05-Aug-2021

Datadog, Inc. (DDOG)

Q2 2021 Earnings Call

CORPORATE PARTICIPANTS

Yuka Broderick
Investor Relations, Datadog, Inc.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

David M. Obstler
Chief Financial Officer, Datadog, Inc.

OTHER PARTICIPANTS

Brent Thill
Analyst, Jefferies LLC

Sanjit K. Singh
Analyst, Morgan Stanley & Co. LLC

Sterling Auty
Analyst, JPMorgan Securities LLC

Kash Rangan
Analyst, Goldman Sachs & Co. LLC

Tyler Radke
Analyst, Citigroup Global Markets, Inc.

Matthew Hedberg
Analyst, RBC Capital Markets LLC

Kamil Mielczarek
Analyst, William Blair & Co. LLC

Brad Reback
Analyst, Stifel, Nicolaus & Co., Inc.

Jack Andrews
Analyst, Needham & Co. LLC

Ittai Kidron
Analyst, Oppenheimer & Co., Inc.

Michael Turits
Analyst, KeyBanc Capital Markets, Inc.

Gregg Moskowitz
Analyst, Mizuho Securities USA LLC

Raimo Lenschow
Analyst, Barclays Capital, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Q2 2021 Datadog Earnings Conference Call. My name is John. I'll be operator for today's call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. [Operator Instructions]

And I will now turn the call over to Yuka Broderick, Head of Investor Relations. Yuka, you may begin.

Yuka Broderick

Investor Relations, Datadog, Inc.

Thank you, John. Good morning and thank you for joining us today to review Datadog's second quarter 2021 financial results, which we announced in our press release issued this morning. Joining me on the call today are Olivier Pomel, Datadog's Co-Founder and CEO; and David Obstler, Datadog's CFO.

During this call, we will make statements related to our business that are forward-looking under federal securities laws and are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995, including statements related to our future financial performance, including our outlook for the third quarter and for the full year of 2021, our strategy, the potential benefits of our products, partnerships and investments in R&D and go-to-market, and our ability to capitalize on our market opportunities.

The words anticipate, believe, continue, estimate, expect, intend, will and similar expressions are intended to identify forward-looking statements or similar indications of future expectations. These statements reflect our views only as of today and not as of any subsequent date. These statements are subject to a variety of risks and uncertainties that could cause actual results to differ materially from expectations.

For a discussion of the material risks and other important factors that could affect our actual results, please refer to the quarterly report on Form 10-Q for the quarter ended March 31, 2021, filed with the SEC on May 7, 2021. Additional information will be made available in our quarterly report on Form 10-Q for the quarterly period ended June 30, 2021, and other filings and reports that we may file from time to time with the SEC. Our filings with the SEC are available on the Investor Relations section of our website. A replay of this call will also be available there for a limited time.

Non-GAAP financial measures will be discussed on this conference call. Please refer to the tables in our earnings release, which you can find on the Investor Relations portion of our website, for a reconciliation of these measures to their most directly comparable GAAP financial measures.

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

Olivier Pomel

Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

Thanks, Yuka. And thank you all for joining us for our morning call today. We are very pleased with our performance in Q2, which was stronger than expected on robust growth with existing customers as well as strong new customer sales. We saw real strength both across product lines and across customer segments.

For a quick review of the quarter, revenue was $234 million, an increase of 67% year-over-year and 18% quarter-over-quarter and above the high end of our guidance range. We ended the quarter with 1,610 customers with an ARR of $100,000 or more, up from 1,016 in the year ago quarter. Those customers generate about 80% of our ARR.

We have about 16,400 customers, which is up from about 12,100 last year. We also continue to be capital efficient with free cash flow of $42 million. And our dollar-based net retention rates continue to be over 130% as customers increase their usage and adopted our newer products.

We are pleased that positive business trends from recent quarters continued in Q2. First, usage growth from existing customers remained very robust. Among other factors, we continue to see the impact of our strong new logo growth in the past several quarters as those new customers grow into their commitment.

Second, new logo ARR was again strong, as we continue to execute against our go-to-market strategy.

And third, churn continues to remain low and in line with historical rates. Taking all these factors into account, we had a very strong quarter of ARR added, with over $100 million of ARR added for the second consecutive quarter.

Next, our platform strategy continues to resonate in the market. As of the end of Q2, 75% of customers are using two or more products, up from 68% a year ago. Additionally, 28% of customers are now using four or more products, which is up from 15% last year. And this quarter, approximately 70% of new logos landed with two or more products.

Our platform saw strong growth in the second quarter, which included another record of ARR added for infrastructure monitoring in a single quarter. This product is still early in its lifecycle. Meanwhile, we continue to see very strong performance with other products in our platform.

Our APM suite, including RUM and Synthetics and log management, together reached over $400 million in ARR. The APM suite and log management also remain in hyper growth mode, but our newer other products are growing even faster. As a result, we are very pleased with the customer uptake of our end-to-end observability platform as well as the beginning of our cloud security platform.

Now let's move on to product and R&D. Our teams continue to innovate and solve customer pain points. We announced 73 new features in Q2 and have continued to ship in Q3. To discuss just a few of these, we announced the general availability of two new security products, Cloud Security Posture Management and Cloud Workload Security, which target security issues around infrastructure.

Cloud Security Posture Management runs continuous configuration audit so customers can track conformance to industry benchmarks and regulatory standards. And Cloud Workload Security performs real-time threat detection directly within the workloads themselves within hosts and containers. These are our second and third GA products in security, alongside security monitoring, which performs threat detection on events and loading data streams.

With these offerings, the first building blocks of our cloud security platform are coming together, and we can start delivering on our vision to break down silos between DevOps and security teams. And with the addition of these two products, we now have 11 GA products on the Datadog platform.

We are also at the beginning of our opportunity to bring observability to the CI/CD space. And we announced the beta of our CI visibility product in late July. CI/CD is a combined practice of continuous integration and continuous delivery, allowing software to be consistently written, tested and released to production.

The problem is that developers also don't have visibility into their CI/CD pipeline. They have a hard time figuring out, the tests are falling and why, and where in their CI/CD pipeline they are experiencing bottlenecks and issues. Our CI visibility product, based on our acquisition of Undefined Labs last August, helps customers gain visibility into their testing pipeline with the goal of lowering costs and increasing efficiency for their developer teams. So, we are excited about those announcements, but we're not standing still on our existing products and we continue to expand features to make each and every one best-of-breed.

In Synthetics, we have enabled cross-browser testing and our customers can now test on Microsoft Edge and Firefox, in addition to Chrome. Mobile RUM will now support Android, iOS and cross-platform frameworks like React Native.

Our RUM product now covers the whole user space, including [ph] web (8:12) applications on desktop, mobile and tablets as well as mobile apps. And finally, we continue to improve the AI/ML capabilities of our platform with our most recent edition, including automatic detection of 4G deployments in APM and anomaly detection in security monitoring. These are complemented by the continued extension of Watchdog Insights, the recommendation engine we are embedding directly into our users' workflows across our platform.

As you can see, our end-to-end observability platform continues to broaden and deepen. Meanwhile, we are beginning to see – to move forward in our cloud security, and we are in the early days with our CI/CD use cases. As always, I want to thank our engineering and product teams for their creativity, their productivity and their continued ability to deliver the right solutions to our customers' problems.

Now moving on to sales and marketing. As hinted by our customer growth this quarter, our go-to-market teams continued to be very productive. So, let's discuss some more Q2 wins. First, we had an eight-figure upsell with a next-gen financial services company, which is experiencing a surge of traffic in their core application.

They rely on Datadog log management as the platform across the organization to find the root cause of issues. We saw a significant increase in usage of our existing products and recently added our Continuous Profiler to better understand their code performance in production.

Next, we had a seven-figure upsell with a European e-commerce company. They were using multiple commercial observability tools and one of their 2021 strategic initiative was to consolidate and reduce costs by standardizing on Datadog to satisfy that goal, while improving their team's collaboration and communication.

Next, we had a seven-figure upsell with a large global accounting firm. This company is experiencing rapid growth with their online product and its teams were forced to jump from tool to tool to try and mitigate problems. With Datadog as their chosen solution for infrastructure monitoring, APM and Synthetics, they are able to decrease mean time to resolution and free up internal resources.

Next, we had a six-figure upsell with a 30 years old analytics software company. This company is moving more work close to Azure. And with this new upsell, they standardized on Datadog for their log management needs. With our Logging without Limits functionality, this company will lower costs by an order of magnitude for log management without sacrificing any of their log data.

And finally, we had a seven-figure land with a large back-office software company. This company is growing rapidly and is planning a move to hybrid cloud. But their previous monitoring adoption rate was very low, which made it difficult for their teams to collaborate.

With Datadog, their entire team now has a single platform for all their observability needs, and they recognize Datadog's impact on improving adoption and alignment across teams.

So, as you can tell, we are incredibly proud of the performance of our go-to-market team this quarter, and I want to thank them for their hard work and for partnering with our customers to deliver another quarter of strong results.

Now moving on to our longer-term outlook. We see businesses now moving forward with their longer-term digital strategy. Businesses must increasingly be digital first. IT platforming remains in its early stages. And we believe we are in a great position to help our customers with our unified observability platform.

Meanwhile, we are making progress on our long-term vision to break down silos between DevOps and security teams. As a result, we are extremely excited about the opportunities we see to democratize data and help customers increase visibility and manage complexity. And we're confident in our long-term plans and continue to work hard to execute on our strategy.

Before turning the call over to David, I want to mention that our teams are busy preparing for Dash 2021, our user conference, which will be held in late October this year. Every year at Dash, we showcase our latest product innovations. And we're excited to show everyone what we've been up to this year. We also expect to hold an investor session at Dash. So, please look out for that announcement in the fall.

With that, I would like to turn the call over to our Chief Financial Officer. David?

David M. Obstler

Chief Financial Officer, Datadog, Inc.

Thanks, Olivier. In summary, we had a very strong Q2. Revenue was $233.5 million, up 67% year-over-year and up 18% quarter-over-quarter. Usage trends were strong and showed broad-based growth. New logo generation was also strong and customers continued to adopt more products across the platform.

To provide some more context. First, growth of existing customers was again robust in Q2, and our dollar-based net retention rate remained above 130% for the 16th consecutive quarter. Usage growth was strong, driven by customers' expanded usage of existing products and the adoption of new products.

Our customers are continuing to pursue their cloud migrations. And as we expand with our customers, we see opportunities for them to standardize on us and consolidate their observability tool vendors.

Next, we saw the second consecutive quarter of ARR adds over $100 million with broad strength across product lines, including our newer products, and strength across our regions. New logos were also very strong. We had a record number of both gross and net new logo additions in the quarter. Both our enterprise and commercial sales teams executed strongly in the quarter, and we continue to see broad opportunities across industries and customer size. Remember, that our – given our usage-based revenue model, new logo wins generally do not immediately translate into meaningful revenue, but do so over time.

Next, our platform strategy continues to resonate with customers and 70% (sic) [75%] (14:54) of our customers are now using two or more products and 28% of our customers are now using four or more of our products.

Lastly, churn remained low, in line with historical levels. Our dollar-based gross retention rates remain unchanged in the mid-90s and they are similar across our customer segments and products.

Billings were $270 million, up 69% year-over-year. And there were no pro forma impacts in the quarter. Remaining performance obligations, or RPO, was $583 million, up 103% year-over-year, driven by strong sales activity and increased contract duration. The increase in contract duration was driven by a higher mix of annual and multi-year commitments relative to the year-ago quarter.

As a reminder, multi-year commitments are billed annually, and we do not incentivize our sales force towards multi-year deals. Current RPO growth was also strong at over 80% year-over-year. I should note that we continue to believe revenue is a better indicator of our business trends than billings and RPO as those can fluctuate relative to revenue based on the timing of invoicing and the duration of customer contracts.

Now let's review the income statement in more detail. As a reminder, unless otherwise noted, all metrics are non-GAAP. We have provided a reconciliation of GAAP to non-GAAP financials in our earnings release.

Gross profit in the quarter was $178 million, representing a gross margin of 76%. This compares to a gross margin of 77% last quarter and 80% in the year-ago quarter. The year-over-year decrease in gross margin was due to investments in our product and platform innovation. We expect gross margin in the mid- to long-term to be consistent with our historical performance.

R&D expense was $71 million or 30% of revenue compared to 27% in the year-ago quarter. We continue to invest significantly in R&D, including high growth of our engineering head count. We're pleased that we are successfully executing on our hiring and onboarding plans in R&D.

Sales and marketing expense was $61 million or 26% of revenue compared to 33% in the year-ago quarter. We continue to make substantial investments in sales and marketing, but revenue growth has outpaced our investment growth. We had only a few in-person events in Q2, but we continue to plan for increased travel and event costs later in this year, of course, depending on local health and travel guidelines.

G&A expense was $16 million or 7% of revenue, down from 9% in the year-ago quarter. Operating income was $31 million, or a 13% operating margin compared to the operating income of $15 million or an 11% operating margin in the year-ago quarter. Although strong in the quarter, we are not optimizing for near-term margins as we see a large and dynamic market opportunity in front of us, and we are striving to invest heavily against that opportunity. But Q2, of course, demonstrates the efficiencies of our business model. Non-GAAP net income in the quarter was $32 million or $0.09 per share on 342 million weighted average diluted shares outstanding.

Turning to the balance sheet and cash flow. We ended the quarter with $1.4 billion in cash, cash equivalents, restricted cash and marketable securities. Cash flow from operations was $52 million in the quarter. After taking into consideration capital expenditures and capitalized software, free cash flow was $42 million with a free cash flow margin of 18%.

Now for our outlook for the third quarter and the full-year 2021. We are optimistic about our long-term opportunities and believe we will deliver high growth for the foreseeable future. We are addressing a very large market and are executing well against that opportunity. Taking this into account with the usual conservatism applied, we are updating our guidance as follows.

For the third quarter, we expect revenues to be in the range of $246 million to $248 million, which represents 60% year-over-year growth at the midpoint. Non-GAAP operating income is expected to be in the range of $18 million to $20 million, and non-GAAP net income per share is expected to be in the range of $0.05 to $0.06 per share, based on approximately 344 million weighted average diluted shares outstanding.

And then for the full year 2021, revenue is expected to be in the range of $938 million to $944 million, which represents a 56% year-over-year growth at the midpoint. Non-GAAP operating income is expected to be in the range of $87 million to $93 million.

Non-GAAP net income per share is expected to be in the range of $0.26 to $0.28 per share, based on an approximate 344 million weighted average diluted shares outstanding.

Now some notes on our guidance. First, while usage growth was strong in Q2, when providing guidance as usual we use more conservative assumptions. Second, our strategic focus remains on investing to optimize for long-term growth. We're planning for continued aggressive investments in R&D and go-to-market through the remainder of 2021.

And next, our model assumes a return to the office and the resumption of travel and in-person events during Q3. That said, we will remain flexible depending upon local regulations, and our highest priority is protecting the health of our employees.

Regarding items below the operating income line. First, we expect approximately $0.9 million of Q3 non-GAAP net interest and other income, which includes the interest income on our cash and marketable securities, and the interest expense on our convertible debt. We do not expect to be a federal taxpayer in Q3, but have a tax provision related to our international entity. And as a result, we expect a tax provision of approximately $600,000 in Q3 and $2 million for the full year.

To summarize, we are very pleased with our results this quarter. Customers continue to consume more Datadog, both using more of their existing products, and choosing to begin using new products.

We added two new products this quarter, and now have 11 products to offer to our customers. Our execution against our R&D and go-to-market goals remain strong. And our ability to help customers to manage through their cloud migration and digital transformation effects continues to grow.

And with that, we will open the call for questions. Operator, let's begin the Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. We'll now begin the question-and-answer session. [Operator Instructions] And our first question is from Brent Thill from Jefferies.

Brent Thill
Analyst, Jefferies LLC

Q

Good morning. If you could maybe provide a little more color around the large customer growth. The last two quarters, you had exceptional results in that segment. Maybe you can just give us a little more color on what you're seeing as these larger enterprises are standardizing on your platform?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yeah. So, we're still seeing some of those. I mean, I think, some of those we mentioned in the call in that category where customers were using something else before, a collection of different things, and they're [ph] landing (24:37) on our platform and which creates a larger land for us. But that's still not the vast majority of our customer acquisition.

By and large, we're still garnering smallish customers and going with them, and then they standardize with us later on, as they're further down the road in their migration to cloud environment. So, we feel – we see some of that in proportion that is comparable to – seen in different quarters, but we don't see any particular trend there yet.

Brent Thill
Analyst, Jefferies LLC

Q

And David, just in terms of the sales hiring plan that you have in the second half versus the first half, can you give us some color on your quota-carrying capacity and what you're expecting to add back half of the year?

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

Yeah. As we said previously, we're trying to grow our ramp quota approximately in line with revenues. And we had, as we said, throughout COVID last year and this year, we have aggressive hiring plans, which we are executing on. And we haven't changed our sort of goals for hiring and quota expansion throughout the last couple years.

Brent Thill
Analyst, Jefferies LLC

Q

Yeah. Thank you.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Just to rebound what David just said that we unlike many companies that have stops and starts, we get hiring steadily, which put us in a great position today. I think, right now, it's an interesting time for hiring because the retail market is very hot and there's also many people taking some time off. So, it's a lot of effort to grow at the level at which we want, but we're happy with the place we're in and we're very happy we made the choice to keep steadily recruiting throughout the pandemic.

Brent Thill
Analyst, Jefferies LLC

Q

Thank you.

Operator: Our next question is from Sanjit Singh from Morgan Stanley.

Sanjit K. Singh
Analyst, Morgan Stanley & Co. LLC

Q

Thank you for taking the questions and congrats on the impressive Q2 results. Olivier, what are the – see if I can get a little more understanding of a comment you made in your script around infrastructure monitoring still being in its early days. From your perspective, what drives that sort of sentiment around infrastructure monitoring? It's been your core product that was sort of the foundation of the company and you're saying that there's still a long runway ahead. Can you just expound upon that line of thinking a little bit?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yeah. I mean, there's two aspects to it. One is in terms of penetration, I think, the intersection of what we have and what's in the cloud in the next gen is still a small fraction of what there is in the market total. So, there's a lot more we can get from that.

The second aspect is that the world is transforming digitally. So, the market, like the overall size of the infrastructure that will have to be monitored five years from now is a lot bigger than what had to be monitored five years ago. So, when you [ph] multiply (27:44) those two things, there's a lot more ground to cover in terms of those market penetration. And so how much stuff we can cover with infrastructure monitoring.

In parallel to that, it's a field that is still evolving, right? There's still – the name of the game in the cloud is that there are ways of innovation and new ways of running workloads. And we've been through a few of those in Datadog. We started with cloud instances and then containers in our [ph] silhouettes. (28:08) We don't expect that to stop there. We think there's going to be new modalities for running infrastructure. And so, we're investing heavily in our products to be at the forefront of all that.

Sanjit K. Singh
Analyst, Morgan Stanley & Co. LLC

Q

Makes total sense. And as a follow-up, I think, one of the words that I heard multiple times in your script was standardization. And what we've been hearing from customers is that APM has really come into its own. How much of a driver has that been? And where would you put sort of the log analytics solution in terms of its maturity? They came out a year or two later after APM where does that capability and product stand from your perspective if we use APM as an analogy?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Well, I love how much it'd run the same. The APM and logs are neck and neck in terms of their adoption across our customer base, and I would say their level of maturity. Both products win in situations where we're starting with those products in the back of grid kind of set up by customers. And they both can serve as the second leg of the stool in managing the infrastructure to be the basis for standardization for customers. And so, what we see today, really proven at meaningful scale is that customers are standardizing on our offering. They buy into the platform. And the three main legs of that stool potentially are going to be APM, logs and infrastructure monitoring.

Sanjit K. Singh
Analyst, Morgan Stanley & Co. LLC

Q

All right. Great to hear. Thank you so much, Oliver.

Operator: Our next question is from Sterling Auty from JPMorgan.

Sterling Auty
Analyst, JPMorgan Securities LLC

Q

Yeah. Thanks. Hi, guys. Given the number of comments that you talked about usage in the prepared remarks is helping drive strength. Can maybe you spend a quick minute talking through – remember, we had the overages item in kind of the first half of last year. How is this different? And how is the kind of usage and consumption growing now?

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

I'll take that. I think, what we said was we had a flattening and an optimization in Q2 of last year. And since that time, which is now Q3 of last year through now, we've had a return to more normal or consistent with the long-term trends. And we continue to see that in Q2, a very strong and similar quarter to what we've seen in the last three, four quarters and very consistent with the company's long-term positions in that. And that is reflective, we feel, of a return to normal in the rolling out of cloud migrations and digital projects. And so, like we said in previous quarters, the usage growth was very widespread, balanced in products and in types of customers, very similar to what we've seen in the history of the company.

Sterling Auty
Analyst, JPMorgan Securities LLC

Q

All right. Great. And then one quick follow-up. In terms of the investment in go-to-market, when you gave guidance for this quarter, I think, similar items. Obviously, sales and marketing came in well below what I think ours and most forecasts had. Can you help give us a sense how much of the sequential increase that is baked into the guidance is from head count versus, as you pointed out, the return to office and the travel?

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

Yeah. Let me start with that. So, we said all along that we have two drivers. One is, in terms of sort of percentage of revenue in the marketing and sort of travel, sort of 3% or so – 3%-plus is sort of a benefit from not having that travel and the event. That does have some volatility depending upon whether you're in a quarter where you have re:Invent and Dash, which is what we're having in Q4.

Net, I think, we've performed, as you can see on the – in the revenue line, sort of above where we were planning. So essentially, we had a positive surprise in the revenues and that sort of drops down to the bottom line.

And second – and lastly, as Oli mentioned, we have very aggressive hiring plans. We are essentially trying to get that done this year. It takes a while to get that done in this market. And so, we expect that growth to accelerate, that sort of people side of things, to accelerate in the second half of the year. And we're already seeing that in our hiring numbers. But we have, over the last couple years, sort of ramped up into our hiring during the course of the year.

Sterling Auty
Analyst, JPMorgan Securities LLC
Q

Understood. Thank you.

Operator: Our next question is from Kash Rangan from Goldman Sachs.

Kash Rangan
Analyst, Goldman Sachs & Co. LLC
Q

Congratulations on extraordinary results. Really awesome to see this, Oli and David. My question is, as you really start to experience the benefits of standardization, what are the sales cycles looking like? And how do we expect the kind of hiring that you do to prosecute these options, which are showing up in the pipeline? And if you could, as a result, talk about how this gets Datadog into the upper end of the enterprise market, as things evolve over the next couple of years that will be great.

And also, if you do have the time to answer this, as the economy – if the economy opens up, your results are fantastic as they are. What could be the incremental benefit of the opening up of the economy where you get to travel and get out there? Thank you so much and congrats.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.
A

Thank you. So, I'll start with the standardization. At this point, it doesn't change our sales cycles too much, because the way we do it is, it mostly starts small and we grow with customers. And then by the time we standardize, we have a solid foothold at that customer and their engineers are using us all the time and it gets increasingly easier to make the case for standardization.

Obviously, there's going to be some changes over time as we cover more and more of the globe with our sales force and that we have customers that have more and more years with us. I do expect to make some changes over time to the way we operate. But at this point, there's no major tweaks to the sales process or the time it takes.

It does – like, the standardization does inform a road map from a product perspective because we are investing more and more in technologies that are not necessarily cloud centric. And we're doing that in order to help our customers who standardize bring some of their legacy IT or on-prem IT back into the – under the same roof as their cloud technology. So, this is something that informs that part of our development. And it will also, in all likelihood, inform some of our efforts around professional services and spending more time bringing those customers across.

On the question on the opening of the economy, I mean, look, we – what's interesting to us is that it looks like the – we're back to the way the world would move into the cloud more or less before the pandemic. And we don't know if things can go any faster. There seems to be some – there was a very steady historical trend for us there and we're back to that steady historical trend, so we're happy with that.

So the main thing that we're working on right now to maintain long-term growth is make sure that we keep building on the platform, so we can add more products, cover the full – solve the full problem or increasingly large part of the problem for our customers, while at the same time, scaling the go-to-market teams, so we can be in all of the conversations everywhere in the world for our customer segments. And we still have quite a bit of work to do in order to achieve that.

Kash Rangan
Analyst, Goldman Sachs & Co. LLC
Q

Thanks a lot, Oli and David.

Operator: Our next question is from Tyler Radke from Citi.

Tyler Radke
Analyst, Citigroup Global Markets, Inc.
Q

Thanks for taking my question. I wanted to ask you just about the pricing environment broadly. Obviously, a year ago, kind of in the depths of COVID, you saw some customers rationalize spend. Obviously, it didn't seem like that was an issue this quarter. But just how do you feel kind of longer term about your pricing strategy? And as you continue to innovate and build out new features, do you feel like you could potentially have that pricing power to charge even more over time? Thanks.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.
A

Yeah. So, I think, there's three parts to that answer. The first one is what we saw last year was not price pressure. What we saw last year was customers really seeing their cloud footprint with Amazon and Azure and the others. And these were the customers with the largest deals because that's how [indiscernible] (38:00) save money when they were facing a lot of uncertainty around cash and that we pull to us. That's one.

Two, when you think long term, the – it's almost a given that there will need to be a different way of charging for some of the – for capturing some of the value provided to customers. That can't just be attached to the straight volumes of data that are being exchanged, because those volume of data are exploding exponentially, while our customers' revenues are not going to explode exponentially. And so that's one thing that we're working on with all of our products.

We have this denomination for one of our products, Logging without Limits, which is basically a way to align the value customers get with the price they pay and give them leverage for that and make sure that we keep unbundling things on our end. So, we would give them the power to do that.

The third answer to that question is that, all the time we made the choice to add new functionality largely in the form of new SKUs when we saw new classes of problems for our customers, which is a way basically to maintain price and increase price as we grow and as we ship that functionality. We like the fact that it also gives us very good signal in terms of the value these products provide and have [ph] strived to get (39:23) the road map of those products.

Tyler Radke
Analyst, Citigroup Global Markets, Inc.
Q

Thanks. And just a follow-up on the competitive environment. Oli, I think you talked about just how customers are consolidating observability tools or maybe you kind of see that opportunity. Just as you've seen more of that, and obviously, the deal sizes have been really, really healthy this quarter, especially around the RPO growth, are you seeing kind of more kind of legacy observability solution replacements? Just help us understand as those deal sizes grow, what that means competitively for you guys. Thank you.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.
A

It's similar to what we've seen before. And the motion is really on-prem or legacy that is being consolidated into the cloud. That's what we see. So, we see that the same trend that we've seen in the past, there's nothing – there's no other very interesting comment to make about that today, but we see what we still see.

Operator: Our next question is from Matt Hedberg from RBC Capital Markets.

Matthew Hedberg
Analyst, RBC Capital Markets LLC
Q

Hi, guys. Congrats on the quarter. Thanks for taking my questions. Oli, obviously, you talked a little bit in your script about really building security portfolio of solutions. Obviously, a little different buyer than sort of core – sort of your core infrastructure or even logging products for that matter. Can you talk about sort of how you're building out the sales motion there and really, really how you see additional leverage there?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.
A

Yeah. So, the sales motion there is very much built on for now and what we had with observability. And as we're building those products, we're leaning on those customers that are already brought into the Datadog platform and that can self-select to start adopting from our security products. So, that's step one.

Step two will be as more and more of those products reach GA and reach the some initial critical mass to actually start pushing them more directly through the sales force. I think, for that, we're actually learning quite a bit from the Sqreen acquisition we've done recently. And we expect that, that will have some interesting things to do in the future. We don't have anything specific to share today, though.

Matthew Hedberg
Analyst, RBC Capital Markets LLC
Q

Got it. Okay. And then David, one for you. You noted in the call that you had a higher level of multi-year commitments. And obviously, we realize you don't necessarily push for that. Just wondering, what were some of the customer conversations that drove that behavior?

David M. Obstler
Chief Financial Officer, Datadog, Inc.
A

I think, it has correlation to larger customers who are investing more in Datadog as their standardized observability and want to commit long term. It generally is pulled from the client rather than we go out. Remember, when land and expand, we often see the motion of growing over time and amending contracts with more commitment. So, this is really more of a factor of enterprise customers and larger cloud natives committing to Datadog as a core platform and wanting that commitment to be longer term.

Matthew Hedberg
Analyst, RBC Capital Markets LLC

Q

Got it. Super helpful, guys. Thank you.

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

Yes, thanks.

Operator: Our next question is from Kamil Mielczarek from William Blair.

Kamil Mielczarek
Analyst, William Blair & Co. LLC

Q

Hi. Thank you for taking my question and congrats on the incredible quarter. So, it's great to hear about the platform expansion. So, you've embedded two offerings. You have Datadog Dash coming up in a few months. And yet research and development expense, I believe, is up 84% year-to-date. Can you give us more detail around the decision to accelerate the level of R&D spend? And how should we think about the pace of new product introductions? And given the increasing diversity of your offerings, what changes do you need to make to the sales organization to support the sale of these new solutions?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yes, we're investing as aggressively as we can on all fronts. So, we – when we have opportunities to accelerate the investment in R&D, which we've done through a few acquisitions also and this is actually largely show up in our R&D expenses on an ongoing basis, so we're doing it. We still think we are very early in what's a very, very, very large opportunity across observability, security, and we mentioned today also the – some of the developer use cases around CI/CD.

But also, later on, there's a lot of things we can do in real-time BI, maybe in [indiscernible] (44:23) – lots of different things we can touch on. So, we're very early. We intend to keep investing heavily in R&D for a very long time. In terms of the impact on the go-to-market is really where we'll see the first need for some changes in the – on the go-to-market side is as we stop pushing the sell side of the security product more aggressively. It hasn't happened yet. It's not something that we're doing today as those products just barely reached GA for a few of them, but it's something that we'll certainly do in the future. So, nothing to share today on that, but it's definitely something that we're working on.

Kamil Mielczarek
Analyst, William Blair & Co. LLC

Q

That's great to hear. And quickly, can you just give me an update on the competitive backdrop? Is there any change in who you're seeing on deals? And have win rates improved? And how might that vary by product? Thank you.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

So, it's very boring. We see the same thing as before. From where we stand, the company's landscape hasn't changed. And our focus is still mostly greenfield, new environments, cloud environments, teams that are going to start more with us and are going to grow with us until they standardize on us for just about everything they do. That's the motion, hasn't changed and/or the landscape around us hasn't changed that much either.

Kamil Mielczarek
Analyst, William Blair & Co. LLC

Q

Sounds good. Thanks and congrats again.

Operator: Our next question is from Brad Reback from Stifel.

Brad Reback
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. Thanks very much. As we think about new customer growth in the platform, is the recent cohort of new adds growing into their commitments faster? So, are they ramping faster than customers a couple of years ago?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

So, it depends a little bit because we also have some larger commitments on day one than we used to. We mentioned that in the previous – on the first quarter calls. So overall, the cores are larger, it starts larger. The ASPs are going up over time, generally. And – but the growth we see is very commensurate with what we've seen in the past in terms of growth in usage on the first month they're with us to 6 months and 12 months and everthing. So, it's a two-part event there.

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

And broadly speaking, when you look at the consistency of the net retention and the longevity of it, it's still very, very similar in the land and expand with cohorts expanding similar to previous periods, and very importantly, expanding for a long time. So, they last – the cohort expansion continues on for quite a long time, which is very consistent with what we've seen in previous periods.

Brad Reback
Analyst, Stifel, Nicolaus & Co., Inc.

Q

That's great. Thanks very much, guys.

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

Yeah.

Operator: Our next question is from Jack Andrews from Needham.

Jack Andrews
Analyst, Needham & Co. LLC

Q

Good morning and congratulations on the results. Oli, I was wondering as you continue to push more to security, what are the lessons learned from the previous conversions of the Dev and Ops personas that could be applied to gaining traction in DevSecOps? And how is this conversion to security perhaps different than when Dev and Ops merged that you need to account for?

Olivier Pomel

Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yeah. So, it's a great question. And there's a lot of commonality in that. A lot of it is about reducing friction and making things that otherwise we go out, look around a lot of it, there's a lot of different people involved and a lot of different departments involved to be very easy and that can do any harm. And so that's – we know how to do that. That's what we've done to our [indiscernible] (48:07) company. And so that's the first part.

The second part, though, is that the buyer is a little bit different, and in some cases, a buyer might need to be addressed a little bit differently. And that's something a few other of the questions touched upon earlier, so I won't repeat myself too much there, but it's still something that we're working on in terms of how we add that to the motion we have with for setting the platform.

Jack Andrews

Analyst, Needham & Co. LLC

Q

Thanks for that. And then just as a quick follow-up. Again, when we think about the broadening portfolio of your solutions, could you just update us in terms of just how you're keeping your sales force and your partner ecosystem just up to speed with their ability to understand the value propositions and the nuances of everything that you are offering these days?

Olivier Pomel

Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yes. So, it's a major effort. The – it's actually one of the areas, Adam, who joined us as the Chief Operating Officer recently. It's going to be a major area of focus today to make sure that we scale the team that does enablement and that teaches everyone on the sales team and all the go-to-market teams what the product offering is, and how it works, and who to bring in into every single deals that we understanding that you know how to match that product to the right customer. So that's one of his major area of focus. So, we're investing in that.

Jack Andrews

Analyst, Needham & Co. LLC

Q

Thanks very much.

Operator: Our next question is from Ittai Kidron from Oppenheimer.

Ittai Kidron

Analyst, Oppenheimer & Co., Inc.

Q

Hey guys. Great quarter. Oli, I want to follow up on the security questions and really talk about the 2 new announcements you've made: the posture management and workload protection. There isn't a security vendor at this point that doesn't have those solutions available as well. So even though the market is early, it seems like everybody is chasing this. Maybe you can help me think about what differentiation you can bring into the security space from your perspective? And also, I know it's still early, but perhaps maybe you could talk about the ARR contribution of your cloud security platform at this point?

Olivier Pomel

Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yeah. So, on the second one, I mean, we don't have anything to share here yet. We're actually – the only thing I can say is that we're very happy with the way it's trending and the way it's growing. And we'll probably share some more at some point, but we don't have anything to say today. On the differentiation, what we'd bring to those categories, we already are instrumenting all those workloads. So, we are present on those machines or agents are running there. The logs are being collected by us already. We already connect to all those cloud configurations. So, there nothing has to be done really by our customers to turn on security, and that's a major, major differentiator.

And we also have all the developers and all the ops people that are watching what we do all day. And they can get – they can consume the security sales as well. They can be part of the solution as opposed to living in a separate silo from the security team. They are tasked with securing those workloads. So, when you combine those two things, I think we have something that's very powerful, very different, and I would say, almost impossible for the competition that comes solely from instrumenting the workload for a security – from a security perspective to replicate.

Ittai Kidron
Analyst, Oppenheimer & Co., Inc.

Q

Very good. Good luck.

Operator: Our next question is from Michael Turits from KeyBanc.

Michael Turits
Analyst, KeyBanc Capital Markets, Inc.

Q

Hi, guys. First, obviously, a great quarter. The pricing discussion, so you talked, Oli, a little bit about the need to change pricing at some point. There has been in the market already some changes from some of the competitors in their pricing, which does seem aimed at commoditizing usage of data in particular. Has that had any kind of impact in terms of competition? And how does that relate to some of your thoughts about what you would do with pricing long term?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

No, it's – so we've seen some of that in the market, but it hasn't had any impact on us directly. But I should say that we are investing – we have been investing a lot in new models for charging customers and putting them in control of their spend and making sure that we're aligned with the volume adjustments of all data volumes they're producing. And that's a lot of what our without limit offerings are doing.

We started with that for logs. We're also doing more and more for APM and infrastructure, and that's something that our customers subscribe to when they standardize on us. I mean, we've mentioned that on the call, some of our customers are about to slash their spending on logs, in particular, because they can spend on what matters to them. They can get over there. They can capitalize and retain it.

We can only index some of it for some of the very basic purposes they need. They can make direct queryable on the main if they want it, like they can do anything they want. We'll give them all the levers, all the flexibility for that so that their bill doesn't grow linearly with data volume. So that's something we've already been investing in. So, it's not a big change for us, just a continuation of what we've been doing.

Michael Turits
Analyst, KeyBanc Capital Markets, Inc.

Q

And then, Oli, you made an interesting – you made an interesting point about legacy – investment in R&D for legacy replacement. I mean, we've done some of that in the past. So, what do you need to do from an R&D or product perspective to enable that? And are we at the point where that could unlock an upgrade cycle that would be very important to you?

Olivier Pomel A
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

I mean right now, we're still early in that, too. I mean we're connecting to all, sorts of, non-cloud equipment, so network equipment, physical network equipment, power distribution units, that sort of stuff. And we'll do more and more of it until we reach a point where a significant part of the market is maturing up in the cloud that it's time for them to standardize.

Today, I would say that the customers that standardize and bring their legacy IT into the cloud are still the ones that are at the fore – or were at the forefront of the cloud migration to start with their leading edge. So, they are signs of things to come, not that we are at that [ph] space (54:55) just yet.

Michael Turits Q
Analyst, KeyBanc Capital Markets, Inc.

Okay. Thanks, Oli. Thank, David.

Operator: Our next question is from Gregg Moskowitz from Mizuho.

Gregg Moskowitz Q
Analyst, Mizuho Securities USA LLC

All right. Thank you and I'll echo my congratulations on a very strong quarter. I guess, the first question, just regarding the cloud security platform. In addition to a la carte, is the plan to offer CSPM, CWS, security monitoring and app security as a suite as well?

Olivier Pomel A
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

There will likely be a few pricing options there. I mean, we haven't communicated any of that yet, but we're thinking hard about the various ways these products can be packaged.

Gregg Moskowitz Q
Analyst, Mizuho Securities USA LLC

Okay. And then, Oli, one of your competitors recently spoke about a large uplift in the number of deals closed with their hyperscaler partners such as AWS and Azure. Can you update us on your cloud partnerships and the go-to-market activity that you're seeing there?

Olivier Pomel A
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

So, we still continued to do with what we've been doing before. So, we're getting more and more from those cloud partnerships. And all of those cloud partnerships are developing more and more. We really see it on the GCP marketplace recently, where there – makes it easier for customers to deploy or partnership with Azure has taken another step forward recently also as we've been integrated directly into the console. There's still a few parts of that partnership that needs to be implemented. So, we're still not completely done yet, but there's still – we're still making progress on that. And we're also working on deeper partnerships with AWS. So, it's happening across the board and the things are trending in the right direction. And at this point, this is not a major part of our success, I would say it's more of a potential upside for the future.

Gregg Moskowitz
Analyst, Mizuho Securities USA LLC

Q

All right. That's great. Thank you.

Operator: And our next question is from Raimo Lenschow from Barclays.

Raimo Lenschow
Analyst, Barclays Capital, Inc.

Q

Thank you. Can you hear me okay?

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yeah.

Raimo Lenschow
Analyst, Barclays Capital, Inc.

Q

Yeah. Okay, perfect. Hey. Thanks for squeezing me in, and congrats from me as well. Olivier, can you talk – going to towards CI/CD now, it's obviously like it's a whole new market, but not many people have really come there before. Like can you talk a little bit about like, how this will play out for you? How big the opportunity is? Like how important it is? Because in theory, it's like that's where everything starts, but like I never thought about it from a monitoring or observability perspective? Thank you.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

A

Yeah. So, it's interesting. It's very early. We know the problem space is very big because engineers spend a lot of time wrestling with testing and deploying. And so, we know it's taking a lot of time and spending involved there. It's interesting to us because it pushes the boundary of where we operate also, and get closer and more closely embedded into the developer workflows, what happens on their laptop when they're writing code and the breaking test loops either on their own environment before they reach even development or steady environment. So, it's very interesting to us for that reason. It's more of a nascent category in terms of observing and optimizing those environments. So, we'll have to see exactly what the market opportunity is there, but we know the problem space is very large.

Raimo Lenschow
Analyst, Barclays Capital, Inc.

Q

Yeah. Okay, perfect. And then one question for David. You were 130% NRR number. You remember last year when the number came down a little bit, you mentioned it. Just – and I know you're not going to give me a number, but like trend-wise, is the number trending higher now? Is there a lag effect? Or like how do we think about it? I know, you're not going to give me a number, but just directionally within that 130% above, what are you seeing?

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

Yeah, we won't give you number, but help you a little bit in trends. Yeah, I think that we said the combination of the strong sales and the continued uptick from both use of more products on the usage side and adoption of products, combined with the compare from the flattening in the second quarter, has resulted in the point in time metrics there increasing in the quarter.

Raimo Lenschow
Analyst, Barclays Capital, Inc.

Q

Perfect. Congrats. Great news.

David M. Obstler
Chief Financial Officer, Datadog, Inc.

A

Yeah.

Operator: And I'll now turn the call back over to Olivier for closing comments.

Olivier Pomel
Co-Founder, Chief Executive Officer & Director, Datadog, Inc.

All right. Thank you. And just to close this call, I'd just reiterate that we are very, very pleased with our performance this quarter. And I also want to thank again all Datadogs worldwide for their very hard work and for a job really, really well done. So, thank you all.

Operator: Thank you, ladies and gentlemen. That concludes today's call. Thank you for participating, and you may now disconnect.