

# HubSpot, Inc. NYSE:HUBS

## FQ3 2023 Earnings Call Transcripts

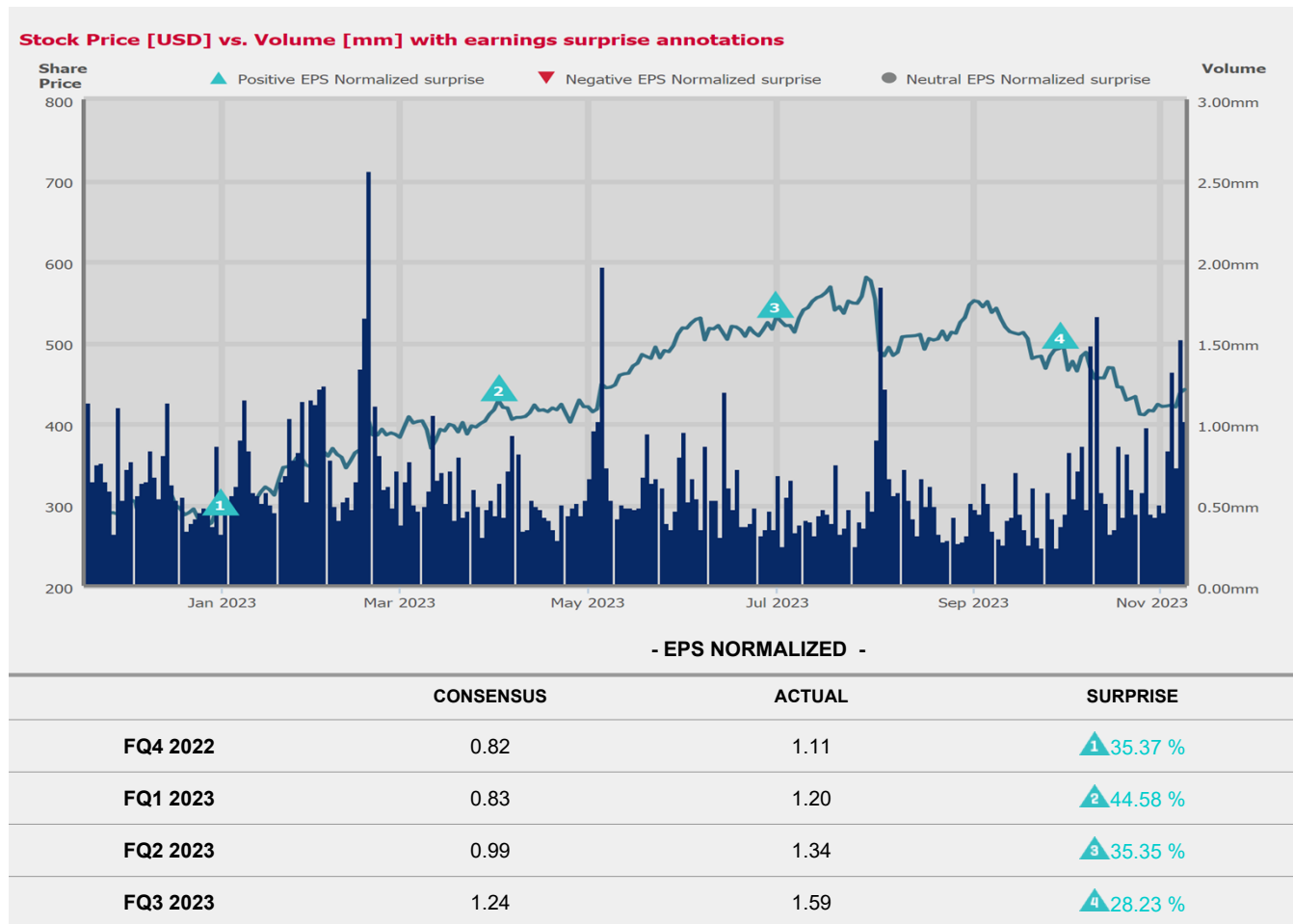
Wednesday, November 8, 2023 9:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2023-			-FQ4 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.24	1.59	▲28.23	1.51	5.30	NA
Revenue (mm)	534.38	557.56	▲4.34	557.15	2121.27	NA

Currency: USD

Consensus as of Nov-07-2023 12:36 PM GMT



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# Call Participants

## EXECUTIVES

**Charles MacGlashing**  
*Corporate Treasure & Senior Director of IR*

**Dharmesh Shah**  
*Co-Founder, CTO & Director*

**Kathryn A. Bueker**  
*CFO & Treasurer*

**Yamini Rangan**  
*CEO, President & Director*

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# Presentation

## Operator

Good afternoon, ladies and gentlemen. Thank you for joining today's HubSpot Q3 '23 Earnings Call. My name is Tia, and I will be your moderator for today's call. [Operator Instructions].

I would now like to pass the conference over to your host, Chuck MacGlashing. Please proceed.

## Charles MacGlashing

*Corporate Treasure & Senior Director of IR*

Thanks, operator. Good afternoon, and welcome to HubSpot's Third Quarter 2023 Earnings Conference Call. Today, we'll be discussing the results announced in the press release that was issued after the market closed. With me on the call this afternoon is Yamini Rangan, our Chief Executive Officer; Dharmesh Shah, our co-Founder and CTO; and Kate Bueker, our Chief Financial Officer. Before we start, I'd like to draw your attention to the safe harbor statement included in today's press release.

During this call, we'll make statements related to our business that may be considered forward-looking within the meaning of Section 27A of the Securities Exchange Act of 1933 as amended and Section 21E of the Securities Exchange Act of 1934 as amended. All statements other than statements of the historical fact are forward-looking statements, including those regarding management's expectations of future financial and operational performance and operational expenditures. The expected timing and benefits of the proposed Clearbit acquisition, expected growth, FX movement and business outlook, including our financial guidance for the fourth fiscal quarter and full year 2023.

Forward-looking statements reflect our views on the as of today and except as required by law, we undertake no obligation to update or revise these forward-looking statements. Please refer to the cautionary language in today's press release and our Form 10-Q, which will be filed with the SEC this afternoon for a discussion of risks and uncertainties that could cause actual results to differ materially from expectations.

During the course of today's call, we'll refer to certain non-GAAP financial measures as defined by Regulation G. The GAAP financial measure most directly comparable to each non-GAAP financial measure used or discussed and a reconciliation of the differences between such measures can be found within our third quarter 2023 earnings press release in the Investor Relations section of our website.

Now it's my pleasure to turn over the call to HubSpot's Chief Executive Officer, Yamini Rangan. Yamini?

## Yamini Rangan

*CEO, President & Director*

Thank you, Chuck, and welcome to everyone joining us on the call. Let me start with our performance in the quarter, share my observations on the macro environment and wrap up with our vision for our customer platform powered by AI and data.

Let's jump into our Q3 results. We had another quarter of solid execution with revenue growing 24% year-over-year in constant currency. We delivered another exceptional quarter of operating margin growth with 700 basis points of margin expansion year-over-year, driving our operating margin to 16%. Total customers grew by 22% year-over-year to over 194,000 customers globally, driven by over 9,100 net customer additions in the quarter. I'm pleased with our team's focused execution and the progress we are making to become the #1 customer platform for scaling companies.

Our Q3 results highlight two consistent themes this year. Our bimodal go-to-market strategy is working, and our product innovation is in high gear, especially coming out of inbound in September. In the lower end of our segments, we saw strength in net customer additions driven by free sign-ups and growth optimization plays in our starter addition. Our value proposition of an easy-to-use, easy-to-scale customer platform resonates within the segment.

In upmarket, we continue to see multi-hub adoption as customers consolidate on fewer platforms and drive better visibility across marketing, sales and service. A great example of a multi-hub customer who's seeing results from consolidating on HubSpot is Knowledge Academy. They are the largest provider of online instructor-led training globally. They started with Sales Hub to get better visibility into their pipeline and then added Marketing Hub to optimize their marketing budget and also added Service Hub to get a complete view of their customers.

Since implementing HubSpot, Knowledge Academy has grown leads by 4x, boosted sales by nearly 2x and increased their average order value by 25%. As you've heard me say before, our hubs are powerful on their own, but the real value for our customers comes from using them together. And we can see this in our results with over 50% of our installed base now on three or more hubs.

Turning to product innovation. We continue to be in high gear, and our launches at INBOUND are driving momentum. While we have launched over 200 new product enhancements this year, the two big moments at inbound, where the Sales Hub relaunched and HubSpot AI launch. So why did we relaunch Sales Hub and we are already seeing momentum within this hub this year? Simple. We want to deliver the best prospecting and deal management solutions that are deeply connected especially for our upmarket customers.

The new prospecting workspace, which is now generally available, gives reps one place to organize their leads and pass so that they can spend less time looking for information and more time connecting with customers. In deal management, we introduced AI-powered forecasting to help sales leaders improve accuracy in revenue projections, very important in any environment. We have a compelling vision to drive sales productivity, and we are hearing positive feedback from our customers, particularly in upmarket about the new found power and sophistication of Sales Hub.

Another highlight that inbound was the launch of HubSpot AI. We believe that every scaling organization deserves an AI-powered customer platform. And that is why we are deeply embedding AI across all of our hubs and our entire platform. We announced a number of features across AI assistance, AI agents, AI insights and ChatSpot. While I'm certainly excited about our pace of innovation, what we are really focused on is driving usage and value for customers. 40% of enterprise customers have already used HubSpot AI features, along with 20% of pro customers. About 2/3 of AI users are leveraging AI assistance to craft marketing e-mails and blogs. Social publishing is proving out to be a sticky use case, drawing in engaged users. In short, when we embed AI into the flow of work it works. I'm pleased to see usage beginning to grow, and we know we're still in the early stages of a major technology shift.

Looking ahead, we're focused on driving discoverability of and differentiation with AI features. We will drive adoption both in product and via customer education. We will drive differentiation by bringing more sophisticated use cases that are more deeply connected with HubSpot data. To summarize, I like the early adoption trends, and our well-defined AI road map to bring innovation to our customers.

Okay. Let's shift gears and talk about what we're seeing in the macro environment. Overall, we continue to operate in a choppy and challenging environment. Sales cycles remain lumpy, budgets are still under scrutiny and buying urgency remains low. It is clear based on my conversations with customers that they still need approvals from multiple decision makers and are continuing to optimize spend. Despite these headwinds, HubSpot's connected value proposition continues to resonate with customers looking to optimize spend and boost productivity. As we look ahead, we will continue to navigate this macro environment by following our playbook to drive product innovation and consistent strong execution.

Now I want to dive deep into our vision for our customer platform and talk about how our recently signed agreement to acquire Clearbit accelerates that vision. Our vision is to give millions of companies the best possible data about their customers in HubSpot. Today, we pull in data from website visits, marketing e-mails, sales calls, support tickets and more. And we unify all of that data on a beautiful, simple customer record. This is arguably the biggest advantage with HubSpot. With Clearbit, we will be able to bring in even more external data that can help our customers connect better with their end customers. So what can we solve for our customers with more unified data.

While we can help our customers identify great fit customers and provide clear signals on buying intent, both keys to increasing their go-to-market effectiveness. Our customers want company data, not just the name of the company and employee count, but they want rich attributes about companies including demographic data, like who is the CIO and techno-graphic data like which automation products are they using? In addition, they want a real-time way to monitor buying intent. Not just based on direct engagements within HubSpot platform but also based on customers' activities outside of HubSpot and around the web.

This is exactly what Clearbit is good at. They have 100-plus attributes for more than 20 million companies from more than 250-plus public and private data sources. We can take all of those data from HubSpot and Clearbit to power generative AI tools to create even more personal messages and insights for customers. Our differentiation will be to bring together a unified customer data with powerful AI tools that can consume that data and our market-leading engagement hub to supercharge our customers' go-to-market efforts.

Finally, why Clearbit? And what are our plans going forward? Clearbit has world-class data, and they share our commitment to helping customers grow. They also have a deep bench of B2B data experts with a bold mission to leverage AI to power insight. In all our conversations with Clearbit, it was clear that the team would be a great addition to our culture. And most importantly, this does not take away from our approach to building great products with cohesive user experiences. We use Clearbit data on our product today,

and we have a very clear vision for how we can integrate their data to provide immediate value for our customers. In addition, we can leverage our product-led partner-led and sales-led distribution engines to get this into the hands of our customers post close. I'm thrilled by the prospect of acquiring Clearbit and our shared vision of solving for the customer. We will share more about our future plans after the deal has closed.

So reflecting on the quarter, we doubled down on product innovation in our core hubs and we established leadership in AI with our customers. Our teams are focused on consistent execution, and we have a clear vision for taking our customer platform to the next level with AI and data to deliver even more value to our customers.

With that, I'll turn the call over to Kate to take you through Q3 results in more detail. Kate?

**Kathryn A. Bueker**  
*CFO & Treasurer*

Thanks, Yamini. Let's turn to our third quarter 2023 financial results. Revenue grew 24% year-over-year in constant currency and 26% on an as-reported basis. Subscription revenue grew 25% year-over-year while services and other revenue increased 31% on an as-reported basis. Domestic revenue grew 22% year-over-year, international revenue growth was 26% in constant currency and 30% as reported, now representing 47% of total revenue.

We added 9,100 net new customers in the quarter, bringing our total customer count to over 194,000, up 22% year-over-year. Average subscription revenue per customer grew 1% year-over-year in constant currency and 3% on an as-reported basis to \$11,500. Our ASRPC growth was driven by continued multi-hub adoption by our professional and enterprise customers, offset by the large volume of starter customers we added at the low end of our bimodal strategy over the last few quarters. Gross retention remained healthy in the high 80s for the quarter, and net revenue retention was up slightly quarter-over-quarter.

We continue to see pressure on net upgrade motions, including seats, contact tiers, additions and portals and expect this to persist in the short term. Nevertheless, we remain confident that we can maintain net revenue retention above 100%. Calculated billings were \$550 million, growing 20% year-over-year in constant currency and 24% as reported. The remainder of my comments will refer to non-GAAP measures. Operating margin was 16%, up 7 points compared to the year ago period. Operating margin in the quarter benefited from lower T&E and other discretionary spend, continued infrastructure optimization and more concentrated hiring in Q3 and Q4 in key areas such as product innovation, AI and internal systems and data. Net income was \$83 million or \$1.59 per fully diluted share.

Free cash flow was \$65 million or 12% of revenue, and our cash and marketable securities totaled \$1.7 billion at the end of September. On October 31, we entered into a definitive agreement to acquire Clearbit for approximately \$150 million in cash. The acquisition is subject to customary closing conditions, including regulatory approval and we expect the transaction to close before the end of the year.

Like Yamini, I am excited about the value we can create for our customers with the combination of Clearbit's world-class data and HubSpot's AI-powered customer platform, and I look forward to welcoming the Clearbit team to HubSpot.

Okay. Before we dive into guidance, I wanted to touch quickly on the macro environment. As Yamini indicated, we continue to operate in a challenging environment. Q3 felt similar to what we saw in the first half of the year. Budgets are still under scrutiny deals are taking longer to close, buying urgency is low and customers are continuing to look for ways to optimize their spend. Our guidance assumes that these weak conditions persist in Q4.

Now let's review our guidance for the fourth quarter and full year of 2023. For the fourth quarter, total as reported revenue is expected to be in the range of \$556 million to \$558 million, up 19% year-over-year at the midpoint. We expect foreign exchange to be a 2-point tailwind to as reported revenue growth in the quarter. Non-GAAP operating profit is expected to be between \$85 million and \$86 million. Non-GAAP diluted net income per share is expected to be between \$1.53 and \$1.55. This assumes 52.7 million fully diluted shares outstanding. And for the full year of 2023, total as reported revenue is now expected to be in the range of \$2.144 billion to \$2.146 billion, up 24% year-over-year at the midpoint. We now expect foreign exchange to have no material impact on as reported revenue growth for the full year.

Non-GAAP operating profit is now expected to be between \$317 million and \$318 million. Non-GAAP diluted net income per share is now expected to be between \$5.66 and \$5.68. This assumes 52.2 million fully diluted shares outstanding. As you adjust your models, keep in mind the following: we continue to expect CapEx as a percentage of revenue to be roughly 5% and now expect free cash flow to be about \$275 million for the full year of 2023. Looking forward to 2024, we expect foreign exchange to be a 1- to 2-point headwind to as reported revenue growth.

And with that, I will hand things back over to Yamini for her closing remarks.

**Yamini Rangan**

*CEO, President & Director*

Thank you so much, Kate. I want to close by reiterating our commitment to balancing growth, profitability and a great culture to build an enduring company. We're driving rapid innovation with our customer platform and HubSpot AI to drive growth. We're focused on improving sales and marketing efficiency and scaling distribution. And on culture, we remain committed to building a high-performing, sustainable and diverse culture. This quarter, we hosted our first-ever Global Leadership Summit, which brought together our top leaders across the globe for workshops, trainings on performance, leadership and strategy. It was just a fantastic week and left me energized about HubSpot's future. A huge thank you to all our employees and partners for their dedication to driving results and to our customers and shareholders for their continued support on this journey.

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

# Question and Answer

## Operator

Absolutely. We will now begin the Q&A session. [Operator Instructions] The first question comes from the line of Arjun Bhatia with William Blair.

### **Arjun Rohit Bhatia**

*William Blair & Company L.L.C., Research Division*

Yamini, you called out macro headwinds. I know that's similar to what you called out in prior quarters, but it seems like despite the challenging environment, we're not really seeing the slowdown take hold in the fundamentals, the net new revs are strong, the new customers are strong. Is this something that you're seeing get worse, get better? Or is this something that you're kind of anticipating in Q4 that there are signals that maybe things are a little bit tougher heading into the holiday season. And if we do kind of continue down this path, how are you thinking about adjusting your bimodal go-to-market strategy between the new and the mid-market upsell existing do you mean heavily -- more heavily one way or another as a result of that?

### **Yamini Rangan**

*CEO, President & Director*

Arjun, yes, thanks for that question. Look, as both I said and Kate said, the environment continues to be choppy and challenging and customer urgency remains low. More broadly speaking, what we are seeing in second half as customer trends is very similar to what we saw in the first half of 2023. It's not gotten better and it's not gotten worse. And when we are looking at our pipeline and we have conversations with customers, we see more decision-makers involved in the process, more budget scrutiny, continued optimization of spend. Deals are definitely closing, but it takes more conversations, more demos and more time.

Now having said that, I think we've consistently executed in this type of a choppy and challenging environment. And when I look at the pipeline going into Q4, when I have conversations with customers, couple of things stand out. One is customers are focused on consolidating on fewer platforms to eliminate spend, this is exactly where HubSpot's value proposition really resonates, and we are helping consolidate point solutions for customers. And the second is they are focused on increasing productivity, especially because they're not increasing head count. And again, our quick time to value and the ease with which they can scale with our products is really helping.

So we are going to remain very laser-focused on executing in this environment, and we are assuming that this environment will continue into Q4 I don't think that changes our bimodal strategy. In fact, what has been good is that we have been consistently executing on a bimodal strategy to increase volume at the bottom and continue to deliver value at the top and we'll continue to drive product innovation to be able to win within this environment.

## Operator

The next question comes from the line of Samad Samana with Jefferies.

### **Samad Saleem Samana**

*Jefferies LLC, Research Division*

Great. Kate, maybe for you. I think the increase in NRR quarter-over-quarter is really encouraging. I guess if you think about the slide at the Analyst Day, where you broke the pieces by what things were changing, consumption versus value. Can you maybe help us understand what you saw quarter-over-quarter and just maybe what the trend line looks like through the first few weeks of the fourth quarter and what you may be assuming for those two trends?

### **Kathryn A. Bueker**

*CFO & Treasurer*

Yes. Sure thing. Thanks, Samad. You rightly indicated, Net New ARR was up slightly in Q3. The drivers of net revenue retention were very much the same ones that we talked about at Analyst Day and frankly, that we've been talking about for the last sort of 4 to 6 quarters here. The highlight continues to be customer dollar retention. Customer dollar retention is holding nicely in the high 80s. We typically see a little seasonal step-up in customer dollar retention in Q3. We did see that again this year.



The downside here is that we continue to see a challenge in this net upgrade motion, and it's both on more downgrades. So more customers continuing to optimize their spend with HubSpot and also less volume of customers upgrading. And it's all the same motion that we talked about at Analyst Day. On the downgrade side, it is the consumption-based motions of seats and contact as well as additions. And it is fewer customers adding seats and contact tiers.

Nothing to report in terms of a change in the net revenue retention trajectory in Q4. As I said at Analyst Day and I'd reiterate here, in order for us to really see that in flex we would really want to see the external environment improve, which we think is first going to show up in downgrade pressure lessening and then we would see a follow-on effect of more customers starting to add the -- starting to add contact tiers. So it's largely a function of the external environment turning around.

**Dharmesh Shah**  
*Co-Founder, CTO & Director*

Yes. And I just want to clarify, we talked about net revenue retention being up slightly sequentially, not Net New ARR. So I just want to make sure that we're clear on that. Thank you.

**Operator**

[Operator Instructions] The next question comes from the line of Mark Murphy with JPMorgan.

**Mark Ronald Murphy**  
*JPMorgan Chase & Co, Research Division*

Yamini, we continue to hear that the decoupling of Sales Hub from the Smart CRM is a big positive development and a major unlock for some future opportunities. Can you walk us through the strategic rationale that we're decoupling is how partners we're referring to it, by the way. Just what was the rationale and how that might open up some new opportunities for companies to engage with HubSpot?

**Yamini Rangan**  
*CEO, President & Director*

Thank you, Mark. And I just love that you picked it up that you're clearly calling out that separation of the Smart CRM from Sales Hub, in particular, but just the hubs. And maybe explaining the strategy. So when we went into this year, we said that, one, we want to become absolute product and thought leaders in terms of our marketing hub, sales hub and service hub. And I credit this to Andy Pitre, our Head of Product, but he came in and he said, we're going to focus on two or three big use cases per hub. And specifically for Sales Hub, we picked prospecting and deal management. And these two are really important because prospecting obviously increases the productivity of sales reps and deal management with AI and forecasting improves the effectiveness of sales management and leaders. And so those were the two things. And at INBOUND, we relaunched Sales Hub we reinvented what prospecting and deal management look like, and that's gotten pretty significant traction.

So the other thing that we did is we separated out smart CRM from each of our engagement hubs. The reason is this, Smart CRM now, we've been investing in it for multiple quarters and it's now become a clear unified customer record that can be customized, that can be extended and where people can kind of bring information and continue to expand the use of HubSpot, and it's clearly different in value from the engagement hubs. And so we separated it out and I think partners love it. Customers now have even more clarity, and it's going to drive the overall adoption of the customer platform.

**Operator**

The next question comes from the line of Brian C. Peterson with Raymond James.

**Brian Christopher Peterson**  
*Raymond James & Associates, Inc., Research Division*

I'll echo my congrats. Maybe a product question for me. Can you discuss some of the AI announcements coming out of INBOUND earlier this year? How is that influencing your 2024 road map? And anything interesting that came out of the OpenAI event this week as it relates to HubSpot.

**Dharmesh Shah**  
*Co-Founder, CTO & Director*

Thanks for the question, Brian. So we're really thrilled with the kind of adoption of HubSpot AI after its launch at INBOUND. And we're particularly pleased with the repeat usage we're getting out of some of the marketing oriented use cases. And as Yamini mentioned in the opening comments, one thing we've learned is that if you can put these AI features right where people do their work, it works. And so we're continuing to double down on that. AI is the -- literally the #1 priority on the HubSpot product road map going into 2024. We're super excited. And one thing we're going to do is take the lessons from the adoption that we've seen so far, and we're taking a ChatSpot, and we're going to kind of leave it through the entire platform. So we have a natural language interface and kind of add the Smart and Smart CRM within HubSpot. So that's kind of high on the list.

In terms of OpenAI in their recent conference they had just 2 days ago on Monday. Super exciting things. Here are things that are most relevant that has -- and we've been working with them on preview releases of what just got announced. The #1 thing is they launched a new version of their model called GPT-4 Turbo, which is as the name implies, is faster. But the thing that's much more exciting about it is that they expanded the context window. And without getting too geeky, the context window defines how much data you can pass, how much information when you prompt the LLM when you ask a question. And they went from 8,000 tokens, which was a default before to 128,000 tokens. And to put that in context, that's equivalent of a 300-page book.

Now here's why that's important for HubSpot. When we're generating, let's say, a sales e-mail that says, "Oh, we want to do an upgrade sales to this particular customer", now we can take all the information that's in the HubSpot Smart CRM on this unified data record and take all that context and pass it to the LLM in real time so that when it crafts that message, it does the best job possible.

What has me even more excited, so it's not just the CRM data that we have now, imagine in the future, we have Clearbit data, where we have all this information, all these 200 attributes, all this intent data, we can bring that all together into one single kind of prompt to the LLM and it can take all that information in real time and craft these really, really pointed effective messages. So super exciting going into 2024.

And then one for Kate here is that one thing they did announce is that the cost for all this kind of invocation of their latest model is going down. Our estimates are somewhere around 50% to 70% based on our usage once this goes into GA. So lots to be excited about AI is massively exciting going into 2024. Thanks for the question.

## **Operator**

The next question comes from the line of Rishi Jaluria with RBC.

## **Rishi Nitya Jaluria**

*RBC Capital Markets, Research Division*

Wonderful. I just wanted to dive a little bit deeper into a Clearbit really exciting acquisition. I heard some good things about the company. Can you talk a little bit about how this is going to impact your relationship with other players in the space? Including ZoomInfo, which is popular to use along HubSpot, Apollo, we actually saw HubSpot speaking at Apollo's user event earlier today. And maybe alongside that, I know privacy is obviously is very, very important. How do you think about just dealing with some of the maybe privacy and governance concerns that might come with something that is serving up data.

## **Yamini Rangan**

*CEO, President & Director*

Rishi, I'll take that multipart question. Maybe start with the vision and then the competitive landscape and then how we're thinking about privacy. Look, we're super excited about Clearbit and how they'll help us accelerate our vision for the customer platform. And what we're doing is we're bringing together this data and powerful AI tools that can consume that data and world-class engagement hubs, and that will help our customers connect and grow better.

And if we step back and think about the rationale for us, the age-old problem with CRM is that when you open up the box and set it up, it's empty. And our customers want us to pre-fill it with data on day 1. They want us to pre-fill it with company data, who else can they sell to, intent data, who else is looking to buy their products and services and contact data, who do we connect to. And this makes complete sense for our customers. And it solves a huge problem for them. And that's why Clearbit makes sense. Like I just mentioned in the prepared remarks, they have 20 million company profiles with rich attributes for each of these companies and makes absolute sense, especially in the world of AI.

And in terms of the competitive landscape, this is not about us entering a database. This is much more about us accelerating our customer platform vision. And vision that we have articulated is we want to have engagement hubs powered by a Smart CRM, powered by data, powered by AI that helps our customers grow. That's what we are accelerating. And the word platform really means

we'll continue to operate in a very open ecosystem. And if our customers choose to work with Zoominfo and Apollo, we welcome that, and we'll continue to have a very open platform as well as ecosystem.

And I think in terms of the final part of your 3-part question, which is how do we think about data privacy. Look, we know our customers value having trust in our security privacy practices. And our level of commitment to security, privacy and governance will not change as we look at integrating the data asset. When it came to e-mail deliverability, we took the right side of the road in terms of how to help our customers deliver e-mails, but do it in a very thoughtful manner, and that's the same way in which we will look at this as we go into accelerating our vision. Overall, super excited. I have to say that the feedback from customers and partners has been really, really positive in the last week.

**Operator**

The next question comes from the line of Alex Zukin from Wolfe Research.

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

Maybe just a quick 2-parter for me. As we think about this macroeconomic environment, I know we're guiding one quarter at a time, but at this point, we're starting to kind of get our models ready for next year. Is it fair to assume that you're kind of planning for this type of environment to persist and continue. And anything that we should think about or keep in mind as we start tuning our models for next year, or thinking about. You mentioned FX and the headwind there. But anything about from either billings or I don't know the -- just the retention environment or the putting in Clearbit into the numbers, anything there would be super helpful. And maybe just as an adjunct, any thoughts around for next year. As we think about AI monetization pathways, is it more around tiering up into more premium hubs? Is it new product modalities? Anything helpful there?

**Kathryn A. Bueker**  
*CFO & Treasurer*

Maybe I'll start and talk through a bit of the -- how do we think about the economic environment in setting guidance. Certainly, Yamini and I said this in the prepared remarks, it continues to be a very challenging external environment. We believe that, that environment will continue to be challenging through the end of this year. It's frankly a little too early to talk about next year. We will give, as you know, formal guidance on our Q4 call.

In February, what you should have heard Yamini say is really like we have very clear focus areas. We're focused on productization, we're focused on AI. We're executing really well. And we feel really good about how that sets us up when the economy does turn. That's the expectation is that things remain challenging, at least through early next year.

**Yamini Rangan**  
*CEO, President & Director*

And I think on the last part of your question from an AI monetization perspective, really no change from what we walked you all through at Analyst Day. We're really focused on delivering that road map, most of the features that we announced at INBOUND are either generally available now or getting close to general availability by early Q1, and that's when we'll share even more specifics about AI, but overall consistent with what we shared with you at the Analyst Day.

**Operator**

The next question comes from the line of Brad Sills with Bank of America.

**Bradley Hartwell Sills**  
*BofA Securities, Research Division*

Great. I wanted to ask a question around the net add strength. Clearly, Starter has been holding up real nicely through the challenging macro. The question is, why is that, do you think? Is it just simply larger customers that might be starting with a higher-priced offering like Pro are starting with Starter in a challenging environment, with plans to go to Pro. And then what do you think about that cohort of customer? It's been three or four quarters since you've cited strength here, in Starter net adds. Is there a cohort of customer in there that you think coming out of the macro, we could see some nice acceleration. Maybe it's just from a better macro or some of the uptake on AI features that might be going into the Pro and enterprise version.

**Kathryn A. Bueker**  
*CFO & Treasurer*

Yes, maybe I will start. Brad, thank you very much. We were very happy with the level of new customer additions for the quarter. You are also right, the increase in the new customer additions quarter-over-quarter is very much driven by the Starter addition. You heard Yamini talk about the bimodal strategy as being one of the things that's really working for us. And as we talked about at Analyst Day, the goal of the low end of the bimodal strategy is really to maximize the volume of customers that we can bring on to the platform. And so as a result, we are constantly running experiments to try to drive volume into our Starter tier. We certainly watch the characteristics of those cohorts to make sure that we feel really good about their ability to retain an upgrade.

This quarter was no different. There were a number of experiments that we ran across pricing and packaging as well as a number of plays that we ran to really lean into activation and conversion of free users into starter customers. So we're feeling really good about it.

**Operator**

The next question comes from the line of Gabriela Board with Goldman Sachs.

**Jacob T. Titleman**  
*Goldman Sachs Group, Inc., Research Division*

This is Jake Titleman on for Gabriela. Congrats on a great quarter. I want to ask the net adds question slightly differently. Before the pandemic, HubSpot was adding closer to 15,000 new customers each year. Since then, net adds have trended over 30,000 annually. Do you view this shift as cyclical? Or are there structural drivers that lead you to believe HubSpot can sustain this level of net adds going forward?

**Kathryn A. Bueker**  
*CFO & Treasurer*

Thanks for the question. I think that it is very purposeful. So we have -- you've heard us talk about the fact that when we entered the early stages of the pandemic, we made a change from a pricing and packaging perspective to really dramatically lower the price point for Starter. And we were frankly surprised at how sensitive to that pricing potential customers work. And so we have taken that learning and really leaned into it through what we've been referring to as the bimodal strategy, but we are getting better and better at running experiments at that low end to drive volume, and we feel good about our ability to continue to deliver that customer adds, call it at the high end of that 7,000 to 8,000 range that we've been talking about for the last couple of quarters.

**Yamini Rangan**  
*CEO, President & Director*

And maybe the point to add here is that the success that we see is a testament to us becoming a platform of choice for SMBs. Part of the strategy is to get companies started early in their digital journey with us, continue to deliver value as they scale. And so that clear strategy and value proposition of making it easy to buy and easy to use and easy to scale, that is what resonates. And so we're pleased with it. And I think we'll continue with that bimodal strategy into next year.

**Operator**

The next question comes from the line of Derrick Wood with Cowen.

**James Derrick Wood**  
*TD Cowen, Research Division*

Yamini, at the upper end of the CRM market in the enterprise, there are a lot of different sales tools being used for things like prospecting, sales enablement, revenue intelligence. I'm curious, do you see that kind of fragmentation in the SMB mid-market? And when you talk about a focus on prospecting and deal management, is this more of a consolidation play? Or is this more of a greenfield and replacing manual efforts.

**Yamini Rangan**  
*CEO, President & Director*

Derrick, I like that. It's all of those. I think in the market that we see, it's certainly, there are customers who've gone through the route of point solutions and they want to be able to consolidate on a single platform to get better visibility. And the fact that we not only have a market-leading sales solution, but it is tightly integrated with a market-leading, marketing solution plays well within the segments that we serve. And so it's point solution consolidation.

The other part of it is that when we look at the environment right now, it is one where people are looking to optimize their spend while improving productivity. And our sales solution does exactly that. We've been able to integrate it obviously deeply with marketing, but also make prospecting deal management, forecasting much more sophisticated over the past few quarters, and it resonates. And there's pretty clear momentum in terms of Sales Hub. And in fact, Sales Hub as a percentage of 3-plus hubs jumped from 49% last year to 56% this year. So clear momentum based on the leadership that we have within the market.

**Operator**

The next question comes from the line of Keith Weiss with Morgan Stanley.

**Keith Weiss**

*Morgan Stanley, Research Division*

Excellent. Congratulations on a really nice quarter and a difficult environment. I wanted to ask a 2-parter a lot of new functionality and new product announced at the user conference earlier back in September. And one of the things you guys talked about was the ability for that to pull people up to sort of higher level SKUs and whatnot, particularly the AI functionality. So part one, have you seen any of that start to impact numbers as of yet or perhaps on average pricing as of yet.

Part two, behind all that product, is there going to be increased investment in distribution or marketing or whatnot? One of the highlights of the past year has definitely been the margin expansion this quarter, 700 basis points year-on-year was definitely above expectations. Is that durable on a go-forward basis? Or should we be expecting more investment behind all this innovation?

**Yamini Rangan**

*CEO, President & Director*

I'll maybe get started on the 2-part question. On the first part, our overall product and pricing philosophy stays the same. From a product perspective, our philosophy is to deliver powerful tools that are just easy to use. And everything that we announced at INBOUND, and we continue to innovate on consistently drives both power and ease of use. Specifically on AI, as I mentioned a little bit earlier, Keith, we're still in the march towards getting a lot of the features from data to general availability. And so we've not yet seen that impact pricing, and that will be what we'll continue to focus on in terms of driving usage and adoption as we go into next year.

So you will hear more about AI pricing in early Q1 and then we'll talk about the trends that you're seeing on the impact to ASP next year on that. But the strategy that you articulated is exactly the case. And then in terms of how we think about scale and distribution and how we're looking at investments, look, we do have a great moat. And the moat that we have in distribution is our ability to scale product led, sales led and partner driven.

And we want to do it in a way where they get efficient over time. And Kate articulated a number of areas at the Analyst Day. And as we look at the next few years, we want to balance growth and profitability. And -- the biggest area in terms of profitability is sales and marketing efficiency. And so we'll continue to make investments. So we increase our distribution moat, but we do it in an efficient manner.

**Operator**

The next question comes from the line of Michael Turrin with Wells Fargo.

**Michael James Turrin**

*Wells Fargo Securities, LLC, Research Division*

I want to go back to the second part of the last one and just ask Kate on margin. You've shown more meaningful expansion this year in this quarter, even with INBOUND we're seeing a bit more uptick. It also looks like head count adds are coming back, albeit at a modest pace. So can you just walk us through the trade-offs you're evaluating going forward as we're still in this what sounds like elongated macro. And what leads you to kind of turn those dials between adding heads and investing into the product side and pushing more margin if growth remains more challenged?

**Kathryn A. Bueker**

*CFO & Treasurer*

Yes. Thank you very much for the question. We do continue to strive for a real balance in growth and profitability. A lot of the profitability that we are delivering this year is a result of the fact that we pulled back pretty dramatically on hiring in the back half of

last year. We did a risk at the beginning of this year, and we've been very focused and targeted on where we're adding investment. The first place we're going to continue to add investment is in product and engineering to continue to drive innovation.

And you're seeing that translate into product introduction and over time, long term and sustainable growth. We're going to continue to invest in the go-to-market to make sure that we have the capacity to service the demand that we are seeing, and we're going to continue to invest in internal product -- internal systems, automation and AI to drive some of these continued efficiency over the next 3 to 5 years as we talked about at Analyst Day.

**Operator**

The next question comes from the line of Josh Riley with Needham & Company.

**Robert Morelli**

This is Rob Morelli on for Josh. If you take a look at your tech customers compared to nontech, have you seen a greater calling in seats over this current cycle? Or has it been fairly broad. And if weakness in the broader economy continues to spread, is there a lag where non-tech customers need to take another cycle of cooling seats similar to the deeper cuts already taken by tech customers?

**Kathryn A. Bueker**

*CFO & Treasurer*

Yes. Thanks for the question. We talked in the past about the diversity of our customer base, and that just remains true. We have a very highly diversified customer base across industries software is our largest, which -- but remains sort of not mid- to high teens in terms of the percentage of ARR. And we have not seen any meaningful shift in the composition of our installed base ARR over time.

**Operator**

The next question comes from the line of Michael Turits with KeyCorp.

**Michael Turits**

*KeyBanc Capital Markets Inc., Research Division*

So first, Kate, no guidance, obviously, for next year, but can you give us something around Clearbit in terms of -- is it kind of a low double-digit millions in terms of ARR contribution. Just something that give us some sense on whether there's any dilution there.

And then for Yamini, if I can add two parts. How do you balance that simplicity plus sophistication of the new products as you roll out such that you don't alienate the base and you appeal up market.

**Kathryn A. Bueker**

*CFO & Treasurer*

Yes, I'll start and I'm sorry to disappoint you, but we are -- our 1 week post signing of the acquisition of Clearbit. We have not yet closed. We are expecting that we will close by the end of this year, but that obviously means that we will own Clearbit for a very short period in 2023. And so not surprisingly, de minimis contribution in terms of revenue or any margin impact. In terms of 2024, like we'll be more explicit with some financial targets or implications of the acquisition once we've closed it, likely on our call in Q4.

**Yamini Rangan**

*CEO, President & Director*

Yes. In terms of the second part of your question on how we balance the power and ease, we just have to do it carefully. And we have conversations with our products and UX leaders and they always are like, "Hey, you really want us to have a consumer-like feel at the lower end for SMB, but you want a sophistication of really amazing products at the top end". And the answer is yes. We want you to do that. So that is a feature, not a bug in terms of what we're asking you to do.

And so what has happened as we have implemented our bimodal strategy is we understand that in order for someone to get started very early in their digital journey. It just needs to be super simple, very intuitive take 60 minutes to set up a website, take 60 minutes to open up and unbox CRM and get going on it, and we want that experience. In fact, we'll keep improving that experience. And that actually plays a lot as we continue to build sophisticated features.

And internally, we talk about opinionated customization. So a lot of software typically ends up becoming unwieldy because the customization takes over. And internally, we really talk about opinionated customization and how do you deliver something that is

simple, opinionated but really, really powerful. And that's super intentional. Huge kudos to our product and UX organization. And Dharmesh, feel free to add.

**Dharmesh Shah**

*Co-Founder, CTO & Director*

Yes, one thing to add here is that the -- one thing that we're most proud of is that we didn't wake up a month or a go. So it wouldn't it be nice to have an easy-to-use product. We've had 17 years of conviction around SMB. We deliberately chose it, and we've been working for those 17 years to kind of maintain that ease of use even as we add more power to the top end. And this is where the bimodal strategy really shows up. So this is not an optional thing, right? It was like, "oh, it would be nice to have an easy-to-use product". We kind of force our hand and we kind of make ourselves have that discipline because if we could not keep that ease of use there, the bimodal strategy just would not work. So it's 17 years of effort by the product team to continue to drive that ease-of-use while continuing to kind of specification on the top end. I'm super proud of the team.

**Operator**

The next question comes from the line of Tyler Radke with Citigroup.

**Tyler Maverick Radke**

*Citigroup Inc., Research Division*

I'm curious on the upmarket and enterprise momentum that you're seeing. If you could just kind of comment on what you're seeing for Q4, especially as it relates to some large renewals that you're seeing at an incumbent. Are you seeing similar sales cycle issues and challenges and expansion. But if you could just kind of compare and contrast what you're seeing up market relative to your core customer base.

**Yamini Rangan**

*CEO, President & Director*

Tyler, I think it's a good question. In terms of upmarket, the customer trends are very consistent with what we have broadly said, which is when I look at the pipeline, we look at upmarket customers, there's a lot of engagement, there's a lot of interest, especially as customers are looking to consolidate on fewer platforms and optimize their spend. We come into the picture, the thing is it does take a few more conversations, few more demos, few more decision-makers in order for them to get approval.

But maybe more broadly, if I step back and think about our upmarket momentum, we've been focused on upmarket for more than a few quarters, both from a product as well as from a go-to-market perspective. our product has gotten much better, and it's meeting the needs of upmarket customers with more customization, more admin features. In fact, there's even more that's coming up that helps our product be easy and powerful. That's a differentiator. The perception of market has also clearly improved. We are gaining momentum, not just within the marketing organization, but other parts of the organization and our ability to co-sell with partners and deliver value to customers upmarket is also great. So there is momentum both on the product side as well as customer driven, but we continue to see a very similar trend up market as we have seen in the bulk of HubSpot customer track.

**Operator**

The next question comes from the line of David Hynes with Canaccord.

**David E. Hynes**

*Canaccord Genuity Corp., Research Division*

Maybe another one on Clearbit. The pricing appears to be volume-based. There's not a ton of color on their website. Can you give us a sense for like a range of potential spend that your average customer might generate if they were to adopt Clearbit? And I guess, like, is that current pricing convention, how you plan to fold it into HubSpot? Any color there would be interesting.

**Yamini Rangan**

*CEO, President & Director*

Yes. Thank you. This is Yamini. I'll start. Well, the deal still needs to go through the regulatory approval process. It can take a few weeks or longer. So between now and closing, we're not digging that deep there, nothing changes. Once it closes, you can expect a couple of integration phases where we'll share a lot more about the pricing strategy. But the initial phases, we'll look to get Clearbit data into our customer base. And Clearbit is already in our app market. They already have an integration with HubSpot. They've already been working with our customers.

So I think it will naturally continue with what they currently have. And then medium term to longer term will more seamlessly integrate their data into HubSpot's products and use cases. And again, our vision is really how do we accelerate our customer platform with this data. And so we'll be very thoughtful and both in terms of pricing strategy, but also go-to-market. And we'll share a lot more once the deal has closed.

**Charles MacGlashing**

*Corporate Treasure & Senior Director of IR*

Thanks, Yamini. I think we've got time for maybe one more question. I know we have a bunch of people in the queue, but time for one more.

**Operator**

Absolutely. The last question is from the line of Ryan MacWilliams with Barclays.

**Ryan Patrick MacWilliams**

*Barclays Bank PLC, Research Division*

Just on your contract duration, are you seeing any customers at this point just from 1 year to monthly contracts? Just asking about the gap between the constant currency revenue growth and the constant currency billings growth? And then are you also seeing any differences in growth contribution from your direct sales force compared to your channel ecosystem this quarter versus the quarter prior.

**Kathryn A. Bueker**

*CFO & Treasurer*

Yes. Thanks for the question. We have been talking about duration for a number of quarters now as we talk about billings. And what we're seeing this quarter, what we saw in Q3 is very consistent with what we have been seeing for quite a bit of time now, which is a slight reduction in overall billing duration of the customer base. So nothing new there. In terms of -- I'll just -- I'll it close out in terms of the partner versus direct contribution, again, very similar. Partners continue to represent in and around 40% of the contribution to the business. They are an important channel for us and will continue to be so.

**Operator**

There are no additional questions left at this time. I will now hand it back to Yamini for closing remarks.

**Yamini Rangan**

*CEO, President & Director*

Thanks, everyone. I really appreciate all the effort by our employee partners, and thank you for your support. We'll speak to you all in the New Year.

**Operator**

That concludes today's conference call. Thank you. You may now disconnect.



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