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# Smartsheet Inc. NYSE:SMAR

*Earnings Call*

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# Call Participants

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# Presentation

**Operator**

Ladies and gentlemen, good afternoon, and thank you for standing by. My name is Abby, and I will be your conference operator today. At this time, I would like to welcome everyone to the Smartsheet First Quarter Fiscal 2025 Earnings Conference Call. [Operator Instructions]

Thank you. And I would now like to turn the conference over to Aaron Turner, Head of Investor Relations. You may begin.

**Aaron Turner**
*Vice President of Investor Relations & Treasury*

Great. Thank you, Abby. Good afternoon, and welcome, everyone, to Smartsheet's First Quarter of Fiscal Year 2025 Earnings Call. We will be discussing the results announced in our press release issued after the market close today.

With me today are Smartsheet's CEO, Mark Mader; and our CFO, Pete Godbole. Today's call is being webcast and will also be available for replay on our Investor Relations website at investors.smartsheet.com. There is a slide presentation that accompanies Pete's prepared remarks, which can be viewed in the Events section of our Investor Relations website.

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

Although we believe that the expectations reflected in the forward-looking statements are reasonable, our actual results may differ materially and/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 to 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.

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 first quarter earnings call for fiscal year 2025.

Q1 finished strong and reflected steady improvement as we move through the quarter. In the quarter, 53 customers expanded their Smartsheet ARR by more than $100,000. We now have 72 customers with ARR over $1 million, up 50% from Q1 last year. We ended the quarter with annualized recurring revenue of $1.056 billion and more than 14.7 million Smartsheet users.

In Q1, we expanded with customers, including Nestlé Purina, Ross Stores and Sephora, among others. We saw a significant expansion with the global media and entertainment company that has experienced growing demand for Smartsheet within its employee base.

This expansion is across multiple dimensions: the number of users, geographically from their core U.S. group to teams in Hong Kong, Singapore and other international markets; and usage across our breadth of premium capabilities. Over the last year, in order to manage the expanding scale of their workloads on Smartsheet, the company's use of Data Shuttle has doubled, and the use of Dynamic View to manage confidential information within the organization has tripled.

In EMEA, the technology and consumer electronics company signed a large 3-year enterprise deal. They were in need of a high-scale data asset management solution to replace a tool built by their agency partners that couldn't meet the growing demands of their business. They saw the value of Brandfolder within Smartsheet's workflows and the security flexibility and power of this integrated content platform. The company will store millions of brand assets for distribution to their subsidiaries around the world.

Going forward, they plan to build out a larger marketing and creative management ecosystem using Smartsheet. This past quarter, we saw a significant expansion that included an upgrade to Advanced Platinum at a major business process service provider. Because much of their work involves providing support to government agencies, our advanced security offering, Smartsheet Safeguard, was key to the deal.

Furthermore, Data Shuttle and DataMesh are crucial to maintaining consistency and standardization of data across their client projects, showcasing the power of Smartsheet's enterprise interoperability. The company sees their IT portfolio management solutions, which are built on Smartsheet, as a competitive advantage and are driving value by leveraging our premium capabilities.

In Q1, we also entered into a collaboration with KPMG, a long-standing Smartsheet customer, who wanted to leverage Smartsheet to enhance their client delivery experience. To support this objective, we teamed with KPMG to develop a globally available, standardized service delivery solution to track and manage value realization on strategic business transformation projects.

As businesses today are under more and more pressure than ever to deliver better, lasting results for stakeholders, Smartsheet enables KPMG and its clients to efficiently track and capture value with real-time collaboration and communication on complex projects. This solution enables Smartsheet to establish deeper engagement within new and existing enterprises as our platform is utilized by the customer going forward.

To unlock greater value for our customers and Smartsheet, I am pleased to share that on June 24, we will be rolling out a new pricing and packaging model. We anticipate it being modestly accretive in the near term and meaningfully accretive in the longer term. The new model provides broader access to Smartsheet features to more users and organizations who will be able to access the entire feature set offered by a plan while providing increased control and greater transparency to administrators.

In aggregate, the new model pairs a greater number of licensed users with a lower price per user on business and enterprise plans. New customers will onboard with this model starting on June 24, while existing annual customers will transition in calendar year 2025. We anticipate this new pricing and packaging model will be foundational for our long-term durable growth.

A key highlight of this change is shifting from a paid creator and free collaborator model in which editors, referred to as members, are licensed. Users external to an organization, referred to as guests, and internal viewers will continue to access Smartsheet at no cost.

The first to do so in the category, Smartsheet will launch provisional member access, which enables people within an organization for a limited time to create and contribute to workflows prior to being added to the subscription. This will drive increased virality by enabling organizations to make available to employees the full breadth of the platform in a low-friction manner while allowing system admins to manage their users more effectively.

While existing customers will transition to the new subscription model with their renewal dates in 2025, we anticipate demand from some organizations wanting to benefit from the new subscription model sooner, and we will accommodate them as appropriate. More information on the near- and long-term financial benefit to incremental bookings will be shared as we onboard new customers and as existing customers convert to the new model.

We continue to see meaningful adoption of our AI tools as they empower teams to unlock actionable insights from the data stored in the platforms. Since Smartsheet AI's GA launch in February, nearly half of our enterprise customer plans have used Smartsheet AI to generate business logic and content with simple, plain language prompts. In May, we released the next element of Smartsheet AI, analyze data, an AI tool that enables users to inquire and get insights from their data more quickly.

Rather than creating customer reports and dashboards, users can get results in seconds, reducing manual work associated with complex data analysis. This type of data analysis is a common need for customers, and Gen AI is significantly reducing complexity. Teams can easily track KPIs, make data-driven decisions and unblock work.

Our vision to bring applied AI to every business worker within the enterprise extends these capabilities to unlock insight across portfolios and align the right people with the right work. A Gen AI-powered build assistant will co-create powerful solutions to business challenges so any user can be a power user. FY '25 marks a pivotal year for our platform as we unveil our comprehensive modernization of Smartsheet's look and feel. This has been a multiyear investment.

In April 2024, we launched our Timeline View, which is generally available to all users on business and enterprise plans. Timeline View offers a modern approach to visualizing and interacting with information stored in Smartsheet. Users can organize work on a horizontal time line to track progress, communicate status and collaborate in real time with stakeholders in a highly visual way.

We're pleased to announce that in July, we will launch Board View, our all-new solution for agile work management. Board View is a Kanban solution that provides teams with superior visibility into the progress of work and organization of assets.

Looking further ahead, we'll launch our new table view by the fall of 2024. This user-friendly experience is designed to be the new hub for project, task and data management. Both Board and Table Views are the modern successors to our existing views. With an innovative, more intuitive UI and category-leading scalability and performance, we believe that time line, Board and Table Views will represent a huge win for customers.

On the client engagement front, 3 weeks ago, we hosted our inaugural EMEA ENGAGE Customer Conference in London, during which 2 customers played a very visible role in our keynote, the International Olympic Committee and Bayer Crop Sciences. As the International Olympic Committee shared in ENGAGE London, they are using Smartsheet to organize the 2024 Paris Summer Olympics, one of the world's most significant live events.

Smartsheet has become their single source of truth, streamlining workflows and enabling deeper connection between their teams. Cross-functional sharing is allowing them to onboard their suppliers to Smartsheet so they can use our platform to drive key work efforts.

Bayer Crop Sciences adopted Smartsheet to help unify global teams to one centralized work management platform. Smartsheet has enabled Bayer to enhance collaboration and break down silos by giving everyone real-time visibility into the data they need. We're proud to help enable Bayer's stated cultural shift towards shared ownership.

And in our ENGAGE press release, we highlighted Amazon as a customer. For over a decade, teams across Amazon have been using Smartsheet to manage their work at scale. For example, the AWS worldwide public sector team uses Smartsheet's business PMO capabilities to standardize processes and create a central source of information.

Previously, their data had been spread across several tools, making it difficult to measure the impact of the team's work. Team members now enter data in one place, and it automatically rolls up to Smartsheet dashboards that leaders have visibility into. Smartsheet is helping drive consistency, productivity and collaboration across the team. It's also creating better visibility into team members' workloads.

In closing, the continued evidence of success within the enterprise, with the convergence of new product innovations, the upcoming launch of our next-gen pricing and packaging model and a reinvigorated go-to-market strategy, solidifies our conviction around our capacity for long-term durable growth. Now let me turn the call over to Pete.

**Pete Godbole**
*CFO & Treasurer*

Thank you, Mark. Our enterprise segment continues to be the fastest-growing segment of our business and generated significant number of large transactions in the quarter. Regarding the change to our pricing structure that Mark mentioned, we expect a modest contribution this year given the timing of the launch and new customers being relatively small part of our quarterly bookings.

Earlier in the quarter, we also announced that we received board authorization for an initial $150 million share buyback. We expect to commence this buyback within the next few days and expect to significantly complete the share repurchases by the end of Q4 of fiscal year '25.

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

Turning now to our quarterly results. First quarter revenue came in at $263 million, up 20% year-over-year. Subscription revenue was $249.1 million, representing year-over-year growth of 21%. Services revenue was $13.9 million. Revenue from capabilities made up 35% of subscription revenue. Annualized recurring revenue, or ARR, grew 19% year-over-year in the first quarter to $1.056 billion.

Moving on to our reported metrics. The number of customers with ARR over $50,000 grew 20% year-over-year to 4,028. And the number of customers with ARR over $100,000 grew 26% year-over-year to 1,970. These customer segments now represent 67% and 54%, respectively, of total ARR. The percentage of our ARR coming from customers with ARR over $5,000 is at 92%.

Next, our domain average ARR grew 16% year-over-year to $9,906. We ended the quarter with a dollar-based net retention rate, inclusive of all our customers, of 114%. The full churn rate increased slightly due to the elevated churn rates in our smaller customer segments and rounds down to 4%.

Now turning back to the financials. Our total gross margin was 84%. Our Q1 subscription gross margin was 88%. Overall operating income in the quarter was $42.1 million or 16% of revenue. Free cash flow in the quarter was $45.7 million. We run the business with an efficiency mindset, managing capital deployment to functions, managing spans and levels and location of talent. This will be reflected in our updated profitability outlook.

Now let me move on to guidance. For the second quarter of FY '25, we expect revenue to be in the range of $273 million to $275 million, and non-GAAP operating income to be in the range of $38 million to $40 million. We expect non-GAAP net income per share to be $0.28 to $0.29 based on diluted weighted average shares outstanding of 141 million.

For the full fiscal year '25, we expect revenue of $1.116 billion to $1.121 billion, representing growth of 16% to 17%. We expect services to be around 5% of total revenue. We expect our non-GAAP operating income to be in the range of $157 million to $167 million, representing an operating margin of 14% to 15%, and non-GAAP net income per share to be $1.22 to $1.29 for the year based on 141 million diluted weighted average shares outstanding. We are raising our FY '25 ARR growth to be 14% to 14.5%.

Regarding seasonality, we continue to expect quarterly ARR growth rates to follow a similar trend as last year with higher growth rates at the beginning of the year. We also expect our FY '25 free cash flow to be $220 million, representing a free cash flow margin of 20%.

In closing, our Q1 performance and updated guidance show the power of our business model. This model is highly accretive, and we are rigorous in how we are managing the business, allowing us to significantly increase our margin guidance from what we guided just 3 months ago.

Supporting this profitability improvement is our continued strength in the enterprise. Our $1 million ARR customer segment is our fastest-growing segment. These customer engagements are highly sticky, given

the criticality of the workloads we are attaching to and reinforce Smartsheet's position as the enterprise work management leader.
Now let me turn the call over to the operator. Operator?

# Question and Answer

**Operator**

[Operator Instructions] And your first question comes from the line of John DiFucci with Guggenheim Securities.

**John Stephen DiFucci**
*Guggenheim Securities, LLC, Research Division*

So Mark and Pete, you put up better-than-expected numbers than you guided up, which kind of, normally, for software, that would be great, but that makes you stand out this quarter. So congrats on that. But when we try to tease out the new business signed in the quarter, the new ARR, it looks like the growth was about the same as last quarter relative to an easier comp, which, again, this is better than most of our coverage universe.

But how are you thinking about -- how should we think about the different parts of the market that you primarily sell into for the rest of this year? So Pete, you talked a little bit about large enterprise. You didn't mention much about -- said a little thing about this. The small business that you've talked about a little more about that in the past, and maybe even public sector, if you can throw that in there, that would be great.

**Pete Godbole**
*CFO & Treasurer*

John, this is Pete. In terms of your question, I'll talk about the segments and sort of how they performed. That's the genesis of your question. When I think of enterprise, enterprise were consistent and remains strong for us in Q1. So it kind of did well for us. On the SMB side of it, our performance followed a consistent sort of trend to prior quarters and played out consistent to what we had said in prior quarters as well. So we saw that as a carryforward in terms of the trends we have seen from the past.

**John Stephen DiFucci**
*Guggenheim Securities, LLC, Research Division*

Okay. Okay. And I know you've talked about -- well, this would be my second question, I guess. You talked in the past -- no, I'm not going to ask that. Let me ask this one. I'm sorry. Is the new pricing model, which sounds really interesting. Does that allow -- or is there sort of a skew in there that allows users to sort of access whatever you sell? Or is it still like à la carte, given some of the different offerings you have?

**Mark P. Mader**
*President, CEO & Director*

John, Mark here. So someone who is licensed in the new model has access to the full kit and caboodle. So they get every single AI component. They get every single content generation component. They can create dashboards, reports, what have you. And that's a really big difference from the previous model, which was you have the haves, the creators, the licensees and the editors who were limited.

And when I think about the maturity of our model, it really had to mature alongside to how our platform is maturing. I mean we have some really big things that customers like, which had been relegated to a minority of their user population. So this is a great leveling of capabilities, which should drive to higher virality, more people creating work on our platform. So we're really encouraged by that.

I think it also is quite interesting with a moderately lower price point, it should spell good performance in the SMB realm as well. So we see this lower price per user, combined with a higher user count, we believe will result in a higher average revenue per customer, but I think it will help the leading edge quite a bit.

**John Stephen DiFucci**
*Guggenheim Securities, LLC, Research Division*

That sounds really interesting. We'll see how that goes, but it sounds great.

**Mark P. Mader**
*President, CEO & Director*

John, the one piece also that you asked about in terms of the capabilities, while we are also refining and simplifying how capabilities are purchased, the notion of à la carte premium offerings as well as bundled premium offerings persist. So the heart of this new model is in our core licensing. Our portfolio and our suite and our cross-selling, that remains alive and well.

**Operator**

And your next question comes from the line of Scott Berg with Needham.

**Scott Randolph Berg**
*Needham & Company, LLC, Research Division*

I guess my first one is kind of a 2-parter. It's about the new pricing impact of packaging. Mark, I'm going to kind of quote you, you talked about being meaningfully accretive over time. How do we frame that, whether it's a time frame or magnitude?

And then, Pete, when you think about the pricing improvements that can start here in the back half of the year, was any of that contemplated in your prior guidance? Or is that contribution a new update to the guidance year-to-date?

**Pete Godbole**
*CFO & Treasurer*

I'll start, John, I'll let Mark on the other part of it. So first of all, our previous guidance did not contemplate this pricing model change. And the change we made in the ARR, which we lifted, was in part due to the fact that we're launching this for new customers, and we expect this to make a modest contribution this year. So that's kind of what's baked in.

**Mark P. Mader**
*President, CEO & Director*

And Scott, I think from a moderately or a meaningful accretive position on the new model, when I look at what we can do for our customers, and we've actually transitioned a number of our bigger customers to this new model already, so we have some sense of what the behavior is in this new frame. We're looking for things like what can we do as a business to deliver more value to customers and to what can we do that could double our licensed user base as quickly as possible.

And I think until you start to move those customers over, you will get -- you won't be able to position to say it will happen within 18 or 24 or 36 or 4 months. But what I can say is we have very high confidence that this will lead to much larger user communities that are licensed within our customers. So I feel very confident that this new model is more conforming also to what IT groups at large organizations expect. And the pairing of the lower price per user, I think, will be only helpful.

**Scott Randolph Berg**
*Needham & Company, LLC, Research Division*

Got it. Very helpful. And then from a follow-up perspective, Mark, you also talked about improvements throughout the quarter. So it's kind of a nice follow-up to John's question just a moment ago about kind of the demand of the business through different segments. If the SMB behavior is staying kind of consistent quarter-to-quarter. How should we view that comments on the improvement throughout the quarter?

**Mark P. Mader**
*President, CEO & Director*

Yes. I think the improvement stem from a couple of things. One, we had Max join us mid-quarter. I think his presence and his immediate impact on the team was favorable. So that was a benefit to us partially in

March and then in April. On the SMB side, as Pete said, we saw pretty consistent performance quarter-to-quarter.

I'm really looking forward to later this quarter when we get to introduce our new offering, and we get almost immediate signal on what happens at the leading edge. Now that's not going to result in a huge amount of bookings out of the gate, but we will have very, very quick feedback on whether the new model can draw more significantly with that lower segment.

**Operator**

And your next question comes from the line of Josh Baer with Morgan Stanley.

**Joshua Phillip Baer**
*Morgan Stanley, Research Division*

Congrats on the quarter. I wanted to stick on the new pricing and packaging. And just wondering what gives you confidence that the slightly lower or lower pricing, higher user count equation results in accretive nature. Any signals from as far as customer behavior or key assumptions that's aligned to that optimistic commentary? And then I have a follow-up.

**Mark P. Mader**
*President, CEO & Director*

Yes. I think some of the proof points come directly from customers who have already moved to the new model. So it's not a research project. It's actually what's happened in real life with some of these firms. Interestingly, as we test both at the super large organizations as well as the SMB, there has been a favorable reaction to both.

And when I think about sales productivity, one of the things that I'm very eager to do this year is how do you delete complexity from the business. And when I think about how someone responds when you say, Mark, what is the cost to license Smartsheet.

The first 2 things that I'm a house can't be, it depends. So the clarity in this new model is super, super high. And I think oftentimes, smaller organizations are actually less patient to learn, and they actually want a more clear model to immediately act on. So large organizations have sometimes longer decision cycles, where they can learn and understand more deeply. So I think this will be quite favorable at both ends of the spectrum.

**Joshua Phillip Baer**
*Morgan Stanley, Research Division*

Very clear. And then I just wanted to ask if you expect any changes to gross margins from these changes to pricing and packaging?

**Pete Godbole**
*CFO & Treasurer*

Josh, we do not We think we are going to maintain the gross margin levels we have because gross margins are a function of the total revenue at the top line, and we view that over time to be meaningfully accretive.

**Operator**

And your next question comes from the line of Terry Tillman with Truist Securities.

**Terrell Frederick Tillman**
*Truist Securities, Inc., Research Division*

Maybe the first question for you, Mark. I've actually asked this repeatedly over the years as the business has grown in scale. If we take a step back, there was a Magic Quadrant that came out. That seemed like an important milestone. You're talking about KPMG, which seems like a GSI partner potentially going forward. Are you starting to see -- and I don't want to put words in your mouth, so tell me if I'm just absolutely wrong on this.

Are you starting to see bigger enterprises, where they have been using different work management tools, start to take a step back? And whether it's an RFP or some sort of strategic vendor consolidation play maybe because of the macro, the more strategic CIO or just C-level purchasing or expansion? And then I had a follow-up.

**Mark P. Mader**
*President, CEO & Director*

We are. And it's really -- what I'm noting with customers is that there's a much higher fluency in the category. So the types of questions we're getting, the types of analysis we're doing around, not just what your core feature set, how does that feature set perform at scale, this notion of how to do plan management across a highly diversified set of business units, being able to apply corporate governance and policy. These are things that, 5 years ago, never even came up in conversation, and they're almost present every single time now.

So that -- so again, how much -- are we getting more yield today from our enterprise strength and features? That, I would say, yes. The median customer, I would say, is developing the highest of the high-end customers, everyone's asking these questions now. There's not a single customer that I've seen who is just willy-nilly approaching it on a feature set to mention. So that plays to our strength.

I would say their conformity and customers choosing to consolidate is still more grounded in future investment and where is the next allocation of capital going as opposed to we need to eliminate all other the tools from our environment. I think CIOs are recognizing that it is a diverse environment. There will be multiple tools, but where they're placing their bigger bets, they are doing that in fewer places.

**Terrell Frederick Tillman**
*Truist Securities, Inc., Research Division*

And I guess, Pete, just last quarter, you kind of split the NRR dynamics across enterprise and SMB. I think you had said 120% for enterprise and then basically 0% expansion or 100% NRR for SMB. Could you give an update on how that played out in 1Q between the 2 businesses? And is there any updated thoughts on how they individually would play out the rest of the year?

**Pete Godbole**
*CFO & Treasurer*

So the enterprise net dollar retention rate stayed over 120%. And from the SMB side of it, it dropped a couple of points, still staying over 100%. So kind of that's how it played out. And when you asked about the outlook, the way I would describe it is, if you leave this year out of it and you extend it into when our customers go on to the new pricing and packaging model, I view that as an opportunity to turn that NDRR in the future as we start to gain more value from customers and they gain more value from our platform.

**Operator**

And your next question comes from the line of Rishi Jaluria with RBC Capital Markets.

**Rishi Nitya Jaluria**
*RBC Capital Markets, Research Division*

I wanted to start going back to the changes in pricing and packaging, totally appreciate the potential upside from here. I guess, historically, when we've seen companies make changes to pricing and packaging, there can sometimes be disruption in the near term. Can you maybe walk us through what is your plan to minimize or mitigate any potential disruption from that? And then I've got a quick follow-up.

**Mark P. Mader**
*President, CEO & Director*

Yes. I think we were really thoughtful about the timing. And we said, well, straight out of the gate, new customers onboarding will conform to the new model. And as you heard, we're really not expecting our existing customers to have to move until the renewal date in 2025. That gives significant time for them to understand the model plan, if there's a budgeting need, they can do that, engage with us in multiyear conversations.

Time is really important. In talking to my peers, who have undergone pricing changes, but one thing they made a very big point of was when you release new pricing to new customers, recognize that every single existing customer will be asking about the impact to them, even if they have to move immediately.

So when we launched on the 24th very good education and communication to the new prospects and customers and very good and robust communications to the existing base. People want to understand what the model and the value is, not just what the price difference is.

So a lot of that is communication can do volumes for your efficacy and bringing people across. And then like be close to your customer. We have a big engaged account management and field sales team. We're going to be right there with our customers. Pete, what would you add?

**Pete Godbole**
*CFO & Treasurer*

I would add that the other part is customers have -- when you think of pricing changes and model changes, customers need flexibility in how they manage. So when you think of how that flexibility comes about, customers get to classify their existing population into members, guests or viewers, and that flexibility and consultative nature with us really makes this model less, what I call it, attuned to any variability.

**Rishi Nitya Jaluria**
*RBC Capital Markets, Research Division*

Got it. That's really helpful. And then, Pete, for you, Look, I recognize we're shifting to ARR as a metric instead of billings. Maybe can you just help us risk the delta between billings and ARR this quarter? It was a pretty big range. Maybe help us understand what went on the quarter to explain that delta? And just how to think about the delta between the two going forward?

**Pete Godbole**
*CFO & Treasurer*

So Rishi, the -- what everyone is aiming to get at when you think of a metric like ARR or billings is estimated implied bookings. And what we've experienced in the past was that billings is impacted by prorated bookings and the associated renewal dates that go with it. A much better metric is ARR, which is why we shifted to providing guidance on ARR. And this quarter is a great example of that. When you look at the bookings that came this quarter from those which had proration associated with previous -- with future quarters, that was a bigger effect. That's why the billings number looked like a different growth rate, and that's why the true measure is ARR, which we've guided to and reported.

**Operator**

And your next question comes from the line of Alex Zukin with Wolfe Research.

**Aleksandr J. Zukin**
*Wolfe Research, LLC*

And I'll kind of go down to some of the same themes that we've been -- that the prior questions were on. I guess, if we think about the linearity of bookings in the quarter, can you maybe just talk about how it looked themselves? And if that was the same or different, just given all the kind of macro noise we hear? And then was the headwind more from elevated SMB churn or lack of seat expansion? And again, how do we model those net new ARR trends as we go through the year? Kind of, is it similar to last year? Or is it even more seasonal? And then I got a quick follow-up.

**Pete Godbole**
*CFO & Treasurer*

No problem. So Alex, we started February slow, and it's sort of traditionally enterprise pipeline building time. But as we went through the quarter, we saw our momentum really shift up, and we finished April strong with a solid Q1. That's the way I'd represent the full quarter.

Now in terms of what we saw in the quarter, I think I stated before that the SMB trends we saw were fairly similar to what we have seen in the past. And there was -- the enterprise stayed fairly consistent, strong. We're reporting all the large number of deals we did and the number of additions to the $100,000 cohort. So strong on all fronts. And then the trend in ARR that we expect is we expect it to trend down as we go through the year, and that's what we noted in the prepared remarks we went through.

**Aleksandr J. Zukin**
*Wolfe Research, LLC*

And what about net new ARR? Sorry, just a clarification.

**Pete Godbole**
*CFO & Treasurer*

Yes, net new ARR, essentially, was, if you think of it, was up. And if you think of how that played out, when I think of net new ARR, you're thinking of it as bookings. So essentially, if you think of bookings, it was a good quarter for us on bookings.

**Aleksandr J. Zukin**
*Wolfe Research, LLC*

Got it. Okay. And then just maybe my follow-up for Mark. I think if we look at some older disclosures, historically, I think like 80% of the users have been unpaid. So as we look at the contribution going forward, what does success look like over the next year, 2 years and changing that kind of user-free versus pay mix? And given the modest impact on this year, how should we think about the NRR dynamics over time as we kind of go through this model transition?

**Mark P. Mader**
*President, CEO & Director*

Yes. I think we're going to learn a lot. As that first big group of customers goes through and does that management that Pete spoke to a second ago about classifying their people as members, guests and viewers, we will really be able to quantify that well. We do have very good visibility into how many millions of people are on our platform monthly, making it as new contributing. When the new model gets released, again, those admins will need to go through that assessment and see who's in, who's out.

The good thing is that, in the old model, where that licensing decision hinged 100% on creation, it's much more straightforward now. If you are contributing to a process and you're within an organization, you are licensed. And in the past, it was much more muddled. So I would expect our ability to drive a much larger population of licensees to play out. I actually don't see a scenario in which we drive fewer members in the future.

The one wildcard potential upside to us is, of those incremental people who used to be editors, who didn't have access to the full portfolio, who are now on fully, to what degree do they have an appetite for buying premium capabilities? So as the population of users grows, what is the added benefit to the rest of our suite of offerings? And that's something that, again, we will comment on as the quarters play out.

**Pete Godbole**
*CFO & Treasurer*

And Alex, to your previous question, just to sort of add a little more texture to it. You asked about implied ARR growth. As we go through the year, we're going to see that growth rate improve as we progress through the quarters.

**Operator**

And your next question comes from the line of George Iwanyc with Oppenheimer.

**George Michael Iwanyc**
*Oppenheimer & Co. Inc., Research Division*

Mark, maybe starting with the EMEA ENGAGE conference. Can you give us an update on what you're hearing from customers there and kind of the overall pipeline internationally?

**Mark P. Mader**
*President, CEO & Director*

Yes. Europe was strong for us in Q1. We have roughly 500 customers, a lot of large caps in attendance. And there remains very high curiosity around the modernization of our application. They're very curious about how we are applying AI. So on the floor where we had our demo booths, I would say the interest level in AI remains very high. We just released, I think, our fourth scale. Half of our enterprise customers have now used AI, and it's all about activation. You're getting people comfortable with it.

So high levels of curiosity. It was our first conference outside the U.S. And as registrations were happening, I was really curious to see how it will play out. The fact that 500 people from all over -- 500 companies from all over Europe showed up was really, really positive. Pete, anything to add in terms of the strength of Europe that we saw in Q1?

**Pete Godbole**
*CFO & Treasurer*

Yes, I think, George, Europe was pretty strong for us this quarter. It was -- you could see the market really starting to pick up on collaborative work management in general. And I think the conference itself produced a high degree of interest, which is manifesting itself in both short-term pipe and long-term interest.

**George Michael Iwanyc**
*Oppenheimer & Co. Inc., Research Division*

Great. And then maybe staying on the AI theme, but with the packaging. As enterprises start to adopt this, how are you including in introducing those AI capabilities with the new packaging?

**Mark P. Mader**
*President, CEO & Director*

Well, one of the big push to the new model is everyone who is a member has access to AI. So again, there's no longer this split between the haves and the have-nots. As we look at how we activate it, the next level of innovation we're doing is not only on the building of new skills, but also how do you introduce the scale at the time that the person may benefit from the skill, whether you're adding business logic through formulas, whether you're looking to generate content in a grid, whether they're looking to analyze data.

What I found in speaking to users is that there is a high, high comfort, and there's a high degree of muscle memory, to which people are really, really latched on to. So you have to go through pretty direct means to introduce them to a new way of working.

When people see it, they love it. But even though we have 50% penetration with our enterprise customers, we are still looking to drive that user penetration up. And it's a pretty consistent theme from what I'm hearing across app companies today.

Pretty good penetration on the company side. Everyone is hungrier for more user engagement. I think a lot of that is education. And how we nudge people in the app, how we educate people in the app, I think will yield quite well in the year to come.

**Operator**

And your next question comes from the line of Michael Berg with Wells Fargo.

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

Congrats on the quarter. I wanted to ask about the sequential improvement in a slightly different manner than asked earlier in the call. Any notable changes in the broader macro or buying behaviors, willingness to open up budgets? Any particular reason that stand out as to why your solution platform has been procured -- what appears to be a healthier rate relative to some other names across software? And then I got a quick follow-up.

**Pete Godbole**
*CFO & Treasurer*

So I think, Michael, it fundamentally comes down to how customers realize value from our platform. When you think of our -- the things Mark mentioned in terms of sophisticated workloads at scale, in a lot of cases, those are things customers need. And we saw that reflected in the number of enterprise customers who moved to over $100,000, number of million-dollar customers. And I think, in that way, companies are just different in how they are perceived by customers and how they are valued by customers. So that's what we saw play out for us in Q1.

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

Got it. And then a quick follow-up on margins. Obviously, you had some very nice margin performance and improvement in the guidance for the year. Outside of topline performance, anything you can think of that's driving the incremental progress there? Or is it just the enterprise unit economics flowing through the model over time?

**Pete Godbole**
*CFO & Treasurer*

I think the fundamental nature of our model is it's highly accretive. But what we've also done is we've -- Mark and I have taken a really close look at how we operate and run the business, which means everything in the business, which roles we hire, which locations we hire them in. And sort of when you look at it and you say, where do I really want to deploy my capital? And so we've been very thoughtful and sort of focused on that. We've seen that bleed itself through in terms of our margin guide.

**Operator**

And your next question comes from the line of Brent Thill with Jefferies.

**Brent John Thill**
*Jefferies LLC, Research Division*

Mark, a good April and a good Europe or not, consistent with most of the industry. And I'm just curious what you think really resonated in Q1. Is it the category? Was it your execution? Did something trigger in the product line? What do you think kind of helped you fly through this headwind that others are really getting bogged down by?

**Mark P. Mader**
*President, CEO & Director*

I think customers and prospects feel when a team is confident. And while we do have quite a few transactions that happen digitally without human interaction, a lot of our enterprises do engage with our team. And I think when the team saw the Timeline View come out and be able to show something that was modern, beautiful, fast, valuable -- perceived as valuable to customers, and they're like, okay, yes, 2 more of these things coming. I got one coming in July and one coming in the fall, there's a little bit of pep in the step.

And I think you combine that with Max, who came in, who landed immediately and effectively, the field team is feeling good right now. And that builds on itself. I talked to our customers at our ENGAGE conference around convergence. I talked about the convergence modernization, the convergence around AI, the convergence around new ways to engage with our company. And unfortunately, you don't get that convergence every year of operations. This happens to be one of the years where it is coming together.

And I think we're going to -- I think customers are sensing that. For a long time, Brent, and you know this, we've talked about futures. But we've talked about them as I trust as they're coming. And the fact that they're now hitting is something where customers are looking for evidence, and I think we're able to show that now.

**Brent John Thill**
*Jefferies LLC, Research Division*

Okay. Pete, are we going to have to wait till June 24? Or do we get any sneak peek here in terms of what this is going to look like?

**Pete Godbole**
*CFO & Treasurer*

No, I think you're going to see it on June 24.

**Operator**

And your next question comes from the line of Steve Enders with Citi.

**George Michael Kurosawa**
*Citigroup Inc., Research Division*

This is George Kurosawa on for Steve. Mark, a few times, you've alluded here to the impact that Max has had on the go-to-market or -- which I think is really impressive given how new he is in the organization. Maybe if you could just double-click on kind of what you've seen him bring to the table and what have you got him focused on for the rest of the year?

**Mark P. Mader**
*President, CEO & Director*

Yes. I think I would say 3 things have really landed quickly. The first is a hyper focus on use cases and how we're getting a fresh set of eyes on why customers are with us, what they're asking for, what our pipeline composition is and aligning these use cases that we're looking to market with how we're deploying our marketing capital, with how we're enabling the team. And then also, with that understanding, having a point of view on what this new pricing and packaging model looks like.

And it's great that we had a few months with Max before we launched those, for him to get ramped, engaged and speaking to customers before having to make that decision cold. So that use case orientation is something that is very, very experience-driven from his background, combined with being ramped and participating in this pricing and packaging modeling.

And then I would describe the last piece is almost like this up-leveling of enterprise mindset, whether you talk about field enablement, multiyear models, ELAs, value realization journeys, I mean you can go on and on. These are the things that we've prosecuted really, really extensively during the interview process, and he has it. And the team -- I think the team is responding well.

**George Michael Kurosawa**
*Citigroup Inc., Research Division*

That's great to hear. And then a quick follow-up on capital allocation. I think the buyback plan makes a lot of sense given how strong the free cash flow generation has been. But the $150 million, it's a pretty significant number. Most of the annual free cash flow kind of getting plowed back into in the buybacks. So maybe if you could just talk about how you guys kind of triangulated in on sizing that. And why not kind of push a little bit more into reinvesting the growth?

**Pete Godbole**
*CFO & Treasurer*

Yes. So we made it with a very disciplined capital allocation decisions to start with. And when we looked at the stock price and how undervalued the stock was, we took that as one input to the equation. We balanced that against having a healthy balance sheet for our customers and then being able to trade off against opportunities we would have in M&A and the ability to invest in M&A. So a combination of those elements led to the $150 million initial stock buyback. We don't think we've shortchanged ourselves on opportunities to invest by making this $150 million buyback.

**Operator**

And your next question comes from the line of Pinjalim Bora with JPMorgan.

**Pinjalim Bora**
*JPMorgan Chase & Co, Research Division*

Congrats on the quarter. Nice to see the good results. Just a number of clarifications on the pricing and packaging. Could you -- are you completely moving away from the free collaborators is what I understand from what I've heard so far? Any way to understand kind of the pace of early customers that you are basing the price elasticity comments you made earlier in the call? And within the existing customers or the early customers, I should say, that have moved to this model, what are you seeing from a conversion point of view for those collaborators?

**Mark P. Mader**
*President, CEO & Director*

So to your first question, the free collaboration is still alive and well in our model. We have this notion of guests. So when an organization shares outside of their domain, all of that access is that at no cost. If someone creates a dashboard for corporate visibility and corporate communication sharing, all of the thousands of people within the company only view it do so at no cost. Those are huge populations of people, which are also really important to establishing touch points and long-term virality. Those remain consistent with what we have today.

In terms of the conversion rate you speak to around collaborators, there really is no notion anymore of a conversion rate from a contributor, an editor to paid because they are paid now. So if you engage in our product and you work within an organization and you're editing, you're commenting, you're adding to it, you are paid.

So the second you engage, and the second you go through this provisional period, you are on the license. So it's -- there's no longer this decision by an administrator on, "Well, they're editing and they're contributing, but do they really need to create?" That decision is now gone. But that user population of free that is cross-company lines is still very, very present and very important to us.

And Pete, did you want to add? Sorry? Go ahead. Why don't you ask the second follow-up question?

**Pinjalim Bora**
*JPMorgan Chase & Co, Research Division*

No, I was just -- I'm trying to understand if the customer -- your existing customer or early customer who has moved to this plan had free collaborators who were also editing, those are moving to paid now, is my understanding. So I'm trying to think if you had that customer had 10, did all of those 10 -- are you seeing all of those 10 kind of move into paid with this new model? Or is it 5% of that, 30% of that? That's what I was trying to get at in terms of conversion.

**Mark P. Mader**
*President, CEO & Director*

Yes. And we haven't disclosed that conversion rate, I think, especially at mega scale. At scale, you also have, what I would call, bespoke user pricing, right? You don't just work off of the MSRP. So I would say, the customers that we've gotten reads off are the ones that are deployed. In most cases, those are large enterprise. We have done testing and research and gotten feedback on all sorts of models all up and down the segments. But in terms of the ones that I was referring to early, those were some of our larger enterprise customers who had already come over.

**Operator**

And your next question comes from the line of DJ Hynes with Canaccord Genuity.

**David E. Hynes**
*Canaccord Genuity Corp., Research Division*

So Mark, you're going to be taking a lot of folks that were previously collaborators, and you're going to give them full access to create and contribute on the platform. How do you, at the same time, educate what were passive users in the past on what's possible, how to use the platform as a creator, get them engaged, help them figure out how to create value. I mean that seems like a really important part of driving incremental long-term value from the new pricing model. So would love any color on how you're thinking about that.

**Mark P. Mader**
*President, CEO & Director*

Yes. I think it's -- as I talked about the importance of driving not only organization penetration or percentage adoption with AI, but actually the user counts. I think when we look -- when we think of R&D, we think of it not only as a discrete feature development, building something new or improving the capability of something, but it's more how do you get somebody engaged in that. We've made a number of changes, for example, around what our sharing model looks like, the actual way in which people know things can be shared in our product. It's not introducing sharing. It's making sharing better and more obvious.

And we've seen really interesting uptick on virality just by those experiential changes. So much like we did with our self-discovery on Data Shuttle and Dynamic View 3 quarters ago. We didn't just silently launch them. When you go and you do an import in Smartsheet now, you are presented with education at the right time on here's what this new fancy thing can do, do you want to try it?

And that is much, much more powerful than silently sending someone an e-mail and say, "Hey, we did this great new thing, and we're going to trust that you really care about our e-mail and then you're going to go explore it," presented to them in the moment.

So this notion of nudging, stuff like when we'll launch Board View soon, you have many, many users who have been using Card View for a long time, the predecessor to this modern view. So one of the things you do is you launch them into new one, and with the easy ability to go back to the Card View, if they wish to.

These are the types of moves you make when you're trying to get people exposed to things and don't rely on good intent and how wonderful your documentation is to pull them through. It's a whole area of development that we built a really interesting research team and design team, and our engineers are very much cognizant of it.

**David E. Hynes**
*Canaccord Genuity Corp., Research Division*

Yes. Okay. Makes sense. And then, Pete, a follow-up for you. So we have pretty limited history with the relationship between ARR growth and net revenue retention. But over the last 4 quarters, as we do have, ARR growth has outpaced NRR by about 5 to 6 points pretty consistently. How would you expect that ratio to trend and look over the course of this year?

**Pete Godbole**
*CFO & Treasurer*

I think the ratio, in terms of how that plays out, you're going to find yourself looking at the relationship being the same. It's going to be -- there's going to be a delta between ARR growth and the NDRR that manifests itself. But one will be lower than the other because you've got some amount of new coming into the ARR growth.

**David E. Hynes**
*Canaccord Genuity Corp., Research Division*

Right. So you think it should be pretty consistent, that 5- to 6-point range?

**Pete Godbole**
*CFO & Treasurer*

It should be.

**Operator**

And your next question comes from the line of Jackson Ader with KeyBanc.

**Kyle Edward Diehl**
*KeyBanc Capital Markets Inc., Research Division*

This is Kyle Diehl on for Jackson Ader. Just maybe 2 quick ones for us. Can you give us some color on where we stand in terms of sales capacity for this year? And if there are any head count plans that you guys have for the remainder of the year, particularly given it looks like we're ahead of our initial profitability targets here?

And then, Pete, I think you had mentioned that capabilities were 35% of subscription revenue this quarter. So that seems to continue to tick up. In terms of the stand-alone purchases that are being made, where are the outperformers and where are you guys seeing success?

**Pete Godbole**
*CFO & Treasurer*

So the first part of your question is we're staying on point on overall sales capacity. But what we are doing is we're weighting our sales capacity a little more heavily towards the enterprise segment. We're adding capacity there. So we're sort of rebalancing where we've applied the sales capacity capital, if you will.

The second part of your question that you've asked was on capabilities and where we are seeing the bright spots. I think the capabilities we've seen very strong performance in advance and capabilities in general. And the capabilities, in general, cut across the same sort of capabilities, which customers love and appreciate. The Control Center, Dynamic View, Data Shuttle remain the top names in the capabilities stars, if you will.

**Operator**

And we have time for one more question. Our final question will come from Taylor McGinnis with UBS.

**Taylor Anne McGinnis**
*UBS Investment Bank, Research Division*

Just one for me, which is when we look at the revenue and ARR guidance, can you perhaps quantify or tell us how much of the uptick was driven by this pricing and packaging change? And understanding that the macro is still tough out there, you don't have many software companies racing in light of the environment. But just curious, is there anything in the quarter that may be downticked or is a little bit softer that's making more [ cost-outs ] for the year? Or is that just mostly conservatism?

**Pete Godbole**
*CFO & Treasurer*

So I'll break down your question into the revenue guide first. So we raised the revenue guide by $3 million at the midpoint, and that was a carryforward. Because, essentially, what we see is an environment where we have some level of understanding of how the rest of the year will roll out, and that's what we feel is prudent -- would be the prudent thing to do.

Now the second part in terms of what we did with ARR, that's a combination of 2 things. The first part is the solid performance we had in Q1 and some measure of it being the implication of the new pricing and packaging model as applied to new customers and prospects, which is where we're starting.

**Operator**

And ladies and gentlemen, that concludes our question-and-answer session. I will now turn the call back to Mr. Aaron Turner for closing remarks.

**Aaron Turner**
*Vice President of Investor Relations & Treasury*

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

**Operator**
Ladies and gentlemen, this concludes today's call, and we thank you for your participation. You may now disconnect.