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Asana, Inc.

Second Quarter Fiscal Year 2023 Earnings Call

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PRESENTATION

Operator

Good afternoon and thank you for attending today's Asana Second Quarter Fiscal Year 2023 Earnings Call. My name is Austin and I will be your moderator for today.

I would now like to pass the conference over to our host, Catherine Buan. Catherine, you may proceed.

Catherine Buan

Good afternoon and thank you for joining us on today's conference call to discuss the financial results of Asana's second quarter Fiscal 2023.

With me on today's call are Dustin Moskovitz, Asana's Co-Founder and CEO; Anne Raimondi, our Chief Operating Officer and Head of Business; and Tim Wan, our Chief Financial Officer.

Today's call will include forward-looking statements, including statements regarding our expectations regarding free cash flow, our financial outlook, strategic plans, our market position, and growth opportunities. Forward-looking-statements involve risks, uncertainties, and assumptions that may cause our actual results to be materially different from those expressed or implied by the forward-looking statements. Please refer to our filings with the SEC, including our most recent annual report on Form 10-K and quarterly report on Form 10-Q for additional information on risks, uncertainties, and assumptions that may cause actual results to differ materially from those set forth in such statements.

In addition, during today's call, we will discuss non-GAAP financial measures. These non-GAAP financial measures are in addition to and not a substitute for or superior to measures of financial performance prepared in accordance with GAAP. The reconciliation between GAAP and non-GAAP financial measures and a discussion of the limitations of using non-GAAP measures versus their closest GAAP equivalents are available in our earnings release which is posted on our Investor Relations website at investors.asana.com.

Lastly, in service of investors and customers who need ESG data for reporting and RSP requirements for our many enterprise deals, we publish comprehensive and easy to use disclosures around ESG on our IR website. You will find downloadable SASB index data and climate data along with our annual ESG report.

With that, I'd like to turn the call over to Dustin.

Dustin Moskovitz

Thank you, Catherine, and thank you to everyone for joining us on the call today.

Asana's Q2 results beat expectations on both the top line and the bottom line. Revenue grew 51% year-over-year and beat our guidance by 6%, driven by strength in the U.S and the Enterprise businesses. We had 462 customers spending $100,000 or more in annualized GAAP revenue and are seeing broad adoption at some of the world's leading enterprises.

Dollar-based net retention rate remained strong overall. Across our customers spending $100,000 or more, dollar-based net retention rate is well over 145%, illustrating that we're not only winning large deals, but these large deals have the highest expansion rate among our customer cohorts. In particular, our Enterprise business is growing more rapidly than our overall growth rate and thus becoming a larger and larger portion of our business over time.

We remain committed to building the most effective, most scalable work management platform capable of serving organizations of all sizes around the world. Evidence of our progress includes our continued success with the industry's largest deployments, plus our end user adoption rate, now at over 2.5 million paid seats.

As a result, we're raising our top line guidance for Fiscal Year 2023 to $544 million to $547 million, representing a growth rate of 44% to 45%. We expect currency headwinds to continue to be a significant factor this year. Excluding the currency impact, our guidance would represent 46% to 47% growth.

We're winning across important industries and with iconic enterprise leaders, and where we have the greatest leverage, we're focusing, growing, and investing to win. The growth we've seen over the last several quarters is being driven by both the trends we see in the market and the way our product strategy delivers on what companies need as a result.

Companies are investing in solutions that offer time to value, help them do more with their technology stack, and better aligns their employees around the work that matters, and the bigger the company, the more true this becomes.

We've recently performed an analysis of how our Enterprise customers get value from Asana and found that the vast majority are using it for cross-functional collaboration. I share this with you because this is truly how we're most differentiated from other work management software. These tools make it easy to track single projects for single teams.

In contrast, more than half of all work tracked in Asana is cross-functional in nature. This number jumps to over 60% for customers spending more than $100,000, and we see an even higher proportion of this cross-functional collaboration in the features we've built as we've moved upmarket, including goals and portfolios.

Asana also creates shared clarity and accountability at every level. Leaders have to know how the work being done delivers on business priorities. Asana uniquely does this, because the Work Graph creates a map for all the work in your organization, including where it stands, the people responsible, and how it connects all the way up to Company-wide goals. That's incredibly powerful, especially when it's critical to keep a large team in sync around changing plans.

The Asana platform serves as a critical hub for your most important business applications, helping customers make better use of existing investments and giving employees a single place to track requests across email, chat, documents, and other frequently used applications.

Asana's built on the foundation of safety, security, and performance at scale that global enterprises expect. Companies are continuing to recognize Asana as an essential partner for solving modern work challenges. This is why we continue to improve on and expand the functionalities required by the largest and most complex organizations.

We have a strong Fiscal Year 2023 product cycle, and on October 11, we'll be giving investors a preview of how we'll be delivering even more value in three big ways that help companies successfully execute on their top priorities.

First, by helping decision-makers quickly understand the health of strategic work across the organization. Asana Goals is already the number one product according to the G2 Enterprise Objectives and Key Results software market, and we're about to make it even better. Customers will soon be able to use the Salesforce for Goals integration, our first out-of-the-box integration with Asana Goals.

When work happens in Salesforce, the progress of linked goals in Asana will be automatically updated, making it easier to monitor impact and make informed decisions. Leaders will also be able to get a bird's-eye view of goals in Universal Reporting, including the ability to report, filter, and group Goals metadata.

We're also rolling out all-new integrations from Asana partners that help our customers improve the productivity and quality of work across their applications. New Rules integrations with Gmail, PagerDuty, Twilio, and more automate work across tools to help teams stay connected and remove bottlenecks.

Context switching between tools makes it hard for individuals to stay focused on the work itself and oftentimes causes that work to fall through the cracks. With the new Asana for Workplace integration with Meta, teams can create Asana tasks, receive project notifications, and see linked previews for important status or milestone updates right from Workplace.

A new independent report by Nucleus found that Asana can cut the time it takes to complete a project by as much as 60% and increase project loads by up to 25% without adding staff. The study also found that users of Asana reduce errors by as much as 90% when automating complex processes.

The third thing to note about our product roadmap this fall is that we're further elevating security, privacy, and compliance. Asana now offers data residency options and flexibility in Australia and Japan to meet customers' needs, in addition to EMEA.

We're also supporting global organizations with enhanced mobile data controls so admins can ensure data stays secure with biometric authentication and restricted attachment sharing, while empowering employees to work from the Asana app anywhere.

For companies that store, consume, and transmit personal health information for different business processes, Asana plans to introduce a HIPAA-compliant offering this fall, and our new API and partnerships will provide IT leaders with data loss prevention, eDiscovery, and archiving solutions for increased control and support of security and compliance controls, while still facilitating important cross-functional connection.

I'll close by acknowledging that we're actively managing our business and staying vigilant as we carefully navigate through the current macroeconomic cycle. We'll continue to balance growth and profitability, which includes managing our investments conscientiously, while maintaining our leadership and product innovation and vision.

Now, I'll turn it over to Anne.

Anne Raimondi

Thanks, Dustin.

It's the conversations we have with our customers that make us so confident in our investments and product innovation. As we move upmarket, our product strategy has successfully evolved to address customers' growing needs. These upmarket product announcements will help to further drive adoption of our Business and Enterprise tiers.

In Q2, the U.S. region and Enterprise segment led our overall growth. This is a good indication that Asana is a great market fit for organizations today, especially with the challenges and opportunities they are facing now and going forward.

Over the last several months, I've been on the road spending time with our customers around the world. The stories they share with me are amazing. These are just a couple of key observations.

First, our conversations in Enterprises are moving up the authority chain. Digital transformation is mainstream, and work management is an essential component of that. In Enterprises, as Dustin showed with the data, cross-functional collaboration is not a thing they do, it's everything they do in order to run their business processes. Asana is a critical platform that allows companies to work the way things get done - cross-functionally. The market fit is clear.

Second, we are closing deals with some of the largest and most recognized brands in the world. Some of the most prominent and successful companies across industries such as Media, Automotive, Financial Services, and Telecom are choosing Asana to help them grow, compete, and leverage their tech stack investments. We now have 462 customers spending over $100,000 on an annualized basis, and these larger deals represent our fastest-growing customer cohort, up 105% year-over-year.

Third, the more our customers use Asana, the more they realize value, and this increases product adoption. We are seeing more new users join existing Asana Enterprise deployments and quickly collaborate cross-functionally with colleagues. Our dollar-based net retention rate for customers over $100,000 is well above 145%.

Fourth, Asana is a beloved brand. Customers love Asana and want Asana to win. One customer who runs an operational team said, "Asana has been a game-changer for our organization. We've been able to streamline how requests for products come to our team and move away from never-ending email chains with overlapping voices and calls for edit. Thanks, Asana." Our brand equity is remarkable.

Overall, we continue to see strong demand and we are closing deals with large customers, and we have strong engagement across our user base. As I look across our customer base, we are seeing broad cross-industry adoption with significant traction in Fortune 100 customers, of which over 80% use Asana. Some of the most important companies in the world are adopting and expanding with Asana this year.

To call out a few, one of the world's largest automotive manufacturers is a growing customer. They are using Asana Enterprise in R&D divisions to improve clarity across the organization about the status of various initiatives and how they are progressing towards their goals.

A well-known and one of the largest container shipping line and vessel operators is another six-figure customer. They're using Asana Enterprise for critical customer contract logistics workflows to ensure shipments are fulfilled in their warehouse and distribution divisions.

One of the largest global grocery and convenience store chains headquartered in Europe is using Asana Enterprise in their online shopping division to ensure efficient execution with cross-functional workflows across sales and operations, and one of the largest telecommunications companies has thousands of employees using Asana Enterprise for managing their global supply chain initiatives, orchestrating their field technicians and retail operations. In fact, in the technology space overall, eight out of the top 10 tech companies in the world are Asana paying customers.

We're also gaining early traction with financial services companies that are using Asana to help automate critical operational workflows, saving time and increasing productivity. In Q2, Morningstar again expanded their use of Asana across research, operations, marketing, and client services. We also signed an expansion deal in Q2 with one of the largest hedge funds headquartered in New York and Chicago, and we are in conversations with other large North American and European banks.

We are seeing an impact in the Healthcare industry as well. As Dustin mentioned, we expect to have a HIPAA-compliant offering broadly available in a few months, which we expect to enhance our position with healthcare customers going forward.

Another big industry that has been going through significant digitization is Media. In the media world, bringing their product to market is their core service and it needs to be done faster and more effectively to stay competitive. Asana is the strategic partner of choice for several major media companies. In Q2, we closed a deal with Vox Media. They've now expanded and up-tiered to Asana Enterprise, using Asana to ensure their core workflows for revenue-generating partnerships from RFP process to deal close. Viacom

CBS, which is now part of Paramount and Discovery, along with other premium media brands, are all customers we're proud to partner with as they embrace the future of work.

As I noted earlier, Telecom is another vertical where we have strong traction. In Q2, we closed a deal with one of Asia-Pacific's largest telcos. This was a land deal and another big industry win for us. Also in Q2, we won Three UK, a British telecommunications and Internet service provider. They're deploying hundreds of Enterprise seats. We are also deployed in the largest telco in the world, who expanded their seats this quarter, and of course there's T-Mobile, an existing customer, using Asana for developing strategies to launch new products.

These companies are leaders in their respective industries and know what it means to leverage innovation and technology to be fast, responsive, and effective. Work is cross-functional, and companies need a platform that allows teams to collaborate across the organization. They are choosing Asana because they believe Asana is the best platform available for work management.

While it's hard to predict how the current macro environment is going to impact our various customers in the short term, we believe the long-term secular trends in digital transformation remain intact and the importance of work management software will continue to grow. We remain committed to our long-term strategy. We believe we can win the category as the awareness grows and our unique capabilities meet customer needs, providing time to value in weeks, not years, and high ongoing return on investment.

With that, I'll hand it over to Tim.

Tim Wan

Thank you, Anne.

Q2 revenue growth showed continued strength in the business overall. Revenues came in at $134.9 million, up 51% year-over-year. This puts us at an annualized quarterly revenue run rate of $540 million, over $0.5 billion. Revenue from the U.S. grew 59% year-over-year, accounting for 60% of our total revenue.

International grew 39% year-over-year, accounting for 40% of our revenue. Currency impacted our international growth rate by roughly 400 basis points and the overall revenue growth rate by 200 basis points. International growth would have been 44% year-over-year and total revenue growth would have been 53% year-over-year without the impact of currency.

At 64% growth, revenue from customers spending $5,000 or more on an annualized basis is a good leading indicator of our core growth. This cohort represented 72% of our revenues in Q2, up from 66% in the year-ago quarter, and speaks to our success as we continue to move upmarket. The revenue growth for this cohort of customers in the U.S. grew even faster at 73% year-over-year.

We now have over 131,000 paying customers at the end of Q2, up approximately 5,000 in the quarter. We have 18,040 customers spending $5,000 or more on an annualized basis, up 41% year-over-year. We now have 1,141 customers spending $50,000 or more on an annualized basis, up 91% year-over-year. Our largest customers remain our fastest-growing cohort.

We have 462 customers spending $100,000 or more on an annualized basis, and the customer cohort is growing at 105% year-over-year. We believe this metric is a good proxy for our Enterprise business, and you can expect us to continue updating this number in coming quarters.

As a reminder, we define these customer cohorts based on an annualized GAAP revenue in a given quarter. We will be sunsetting the use of $50,000-plus and total customer stats over the next two quarters and instead plan to use $5,000-plus and $100,000-plus stats as key indicators for the health of our business moving forward, as we believe they are more aligned to our core business growth and future success with Enterprise customers. We'll continue to disclose the current metrics on our IR website through the end of the fiscal year.

Our dollar-based net retention rates remain strong across every cohort. Our overall dollar-based net retention rate was over 120%. Among customers spending $5,000 or more, our dollar-based net retention rate was over 130%, and among customers spending $50,000 or more, our dollar-based net retention rate was over 145%. As a reminder, our dollar-based net retention rate is a trailing four-quarter average calculation.

As I turn to expense items and profitability, I would like to point out that I will be discussing the non-GAAP results in the balance of my remarks.

Gross margins came in at 90.1%, improved from 89.2% in the year-ago quarter.

Research and development was $50.4 million, or 37% of revenue. We continue investing to win and fuel innovation in our proprietary technology which will help us deliver on our vision.

Sales and marketing was $94.7 million or 70% of revenue. We front-loaded many of our customer-facing roles this year to build sales capacity and infrastructure for the second half and beyond.

G&A was $39.1 million or 29% of revenue, which includes $2.5 million in costs related to a reduction in the size of our recruiting team. Excluding the one-time cost, G&A as a percentage of revenue would have been 27%.

Operating loss was $62.6 million and the operating loss margin was 46%. Net loss was $64.3 million, and our net loss per share was $0.34.

Moving on to the balance sheet and cash flow.

Cash and marketable securities, including long-term investments, at the end of Q2, were approximately $239 million. Our remaining performance obligations, or RPO, was $261.6 million, up 53% from the year-ago quarter. Eighty-seven percent of our RPO will be recognized over the next 12 months. That current portion of our RPO grew 55% from the year-ago quarter.

Total deferred revenue at the end of Q2 was $210.2 million, up 51% year-over-year. While we don't normally comment on calculated billings*, since currency had such a significant impact this quarter, I wanted to call out that calculated billings grew 43% year-over-year when we factor in the currency impact.

Our free cash flow is defined as net cash from operating activities less cash used in property and equipment and capitalized software costs, excluding non-recurring items. In Q2, free cash flow was negative $42.3 million or negative 31.3% on a margin basis.

Moving on to our outlook.

For Q3 Fiscal Year 2023, we expect revenues of $138.5 million to $139.5 million, representing growth rates of 38% to 39% year-over-year. We expect non-GAAP loss from operations of $66 million to $63 million, which is a significant decline in growth of operating expenses year-over-year. We are targeting flat operating margins quarter-over-quarter at the midpoint, and we expect net loss per share of $0.33 to

$0.32, assuming basic and diluted weighted average shares outstanding of approximately $203 million, which includes the newly issued shares.

For the full Fiscal Year 2023, we expect revenues to be $544 million to $547 million, representing a growth rate of 44% to 45% for the full year. We expect FX to negatively impact our full year growth by approximately 200 basis points. Excluding the currency impact, our growth would have been 46% to 47% year-over-year. We expect operating loss margins to be between 45% to 44% for the full fiscal year.

As you can see from our guidance, we've front-loaded our investments for the year. You should expect two percentage points of operating loss margin improvement in the second half of the year versus the first half, and even more improvements next year.

In addition, as you have seen in today's press release, we announced a private placement by our CEO. Dustin purchased approximately 19 million shares of Class A common stock at $18.16 per share, which was the closing trading price of our Class A common stock on Friday, September 2, 2022. This investment of $350 million will increase our cash balance to over $585 million in total. We believe this additional capital will provide sufficient funding to execute on our current strategies and for us to achieve positive free cash flow, which we are targeting before the end of Calendar Year 2024.

In addition, here are some of the major initiatives we are undertaking as part of our focus on efficiencies.

We've moderated headcount growth significantly, and you'll begin to see it manifest in G&A and R&D expenses first. We've already slowed headcount growth from 13% sequentially in Q1 to 5% in Q2, showing a change in momentum and highlighting our commitment to expense management.

We are focused on leveraging the existing infrastructure that we've built over the last several quarters; for example, ensuring our sales reps are successfully ramped. We're also pacing out other investments in various geographic markets and prioritizing the highest ROI go-to-market initiatives. We are actively working to drive more leverage in our cost structure and have taken significant measures to manage spend.

With strong top line growth, high gross margins, and our focus on increased efficiencies, we believe we are on a solid path to generating free cash flow. Importantly, there are no changes to our long-term product strategy that has to date helped us succeed at being the most scalable and most widely deployed platform across our space. For example, we will continue to invest in product and marketing activities to support the momentum behind our Enterprise product announcements in October. These will continue to drive high growth and success in the Enterprise.

With that, I'll hand it back to Dustin for some final closing remarks.

Dustin Moskovitz

Thanks, Tim.

I'm investing further in Asana because I strongly believe the market opportunity is enormous and that the Work Graph is the best possible solution for helping enterprises achieve their most important goals, which always involve cross-functional workflows and necessitate clarity at every level. The market is ready, and our customers are validating our strategy every day. Finally, I know our team is the very best in work management and hungry to achieve our mission. We're still in the earliest stages and we intend to win.

Catherine Buan

With that, I'll turn it back to the Operator for questions.

Operator

Thank you.

Our first question is with Brent Bracelin from Piper Sandler. Brent, your line is open.

Brent Bracelin

Thank you. Good afternoon.

I wanted to double-click into the large customer cohort, triple-digit growth in the $100,000-plus cohort customers. It sounds like cross-functional collaboration's really resonating here. What is driving the momentum in large customers, I guess, for maybe Anne or Dustin, and are there things you can do to maybe emphasize the strength in large enterprise, redirect some sales and marketing dollars to what appears to be a segment of the market where you're having a tremendous amount of success?

Dustin Moskovitz

Yes. Thanks for that question. This is Dustin.

I think a lot of it is really the product strategy, which is—it really shines and differentiates from our competitors when you have larger organizations, because they're doing more strategic cross-functional work, and we're finding that the majority of all collaborative activity in Asana is cross-functional in nature, so I think people are finding that value proposition and using it.

We want to make that a nice feedback loop, so we're investing further in the product roadmap to emphasize the functionality that's most used cross-functionally, and so it's things like Goals, and we're doing a launch that includes some Goals improvements in October: improving Portfolios—that's a lot of our roadmap over the next year is going to make those even more powerful; improving Reporting—we talked a little bit about being able to report on Goals and Reporting, but also there's a lot of great enhancements there.

That really helps us really accentuate the value of the Work Graph for these large organizations, make it more useful to larger teams, make it more useful to senior leaders and executives, and then we feed that right back into our sales approach, so teaching the sales team how to do value-based selling around not only the productivity increases we can give to the team broadly, but to the insight and clarity we can give to senior leaders as they're able to understand what we sort of think of as the upper levels of the Work Graph, or what we sometimes call pyramid of clarity.

So there's a lot more we can do there, and then yes, feeding that right back into our marketing approach as well, having more messages that appeal to large organizations, making sure we're targeting our spend in channels that can find those types of personas and buyers, and then having that feed all the way through the customer journey.

Brent Bracelin

Thank you, and then just a follow-up here for Tim.

It's great to see the additional $385 million cash infusion. It sounds like this provides a healthy bridge to positive free cash flow. How are you thinking about getting there in the next two years? Where are you going to drive most of the improvement? Seventy percent of revenue tied to the sales and marketing still seems hot on a relative basis through peers. Is that really where you see you could drive the most amount of leverage here in efficiency over the next couple of years? Any color there on how you get to positive free cash flow within two years would be helpful. Thanks.

Tim Wan

Yes. Hey Brent, this is Tim. Great question.

What I would say is we're incredibly focused on gaining efficiencies across the whole organizations. I think where you'll first kind of see where gains in efficiencies in the operating income statement is G&A and R&D, and then over time that you can expect us to see improvement in sales and marketing as we kind of focus and divert our attention, moving upmarket.

As you can see, the momentum that we've seen in North America and in Enterprise, which grew 59%, those are the areas that we're going to continue to double down in and invest in, and in those markets where the payback may be longer or the ROI may be more unknown, I think you'll see us pull back investments in, so we're trying to be really mindful of the investments that we're making, but also have a really rigorous focus around what we can get with the existing infrastructure.

Operator

Our next question is with Alex Zukin from Wolfe Research. Alex, your line is open.

Alex Zukin

Perfect. Hey, guys. Can you guys hear me okay?

Dustin Moskovitz

Yes, we can hear you. Go for it.

Alex Zukin

Perfect.

I guess maybe, Dustin, just, or Anne, the first one for you guys, as you're having conversations with senior leaders at some of your larger customers or prospects, when you think about the kinds of conversations you're having and how they dovetail with the prospects for a tougher macro environment, a lot of companies are talking about lengthening sales cycles in the enterprise or larger deals that get de-scoped.

I think even some investors when they're asking us questions about mission-critical must-haves versus nice-to-haves, there's a healthy amount of debate in terms of where this type of software falls in that category, so it's a long way of asking what kinds of conversations are you kind of seeing right now? How is that impacting sales cycles, if at all, or is it actually helpful to you? And then, I have a quick follow-up.

Anne Raimondi

Yes. Hey Alex, it's Anne. Thanks for that question. I'll start off.

We're conscious that the macro environment is clearly impacting software purchasing overall, but what we're seeing in work management is it's still early and seeing some of the highest growth, given the problems that we solve are persistent.

So I've been able to be on the road meeting with customers, which has been great, and I think what we're seeing the response to, as Dustin mentioned, is our differentiated product strategy, so specifically conversations around Goals with CEOs, COOs, CIOs, who are trying to figure out how they can rapidly adjust plans and cascade those throughout their organization, and so with Asana, they're able to do that in a really agile fashion, and so the conversations we're having are much more about how they can respond in this environment quickly.

You asked a specific question about deal cycle times, and certainly, as we move upmarket and are working on larger deals, we're going to see that those cycle times are a bit longer than where we've come from, and we're also monitoring that because customers are scrutinizing spend, but overall, in terms of higher-level conversations we're having in organizations, it's been very positive because of our Goals products.

Alex Zukin

Perfect, and then I guess just another question around the incremental profit profile of the company.

I guess as we think more out year focused, you're calling around I think exiting Calendar '25 or getting to cash flow profitability in Calendar '25. What kind of a balance of growth to profitability are you contemplating that entails? Is that you get to breakeven and you stay there, funding a higher growth rate, or is the goal to kind of start to get closer to that long-term operating margin target that you are able to accelerate that progress driven by the move upmarket and the contribution profile of these higher-margin customers?

Dustin Moskovitz

Hey. This is Dustin.

I just want to clarify actually that the timeline we laid out was before Calendar 2025, so by the end of Calendar 2024, and that's in the foreseeable future, but it's also a long way out, so it's a little hard to predict exactly how we'll manage the business as we cross the line, but we want to make sure that we're managing cash well and investing in our best growth opportunities, and as you said, that's going to happen naturally as we move upmarket because there's a much better sort of cost profile for those larger customers.

I certainly hope to have real margins and not just sort of be holding the line, but we also are in it to win the category, and so we're going to look for the opportunities to invest in growth, and it will depend somewhat on what's available at that moment in time, so, I think the long run—the long-range profit margins we've given in the past also come with a slower growth rate.

I think that that should hopefully be a sort of favorable trade-off for investors either way. Either we're growing really quickly, and so we decide to continue investing in that growth, or we're growing somewhat slower, and then we'll seek to expand the margin profile.

Operator

Our next question is with Andrew DeGasperi from Berenberg. Andrew, your line is open.

Andrew DeGasperi

Yes, hi, everyone.

Just on the framework for the full year guidance, I was just wondering, are you assuming any worsening conditions in the back half of the year, and maybe could you also discuss whether, in terms of the customer metrics, has churn in any way meaningfully increased or has it stayed steady? Then I have a follow-up.

Tim Wan

Hey, Andrew. This is Tim.

I would say with respect to guidance, what we've baked in is really the momentum that we're seeing in North America and in Enterprise, and then also then adjusted our outlook for international, particularly in Europe. We also feel really good kind of about our operating margin guidance, knowing that we have a number of different levers within our control.

With respect to the net retention rate, we're expecting it to hold steady. We haven't seen any dramatic changes or deterioration there at the moment and feel really good about the—especially on the large Enterprise and larger paying accounts where the net expansion rate continued to hold above 145%.

I would just say the biggest unknown, quite frankly, and probably for all the different software companies is the degree of the economic impact in Europe. Will it be contained within Europe, or will it have a cascading effect? We just don't know, but hopefully what I just kind of commented will provide some additional color on how we thought about guidance.

Andrew DeGasperi

Great, and then maybe, Dustin, in terms of your investment, I was just wondering if the size of it itself makes sense, I guess, to build a buffer to get to free cash flow-positive, but are we to expect to see you to continue to invest here from time to time in Asana going forward?

Dustin Moskovitz

Hey, that's a great question.

I don't think I can say anything about what the future holds, but this is a really big investment even relative to past investments I've made, and it's not something I'm looking to do as sort of like an ongoing program, but just when it makes sense from the investor standpoint, and I just want to reiterate that—I talked about this a little bit on the last call, but these are always somewhat slow and diligent decisions for me, and it's really about the long-term potential of the stock and how big the market opportunity is, and so I just think it's important to always see the investment decisions through that lens rather than reactions to short-term changes in the market.

Operator

Our next question is from Brent Thill from Jefferies. Brent, your line is open.

Brent Thill

Thanks.

Dustin, just following up on your ownership, obviously, a considerable stake that you've made over time, and I guess many are curious, why not broaden the base? Did you consider opening this to a broader list of investors? Just walk through kind of your thoughts on why this made the most sense.

And for Tim, can you just go through—many are asking why are we not seeing more leverage in sales and marketing, and you're still running 70% of revenue, which is an extremely high number? Is the throttle just full force because you feel that it's so underpenetrated? Give us a sense just perhaps on when you start to see more leverage there, because it seems like that's the biggest line item you can get leverage out of.

Tim Wan

Yes. Maybe I'll start commenting on the sales and marketing, and then I'll also take the question related to the funding.

With respect to sales and marketing, I think we've mentioned this on the call where we front-loaded many of our sales hiring for this year, and the investment was really very much front-loaded, and we expect to have that capacity kind of in the back half and ramp—and enable those sales reps to be much more productive next year. So I think you should expect kind of the back half, maybe Q4 and next year, to see more leverage in sales and marketing as we enable those reps and make them be more successful over time. So that's one.

With respect to the funding and the different considerations, a lot of the information is actually in the 8-K. We did have a special committee of the independent Board members to evaluate all the different options that were available to us, and we agreed that, with the special committee and the Board and Management, that this was the best option, but you should definitely read the 8-K, and there's a lot more details related to this placement.

Brent Thill

Thanks, Tim.

Operator

Our next question is with Steve Enders from Citi. Steve, your line is open.

Steve Enders

Hi. Great. Thanks for taking the question here.

I guess as we do think about the view into Fiscal '25 and your reaching kind of breakeven, is there any change in kind of the investment plans that you're making that would be needed to get there versus kind of what you were thinking before.

I guess, similarly, as we look at the kind of EBIT outlook, and it still seems to be trending, at least on a dollar basis, downward, how should we think about when that begins to reverse and we begin to see some leverage happen in the model here?

Tim Wan

Yes. Let me kind of answer the second part of that question first in terms of how we would expect the model to turn and when you should expect to see leverage.

So for the back half of this year, you should expect about 2 points improvement in operating margin, but then to see much more significant improvements in our operating margin and free cash flow margin starting next year. Again, we front-loaded many of the investments that we've made this year. We've dramatically moderated our headcount growth, but many of that headcount's going to really come online in this back half and next year for us to help drive growth and get a lot more efficiency off the existing infrastructure.

It's going to take a little bit of time, but we do see a path to improving operating margin and free cash flow margin and have a plan in place now to get to positive free cash flow before the end of Calendar '24.

Dustin Moskovitz

This is Dustin. I'll do my best to add some color around how the plans have changed.

It's a little hard to be concrete about this first potential counterfactual, but some of the things that have definitely been coming up is just more of an emphasis on focusing on where we're strong, where we know that we have sort of per channel and geographic profitability dynamics, and that comes at basically an opportunity cost of not investing in more speculative areas, more emerging markets.

I think in a stronger economy, those more speculative investments made more sense. There was just more money around in the economy to sort of take us up on those offers, we had easier access to capital, and just with the currency exchanges, just mechanically, it was more profitable, and now just relative to this time last year, the same number of seats, the same number of customers is going to result in less revenue and less profit for us.

So we're just focusing more of where we're hiring, where we're putting programmatic spend into the developing markets and upmarket, and as a consequence, that shortens our timeline to profitability, but it also means we're not sort of doing the sort of broad, go after every segment in every region at the same time, and so it may mean that there's a bit of a limit to our growth rate in the next couple of years as well relative to the counterfactual, but again, it's a different economy, and so it doesn't make sense to operate with dual plans.

Steve Enders

Okay. Perfect. That's very helpful.

I guess on the—as you think about kind of the Business and Enterprise tier adoption, I guess, how have you been kind of seeing that resonate in the current environment, and how should we kind of think about the mix of expansion that came in the quarter from kind of the fees versus upgrading to some of those higher-priced tiers?

Anne Raimondi

Yes. Hey, this is Anne. I'll answer that question.

We are seeing strong growth in both Business and Enterprise tiers, so they're contributing 67% of revenue in Q2, which is an increase of 69% year-over-year, so that's a really positive signal, especially for larger customers, that those two tiers are really important to them and they're finding a lot of value in that. So we're continuing to make sure from a go-to-market standpoint that we're adding a lot of value in both of those tiers. We had mentioned the upcoming announcements and improvements in Goals, and we see strong adoption of Goals sort of driving both of those tiers as well

Operator

Our next question is with George Iwanyc from Oppenheimer. George, your line is open.

George Iwanyc

Thank you for taking my questions.

Anne, following up on your answer, can you maybe give us an update on the competitive environment and maybe what you're seeing from a wall-to-wall deployment perspective? Is that growing in many cases or pretty much staying consistent?

Anne Raimondi

Yes. Thanks so much for that question.

We are seeing in our sort of mid-market segment in particular that wall-to-wall, especially as companies are adopting our Goals product from a tops-down perspective, that that continues to grow. As Dustin mentioned, a lot of that is due to the fact that we are really helping our customers with their most important cross-functional initiative, and so the more that that work is being done in Asana, it sort of naturally brings in other colleagues who want visibility into Goals.

Then we're providing top-down visibility when executives are coming in to make sure that they are seeing, like where are their bottlenecks, where are their opportunities, and how they can make planning decisions in a more agile fashion. Something that we're really excited about is as we enter the season where a lot of our customers and prospective customers are doing strategic planning, they're doing goals planning, that's also driving much more interest in Asana.

George Iwanyc

Yes, and Anne, maybe could you give us some perspective on just the new customer pipeline, and I understand the macro uncertainty around expansion, but are you seeing any changes with new customer generation?

Anne Raimondi

Yes. The way that we really think about our pipeline is we have a lot of opportunity to expand with existing customers, so we are in 80% of Fortune 100 companies, but we still have a lot of opportunity for seat growth, and so we have a lot of focus on that opportunity.

Then the other way that we also think about it in this environment is we are incredibly vigilant in managing and monitoring pipeline on a weekly basis. I'm super grateful to our team around the world on how hard they're working to make sure we're reaching and serving customers really quickly in this environment.

Operator

Our next question is from Shebly Seyrafi from FBN Securities. Shebly, your line is open.

Shebly Seyrafi

Yes. Thank you very much.

You just slowed down headcount growth materially. What kind of headcount growth are you anticipating in the back half of the year?

Then related to that, consensus has your revenue growth at 31% next year, Fiscal '24? How do you think the slower headcount growth impacts your revenue growth?

Tim Wan

Hey, Shebly. This is Tim.

What I would say is we, again, front-loaded many of our hires this year. The macro environment has changed. We're being, I would say, very rigorous around how those reps are ramping and what markets and how successful they are, and as we continue to gain more traction and enable those reps to be more successful, I think those reps—that will in itself help drive and provide a lot of growth for us.

We're probably not ready right now to kind of provide guidance for next year. We'll do that kind of at the—on our Q4 earnings call. We've given guidance for this year and for the back half, so hopefully, that's enough data to kind of have a sense of how we're thinking about the business.

Shebly Seyrafi

Okay, and secondly, a lot of your software peers have noted an elongation in sales cycles, deal compression, needing more C-level approvals. Are you seeing any of that in the United States, at least so far, and do you anticipate seeing that in the back half of the year?

Anne Raimondi

This is Anne. I'll answer that.

We're certainly seeing that in this environment, in the buying process, especially in larger enterprise companies, there are more decision-makers involved. I think we also just expected that as we move upmarket and serve larger customers, but we're certainly conscious of that and monitoring our deal cycle times. Something to also keep in mind is we continue to have a very healthy commercial business, which has much faster cycle close times.

Operator

Our next question is with Robert Simmons from D.A. Davidson. Robert, your line is open.

Robert Simmons

Hey, thanks for taking the question.

Kind of following up on the last one, what are you seeing in terms of more kind of top-of-funnel type activity, free-to-paid conversion, and then also on the flip side of things, average seat reduction and gross churn?

Tim Wan

Yes. I would say on the gross churn, we haven't seen any material change, particularly in our large customers. Those continue to maintain at low single-digits, so I think that really demonstrates the value that we add and the cross-functional nature of the platform and how it allows teams to expand.

I think back to your first point in terms of the top of the funnel, we haven't seen any dramatic shifts in top of the funnel. Certainly, I think part of our focus is to continue to move upmarket and win in the Enterprise, so there is, I would say, kind of a shift even in our own go-to-market in terms of where we're focusing.

Anne Raimondi

Yes. I'll add on to that. The way to think about it is we're continuing to turn the dial on our paid acquisition spend to segments and markets that are better aligned with our direct sales motion and customers with higher lifetime value, so that's maybe how to think about our top of funnel.

To answer your question on free to paid conversion, we're not seeing any change in that quarter-over-quarter.

Robert Simmons

Great.

Dustin Moskovitz

Can I jump in on that one as well real quick? I just want to point out, just reading between the lines, sometimes people look at the total customer count as sort of indicative of the top of funnel health, and I think it's just worth pointing out that when you have a high-volume customer business like ours and some of the other work management companies, those numbers are really dominated by very small customers, not just SMBs but actually very small businesses, sometimes less than 10 employees.

Given our shift to be focusing more upmarket, it's less of a good leading indicator for us, because there can only be 100 total first-time paying customers in the Fortune 100, and that's really where we're focused, so a lot more of our business and our growth over time is focused on expansion, and that's why we like to report on things like total paid seats. I think that's a really important metric for evaluating the scale and health of work management companies in the public market.

Additionally, I think it sort of ties back to the prior question about how we'll grow next year. A lot of our growth will be in developing and expanding our existing customers, not in acquiring a high volume of new customers. I'll just point out, our net dollar retention is over 120% overall, and then again, as you get into those bigger customers where we're growing the fastest, that number just keeps climbing, so it's over 145% for customers spending $50K or more, and that does translate to a similar number or better in that $100K cohort as well.

Operator

Our next question is with Pinjalim Bora from JP Morgan. Pinjalim, your line is open.

Pinjalim Bora

Great. Hey, thank you for taking the questions.

Dustin, you're obviously seeing really great traction in the large customer front. Over 80% of Fortune 100 is a solid number, but some of your peers also claim similar kind of a mix or higher. Clearly, a lot of CWM players probably coexist in a number of these very large accounts. How do you think about the opportunity within these accounts over time? How do you see this kind of game play out?

Dustin Moskovitz

Yes. Thank you for asking that question. I love to hear exactly that type of thing.

Our whole product strategy is really designed to give you increasing returns to scale as you deploy Asana further into more of the company. It really becomes horizontal infrastructure that's used by everyone in the team, and it's really just a special difference when you get to this place where you know if you want to assign a task to somebody or find out some information, you can trust that they're using Asana, you don't have to figure out which work management tools they're using first, and we're seeing a lot of signs of strength through that, including what we see as the largest work management deployment in the industry.

We do hear about coexistence with competitive products, but from our experience and talking to these customers and mapping the accounts, those deployments are much smaller, tend to be used in small pockets of the organization, tend to be used in siloed functions, and we've talked about our largest deployment is 100,000 seats right now all in one single company.

I haven't heard anything like that from these other competitors that are, in theory, coexisting with us. They tend not to talk about their largest deployments at all. Sometimes they talk about active users, but that's different than paid seats, so I feel pretty confident that we have the farthest reach into those big customers, and we intend to double down on that success.

Pinjalim Bora

Understood. Thank you.

As you move towards cash flow breakeven by the end of Calendar '24, how are you thinking about building the indirect channel? How important would that be for this to reach kind of this goal as you especially slow down hiring? Maybe help us understand the portion of bookings coming from indirect channel today versus what it might be in the next two years.

Anne Raimondi

Yes. I can speak to indirect channels. It's still a small part of our business, but we're seeing some great traction with partners all over the world. We have great traction in India. Throughout Europe, we're seeing great partners kind of bring us into both industries and geographies to extend our reach, so we'll continue to invest in that. It's an important part of our business, but I would also just say that we see ourselves as still early in that.

Operator

Our next question is with Josh Baer from Morgan Stanley. Josh, your line is open.

Joshua Baer

Great. Thanks for the question.

I think in various software markets over the years, we've seen a pendulum swing of preference as far as best-of-breed solutions versus suites, so I'm wondering in your work management market, what's the state of that dynamic between best-of-breed versus suites, and has that changed over the last three to five months, just given the macro environment? Thanks.

Dustin Moskovitz

Yes. That's a great question.

Certainly, we're big believers that companies want the best-of-breed product for work management, and I've talked sometimes over the years about this. When we think about the various categories within software, work management is one of the richest and has the most surface area for product differentiation and really achieving differentiated value outcomes for customers, so I think that it's a dangerous place to sort of compromise in order to bundle it with part of your suite.

We really haven't seen a whole lot of that behavior right now. It's difficult to even think of particular examples, and honestly, I thought it would be more of a factor at this stage in the category development, just given who some of the larger players are, but really, we're still seeing most customers engage with thinking about the work management product itself. We honestly even have some customers that are divisions within those larger organizations that sell suite products that include work management, and they still see Asana as the solution for their sort of local team.

So that's still what it looks like for the foreseeable future. I definitely haven't seen anything market change as part of the macro context.

Joshua Baer

Great. Thanks, Dustin.

Operator

Our next question is with Patrick Walravens from JP Morgan. Patrick, your line is open.

Patrick Walravens

Oh, thank you. It's JMP.

Maybe Anne or Dustin, it seems like there's a major opportunity for Asana probably in the federal government with all those employees in the armed forces, so is Asana FEDRamp authorized, and if not, where are you in that process and how do you feel about that opportunity?

Anne Raimondi

Hey. Thanks for that question.

I think we believe that there's an opportunity for Asana everywhere that there's cross-functional collaboration, and so as we think about which industries and verticals, we're certainly looking to government. Government is super broad from both local and federal. We are early in the FEDRamp process. Dustin mentioned, we're really focused on finishing out HIPAA compliance for our healthcare customers, but I think you'll see us take the same approach is looking at demand and interest and then making sure that we're meeting customer needs, especially around things like compliance.

Patrick Walravens

Great. Thank you.

Operator

That concludes our Q&A, so I will now hand the conference back to Catherine for any closing remarks.

Catherine Buan

Thanks, everyone, for joining us today.

Before we close out, I just wanted to remind you we do have an event on October 11 here in San Francisco. It's an intimate Q&A with one of our best customers. It'll be the CIO, and they'll be talking about how they're using Asana for some amazing strategic initiatives, so look out for the invitation and we're looking forward to seeing you.

Thank you.

Operator

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

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*Calculated Billings
We define calculated billings as total revenue plus the changes in deferred revenue in the period.