in isolation from, a substitute for, or superior to our GAAP results. We encourage you to consider all measures when analyzing our performance.

For information regarding our non-GAAP financial information, the most directly comparable GAAP measures and a quantitative reconciliation of those figures, please refer to today’s earnings press release, which can be found on our website at investor.docusign.com.

I'd like to turn the call over to Allan.

Allan Thygesen

Thank you, Matt, and good afternoon, everyone.

Q2 was an outstanding quarter. Platform innovation launches and the long-term focused go-to-market changes introduced in Q1 drove strong performance in Commercial and Enterprise customer segments across eSignature, CLM, and our AI-native Docusign Intelligent Agreement Management platform.

Q2 business results outperformed our expectations. Revenue was $801 million, up 9% year-over-year, and billings were $818 million, up 13% year-over-year. Q2 topline performance accelerated and represented one of our strongest growth quarters over the past two years, with improved fundamentals across eSignature and CLM customers, and growing contribution from IAM demand. Beyond an individual quarter, we are excited to see billings begin to accelerate on a full-year basis, and more so when we adjust for early renewals.

Profitability benefited from topline strength combined with our ongoing commitment to driving efficiency. Non-GAAP operating margins were 30%, as we continue to maintain strong profitability. Free cash flow margins improved modestly year-over-year to 27%, which supported significant share repurchases, with $200 million in buybacks this quarter.

As we make progress towards our goal to realize long-term, profitable, double-digit growth, we continue to execute effectively on our three strategic pillars: strengthening our routes to market, accelerating innovation, and improving operational efficiency.

Let's start with our Omnichannel go-to-market this quarter. At the beginning of the year, we made meaningful changes to the Direct Sales organization, which included introducing new sales segments, territories, and performance-based compensation, all focused on maximizing Docusign's long-term opportunity and multi-year growth acceleration. In Q2, we saw initial success from those changes, resulting in strong direct sales performance and growth in gross new bookings.

Dollar net retention also reflected that strength, increasing to 102% on the back of higher gross retention rates. Continued steady growth in envelopes sent and year-over-year improvement in contract utilization reflect strong execution and eSignature demand. International growth continued to outpace domestic, and digital revenue continued to grow faster than the overall business.

In Q1, we relaunched our Partner program to align partners with our IAM strategy and build solutions with IAM that deliver value to customers. Our largest deal in Q2 was transacted through the Microsoft Azure marketplace. Also, a new partnership with the U.S. Federal Government's General Services Administration creates an opportunity to expand our existing eSignature sales to federal agencies, with IAM to follow.

Specific to IAM, the go-to-market changes are focused on realizing the massive multi-year opportunity ahead. In Q2, customers moving to the IAM platform represented a greater share of direct deal volume and total gross bookings than in Q1. We're also finding that when customers move to IAM, they increase their eSignature usage. Commercial SMB customers continued their strong pace of investment into IAM, with companies like Kindsight, Cimplifi, and Justpoint, a VC-backed legal AI company, using IAM to speed up sales cycles and gain a deeper understanding of their agreements. We remain on track for IAM customers to represent a low double-digit percentage of our book at year-end.

In Q2, we also saw encouraging demand for IAM from Enterprise customers. While still early days, more than 50% of our Enterprise account reps closed at least one IAM deal during the quarter. Notably, average overall deal size also increased in Q2, with IAM making inroads with large organizations like Sensata Technologies, a global sensor manufacturing leader, which has accelerated its workflows and is beginning to use the Docusign Iris AI engine to surface insights from agreements.

Docusign CLM saw improved momentum in Q2, delivering one of the strongest quarters in year-over-year quarterly bookings growth in the last several years. CLM continues to be a top choice for Enterprise customers with sophisticated Enterprise workflows, like T-Mobile, which has cut agreement processing time by 44%. Also, Docusign was recognized as a leader in the *2025 IDC MarketScape AI-Enabled Buy-Side CLM* report, which acknowledged that IAM is core to the Docusign strategy of replacing legacy and fragmented systems.

On the Product side, our rapid pace of innovation demonstrates consistent progress against our ambitious public roadmap and a steady increase in the value that IAM creates for customers. The IAM platform delivers end-to-end agreement management, empowering organizations to create, commit to, and manage their agreements at unprecedented scale and efficiency.

IAM is an AI-native platform that combines proprietary AI models with best-in-breed LLMs, drawing on Docusign's vast agreement library, unmatched domain and workflow expertise, and seamless integration with important third-party systems. Over the past two quarters, the number of documents ingested and available in Docusign Navigator, our intelligent repository, has increased by over 150%, and customers are processing tens of millions of agreements per month.

Customers tell us IAM is delivering significant value by performing tasks in minutes that used to take hours or even days. Docusign covers a far broader range of agreement workflows than any other vendor, and the deep integration of cutting-edge AI lets customers leverage years of agreement data with the leading ease of use, security, trust, and scalability they've come to expect from Docusign. In the coming months, we will launch AI agents within IAM, enabling new customer use cases and expanding our addressable market opportunity.

In Q2, we launched several new AI-powered IAM capabilities to help customers unlock value across the entire agreement management lifecycle. These include Custom Extractions, which let customers identify and capture organization-specific agreement information or client-specific terms without manually reviewing hundreds or thousands of contracts.

We also recently launched Agreement Preparation, which enables IAM to detect the type of agreement you're creating, build a template, and automatically suggest and position relevant fields. And to address the Enterprise need for efficient, secure, and scalable user management, SCIM for Docusign allows customers to automatically provision users through their existing identity providers.

In closing, we're proud of our strong execution and performance in Q2 and encouraged by the positive feedback we're receiving from IAM customers in the Commercial and Enterprise segments around the world. We believe IAM and the Docusign Iris AI engine are uniquely positioned to transform how organizations operate their businesses with deeper insight and actionability from their agreements. As we deliver greater value to customers, we're doing it more efficiently, at nearly the highest levels of profitability and capital returned to shareholders in our history.

I want to thank the entire Docusign team for their hard work, passion, and customer focus. I also want to acknowledge the announced changes to our Board of Directors and thank Maggie Wilderotter for her leadership during a time of transformative change in our Company, congratulate James Beer for becoming our Board Chair, and welcome Mike Rosenbaum to the Docusign family.

Docusign is the leading provider of AI-driven Agreement Management Solutions, and we're incredibly excited about the enormous opportunity that lies ahead.

Now I'll turn it over to Blake to discuss our financial results.

Blake Grayson

Thanks, Allan, and good afternoon, everyone.

Our performance was strong across the business in Q2, a testament to our continued execution against our three strategic pillars, accelerating product innovation, strengthening our go-to-market channels, and improving our operating efficiency.

In Q2, total revenue was $801 million and subscription revenue was $784 million, both up 9% year-over-year. There was no material impact on revenue growth related to foreign currency. Revenue outperformance this quarter was driven primarily by our Direct Sales channel, particularly within our e-Signature business.

Q2 billings were $818 million, up 13% year-over-year. This included a foreign currency growth tailwind of approximately 1% year-over-year, just slightly ahead of our expectations. Billing's outperformance this quarter was driven primarily by three different factors, with each having a relatively similar level of impact.

The first factor was strengthened direct customer demand and improved gross retention in our e-Signature portfolio. Although it represents a much smaller share of our business, CLM also had a strong quarter as the CLM business grew well into the double digits year-over-year in Q2.

The second factor was due to early renewal strength and the favorable timing of deals booked in Q2. While we saw higher early renewals than forecasted, the health of those renewals continued to improve year-over-year as the percentage of early renewals with expansion grew and the share of those that were flat or included partial churn declined. This dynamic is consistent with the trend we saw in Q1, where a byproduct of sales incentive adjustments resulted in healthier early renewals. We are encouraged by the consistency from Q1 to Q2, still recognizing that the timing of renewals can impact quarterly billings.

The third factor of outperformance was driven by a slightly higher payment frequency shift to annual billing contracts. While the vast majority of our direct customers are billed on an annual basis, the share was slightly higher than forecasted. When removing the impact from timing relative to our forecast, billings growth during the quarter was approximately 10% year-over-year. As a reminder, quarter-to-quarter billings can meaningfully fluctuate due to the timing of customers signing contracts. As a result, we are actively evaluating potential updates to our future top-line reporting, including replacing billings with an alternative measure. We plan to provide more details during our third quarter earnings call in December.

Dollar net retention rate rose to 102% in Q2 from 101% in Q1 and increased year-over-year from 99% in Q2 of fiscal 2025. We are pleased to see the modest improvement in DNR, which continues to be mostly driven by better gross retention. Usage trends also continue to show improvement.

Consumption, a measure of envelope utilization, improved across all customer segments and nearly every major vertical in Q2, and the volume of envelopes sent in Q2 increased year-over-year at a rate consistent with prior quarters.

IAM sales maintained strong momentum this quarter, which slightly outpaced our expectations as we continue to scale the platform. In Q2, we saw an increase in average IAM customer deal size, an encouraging sign, as we took the first steps upmarket with the IAM Enterprise ramp. We remain on track for IAM customers to contribute a low double-digit percentage share of the Subscription Book of Business exiting Q4.

International revenue represented 29% of total revenue and grew 13% year-over-year. We're encouraged that the Asia-Pacific region was our fastest-growing International region this quarter. Allan, Paul, and the team just held momentum events in that region in August, and we're pleased to see the growth there.

Digital revenue continued to deliver results with growth outpacing the overall business. In Q2, total customers grew 9% year-over-year, ending the quarter above $1.7 million. Large customers spending over $300,000 annually increased by 7% year-over-year to $1,137 in Q2.

Turning to the financials, our focus on operating efficiency continued to yield strong results this quarter.

Non-GAAP gross margin for Q2 was 82.0%, relatively in line with the prior year, as higher revenue mostly offset the impact of cloud migration costs. We delivered record-high non-GAAP operating income in Q2 at $239 million, with our performance versus our expectations attributable mostly to top-line strength.

Operating margin was 29.8%, down 240 basis points versus last year. As a reminder, we expected Q2 to have the most challenging year-over-year operating margin comparison of any quarter in fiscal 2026 due to several factors, including the timing and impact of our Compensation programs, specifically the shift to cash from equity for some employees. As you may also recall, Q2 fiscal 2025 also had a one-time operating margin benefit of approximately 150 basis points associated with insurance reimbursements and the release of a litigation reserve. Our cloud computing migration also continues to provide a year-over-year headwind to margins.

We ended Q2 with 6,907 employees, up slightly versus 6,838 at fiscal 2025 year-end. This reflects our measured approach to hiring in fiscal 2026 to support our strategic initiatives while maintaining efficiency.

In Q2, we delivered $218 million of free cash flow, a 27% margin, which was a slight increase versus Q2 of last year, as our collections efficiency remained strong, combined with in-quarter billing strength. We do expect to see a lower free cash flow yield in Q3 versus Q2, primarily from the timing of billings.

Our balance sheet is healthy, ending the quarter with approximately $1.1 billion of cash, cash equivalents, and investments. We have no debt on the balance sheet.

In Q2, we slightly increased the pace of our buyback activity and repurchased $200 million in share value, effectively redeploying the bulk of our quarterly free cash flow generation back to shareholders. We will continue to opportunistically repurchase shares, and while the pace of this activity may fluctuate quarter-to-quarter, share repurchases underscore our commitment to returning excess capital to shareholders.

Non-GAAP diluted EPS for Q2 was $0.92 compared to $0.97 last year. GAAP diluted EPS was $0.30 versus $4.26 last year. As a reminder, in Q2 of fiscal 2025, related to our GAAP financials, we released a valuation allowance on certain existing deferred tax assets, decreasing our non-cash tax expense by approximately $838 million. Diluted weighted average shares increased slightly year-over-year to $211 million, whereas basic weighted average shares decreased slightly year-over-year to $203 million due to the impact of the repurchase program.

With that, let me turn to guidance. We expect total revenue between $804 million to $808 million in Q3, or a 7% year-over-year increase at the midpoint. For fiscal 2026, we expect revenue between $3.189 to $3.201 billion, or a 7% year-over-year increase at the midpoint. Of this, we expect Subscription revenue of $786 million to $790 million in Q3, or a 7% year-over-year increase at the midpoint, and $3.121billion to $3.133 billion for fiscal 2026, or an 8% year-over-year increase at the midpoint.

For billings, we expect $785 million to $795 million in Q3, or a 5% year-over-year growth rate at the midpoint, and $3.325 billion to $3.355 billion for fiscal 2026, or a 7% year-over-year growth rate at the midpoint. Q3 billings guidance reflects a renewal timing headwind that is similar in magnitude to the Q2 early renewal timing benefit as discussed earlier. As continually shown in recent quarters and years, billings are heavily impacted by the timing of customer renewals, leading to meaningful variability from period-to-period. Also, our outlook for Q3 and Q4 factors in a more challenging year-over-year comparison versus billing strength in the second half of fiscal 2025.

Our updated full-year top-line guidance reflects the following dynamics present in our business and the external environment.

For full-year revenue, the annual guidance midpoint is increasing by $38 million from last quarter's full-year guidance. The increase is driven primarily by Q2 business strength and the expectation that a portion of these trends will continue into the second half of the year. For full-year billings, the annual guidance midpoint is increasing by $28 million from last quarter's full-year guidance.

This increase reflects a positive impact from Q2 business strength but does not include the timing benefit from early renewals that we saw in Q2, as that will largely be offset in the remainder of the year. As a reminder, we have a hard comparison against last year's higher volume of early renewals, particularly in the second half of the year. Adjusting for early renewals compared to last year, we continue to expect full-year billings growth will be approximately 1 percentage point higher year-over-year, leading to modest acceleration over last year.

For profitability, we expect non-GAAP gross margin to be 80.3% to 81.3% for Q3 and between 81.0% to 82.0% for fiscal 2026. We expect non-GAAP operating margin of 28.0% to 29.0% for Q3 and 28.6% to 29.6% for fiscal 2026. For the full year, we included the following two considerations in our non-GAAP profitability guidance.

For gross margins, we continue to expect approximately 1 percentage point of headwind year-over-year from our ongoing cloud data center migration efforts. This headwind was slightly lower than anticipated in both Q1 and Q2 due to a shift in migration timing out to the remainder of fiscal 2026. We continue to expect a gradual easing in migration cost impacts in fiscal 2027 and beyond.

For operating margins, we continue to expect an approximate 1.5 percentage point operating margin headwind due to the combined impact of cloud migration, the shift of some roles to cash compensation from equity, and the comp against one-time professional fee savings last year in Q2 of 2025. We expect non-GAAP fully diluted weighted average shares outstanding of $207 million to $212 million for both Q3 and fiscal 2026. Please see the modeling consideration slides in our Q2 earnings deck for a full summary of guidance context.

In closing, Q2 represented another quarter of DocuSign's commitment to product innovation, enhanced go-to-market motions, and improved operational efficiencies. As we look ahead, our focus remains on sustaining this momentum while continuing to generate significant cash flow and returning capital to shareholders through strategic buybacks. That concludes our prepared remarks.

With that Operator, let's open up the call for questions.

Operator

Thank you. We will now be conducting a question-and-answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation code will indicate your line is in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handphone before pressing the star key. One moment, please, while we poll for questions. Thank you.

Our first question comes from a line of Robert Owens with Piper Sandler. Please proceed.

Robert Owens

Great. Good afternoon, and thanks for taking my question. While the early success in IAM is compelling, I actually wanted to drill down into improved fundamentals across your core e-Signature. And you spoke to improvement in Consumption, growing volumes, and really what's underpinning this? Is it economic? Is it evolutionary? Are you using (phon) utilization driven by attach of IAM? Thanks.

Blake Grayson

Yes. I'll take a stab at this and Allan can jump in. Thanks for the question. You know, this is a trend we've been seeing pretty consistently over the past year. So, like especially not in Q2, we saw certain verticals, you know, just to highlight a couple, Financial services, Healthcare, Business services, all growing, you know, super well for us on a year-over-year basis. People ask about real estate. That's growing a little bit slower than average, but still growing at a positive rate year-over-year.

You know, it's anecdotal, of course, but it's all dependent on how our customers' businesses are working, whether or not they're adding use cases, because we're seeing that in some existing customers also, and then just also macro effects for them as well. But it's not—I just want to make sure, like the consumption and the envelope send trends really are things that we've seen pretty consistently over the last 12 months, and we highlight them I think pretty consistently as well. And so I'm just excited to see that.

Allan Thygesen

Yes. Overall I don't think we're seeing any significant evidence of macro weakness in our numbers or in the contract volumes or utilization numbers.

Robert Owens

All right. Thanks for the color.

Operator

Thank you. Our next question comes from the line of Tyler Radke with Citi. Please proceed.

Tyler Radke

Thank you for taking the questions. I wanted to ask you about CLM, which, you know, it seemed like it had a breakout quarter with some of the large deal momentum you referenced, you know, including T-Mobile. Can you just talk about the pipeline that you're seeing in that business? Would you sort of say that this was a timing benefit, or do you think this is kind of the start of a more sustainable trend? Thank you.

Allan Thygesen

Yes, look, I think we think that the overall trend in the market is positive. I don't know that there's—I wouldn't over-interpret the second quarter as a breakout for the category or for us. I think it was a very strong quarter, and we closed some very large deals. Really exciting and great to see, but a little too early to call a broader category trend. But they're definitely encouraging.

Operator

Thank you. Our next question comes from the line of Jake Roberge with William Blair. Please proceed.

Jake Roberge

Yes, thanks for taking the question, and congrats on the great results. Nice to hear that more than 50% of your Enterprise reps have already signed at least one IAM deal. Could you talk a little bit more about how the rollout of your newer markets, like Enterprise and International, have progressed compared to your core North American Commercial market, and just whether that pricing uplift that you originally saw has held as you've entered into those new markets?

Allan Thygesen

Yes, there was a lot there. Let me try to unpack that. First, just as a reminder for everyone, we launched initially to Commercial customers in North America, and then we rolled it out globally. Our first Enterprise release was in December, and we've since released multiple features aimed specifically at Enterprise customers. And I think the noteworthy thing here in Q2 is that we started to see some larger deals with Enterprise customers, which is very exciting because that's an even larger market opportunity for us in the long run. We're not relying on a lot from the Enterprise segment this year, but we feel that over time that could become even bigger. So as we ramp up our capabilities, both on the product and go-to-market side, it's nice to see larger deals with big, sophisticated clients, and I think there's more to come there.

So very encouraging. And, of course, this is what we were laying the groundwork for at the beginning of this year, setting ourselves up to go deeper with customers of all sizes, but in particular Enterprise customers. And those changes have now landed well, I think, and we are really pleased with how the team has settled in, and there's more to come.

Blake Grayson

And I'm just going to add on top of that. It's exciting to see the International regions embracing IAM. That's been something exciting to see just on a vintage basis. Obviously, you know, IAM did launch in most of our International regions later than it did in North America. And then, you know, to your question on the expansion rate side, we don't break that out. But one thing that we have said previously and it continues to be the case is we see a meaningful expansion for customers that are moving from just the e-Sign platform over to IAM, and it's been remarkably consistent. And so that's great, and we're going to continue to watch it. It's still very early days for us. But that's been exciting from my perspective to see.

Jake Roberge

Great. Thanks for taking the question, and congrats on the results.

Operator

Thank you. Our next question comes from the line of Josh Baer with Morgan Stanley. Please proceed.

Josh Baer

Congrats on a very strong quarter. Appreciate all the detail with kind of breaking out the outperformance in billings between, you know, gross retention, CLM, early renewal strength, duration, a number of other factors. I don't think IAM was really one of them as far as driving the outperformance. I was hoping you could talk about that a little bit and really just straight, you know, being straightforward, what are the economics when a customer adopts IAM? Is it accretive to growth and by how much?

Blake Grayson

Sure. So, yeah, so the biggest drivers of the billing is outperformance. You know, as mentioned in the prepared remarks, stronger bookings primarily in our e-Signature business, right? It's obviously the vast majority still of what DocuSign has in its portfolio. But also, you know, then timing and then also billing's payment frequency regards to IAM. It did slightly outperform our expectations, but it's still very early days for us in that area and that platform. And so what led to the beat versus our guidance was predominantly that e-Signature base.

With regards to expansion, we don't break it out. It's still super early for us. We have to see how this goes, especially as we move up market. But it's very clear, and we said this before, we see a meaningful expansion for customers when they move from an e-Signature only situation to an IAM. There's just so much more value that we're providing to a customer. And its early days, but frankly, customers are seeing that extra value and they’re willing to share that with us. So we're really excited about that, but no other detail besides…

Allan Thygesen

Yes, if I could just add a couple comments. First of all, IAM is a critical factor year-on-year growth and an even more important factor in the growth acceleration that I think we and you are all excited to begin to see and are projecting for the future. We're kind of right where we want to be with IAM for this year. We reiterated our guidance that we expect IAM to be a low double-digit percentage of our overall book, which is pretty impressive for a new platform. Look, it's a critical part of our story. As Blake said, e-Sign is so large now that just on pure dollars it's always going to dwarf everything else for a little while. But we can't get to where we want to go without growth acceleration from IAM as well. And so the fact that we had a strong and healthy e-Sign quarter coupled with continued growth in IAM, that's really the magic formula for the Company, and I think that's what produces the strongest results.

Josh Baer

Yes that's really helpful. I mean, you sound great, and there's a lot of—and this quarter was really strong. There's a lot to like. I mean, it would be super helpful if IAM is going to be a double-digit percentage of bookings to just better understand the economics of, you know, the uplift with moving over to IAM and what other factors are changing in the contracts. Like that would really help to unlock that story. But something it sounds like we'll look forward to as you have a couple more quarters actually, you know, selling to the enterprise and upmarket. But congrats again. Thank you.

Allan Thygesen

Thanks.

Operator

Thank you. Our next question comes to the line of Kirk Materne with Evercore ISI. Please proceed.

Bill

This is Bill on for Kirk, and thanks for taking my question. Can you dive into some of the drivers behind the improved gross retention, and is there more to go on that front in the second half of this year and into next?

Blake Grayson

Sure. You know, this is a trend we've seen, gosh, over the past at least 18 months for us. Like if you look at our dollar net retention rates, we've been able to improve from I think about a low of 98% about 18 months ago in Q4 of '24 to the 102 that we adjusted for Q2. I would just say operational execution plays a huge part of this. We have folks at Docusign now spending a much greater portion of time with regards to staying in front of these renewal opportunities, getting in front of them, you know, months, many months in advance to be able to address any concerns that a customer might have, whether it's for potential expansion or issues that they're having. So we've seen the fruits of that labor, I think, you know, kind of pour into this business, and there's still a lot of opportunity left for us. I'm not going to make a forecast regarding for the next second half of the year, but for this business, we have opportunities both on improving our gross retention rates of our core portfolio and then also expansion, which is driven predominantly by IAM. And when we can get both of those things working together, that's where we really believe we have the ability to unlock the flywheel for us for the long term.

Bill

Great. Thanks for taking my question.

Operator

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

Brad Sills

Oh, wonderful. Thank you so much. I wanted to ask about the partnership with the U.S. Federal General Services Administration. It seems like a big deal. Just curious what this means for your Federal business, your Federal pipeline, and what we should expect out of that segment of the business going forward.

Allan Thygesen

Yes, no, we were really pleased to do that. In fact, I'll be in D.C. next week meeting with a number of folks across many different departments in the Federal government, and it's great to see the engagement. This contract is really sort of a facilitation, making it easier to buy for any federal department. We don't have—I would say our Federal business is relatively modest today. While we're present in, like, all 15 cabinet level departments, so we're certainly, you know, used. Relative to our opportunity, there's just a lot of headroom. Interestingly, we do better and have historically had a bigger business in state and local, and that continues to do well, but we felt we had a big opportunity in Federal. So I think the GSA was interested in partnering with us because, you know, we're a very natural partner for bringing more efficiency and customer service to the Federal government, and we were, of course, excited about that opportunity.

So it's a big growth opportunity for us, but it's still early days. It's not a meaningful contributor to the business yet, but I'm spending time on it, as are several other executives, so we're hopeful.

Brad Sills

Excellent. Sounds exciting. Thanks, Alan.

Operator

Thank you. Our next question comes from the line of Austin Cole with Citizens. Please proceed.

Austin Cole

Great. Thanks for taking my question. I wanted to ask on the go-to-market front and those changes that were made at the beginning of the year. How do you feel about how reps have adapted to those changes? Are they kind of well-equipped and incentivized to sell IAM, or might there still be some changes to make down the road? Thanks.

Allan Thygesen

No, I feel really good about it. Look, we made those changes to position us for the long term to accelerate our IAM business and just more generally be able to go deeper with customers, and I think the reps have responded really well. We put in a lot of enablement. We put in new incentive systems, new quotas, territories. It was a lot, but I'm very proud of how the team responded to that. As you can see here in Q2, the Direct Sales team did a really nice job in Q2, so shout out to them.

And yet we have—it’s so early, we have so much headroom. I think in terms of not planning any meaningful changes this year and nothing of that magnitude in the foreseeable future, but it's great to see the bold changes that Paula led, so I just want to tip of the hat to her for having both conceived of all the changes, driven them, and landed them. So well done.

Austin Cole

Great. Thank you. Thank you.

Operator

Our next question comes from the line of Mark Murphy with J.P. Morgan. Please proceed.

Mark Murphy

Thank you very much. Alan, is there any way to approximate the kind of customer acceptance for opting in where they would have Iris AI scan their agreements and, you know, learn from them or index them? It's hard externally to understand if they just do that by default or not. Then is it common enough that you can build up an agreement library that would with enough intelligence that, you know, you can kind of move the risk scoring and the cycle times to a different level?

Allan Thygesen

Yes. Actually, I think that's perhaps one of the strongest aspects of our story right now. So, yes, we ask customers explicitly to opt in and consent to sharing their agreements, and that unlocks a lot of the AI features. And, I mean, practically everybody's doing that. We now have—we're approaching 100 million agreements just with InterNavigator available for AI processing, and it's just such a diverse group. It's everything from sales agreements to procurement agreements to employment agreements and really every function in the Company. I don't think there's anybody who comes close to that.

As you know, one of the key drivers of AI quality is data. So we're in a great position to leverage that, and that's what allows us to do this right out of the box. You know, one of the things that's not as well understood is we often have your agreements already. So if you consent to this, we can make the AI features available instantly and the average customer goes live in a few weeks. I mean, that's just unheard of for Enterprise software. And so just the time to value coupled with the potential value unlock in the agreement library is very significant and our scale is just very different from others in that business. So it's part of what I think makes us all so excited about the future.

Mark Murphy

Thank you.

Operator

Thank you. Our next question comes from the line of Brent Thill with Jefferies. Please proceed.

Brent Thill

Hey, Blake. On the margin, I know you're kind of stalling the margin progression this year versus last year. I guess many are asking when do we see the fall through on the top line? We're not necessarily seeing—we saw a good quarter of it in terms of just overall real-to-real acceleration. I think Alan's aspiration would be back to double-digit. How do you think about that tradeoff? And where are all these investments going this year? Does it go to market? Is it in products? All the above? Any color there would be helpful. Thanks.

Blake Grayson

Yes, I appreciate the question. So we have three hard comps for us this year. Their particular impact into this quarter that we saw, right? We've got the higher hosting costs for cloud migration. We have a hard comp against some one-time legal benefits from an insurance reimbursement litigation credit. And then we also this year have some headwind really starting this quarter with regards to shifting some roles to cash versus equity as we manage the long-term solution.

You know, those three components in the prepared remarks, you'll recall, provide about 150 basis points of pressure. Our full-year guide now for operating margin reflects only about half of that pressure. So we've been able to offset a portion of that, actually, above and beyond, you know, what we had originally expected. So I'm excited about that. And so it's all about this balance right now of maintaining the gains that we worked really hard to get. I think over the last two fiscal years we've increased non-GAAP operating margins from around 20% to 30% and so those are some tough decisions that we had to make. So maintaining them are important. And so we're doing that.

But also while making these investments in a little bit in the go-to-market and particularly into R&D with regards to the IM, you know, development and launch. And so we can spin that top line number, the flywheel really does drop to the bottom line, Brent. So I think for us that's where the future leverage opportunity that we have to get to that double-digit top line growth. I think provides, you know, a lot of output for us in terms of opportunity for leverage. So really happy with the consistency and the path we're on. I think we're balancing this kind of this investment between growth and efficiency really well. But we've got some opportunities longer term for sure.

Brent Thill

And just real quick, on the cloud transition, when do you approximate that will be less of a headwind? When does that actual transition end?

Blake Grayson

Yes, so this is the peak year for us that we've got. So we should start to see those, you know, start to be less of an impact for us in FY'27 and then even later into beyond. And I just want to make sure folks remember, like, hosting costs are a big chunk, you know, for us for our cost of revenue, but it's not the majority of it, right? We've got a lot of people in there and things like that. But, no, we definitely expect to see that pressure kind of start to mitigate for us next year.

Brent Thill

Great. Thanks**.**

Operator

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

Alex Zukin

Hey, guys. Thanks for taking the questions. Just two quick ones. On IAM, clearly you're continuing to see maybe on the broader business early renewal strength and the percentage of early renewals with expansions continue to grow. Are any of those starting to be driven by IAM attached? I think before you talked about it more heavily skewed towards new users. But I'm curious if the sales changes and some of the momentum you're seeing is kind of shifting that—or not shifting, but in addition to that, also now grabbing some of the existing customer relationships that you have. And then I have a quick follow-up.

Allan Thygesen

Yes, I would say, yes, it does. It's just we've just got to remember, again, just the relative size that we have in this book of business. We're now actually just starting to lap the first full year from our customers that we were really just signing up an IAM this quarter last year, the very early days of that. It's encouraging. We're seeing gross attention rates higher than we are for e-Sign. It's still early. It's a small sample size. But we're excited about it, and we are seeing those conversations lead to it. But it's not like it's the overarching component. I think the e-Signature business; the foundation is strong and held up well this quarter.

Alex Zukin

Perfect. Then maybe just a broader question. I'm sure you can appreciate there have been a lot of questions about how changes in this kind of search and SEO are affecting top-of-funnel dynamics for a lot of companies.
Anything that you guys are seeing there, or maybe you're completely immune to it or you course-directed a while ago, and are you seeing any changes to top-of-funnel? What percent of top-of-funnel is SEO-related, et cetera?

Allan Thygesen

Yes. We're not seeing anything yet. I think we're very pleased with our organic traffic, and you know Docusign has an amazing brand and recognition, reputation, and I think that plays well both in an SEO world and a GEO world. With that said, look, behavior, consumer and enterprise buying behavior, is changing as a result of LLMs. And so I think we're keeping a very close eye on those changes and how that affects behavior throughout what we've historically talked about as the funnel. So that's number one. And we continue to look to acquire new customers and acquire a substantial number every quarter, and that will continue to be a focus.

But the big opportunity for us is to upsell our existing 1.7 million customers, pretty much all of these e-Sign customers, to IAM. And we are hyper-focused on that as an opportunity at all levels, and that's what's driving the bulk of the IAM results, and that's where the big dollars are. And so we want to continue to feed the top of the funnel with new customers, and that's very important for the long-term health of the business. But I don't want to get distracted. I think the number one big expansion opportunity for us is to move people from e-Sign to IAM, and we're making good progress on that with a lot of head room.

Operator

Thank you. Our last question comes from Rishi Jaluria with RBC Capital Markets. Please proceed.

Rishi Jaluria

Wonderful. Thanks so much for squeezing me in. Nice to see continued strength in the business and broad-based momentum. I want to maybe drill and ask a little bit philosophically about IAM. You know, obviously you've discussed all the use cases and the real unlock, especially with AI. Now, the question I want to ask is, we hear a lot of, you know, AI vendors talking about one of the use cases for LLMs and search and reasoning being, you know, analyzing contracts, finding the right answers, being able to synthesize information from multiple contracts, et cetera.

And it almost feels like they're trying to tackle that same problem, you know, in a different way. Maybe can you help us understand, even with others kind of looking into that use case, what gives you that kind of continued right to win, and where are investment opportunities that you can make to drive further differentiation versus those so this doesn't become more competitive or more commoditized? Thank you.

Allan Thygesen

Yes, thanks for that question. Look, I think AI is a massive tailwind for DocuSign. And it's both a tailwind because of the overall sort of category enable, and we can do so many more things with contracts now. They used to be dump flat files, and, you know, there wasn't much anybody could do with them. But to your point, that's an elevation of everyone's capability. But then it plays into our strengths. We have deep knowledge of agreement structure. We're embedded in agreement workflows. We have exceptional scale. I just referenced, no one else touches, you know, at this point now, you know, 100 million proprietary customer agreements with consent and an incredibly rich agreement diversity.

Of course, we're integrated into practically every enterprise system, whether you're the Salesforce or a SAP or Microsoft or ServiceNow or Google or Workday customer. Customers typically use DocuSign as a complement to those systems. So it's easy for us to roll things out and for customers to access DocuSign Insights in whatever tool they prefer. So you never want to be naive about these things. There’s certainly a tremendous amount of innovation and investment that's happening. But I think our unique proprietary position from a modeling, from a data perspective, from a workflow perspective, from a customer access perspective, I think it's a very strong tailwind for us. And I think it's partly what gets everyone in the Company so excited about our future.

Rishi Jaluria

Very helpful. Thank you.

Operator

Thank you. I would now like to pass the call back over to Management for any closing remarks. Yes.

Allan Thygesen

Thank you, Operator. Thank you to all who joined today's call. I want to thank the entire DocuSign team for their commitment to putting our customers first after delivering the powerful AI native value through the IAM platform. And to our investors, we will continue to manage this business in order to realize its full potential over the long term. So thanks for sharing your time with us, and we look forward to speaking with you next quarter.

Operator

That concludes today's teleconference. You may now disconnect your lines. Thank you for your participation.