S&P Global
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Smartsheet Inc. NYSE:SMAR

Earnings Call

Thursday, December 7, 2023 9:30 PM GMT

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Presentation

Operator

Good day, and welcome to the Smartsheet Third Quarter Fiscal 2024 Earnings Call. Today's call is being recorded.

And I would now like to turn the conference over to Aaron Turner, Head of Investor Relations. Please go ahead.

Aaron Turner
VP of Investor Relations & Treasurer

Thank you, Lisa. Good afternoon, and welcome, everyone, to Smartsheet's Third Quarter Fiscal Year 2024 Earnings Call. We will be discussing the results announced in our press release issued after the market closed today. With me today are Smartsheet's CEO, Mark Mader; and our CFO, Pete Godbole. Today's call is being webcast and will also be available for replay on our Investor Relations website at investors.smartsheet.com. There is a slide presentation that accompanies Pete's prepared remarks, which can be viewed in the Events section of our Investor Relations website.

During this call, we will make forward-looking statements within the meaning of the federal securities laws. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends. These forward-looking statements are subject to a number of risks and other factors, including, but not limited to, those described in our SEC filings available on our Investor Relations website and on the SEC website at www.sec.gov. Although we believe that the expectations reflected in the forward-looking statements are reasonable, our actual results may differ materially or adversely -- and/or adversely.

All forward-looking statements made during this call are based on information available to us as of today, and we do not assume any obligation to update these statements as a result of new information or future events, except as required by law. In addition to the U.S. GAAP financials, we will discuss certain non-GAAP financial measures. A reconciliation of the most directly comparable U.S. GAAP measures is available in the presentation that accompanies this call, which can also be found on our Investor Relations website.

And with that, let me turn the call over to Mark.

Mark P. Mader
President, CEO & Director

Thank you, Aaron, and good afternoon, everyone. Welcome to our third quarter earnings call for fiscal year 2024. Smartsheet revenue for the quarter exceeded our guidance and grew by 23% year-over-year to $246 million, and billings grew 22% year-over-year to $268.5 million. In Q3, we generated non-GAAP operating margins of 8%, and free cash flow was $11.4 million. We ended the quarter with annual recurring revenue of $981 million and more than 13.9 million Smartsheet users.

In Q3, 89 customers expanded their Smartsheet ARR by more than $100,000 and 256 companies expanded by over $50,000. Additionally, we now have 59 customers with ARR over $1 million, up from 40 a year ago.

Our strength in the enterprise continued in Q3 with expansions at companies such as Cushman & Wakefield, Cintas Corporation, biotech company, BeiGene, and CommVault Systems, among others. Q3 was also a strong quarter for our suite of capabilities-based products. Similar to last quarter, capabilities were present in each of our top 10 expansions. Smartsheet Advance, which is our bundle of our capabilities, was included in 250 of our expansions in Q3. Advance played a key role in a multiyear, multimillion-dollar deal with a Fortune 500 specialty beverage company. Their expansion to Smartsheet Advance Gold will help support the company as it executes high-impact projects, including new product rollouts and associated equipment deployments, network upgrades as well as new store openings and store improvements.

In Q3, we also saw a significant expansion that included an upgrade to Advance Platinum at a major airline. For a number of years, Smartsheet has powered aspects of the carrier's flight ops, flight products and tech ops units. Due to growing demand for Smartsheet from other departments, they decided to upgrade to Smartsheet Advance. By implementing the platinum tier of Smartsheet Advance, they were able to consolidate their licenses and bring them all under IT's purview to give these divisions access to all of our capabilities such as Control Center, Dynamic View and Bridge.

This consolidation means that the airline has an opportunity to increase visibility into its IT spend and empower Smartsheet users as it brings greater efficiency to critical activities like resource management, maintenance and scheduling. And that resulted in a 3-year commitment with a total contract value of $4.5 million and an opportunity to further scale Smartsheet across the organization.

The ability to rapidly scale was also key to an $850,000 deal at one of the country's largest quick service restaurant brands. The company is in the process of a multiyear transformation initiative and selected Smartsheet Control Center and Resource Management to help drive its global digital transformation and implement portfolio reporting on day-to-day and annual operating plan projects for the senior executive team. By using Smartsheet, the company has been able to enhance and simplify collaboration across over 30,000 locations, and in doing so, rendered a number of other applications obsolete.

Another customer example relating to scale is the significant expansion at a global media and entertainment organization that was looking to streamline its tech stack. The company was already using Control Center to manage 14,000 projects and 12,000 workflows in Bridge to track and manage their portfolio of projects. Because that work went across its retail, events, theme parks and publishing divisions, Smartsheet was well positioned to win this consolidation. Going forward, the company will extend its use of Smartsheet to other initiatives such as improved speed to market for technology projects, efficient headcount management, cost controls and profit improvement initiatives. This expansion brought the company's ARR to over $4 million.

On the product front, in Q3, we introduced a new way for our customers to discover and use 2 of our premium capabilities without the need to first contact a Smartsheet rep or partner. We believe empowering frictionless self-discovery of high-value Smartsheet capabilities will drive greater adoption of these premium offerings, and early results have been promising with hundreds of trials started with just within the first few months.

One of those trials occurred at a mid-cap biotech company and directly led to the purchase of Data Shuttle to migrate significant amounts of data into Smartsheet from legacy clinical storage systems. While the company has been a customer for years, it had never utilized our premium capability. Once discovering Data Shuttle, the company's clinical trial team launched automated workflows to import data they use to track the progress of its research on cancer and rare disease therapies.

They found that it had a positive impact by allowing them to centralize view and manage data from these disparate sources, and their success with Data Shuttle has now led to interest in other premium capabilities. Over 40% of these deals in Q3 that were closed as a result of capability self-discovery were with customers buying a premium capability for the first time.

We continue to make strides integrating AI across the Smartsheet platform. We now have approximately 50,000 enterprise users in early access to AI-powered skills that allow users to generate formulas and content directly in their sheets. Both these skills will be generally available later this quarter to enterprise customers. The feedback from early access users confirms that our AI features will help power enterprise processes and make it simple for any user to gain insight into the work being done across teams. These AI skills are helping customers achieve their desired outcomes even more rapidly with the Smartsheet platform. Additionally, AI-powered skills will roll out to eligible early adopters next month.

We continue to invest internationally in response to increasing global demand. To support data residency requirement for our international customers, we launched a Smartsheet platform instance in Germany in 2021, and we will launch an instance in Australia next year. This new Smartsheet region will enable Australian customers to comply with important data residency requirements and offer them the flexibility to choose where they want their content to be hosted. We will be pursuing IRAP certification, ensuring that it will have the right policies and security controls to meet Australian government information security requirements. This enables Smartsheet to serve a growing regional customer base, including organizations and agencies with the most demanding governance and regulatory requirements.

Q3 was also a productive quarter for our federal government business in the U.S. reaching some notable milestones. We signed a 6-figure expansion at a large government agency, which brought its ARR up to $1.6 million. This agency uses Smartsheet for critical workflows from purchase management to managing grant funding to using Control Center to manage travel budgets and expense management across its multiple regional offices. Additionally, we now have a presence in all 15 U.S. cabinet-level departments and have 2 government agencies with ARR over $1 million.

In closing, as we approach crossing the $1 billion ARR milestone this quarter, we remain focused on both product innovation and customer value by continuing to execute as the user-preferred enterprise work management leader.

Now let me turn the call over to Pete.

Pete Godbole
CFO & Treasurer

Thank you, Mark. We outperformed all aspects of our guidance in Q3. Similar to previous quarters, our enterprise business continues to perform well, which is reflected in the growth of our higher ARR customer cohort tiers and volume of large deals. We continue to see macro-related pressure on our higher velocity transactions and on our SMB customer segments. Given these pressures, we are maintaining our prudent approach to our Q4 and full year guidance.

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

Third quarter revenue came in at $245.9 million, up 23% year-over-year. Subscription revenue was $232.5 million, representing year-over-year growth of 25%. Services revenue was $13.4 million. Revenue from capabilities made up 33% of subscription revenue.

Turning to billings. Third quarter billings came in at $268.5 million, representing year-over-year growth of 22%. Approximately 94% of our subscription billings were annual with about 3% monthly. Quarterly and semiannual represented approximately 3% of the total.

Moving on to our reported metrics. The number of customers with ACV over $50,000 grew 26% year-over-year to 3,719. And the number of customers with ACV over $100,000 grew 32% year-over-year to 1,779. These customer segments now represent 65% and 51%, respectively, of total ARR. The percentage of our ARR coming from customers with ACV over $5,000 is at 91%.

Next, our domain average ACV grew 16% year-over-year to $9,225. We ended the quarter with a dollar-based net retention rate, inclusive of all our customers, of 118%. The full churn rate was 4%. We expect to exit FY '24 with a dollar-based net retention rate of around 116%.

Now turning back to the financials. Our total gross margin was 84%. Our Q3 subscription gross margin was 87%. We expect our gross margin for FY '24 to remain at or above 83%. Overall, operating income in the quarter was $19.4 million or 8% of revenue. Free cash flow in the quarter was $11.4 million.

Now let me move on to guidance. For the fourth quarter of FY '24, we expect revenue to be in the range of $254 million to $256 million and non-GAAP operating income to be in the range of $21 million to $23 million. We expect non-GAAP net income per share to be $0.17 to $0.19 based on diluted weighted average shares outstanding of 140 million.

For the full fiscal year '24, we now expect revenue of $955 million to $957 million, representing growth of 25%. We expect services to be 6% of total revenue. We expect our non-GAAP operating income to be in the range of $82 million to $84 million, representing an operating margin of 9%, and non-GAAP net income per share to be $0.68 to $0.69 for the year based on 138 million diluted weighted average shares outstanding.

We expect our Q4 billings to be $339 million, bringing our FY '24 billings growth guidance to 20%. This includes the impact of our decision to invest more in our partner network that will include shifting more services delivery to this channel. The impact of this shift will be a reduction of around $3 million to billings in Q4. We are raising our free cash flow guidance for FY '24 to $130 million.

To conclude, we outperformed all aspects of our guidance in Q3 and are encouraged by the signals we are seeing from our incremental growth drivers such as self-discovery of capabilities and the new AI features. Now let me turn the call over to the operator. Operator?

Question and Answer

Operator

[Operator Instructions] We'll take our first question from Scott Berg with Needham.

Scott Randolph Berg
Needham & Company, LLC, Research Division

Really nice quarter here. I wanted to start on the billings side. You saw some acceleration in the growth quarter-over-quarter, speaks to some of the large deal environment there. But how do we think about kind of pipeline and demand trends going into Q4? Do they like kind of normal and similar from what you've seen last quarter or 2? Or do you see any changes either up or down further?

Pete Godbole
CFO & Treasurer

Thanks, Scott. This is Pete. As we looked at the pipeline, we are seeing basically the same strength in enterprise continuing into Q4. Obviously, it depends on the composition of deals and closing those deals. And what we're anticipating in Q4 is on the SMB expansion, the trend we saw in what I would call Q3, which was a degradation in the expansion rate, we're extending that out in a trended basis into Q4 as well.

Scott Randolph Berg
Needham & Company, LLC, Research Division

Got it. Helpful there. And then from a follow-up perspective, your operating margins have kind of lowered the last couple of quarters. I know that's in line with guidance. Your sales and marketing expense is up a little relative to subscription growth rates that are down a little bit there. Is the higher sales and marketing expense -- is that all related to the partner enablement activities that you're going through? Is there some other increased costs that we should be aware of?

Pete Godbole
CFO & Treasurer

I think when you think of the sales and marketing expense in Q3 and you look at that trend, remember, sales and marketing in Q3 is a function of the event we had in Q3, which was the ENGAGE event that plays into that spending. And then there's, what I call, investments that we are making as needed in the right parts of the sales and marketing machinery.

Operator

We'll take our next question from Michael Berg with Wells Fargo Securities.

Michael H. Berg
Wells Fargo Securities, LLC, Research Division

I wanted to ask on the demand dynamics in a different way. Anything to point to in the renewable environment outside the SMB vertical? Is it improving? How does it relate to the first half of the year? And how is it trending as we look into calendar 2024?

Pete Godbole
CFO & Treasurer

I think in general, our renewals are staying pretty strong. There's no big difference in the environment that we've seen between the first half and the second half. But remember, our business is pretty well diversified across all verticals. So we get the benefit of that, but we're not seeing any big changes in the renewal environment.

Michael H. Berg

Wells Fargo Securities, LLC, Research Division

Helpful. And then one quick follow-up on capabilities. It's been in the 30 -- low to mid-30s for several quarters now, and it seems to be a high-value proposition type of product. Maybe you can help us think about -- is there anything preventing further incremental adoption of that, whether it be driving home the ROI equation, budget priorities, just macro and budget scrutiny? Just any way we can think about how that adoption could accelerate?

Mark P. Mader
President, CEO & Director

I think when we look at -- this is Mark. When we look at the various phases or elements of driving growth in this area, one of the big initiatives for us in the second half has been how do we get them more aware to people at the right time. So that was part of the self-discovery effort. One of the things that we can see in next year and the years out is how do we not only increase discovery, but also how do we dramatically accelerate the transaction on those types of things. So we see a future in which the entire portfolio is visible to people, can be utilized by people and can also be transacted by people in a variety of methods, whether you speak with a partner, whether you speak with a direct rep or whether you do that online. And we continue to see that aperture opening. But the first phase of the game is how do you get in front of people. And I think we've made really good progress in the second half on that.

Operator

Let's take our next question from Josh Baer with Morgan Stanley.

Joshua Phillip Baer
Morgan Stanley, Research Division

Wanted to follow up on capabilities, Mark. Just wondering, like, what percent of your customer base do you think capabilities can apply to. I think that 1/3 of revenue is generated by only 6% of your customers. Just wondering where that number can go.

Mark P. Mader
President, CEO & Director

Yes. I'm -- I think I'm the eternal optimist on this one. I think this relates to every single person in our community. We have a wide portfolio. It has to do with being able to bring information and data into our system, with integrating our system, with visualizing our system, sharing our system. These are all things that virtually every person on our platform does. And I think when you reduce the cost of -- reduce the hurdle height on what it takes to experience and give people multiple options how to transact at a very low -- cost-effective way to start all the way up to really massive enterprise deployment, that penetration should go well into the double digits. And yes, I think over the next -- over a 5-year frame, I think 50 -- our median customers should be buying capability from us.

Joshua Phillip Baer
Morgan Stanley, Research Division

Really helpful. And then just wanted to dig in one more time on billings, Q3, Q4. Like you did show some nice upside and acceleration in Q3 off of an easier compare. The comp gets easier yet again in Q4, but the guidance implies a little bit of decel, like, even adjusting for the shift in the partners. So anything else to call out between Q3 and Q4? Or is kind of Q4 just embedding sort of the normal type of prudence in guidance?

Pete Godbole
CFO & Treasurer

So Josh, our approach this year has been very consistent. The performance every quarter, sort of irrespective of direction, hasn't materially changed our view of the year. Within a quarter, there's many reasons for variability. It's the timing of billings. It's the lumpiness of deals. It's seasonal variances, which tend to sort of offset over a full year term. We provided commentary based on actual sort of data we see in the quarter, but we've been very constant in our view of the year. And the way we see it is, given our performance over the past 2 quarters, we like the set up in Q4 to hit our 20% full year billings guide. So that's the way we see it.

Operator

We'll take our next question from Jake Roberge with William Blair.

Jacob Roberge
William Blair & Company L.L.C., Research Division

Mark, now that you've had those AI solutions in beta for a few months and in the hands of customers, what's been the early feedback on those? Are there any features that you're really seeing outsized demand for?

Mark P. Mader
President, CEO & Director

It's interesting. As I talk to peer CEOs who have launched AI features into the wild, I think what the market is seeing is that I think people are assigning higher value but lower frequency, lower usage to some of these things.

So when I look at a company saying, hey, we really assign value to the ability to generate configurations through advanced formulas or content generation, it's not something where we see this being hammered away at 10, 50, 100 times per day. We're seeing a configuration at our large domain sort of a configuration being created daily. So it's not like every single user is using us all day long, but it's actually quite encouraging because people are utilizing it consistently. And I think as the surface area grows, not only from creating a logic, but then having an assistant and having the ability to do insights and having the ability to find templates through an AI mechanism, I think that frequency will climb. But I would say pretty consistently across the peers that I speak with, a lot of investments are out there. And I think the frequency of usage is probably a little bit lower than people had anticipated. But when I look at the feedback we've received across favorable, neutral or negative, almost exclusively neutral or positive. And that's a really good leading indicator that tells us continue to invest in this area.

Heading into Q1 will be the first time where we have something available in our enterprise product, which can really be presented to a business user that they can associate you very cleanly. Like in the past, very often, enterprise plans tie out to security features and things that IT and governance really values, this will be the first foray into giving the business users something that they can get excited about. So again, super early days. I'm really pleased to see the neutral or positive feedback on this. And it's like it's the first inning of this game. But again, no -- definitely, the game is being pursued fully.

Jacob Roberge
William Blair & Company L.L.C., Research Division

Very helpful. And then I know a lot of the solutions are still in beta today and will obviously take some time to roll out. But just in terms of that time line, what do you view as the kind of the biggest product hurdles you have left before getting these solutions really GA and lives in the hands of customers and really starting that upsell motion?

Mark P. Mader
President, CEO & Director

I think especially in this arena, there are 2 factors. One, for many people, this is their first time interacting with an AI experience. So the importance of being correct, having -- giving the customer high confidence in that interaction, we care deeply about that. So as we think about leaving some of these things in the oven, if you will, for an extra month or 2, we think it's a really smart move. So we're getting the first 2 skills out at the -- before the end of Q4. And I think with each of these skills, it's important to really understand what the feedback and interaction with that skill is as opposed to doing a drag right and say, well, it worked well for the first 3 skills, let's just do that for the next 5. I think you really have to prosecute these independent of one another.

I think the other piece of this equation is what the posture of the buyer is. So when I look at some of our largest organizations, we have about 5,000 organizations in the Early Adopter Program, spanning tens of thousands of users. There are some organizations -- even with our approach to AI, which is unbelievably contained, like we don't ship data across the boundary. Even in those situations, the procurement teams and security teams are taking extra care to really understand what their internal policies are. So we've actually had some of our largest clients who are taking an überconservative approach say, we will wait until it's out of EAP, as they're getting their internal controls defined. And I think a lot of customers are being very prudent in that approach.

Operator

We'll take our next question from John DiFucci with Guggenheim.

John Stephen DiFucci
Guggenheim Securities, LLC, Research Division

I appreciate the prudence in guidance relative to the SMB expansion deterioration, Pete. But can you comment at all on the linearity in this quarter? And just give us any kind of read into how November and the beginning of December seem to be tracking.

Pete Godbole
CFO & Treasurer

Yes. So the first thing is we always have seasonality in the quarter. Our first month is the smallest compared to all 3 months. So as we went through the quarter, we did see, what I call, strength in the enterprise build up. And on the other side of that token, we did see the SMB expansions continue to be impacted by expansion pressures. We saw that trend in SMB expansion pressures continue into November. And on the enterprise side of it, November was per our expectations. So that's a little bit of the -- how the quarter played out.

John Stephen DiFucci
Guggenheim Securities, LLC, Research Division

Okay. That's helpful. And I guess, Mark, you mentioned the example in your prepared remarks on self-discovery of Advance features. Can you give us any metrics at all on how we should be thinking about that as far as traction moving forward?

Mark P. Mader
President, CEO & Director

I think we'll probably provide more texture on that as we give the painted picture for the upcoming year with our Q4 results. I mean right now, we're looking at this contributing nearly $1 million of bookings in the quarter. It's a great green shoot. We have really positive feedback in terms of how people are seeing these things. But I would say still pretty early innings. We're talking about hundreds of trials with conversions, again, accumulating to a little less than $1 million. But I mean, I think with another quarter under our belt, we'll feel more confident and be able to frame that in the year ahead -- for the year ahead.

Operator

We'll take our next question from Steve Enders with Citi.

Steven Lester Enders
Citigroup Inc., Research Division

I guess I want to ask about the international opportunity. I mean good to see the expansion into Australia for data residency. But how are you thinking about, I guess, kind of broader international initiatives? And is there going to be any kind of further go-to-market investments, marketing campaigns or partner build-out to kind of go after that opportunity?

Pete Godbole
CFO & Treasurer

Steve, this is Pete. So we think of -- international is a huge opportunity for us. It's 16% of our revenue and clearly, one of the areas we go after. But we think of it as a combination of all the changes we're making on the product with PLG and making it easier to have this product found, be able to expand, all those things. On the other side, we're investing in the go-to-market capability as well, combined with how customers that we deal with would want their data to be treated. So think of it as go-to-market with data centers. So we'll continue to invest in the international dimension. But just like our business here, it's going to take a while because customers with us start small and then they expand with us. So that's the trajectory you should see.

Steven Lester Enders
Citigroup Inc., Research Division

Okay. Perfect. That's helpful context. And then on the net retention, I think a little bit of a downtick at least for how you're thinking about for the fiscal year guide. I guess anything to call out? What's kind of the incremental difference there? And then, I guess, secondarily, how should we be thinking about where that could potentially bottom out at?

Pete Godbole
CFO & Treasurer

Yes. So Steve, when we think of the net dollar retention rate, generally, things were pretty much consistent between quarters. The only difference was the incremental SMB expansion, which is what you're seeing in the number we've laid out that's included in there. Now that's the first part. And the second part of what you asked for, what's the direction of this, we've got a big Q4 to go -- kind of go execute on, not just in terms of the total dollars we need to go through. But these green shoots that Mark talked about, we want to see how those play out. All of that, combined with the environment we see in Q4, will really inform what we think net dollar retention rate will look like in FY '25.

Operator

We'll take our next question from Pinjalim Bora with JPMorgan.

Pinjalim Bora
JPMorgan Chase & Co, Research Division

Congrats on the quarter. Mark, can I ask you, based on your conversations with customers, how do you think kind of the enterprise budgets are getting set for 2024 so far? Do you think purse strings might open up a bit or not so much?

Mark P. Mader
President, CEO & Director

I think it's largely a function of a provider's ability to connect to value and helping understand how they realize that value. I think -- and this goes back starting, in a really pronounced way, probably 3 years ago, where the higher we got in an organization and the bigger project we were talking with them about, the greater the need was to connect it to a prioritized pursuit that they have and be able to articulate how they could, within a certain time frame, realize that benefit. So when I think of where we're investing, not just from a product standpoint or a partner standpoint, but our articulation of how we deliver value, that is a direct tie into whether a purse string gets tighter or gets more loose. And so I think it's -- there are absolutely macro things that one needs to be aware of, but there are a whole litany of things that are within one's control that can help adjust that.

Pinjalim Bora
JPMorgan Chase & Co, Research Division

Understood. And one follow-up. How are you thinking about the sales capacity going into next year? Do you have the capacity for your plan? Do you expect to build capacity higher? And then how should we kind of think about that in context of potential margin improvement for next year?

Pete Godbole

CFO & Treasurer

So Pinjalim, this is Pete. So when you think of sales capacity and you think of needing sales capacity, we think of it as we have a pretty well-trained team of sales professionals we've hired. We've continued to invest in making them capable. That's the effort we've been on for several quarters. We see the first sort of -- the first shot as just the capacity and the productivity of those reps improving. That's the fundamental. Now will we add resources as we enhance the sales process and specific roles? We will. But I don't think it will be a huge drag on the margin. So as you look at FY '25 and you look at margins, we're not giving guidance on that yet. But the way I would describe it is overall margins, you should see those continue to improve. What slope or gradient that improvement takes will be a function of what growth expectations we have.

Operator

We'll take the next question from Taylor McGinnis with UBS.

Taylor Anne McGinnis
UBS Investment Bank, Research Division

Sorry to press on billings again. But just one follow-up to one of the questions that was asked earlier. So Pete, I think you mentioned that there could be quarter variability in timing, which I know we all appreciate in billings. But just given the strength in 3Q, did you see any renewals that pulled forward from 4Q into 3Q? And then maybe you can talk about like the bookings linearity you're seeing so far and if that's trending to be more back-end loaded and if that -- if there's any assumptions of that embedded in the guide.

Pete Godbole
CFO & Treasurer

So Taylor, there was nothing unusual in the quarter. Every quarter always has the normal pulls and pushes that happen, but nothing unusual this quarter that played out. I would go back and say we're seeing sort of bookings linearity being very consistent. There's no big trend to report out there. I'd say the only delta in bookings that we're seeing, which I called out a little bit, was on the SMB expansion side of it. So we're seeing some degradation that we had in Q3 on these expansions. And we're extending that trend forward into Q4, the assumption that, that trend continues.

Taylor Anne McGinnis
UBS Investment Bank, Research Division

Got it. That's really helpful. And one last one for me is -- so appreciate that there can be timing and quarterly variability into billings and sometimes that metric can be noisy. But I guess if you look on trailing 12 months, it's been growing somewhere in the low 20s. But ARR growth has been hanging in there in like the mid-20s, maybe low end of that. So just as we think about what the underlying business is doing and the momentum you guys are seeing, when we look forward, any thoughts on which is the better leading indicator or how we think about the difference between these 2 metrics?

Pete Godbole
CFO & Treasurer

I think when you think of billings in ARR, I think they both are different, but they both lead you to the same answer when you finish the year. They're pretty close, even if it's not an identical answer. So when I'm thinking about quarterly changes, I tend to rely more on ARR because it has a better sense of -- the timing elements are a little less pronounced. But when you think of the full year, they're both the same.

Operator

We'll take our next question from Keith Bachman with Bank of Montreal.

Keith Frances Bachman
BMO Capital Markets Equity Research

I wanted to ask 2 things that are related. And Pete, one is on micro and then a bigger picture question. On the micro, when you talk about SMB and you assume the degradation continues. But just to be clear, are you assuming it gets worse or just stays the same? And then for my follow-up question, I'll just ask them successfully. When you think about the gen AI opportunity, and I was out in Seattle for your customer event, seemed like a lot of excitement. Can it contribute to ARR growth and billings growth in what would be fiscal year-end in January '25? Do you see that actually being a contributing factor to potential growth? Or is it still, you think, going to be more discovery at that point? And Pete, anything else you want us to think about as we're building our models for FY '25 from a demand perspective, you already addressed the margins, but anything else you want us to keep in mind in advance of giving the formal guidance?

Pete Godbole
CFO & Treasurer

So Keith, I'll answer your questions as you asked them. First question you had was on SMB expansions, and we are assuming that there is a continued degradation in Q4. So it -- we have assumed it moderately worsens in Q4, taking that trend line. So that's the first part of it. The second part of your question on gen AI opportunity in the ARR assumptions in FY '25, it's a little early to call it out because we've got a few customers sitting in the EAP program. We've got good positive feedback. But I think after we get through another quarter of that feedback and as we get ready to put this into, what I call, GA, I think we'll start to get a little bit of a sense of what that looks like. So I think it's a little early to call out.

Keith Frances Bachman
BMO Capital Markets Equity Research

Okay. Anything else, Pete, that you want us to think about as we model the demand side in FY '25?

Pete Godbole
CFO & Treasurer

No, I think it's a little early to talk through '25, but nothing specific to call out at this time.

Operator

We'll take our next question from Terry Tillman with Truist.

Terrell Frederick Tillman
Truist Securities, Inc., Research Division

Nice job on the earnings in the quarter and the cash flow. One quick question I had, maybe Mark, first for you on self-discovery. I think you gave us a nugget there in terms of $1 million of bookings -- or billings and you called it like an early green shoot. Just given the work you're doing there and all the trials you're doing there initially, I mean, do you expect that though to ramp pretty notably from the $1 million level in 4Q? And how would that happen? Is it you just got to put more kind of seeds in the ground with more trials or you're working through the flow of the existing trials or maybe even add more capabilities in the self-discovery? And then I have a follow-up.

Mark P. Mader
President, CEO & Director

Yes. It's multifaceted, Terry. It's how do you not only serve up the capability to someone to utilize, but then how do you help prosecute that with the existing customer, right? It's moving it from being utilized to being transacted upon. And those are the motions that we're learning. So for these first deals that have closed, there are some things we're like, wow, we got that totally right. And we also found other things where we can further reduce the friction. And as we scale that from tens of thousands of people who have been exposed to it to well over 100,000 organizations, I would expect that friction to reduce. So I would be -- I will bet the over on things continuing to improve in this camp.

And I think the other piece is as we look at getting more and more of the portfolio in, we're going to have more at bats. So when an organization trials a capability, you have multiple opportunities to trial. It's not one organization, it's people within that organization. So even if you miss on the first opportunity with an individual, an organization, their neighbor can start trialing that capability. So it's a repeated opportunity to sell into an organization and to deliver value. That's one of the things that I really like about this opportunity.

Terrell Frederick Tillman
Truist Securities, Inc., Research Division

Got it. That's great to hear and the betting on the over. My follow-up question, I don't know if this is for you or Pete. But in terms of the services, the partner enablement, we see where some of the billings are going to go to partners, so it's explainable. I'm actually curious about sales enablement. So I'll build on this question. Over the last year, your $1 million customers have expanded quite a bit, 59, that's a lot. You've got customers paying you $4 million. I think you mentioned on the quarterly call, I think you got bigger ones than that. To me, that starts to seem interesting to a partner ecosystem, whether it's GSIs and others. So I would like to hear more about how sales enablement and influencing new businesses going with potential different types of partners.

Mark P. Mader
President, CEO & Director

Yes. Terry, I really see 2 very different elevations of partnering. And one is the broad base, the hundreds of partners who came to engage and wanted further clarity on what our intentions were to build our service line versus supporting them explicitly. That's a really exciting growth opportunity, both in the States as well as in countries which are partner-first oriented. I view that as very different than our go-to-market motion with the GSIs and many of whom are huge customers of ours.

How we go to market with them is both as a customer as well as getting Smartsheet utilized as they deliver their services to their clients. And so it's really a multipronged relationship where we serve them as a client. We team with them to get it introduced to their clients and then figuring out ways where they can build a book of business on the back of the Smartsheet platform to continue that relationship. That's really different than the next newest partner in a remote region which is targeting SMB, which is still valuable to them, but again, different motion. So we have different folks within our enterprise team, within our services team, which are targeting GSIs. And we have the broad-based partner program, which is catering to a much larger population.

Operator

And we'll take our next question from Alex Zukin with Wolfe Research.

Ethan Bruck
Wolfe Research, LLC

This is Ethan Bruck on for Alex Zukin. Congrats on the nice numbers. Kind of looking to 4Q as the biggest renewal period, I'm just curious if you're seeing any change in customer behavior, whether it's -- [let's go term it] smaller expansions. If gen AI is playing a little bit more into this up-tiering at renewal? Just I know we have the guide for the 116% for 4Q. Just curious how those conversations have started to play out in 4Q. And then I have one follow-up.

Pete Godbole
CFO & Treasurer

Ethan, I don't think those expansion conversations and those renewal conversations are going any differently. I think there's nothing unusual about it because gen AI and all of that is pretty early stage. Remember, it's in EAP with a limited number of customers. So that's not playing into the conversation yet because when you think of renewals and you think of all those things, it ties directly to what am I going to do with it? How is it going to come into my environment? And we're probably a little bit removed from that spot at the present time.

Ethan Bruck
Wolfe Research, LLC

Okay. I got you. And I guess, Pete, I know you're not guiding explicitly for next year. But I guess as we think about maybe a derisked or conservative way to think about next year, kind of help us frame numbers. Is it fair to think like, I guess, a derisked way for kind of building outlook is kind of below what is implied in the 4Q guidance?

Pete Godbole
CFO & Treasurer

I think, as I said before, it's a little early to call out next year just because Q4 is a big quarter. We've got to go execute it. I think we're all heads down trying to make sure we get the best outcome we can in Q4. That's one part of it. And the other part is clearly the fact that a lot of the things we've put into play are like, call it, just recently in the pan, if you will. So we've got to let those things play out, see what those do to be really able to put a perspective on what FY '25 looks like.

Operator

We'll take our next question from DJ Hynes with Canaccord.

David E. Hynes
Canaccord Genuity Corp., Research Division

Mark, as I think back to the IPO, I remember we used to talk about $5,000 as the threshold at which you would typically see customer spend start to inflect up. And maybe that's still true. But obviously, it's a much different and scaled business today. As you look into the mid-market or low enterprise, however you want to qualify it, is there a spend threshold in that cohort or any other signal that you see where spend typically starts to inflect up again? Or is it more linear progression higher up?

Mark P. Mader
President, CEO & Director

Yes. Isn't it interesting how our frame of reference changes from 5 years ago? I was talking to Pete yesterday about our average time to progress a customer from $0.5 million to $1 million. And again, so radically different from what we spoke about in the IPO. And I will stay away from pointing to one inflection point because there are so many phases to this game. We're seeing an acceleration of our moves from $0.5 million to $1 million. We're seeing, again, almost a double up of our $1 million customers. So I think whenever a company gets tempted to focus on an inflection point, it's also known as a missed opportunity when focusing at a higher inflection point.

So we're really trying to, as I just spoke to in terms of how we're viewing the partner ecosystem, recognize that there are multiple points at which you can exert energy or deliver value to a customer, which will compel them to move higher and faster. And don't view that as one, but view that as you have one at your very large enterprise, one at your emerging enterprise, one at your mid-major and one at your emerging customer and treat those all as important. So it's -- I think we've learned over the last 5 years, and I think we're trying to arrange our capital and our resources to go after those.

David E. Hynes
Canaccord Genuity Corp., Research Division

Yes. Okay. Makes sense. And then maybe a quick follow-up to Terry's question on the self-discovery. So you kind of alluded to -- in the answer to his question, that you would roll more capabilities into that motion. Just from a technical perspective, will it be easier to enable the next product for self-discovery now that you've already done a couple of them?

Mark P. Mader
President, CEO & Director

Yes, absolutely. And I think when we think about self-discovery, it's not simply the enablement of a feature, it's how do you give the people who are responsible for managing that environment the confidence, the visibility, the ability to control those elements. So we're creating these frameworks and these heads-up displays within an administration console so that the administrators and the budget holders can have very high confidence and very efficiently manage these situations. Once that framework is set, adding that next one, you don't have to rebuild that infrastructure. We're making -- we're building that in a modular way and building upon some of those early foundational investments.

Operator

We'll take our next question from Brent Thill with Jefferies.

Sang-Jin Byun
Jefferies LLC, Research Division

This is John Byun for Brent Thill. My first question was, as you've noticed, you had very good activity with the larger enterprises with your offering. I'm wondering if there are any notable drivers to call out? Anything to really help -- I don't know if -- any sort of unusual tailwinds from the ENGAGE conference?

Pete Godbole
CFO & Treasurer

So I think your question is about the strength in the enterprise. I think it's user-compelling nature of the solutions and the enablement we've done with the field in sort of building that out. These deals that happened in Q3 weren't a result of just what happened in Q3 or just what happened at ENGAGE. It's a series of plays to start with an opportunity, build a compelling value for the customer and then grow that opportunity over time and then find the right way to describe that value to close the transaction. So that's what we've seen. I don't think it's a special magic bullet, but just running through it.

Sang-Jin Byun
Jefferies LLC, Research Division

Good. That's helpful. And then in terms of follow-up, for -- in your guidance comments, you talked about enabling services to do more of the service work and having a $4 million impact on billings. Wondering, was that embedded already in the previous full year guide of 20% growth? Or was that kind of maybe a little bit newer development?

Pete Godbole
CFO & Treasurer

It's a newer development because we specifically called it out. And so it's -- think of that as incremental to prior guidance.

Operator

We'll take our next question from Rishi Jaluria with RBC Capital Markets.

Christopher Harrison Fountain
RBC Capital Markets, Research Division

This is Chris Fountain on for Rishi Jaluria. So you mentioned a really large expansion deal in the prepared remarks and that there's still further opportunity to do more with that organization. So I was just wondering, what features are they still evaluating? Or what really drives that next leg of expansion with a customer of that size?

Mark P. Mader
President, CEO & Director

The key driver there is we're serving a subset of their employee population. And one of the things that we've done in doing a multimillion-dollar, multiyear deal with them is not do a discounted by 90%, give away all the users, but really being thoughtful about how we grow with them over the years. And when I look at that customer and how they started with us as a $5,000 or $6,000 customer years ago and where they are today, we're seeing that as an upward trajectory for many years to come. But the key driver there is there are still very nice, large populations who are not yet utilizing the Smartsheet platform. And the nice thing is once you have flight ops and the product teams using it, you have these examples then you can show these adjacent teams. And when you're speaking the language of that carrier, the likelihood of them having higher confidence in following suit, I would argue, goes up. That's what we've seen in our other very large accounts.

Christopher Harrison Fountain
RBC Capital Markets, Research Division

That's helpful. And just a quick follow-up. Going back to the macro environment on the SMB side. Any industries to call out that have remained more pressured or on the flip side have started to show some green shoots?

Pete Godbole
CFO & Treasurer

I think when I think of the vertical focus, what we've seen is we've seen good strength in sort of, what I call, the retail, the education vertical and some of the gov. Obviously, gov is a pretty big quarter -- Q3 is a pretty big quarter for gov. And on the, what I call -- where we've seen some level of, what I call, pressure, it's come in energy, utilities, tech. Those are the vertical slices we've seen. But in general, across the SMB, we've seen really good logo growth all through the year. That stayed consistent. We have seen that pressure in SMB expansions. So just to make sure it's parsed out.

Operator

And that concludes today's presentation. I'd like to turn the call back over to Aaron Turner for any additional or closing remarks.

Aaron Turner
VP of Investor Relations & Treasurer

Great. Thanks, Lisa, and thanks, everyone, for joining us today. We'll speak with you again next quarter.

Operator
Thank you. That concludes today's presentation. Thank you for your participation. You may now disconnect.