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# HubSpot, Inc. (HUBS)

Q3 2021 Earnings Call

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Good afternoon. My name is Jen, and I will be your conference operator today. At this time, I would like to welcome everyone to the HubSpot Q3 2021 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speaker's remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Chuck MacGlashing, Head of Investor Relations, you may begin your call.

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### Charles Tupper MacGlashing

*Vice President, Treasury & Investor Relations, HubSpot, Inc.*

Thanks, operator. Good afternoon, and welcome to HubSpot's third quarter 2021 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 the statements of historical facts are forward-looking statements, including those regarding management's expectations of future financial and operational performance, and operational expenditures, expected growth, the leadership transitions and business outlook, including our financial guidance for the fourth fiscal quarter and full year 2021.

Forward-looking statements reflect our views only as of today, and if – 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 the 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 2021 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?

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### Yamini Rangan

*Chief Executive Officer & Director, HubSpot, Inc.*

Thank, Chuck, and greetings, everyone. Thank you for joining us today as we review HubSpot's third quarter 2021 results. I hope you were all able to join us a few weeks ago for our Annual Analyst Day at INBOUND. We covered a lot of ground as part of those sessions. So today, what I want to do is to focus on the great results in

Q3, as well as the strategic pillars guiding us on our path to becoming the number one CRM platform for scaling companies.

Let's kick things off with a look at our Q3 results. We're continuing to see strong performance across the business, with revenue growth of 47% in constant currency year-over-year, and total customers growing 34% year-over-year to more than 128,000. As we've seen over the past year, small and medium businesses continue to embrace our modern CRM to connect with their customers, drive insights from customer interactions and transform their businesses for the digital age. Our strong results speak to the fact that HubSpot is providing the right foundation for these companies to scale.

At our Analyst Day, I provided an overview of our long-term growth strategy and introduced the four strategic pillars guiding our investments. So today, I'd like to share how our recent product announcements at INBOUND are helping us make meaningful progress towards our long-term goals.

Our first strategic pillar is to deliver a world-class front-office platform by investing in new and existing hubs as well as driving the extensibility of our platform. We're always looking for ways to address the evolving needs of our customers and expand our addressable market.

We'll continue to explore the development of new hubs, invest in anchor hubs like marketing and sales, and accelerate innovation around emerging hubs like operations hub. Earlier this week, we officially launched Operations Hub Enterprise. This is a great example of how we are accelerating innovation in emerging hubs.

As you all know, we first launched Operations Hub Starter and Professional earlier this year to help customers get all of their data into HubSpot and build more advanced automated workflows. Now with Operations Hub Enterprise, our customers are able to report on that data in more connected and consistent ways to generate insights to drive growth.

We also announced important improvements to Service Hub, including custom surveys and a new customer portal that's currently in public beta. We'll continue to invest so that our individual hubs are powerful and easy to use.

But, we also know that much of HubSpot's magic comes from how our hubs seamlessly work together. And with more than half of our customers adopting multiple hubs, we know that more and more companies are realizing the unique advantage that comes from managing their entire front office in one platform.

A great example of this multi-hub approach in action is Triage, a staffing agency that arranges assignments for traveling nurses across the US. After connecting its back-office systems to our platform and implementing our marketing, sales, CMS and Operations Hub, Triage has seen increased efficiency and performance across the company.

Their e-mail click-through rate double, their sales team's capacity grew by 60% and they are now able to quickly mobilize for flu or COVID vaccinations. There is still plenty of runway left, when it comes to going broad and deep with our hubs and platform. I'm really excited to see where the needs of our customers will take us next.

Our second strategic pillar is to strengthen our segmentation approach across product and go-to-market. And this is driving product innovation at HubSpot in two key ways. First, we're bringing high-end features that have traditionally only been available to large enterprises down to our small and mid-market customers. And second,

we're bringing a human-friendly product and purchasing experience, traditionally seen in small and mid-market businesses up to large enterprises.

At INBOUND this year, we focused on the latter half of the strategy, announcing new, powerful and easy-to-use features that add tremendous value to our enterprise tier. In addition to new platform-wide governance features, like permission sets and audit logging, we also launched sandboxes, a feature that enables customers to test changes to their portal without impacting their primary account.

In Marketing Hub Enterprise, we introduced business units, a new feature that enables customers to manage multiple brands to ensure a more consistent and targeted experience for their audiences.

And new enterprise-level forecasting tools in Sales Hub and Service Hub, help managers keep track of their team's progress towards their goals. All of these enhancements help our larger customers customize their usage of HubSpot without adding complexity as they continue to grow.

We're seeing success in our segmentation approach. On the high end, we are consistently closing more large deals and have seen an 81% year-over-year increase in Q3 large deals. Our starter addition is also fueling customer acquisition. That segment has grown from a small percentage of our customer base a few years ago to more than 50% of our total customers as of Q3.

Now, let's turn to our third pillar, investing in commerce and payments. As I discussed during our Analyst Day, commerce has traditionally been thought of as an extension of the back office. It was sold to finance leaders. It was about collecting revenue and driving cost efficiencies. But commerce as a part of CRM is fundamentally different and it's about enabling growth, not saving money.

We're excited about the long-term opportunity for an integrated payment solution. That said, we're still in very early stages of this opportunity, and there are years of runway for growth. For now, we're focused on reaching US-based B2B companies with fewer than 100 employees so that we can deliver a strong product to market fit before expanding internationally.

Having the product market fit in one geography ensures that when we go international, we're able to capture a significant portion of GMV of any country we enter. And while it's only been available for about a month, we have seen nice momentum with our open beta as customers tap into the ability to quickly and easily start taking payments.

One early adopter is ZenPilot, an operations consulting business that needed to scale operations, but was being held back by a labor-intensive payment system. ZenPilot's previous system could only process credit card transactions and required manual work to process payments via ACH.

With HubSpot Payments, ZenPilot is able to accept ACH payments with ease. The sales team is able to focus more on lead generation activities and therefore, have increased leads by 30%. The early feedback from customers like ZenPilot is evidence that we are on the right path in enabling our B2B customers to deliver a consumer-grade buying experience. I'm very excited about what the future holds for HubSpot Payments in the long-term.

Our fourth and final pillar is to continue to scale HubSpot. As you've heard Brian and Dharmesh say before, we want to build a company that future generations can be proud of. As part of that vision, we're investing in hiring

and growing diverse talent, working on our environmental initiatives, and doubling down on protecting our customers' data and scaling our systems to meet their needs.

By investing in these four pillars, we're building a strong foundation that will serve both HubSpot and our customers as we chart our next phase of growth. I'm incredibly excited about our long-term opportunity, and I'm very confident that we have the right strategy, the right investments and the right team in place to help us execute and win.

With that, I'll turn it over to Kate to give an overview of our fantastic financial results. Kate?

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## Kate Bueker

*Chief Financial Officer, HubSpot, Inc.*

Thanks, Yamini. Let's turn to our third quarter financial results and our guidance for the fourth quarter and full year of 2021. Third quarter revenue grew 47% year-over-year in constant currency and 49% as reported. Q3 subscription revenue grew 49% year-over-year, while services and other revenue increased 39%, both on an as-reported basis. The momentum we've seen over the last 1.5 years continued into the third quarter with broad strength across the business. We saw continued strength in revenue retention in Q3, trending nicely above our new target level of 110%, with healthy customer dollar retention continuing to be a big driver of our overall strong retention performance.

Net revenue retention also continues to benefit from multiple upgrade drivers, including strong cross-sell activity and seat expansions. Domestic revenue grew 41% year-over-year in Q3, while international revenue growth was 54% in constant currency and 58% as reported. While our international and domestic revenue growth rates in constant currency remained flat quarter-over-quarter, international revenue as a percentage of total revenue increased three points year-over-year to 46%.

We added 7,100 net customers in the quarter, growing our total customer count by 34% year-over-year to 128,000. Average subscription revenue per customer grew 9% year-over-year to \$10,500 as we saw a continued positive mix shift towards our professional and enterprise tiers, along with strong installed base selling.

As we've discussed over the last couple of quarters, we expect these trends to continue into Q4 with net customer additions of about 7,000 and high single-digit year-over-year growth in ASRPC. Deferred revenue as of the end of September was \$376 million, a 45% increase year-over-year. Calculated billings was \$353 million, growing 45% year-over-year in constant currency and 43% as reported. Billings growth in Q3 was impacted by the strong installed base selling mix in the quarter, slightly lower billing duration and a more difficult comparison as a result of COVID-related customer plays in the year-ago period.

The remainder of my comments will refer to non-GAAP measures. Third quarter gross margin was 80%, down two points year-over-year as a result of increased customer usage and the launch of our new EU data center. Subscription gross margin was 83%, while services gross margin was negative 9%. Third quarter operating margin was 10%, up two points compared to the same period a year ago.

At the end of the third quarter, we had nearly 5,500 employees, up 38% year-over-year. Net income in the third quarter was \$26 million or \$0.50 per fully diluted share. CapEx, including capitalized software development costs, was \$16 million or 5% of revenue in Q3. Free cash flow in the quarter was \$38 million or 11% of revenue. We continue to expect CapEx as a percentage of revenue to be about 5% in 2021 and now expect free cash flow to be about \$180 million for the full year. Finally, our cash and marketable securities totaled \$1.3 billion at the end of September.

And with that, let's dive into guidance for the fourth quarter and full year of 2021. For the fourth quarter, total revenue is expected to be in the range of \$356 million to \$358 million, up 42% year-over-year at the midpoint.

Non-GAAP operating income is expected to be between \$34 million and \$36 million. Non-GAAP diluted net income per share is expected to be between \$0.52 and \$0.54. This assumes 50.9 million fully diluted shares outstanding. And for the full year of 2021, total revenue is now expected to be in the range of \$1.287 billion to \$1.289 billion, up 46% year-over-year at the midpoint.

Non-GAAP operating income is now expected to be between \$113 million and \$115 million. Non-GAAP diluted net income per share is now expected to be between \$1.76 and \$1.78. This assumes 50.7 million fully diluted shares outstanding.

As you adjust your models, keep in mind the following: At current spot rates, we expect FX to be a slight headwind to as-reported revenue in Q4 and still expect a three-point tailwind for the full year.

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

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## Yamini Rangan

*Chief Executive Officer & Director, HubSpot, Inc.*

Thanks a lot, Kate. Before we wrap up, I want to extend a huge thank you to our customers, partners and employees for your support over the last quarter. It was such a joy to connect with you all during INBOUND, and I have felt so welcomed and energized as I transitioned into the CEO role.

As you heard me talk about at INBOUND, we're now in the age of the customer, customers want and expect a frictionless connected consumer-like buying experience at every step of their journey. Fortunately, we've been building for this new era at HubSpot and are uniquely suited to meet the moment as evident in this quarter's strong financial results.

Our most recent product announcements are designed to help companies create customer relationship magic and our four strategic pillars will enable us to continue to deliver on our mission of helping millions of companies grow better in the future.

And with that, operator, please open up the call for some questions.

## QUESTION AND ANSWER SECTION

**Operator:** [Operator Instructions] Your first question comes from the line of Alex Zukin with Wolfe Research. Mr. Zukin, your line is open.

**Alex Zukin**

*Analyst, Wolfe Research LLC*

Q

Hey, guys. Thanks so much and congratulations on a great quarter. Yamini, maybe the first one for you, particularly on the demand environment. Can you talk about what you saw in the quarter? Did you see any seasonality, summer holiday weakness internationally?

And then obviously in the news, we're hearing, we see headlines of supply chain issues. You hear the reports of the advertising companies, having a little bit of consternation. Are you seeing any impact from that at all? And any commentary on kind of the pipeline for either new customer growth or existing customer expansion into Q4?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Hey, Alex, thanks a lot for the question. We are seeing the same headlines that you mentioned in terms of supply chain challenges, macro environment. But I'll say that there's not a set of factors that have outsized exposure to here at HubSpot. In terms of the demand environment and the demand patterns, it's really solid. And if I step back and look at why we feel very good about the demand environment, it's two things.

One, the world has changed since the start of the pandemic, customers have looked for digital solutions and the buyer expectations have changed pretty significantly where they need a consumer-like buying experiences. They want to be able to connect to their customers digitally and they want to be able to grow and accelerate growth in this environment. And two, we have the perfect solution for that. HubSpot has a very unique value proposition. We have crafted the solution and we provide consumer-like user experience with enterprise-grade features, and that is resonating really well in terms of the market. So I feel very good about the demand environment and what we are seeing in the pipeline. And this reflects both across our North America business as well as international business. So feeling pretty good.

**Alex Zukin**

*Analyst, Wolfe Research LLC*

Q

Got it. And then that's super helpful. And Kate, for you, I mean, I think look, one of the questions I know I'm going to get tomorrow is for the last, I don't know, call it, six quarters or so, billings has been ahead of revenue growth in the quarter, even on an adjusted basis, from a constant currency perspective. This quarter, you mentioned there were some headwinds on the billings that is important to take into account. So maybe can you just walk through them, particularly on the deferred side what you're seeing and why it's not necessarily indicative of – I mean it's usually not indicative, but in this case specifically, why it wouldn't be indicative of kind of the way to think about future revenue growth, because I think your guidance suggests again, also very strong growth for Q4 subscription revenue?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A



Yeah. Sure thing. I would just start by saying that we actually feel really good about delivering constant currency billings growth in the mid-40s, especially when you look at the sort of tougher comparison that we have here in Q3 relative to Q2, it's basically 12-or-so points more difficult. That's what I did mention a few things that were headwinds to constant currency billings in the quarter. There's a little bit of a headwind from duration. And you may recall in my prepared remarks that I noted that this was a very strong installed base selling quarter that also has a little bit of a headwind as it relates to billings. Particularly around deferred revenue, FX on deferred is very tricky. And you may recall, in particular that the euro weakened against the dollar pretty dramatically over the course of Q3. And so the impact on deferred revenue from FX was much more acute. There is about a four-point headwind to deferred revenue on a constant currency basis versus an as-reported basis.

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**Alex Zukin**

*Analyst, Wolfe Research LLC*

Q

Got it. That's super helpful. Thank you, guys. Congrats, again.

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**Charles Tupper MacGlashing**

*Vice President, Treasury & Investor Relations, HubSpot, Inc.*

A

Operator?

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**Operator:** Your line is open [ph] Mr. Morgan (23:12).

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**Charles Tupper MacGlashing**

*Vice President, Treasury & Investor Relations, HubSpot, Inc.*

A

Hey, [ph] Mark (23:16), are you there?

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Q

Yes, I'm here. Sorry, I never heard my name called. So I don't know if I was disconnected for a moment.

[indiscernible] (23:24 – 23:29)

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Q

No, worries. Yes. I'm flattered to be called [ph] Mr. Morgan (23:34). So Yamini, at the Analyst Day, you had mentioned the touchless sale. And I think the fact that most B2B companies haven't started on it yet. I'm wondering how is that vision of the touchless sale resonating with your customers who are in this open beta of HubSpot Payments? And what is their feedback to you so far?

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**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Yeah, great question, [ph] Mark (24:02). So at the Analyst Day, what I said was that in terms of B2B, there are two ways that companies typically sell. One is the touchless sale and then the other is the rep-assisted sale.

Now, in terms of touchless sales, B2B companies haven't just gotten started in terms of online processing of services and software. And our hypothesis is that we can really help them and enable new revenue streams for our company.

Now in the prepared remarks, I mentioned an example of a company, ZenPilot. They are in the consulting business. They wanted to start processing. And that's an example of a touchless sales.

In terms of the open beta, that's also where we are seeing interest, [ph] Mark (24:53). We're seeing companies that are in services that are thinking about new online revenue streams that haven't done it before, and this is an easy and seamless way for them to grow. It's pretty early days. We've been in open beta just for a few weeks here now, but we're definitely seeing interest in terms of opening new revenue streams. So we'll keep watching.

Q

Okay. Understood. And as a quick follow-up, Kate, we're noticing the growth is superb. Sequentially, revenue growth is actually stronger than pre-pandemic in Q3. So, it's interesting to see the growth is stronger without reliance upon a blowout number of customer adds.

So I'm just curious where are you seeing the ASP increase most noticeably? Part of what I'm wondering is custom objects unlocking some of the larger accounts at the top of your target range with the Enterprise Hubs of sales and marketing? Or is it more across the board or even more kind of down market?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yeah. Thanks for the question. I think the good news is that our KPIs of customer additions and ASRPC kind of came in exactly where we told you that they were going to. We did see that nice pickup in ASRPC, really in that high single-digit range.

And again that positive momentum in ASRPC is a mix-driven calculation, the customer mix is moving towards that Pro and Enterprise. And we – again, I had the strong installed base selling commentary for Q3. And both of those things are like key drivers of ASRPC growth.

Q

Excellent. Thank you very much and congrats on a great result.

**Operator:** Your next question comes from the line of Samad Samana with Jefferies. Your line is open.

**Samad Samana**

*Analyst, Jefferies LLC*

Q

Hi, good evening. And I'll echo the congrats on just a great quarter, even as the comps get tougher. So maybe first, Yamini, for you, I have a follow-up on the payment side. Can you talk about the front-office CRM approach HubSpot is taking to payments and the advantages that HubSpot has over other more entrenched back-office-centric competitors that are more closely tied to accounting systems?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Thank you, Samad. That's really like my favorite question about payments, because the way we think about payments, commerce as part of CRM is fundamentally different. It is about enabling revenue growth for our

customers. And it's very, very different from commerce as part of back-office, where traditionally, it is about talking to the finance leader and focusing on collecting revenues and cost efficiency. And over the past few quarters, as we have gone back to our customers and ask them how we can enable growth, it became really clear that we needed to embed commerce and payments as part of CRM.

And there are three ways in which we can drive that growth. The first one is what I just talked about with [ph] Mark's (28:19) question, which is enabling new revenue streams. So if you think about touchless, this is not where B2B companies have traditionally focused, and so we want to enable new revenue streams and provide opportunities for growth there.

The second area for growth is really helping with the rep assisted last mile sales. So what I mean by that is HubSpot historically, we have focused on rep-assisted sales. But the last mile, which is core to cash has been the hardest nut to crack. And we want to focus on that. We want to streamline, simplify it so that the reps can now focus on growth initiatives, on demand generation activities. And so we do that right, we're going to actually enable growth for our customers.

And then the third thing which I'm super excited about is commerce brings context to every customer interaction. If you can imagine, having a commerce object deeply embedded within CRM, you now have more information when you run marketing campaigns. You can run marketing campaigns on abandoned cart. You have much more information in terms of sales interactions because you know where the invoice stands. You have much better service interactions, because it's prioritized by the purchase history. So commerce deeply embedded CRM is just really valuable in terms of enabling growth. And so I think we're taking a very different approach and enabling growth for our customers. So I'm excited about the longer-term opportunity here.

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**Samad Samana**

*Analyst, Jefferies LLC*

Q

Very helpful. And then maybe a follow-up for Kate. Hey, Kate, the 47% growth on constant currency staying the same quarter-over-quarter despite a tougher comp was impressive. And I think one of the things related to that is the stat around an 81% increase in large deals in the third quarter. I haven't really heard the company talk about large deals, more just, which SKU is being adopted. So I'm curious if you can maybe just help us understand how we should think about large deals and how you're defining it? And then maybe just how should we think about that going forward from a contribution standpoint?

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**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yes. I think I talked a little bit about that at the Analyst Day when we tried to highlight the strategic pillar around segmentation. Internally, we look at what we call large deals as anything that is greater than \$3,000 MRR. And we've seen that the volume of those deals increased 81% year-over-year.

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**Samad Samana**

*Analyst, Jefferies LLC*

Q

Okay. Great. Thanks, again, for taking my questions

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**Charles Tupper MacGlashing**

*Vice President, Treasury & Investor Relations, HubSpot, Inc.*

A

Thanks, Samad.

**Operator:** Your next question comes from the line of Ken Wong with Guggenheim Securities. Your line is open.

**Ken Wong**

*Analyst, Guggenheim Securities LLC*

Q

Great. Thank you for taking my question. First question, I just wanted to get a sense for – I think earlier it was mentioned some of the advertising peers out there are running into kind of the occasional issues with IDFA. How do you see that potentially impacting HubSpot's business? Does that push customers more towards an INBOUND strategy? We'd love to see if you guys are running in any tailwinds, headwinds on that front?

**Dharmesh Shah**

*Co-founder, Director & Chief Technology Officer, HubSpot, Inc.*

A

Thanks for the question, Ken. So just taking a step back, the reason we get into trouble sometimes in our personal lives, get sent to the doghouse is when we forget things like an anniversary or birthday. The reason we get sent to the doghouse in a privacy-centric world is when we remember and know too much. And that's, I think, what's caused some of the recent developments here.

Now having said that, HubSpot's genesis in the beginning, as you noted, has been around this idea of INBOUND marketing, which is a very kind of consumer-friendly privacy-forward approach. And we've kind of stuck to that for all 15 of our years. So as developments have happened in the industry that are kind of moving privacy forward, they've been neutral to positive to HubSpot.

And some of the recent developments, I don't think are any different, specifically on some of the app tracking stuff that's happened recently, the companies most impact are the ones that if you're running a massive advertiser network, or you're running a massive mobile applications for which tracking is super important, you're going to feel the direct impact of some of these recent changes. HubSpot doesn't fall into either those categories. So we don't really expect any meaningful impact on our business at all as a result of some of these developments that are happening.

**Ken Wong**

*Analyst, Guggenheim Securities LLC*

Q

Got it. Got it, I really appreciate that Dharmesh. And then, Kate, just thinking about the shape of the quarter, I think in the past, you guys had mentioned that, I think, in July, HubSpotters were given a break also potentially saw higher than typical PTO. Any sense of kind of how the kind of the linearity played out from July through September and to the extent that you can comment on October, November kind of how that demand life cycle look?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yeah. I mean, I think I'll pick the Q3, but you're exactly right and have a great memory. We made a decision to give the organization a break at the very beginning of the quarter, and we had a global [ph] decompressed (33:35) for all of our employees.

And that obviously creates a bit of a slow start to the quarter. We feel great about where we landed for the full quarter, but we definitely saw momentum in the second couple of months as a result of that, I would say well-deserved break on behalf of our employees.

**Ken Wong**

*Analyst, Guggenheim Securities LLC*



Got it. Perfect. Thank you so much.

**Operator:** Your next question comes from the line of Stan Zlotsky with Morgan Stanley. Your line is open.

**Stan Zlotsky**

*Analyst, Morgan Stanley & Co. LLC*



Perfect. Thank you so much, guys. I wanted to touch on the Payments business a little bit. I'm sure you're getting a lot of questions from investors on that one. How are you thinking as far as like disclosing the traction that you're seeing in that business as it starts to ramp? What are the milestones that we should be looking for and you'll be looking for, as far as really just broadening out the initial set of customers that are involved in the beta program?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*



Stan, thanks for the question. I'm going to maybe address this from a broad strategic perspective. And then, I'll have Kate to address it in terms of how we'll be tracking it. As you heard us talk about at the Analyst Day, this is a long-term opportunity that we are very, very excited about.

And specifically, we have a targeted approach. The target market that we're going after US companies with 100 employees or less that are B2B, mostly focused on services and software. The reason we are focused on that market is, first, it allows us to build a delightful product experience that customers can love.

And even within that market, we see it as a pretty large market, tens of billions in GMV within that segment. And we want to start with that market. And we're going to make sure that in terms of both the payment features as well as commerce features, we are focused delivering and driving market adoption. And I think longer term, there is a significant opportunity for us to grow both upmarket domestically as well as international. And I'll pass it to Kate, so she can address your question on how we will track and [ph] share overall (36:07).

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*



Yes. Thanks, Yamini. So if I just take a step back and look at the specific customer segment that Yamini outlined in the US-based customers with 100 or less employees in that sort of B2B software and services space, Yamini said we think that's a tens of billions of dollars of GMV market for us. And that would translate into something that looks more like hundreds of millions of potential payment volume for us over the next couple of years.

And as I covered at the Analyst Day, HubSpot is going to earn a transaction fee on this payment volume. And the amount of that transaction fee is going to depend on the payment method. It's going to depend on the transaction size, and we will recognize that fee as revenue to HubSpot. There'll be an associated cost with that transaction, most notably for credit card transaction that interchange fee. And so, the gross margin for the Payments business is going to be a much different and lower gross margin than what we're used to on the software side.

That said, the sales expense in growing the business is also going to be very different than the core software business, and we feel really good about the overall margin for HubSpot over time with respect to payments. We will likely in the near term record any revenue under that what we call services and other revenue stream. And as we ramp up over time, we will have to evaluate when it is the appropriate time to break that revenue out.

**Stan Zlotsky**

*Analyst, Morgan Stanley & Co. LLC*

Q

Got it. Got it. And then, Kate, just wanted to go back to billings for a quick second. I mean I think you did a great job of outlining the FX – material FX headwind to billings at the end of the quarter versus the FX tailwind that we actually saw in revenue. But just on the duration component of billings, if you were to kind of just put together the overall kind of headwinds that you saw in the quarter to billings between FX and duration, which one was the more material one? And kind of maybe give us a little bit of a magnitude of what the billings duration headwind may have been as well?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yes. So, the FX headwind to billings overall was 2% headwind, right? And that's a combination, as you are indicating of a tailwind to revenue with a more extreme headwind to the deferred revenue component of billings. In terms of the relative impact of duration versus FX. I think it's a combination of duration and the fact that, that we have a higher mix of installed base selling that sort of make up the other part of the difference between constant currency revenue and constant currency billings.

**Stan Zlotsky**

*Analyst, Morgan Stanley & Co. LLC*

Q

Got it. All right. Thank you so much, guys. Congratulations on a good quarter.

**Operator:** Your next question comes from the line of Brad Sills with Bank of America Securities. Your line is open.

**Brad Sills**

*Analyst, BofA Securities, Inc.*

Q

Oh, great. Thanks, guys, for taking my question. Congratulations on a nice quarter. Maybe I'll ask another question on the ASP question in another way. With the kind of growth you're seeing there, net revenue retention has been accelerating now for several quarters. Are customers landing with multiple hubs more so than in the past? I think historically, we think of HubSpot where a customer will start with marketing or sales or CMS, those are great entry points. And then, you'll see the cross-sell a year or two later.

Now that you're kind of moving upmarket in these more enterprise additions, are you seeing customers commit to multi-hubs kind of an initial land deal more so? And what does that mean for kind of future expansion opportunity potentially?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Brad, thanks for the question. I'd say that we see three things that happen across our customer base. The first is what you said, which is more multi-hub. And you can see that reflected in the numbers that Kate shared at the Analyst Day. And so we definitely see the multi-hub customers land. We're seeing still really good front doors with marketing, sales hubs. Each of those hubs has gotten really good over the past 12 to 18 months and so they are very good front doors. And so we see that land and expand motion.

And then as you know, we launched the CRM suite, both at the starter level as well as the go level and those are also really good front doors. And so across the board, we are seeing all three motions.

Now, I will say in terms of multi-hub, when our customers adopt multi-hub, the value that they get, because it's a seamless user interface, because it's a single data model, because there is a single view of the customer is just much higher.

We see when customers adopt Sales Hub plus Marketing Hub, they get much more leads, when they just had Marketing Hub or Sales Hub alone, the same powerful combination with Marketing Hub and CMS Hub or Sales Hub and Service Hub.

And so I think what you're seeing is that, there are great front doors into adoption. There is also a growing trend towards multi-hub as well as suite adoption, the combination of all three are kind of what you see as the results in terms of ASRPC growth.

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**Brad Sills**

*Analyst, BofA Securities, Inc.*



Great to hear. Thanks, Yamini so much. And then one on the Service Hub, if I may, there's kind of a view that service – customer service is more of an upmarket-type solution, small business don't necessarily run a separate support desk, [indiscernible] (42:22) a lot of it can be done within sales.

As you guys – well, one, do you agree with that view? And then two, as you guys are moving into this kind of up-market business, more enterprise focused, could we expect perhaps an acceleration? We've already seen good strong results out of Service Hub, but potentially even greater attached there? Thank you.

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**Dharmesh Shah**

*Co-founder, Director & Chief Technology Officer, HubSpot, Inc.*



Yeah. So in terms of Service Hub adoption or interest on the lower end. We don't think it's relegated just to larger enterprises. We think an increasing number of customers want to provide online support, even if it's not a call center, it might be over e-mail or over a chat. And so that is definitely a need.

In terms of Service Hub, the product is doing really well. And the path that we're kind of progressing is similar to what you saw with Sales Hub over the last several years, which there are some key features that we're looking for in Sales Hub for instance, custom objects was one of them.

And once we start knocking those domino's over, we see the adoption rate go up. And then we see that Hub becoming on ramp and front towards the upside platform. We're seeing something similar will happen with Service Hub. We just recently launched a recent INBOUND, the feature of a customer portal where customers can log in and see their tickets and interact with their data and with their accounts.

That was one of those big domino's in our minds that the customers have been kind of asking for repeatedly and it puts us further down the path where we need to be. So we think 2022 is going to be an exciting year for Service Hub. The market opportunity is massive across our sector of 1,000 to 2,000 employee customers, and we sort of know what the customer needs are, and we're just looking at that SKU.

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**Brad Sills**

*Analyst, BofA Securities, Inc.*



Great to hear. Thank, Dharmesh.

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**Operator:** Your next question comes from the line of Brian Peterson with Raymond James. Your line is open.

**Brian Peterson**

*Analyst, Raymond James & Associates, Inc.*

Q

Hi. Thanks for taking the question. I actually wanted to follow up Yamini, your answer to Brad's question. And I'd be curious to what extent customers are really kind of understanding of what this new frontier is going to look like for digital engagement models? And I say that because are they still at the point or I guess are they at the point now where they're willing to kind of buy, not even just 1 or 2, but 3 or 4 hubs at once, right? Or are they seeing that digitally across all hubs or all channels – or is it – do they have the vision? Or are they still going to have to kind of pick one at a time just given maybe their limited ability to execute. I'm curious what you're hearing from customers in regards to this new frontier in terms of digital engagement?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

It's a good question, Brian. I think it's across the board, the levels of maturity within our customer base are quite different. So you have some customers that are pretty early, and this – they've realized in the past couple of years that they need to be digital-first, digital-ready, and they are kind of putting their toe and starting with one hub and then expanding.

And then there are customers like the use case example that I gave in the prepared remarks of Triage where they realize that they need complete digital front office platform that is all in one in order for them to be able to accelerate their growth given all of what they're seeing.

And so it really depends on the maturity of the customers. The one thing that I would say is that our approach has been resonating really well with customers. We've taken a very, very different approach to building, hand crafting our solutions, and it's unique. So customers don't have to cobble together a bunch of different applications within their tech stack. They can start with one, our multi-hub or go all in, but the crafted way in which we approach building products and therefore, the value that our customers see in our full suite is really resonating within the market.

**Brian Peterson**

*Analyst, Raymond James & Associates, Inc.*

Q

Great. That's good to hear. Maybe a quick follow-up for Kate. One of the bullish takeaways for me at the Analyst Day was the net revenue retention above 110%. I believe you indicated it, that would kind of be the new normal going forward. I think I have that right. But I'm curious, how can we frame that in terms of the average revenue per customer trend? I know it's not the same cohort overall. But should we think about that maybe lagging the 110% figure by a couple of points? I'm just curious if there's any read-through from the NRR that we should be looking at in terms of the revenue per customer growth? Thank you.

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yes. Thanks for the question. I think that you are right at Analyst Day, we shared a new target level for net revenue retention at or above 110%. And what we talked about was a couple of different drivers. The first of those drivers was really strong customer dollar retention. That's what we call it internally may refer to it as gross retention. And what we said is about half of the impact on total net revenue retention was associated with improvements on customer dollar retention.



The other piece of that is that our upgrades are improving, and we have a diverse set of upgrade drivers that are helping to increase net revenue retention that sort of second half, those drivers will also help drive ASRPC growth, right? So it's not that retention is driving. It's the same core adoption of a greater portion of the platform that is driving both the net revenue retention and higher ASRPC.

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**Brian Peterson**

*Analyst, Raymond James & Associates, Inc.*

Q

Great. Thank you.

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**Operator:** Your next question comes from the line of Michael Turits with KeyBanc Capital Markets. Your line is open.

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**Michael Turits**

*Analyst, KeyBanc Capital Markets, Inc.*

Q

Hey, guys. Thank you very much. So, two questions, Yamini, for you. Obviously, everyone is very excited about the payments. Can you talk about how you're thinking longer term about e-commerce more broadly? And then, I've [indiscernible] (48:25) for Kate.

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**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

I think like, yes, we are excited about payments, but we're equally excited about the core business, I will say that. In terms of the longer-term payments opportunity, if we really step back, there is just a lot that we can do to help our customers grow.

And the way we are going to focus on this, and we've said this in a couple of different ways, is that, first of all, from a payments perspective, we're going to just embed this in almost every way. Embedded payments, which as the name suggests is embedding it in forms in web pages, in meeting requests and really, that will help us drive adoption. And so from a road map, you will see us drive payment adoption.

I think the second part of what I'm excited about in the road map is building that commerce context into CRM and vice versa. That's where we see significant value that we can deliver to our customers, by making sure that the commerce context is there in every interaction, whether it's marketing or sales or service, and both of those are going to open up a huge opportunity for us, but also it's going to enable growth for our customers.

So that's how we think about the road map and longer-term opportunity in terms of payments. But I'll also point that, as we've talked about, the core business is really strong, and the core business is growing really well, and we're continuing to invest in terms of all of our strategic pillars and focused on driving a world-class CRM platform. So it's kind of balanced across new opportunities, as well as core business.

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**Michael Turits**

*Analyst, KeyBanc Capital Markets, Inc.*

Q

Thanks. And then Kate, you said that for 2022, not to expect a meaningful improvement in margins. Can you just talk about what some of the puts and takes are there? And how they may or may not be shifting in terms of what's the headwind? And what's the tailwind to margins? How that balances out next year?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yeah. I guess, the way that I would think about it is – and we tried to talk a bit about this at the Analyst Day was how we balance growth and profitability.

And overall, if you just sort of at the highest level, think about it, what we have been trying to do and what we continue to try to do is focus on building really durable long-term growth for the company. And we will clearly look for ways on a regular basis to expand margins. And we leverage our long-term financial framework to try to do that.

What we don't want to do is forgo really high conviction, really high return opportunities to drive future growth so that we can deliver very specific leverage targets from one year to the next. And so you heard us talk about at the Analyst Day, you hear Yamini talk about it now. We feel really good about the opportunity in front of us, and we want to make sure that we continue to invest into that opportunity. And so the areas where you're going to see us invest in 2022 are going to be the same areas where you've been seeing us invest over the last couple of years.

In particular, we want to make sure that we are leaning into our R&D organization to drive innovation because we think that's the engine for strong and durable growth. So I don't have specific puts and takes in 2022. What I would tell you is we're going to continue to invest in the places where we have been seeing strong ROI, and we believe that we can continue to see strong ROI and that's primarily in the innovation of the product.

**Michael Turits**

*Analyst, KeyBanc Capital Markets, Inc.*

Q

Thanks, Kate. Thanks, Yamini.

**Operator:** Your next question comes from the line of Michael Turrin with Wells Fargo. Your line is open.

**Michael Berg**

*Analyst, Wells Fargo*

Q

Hi. This is Michael Berg for Michael Turrin. Congrats on a great quarter. I have a quick question and then a follow-up for Dharmesh. In this environment, we're seeing right now, it appears to be a pretty strong or difficult hiring environment. And with HubSpot being such a focus on culture and retention. Can you kind of walk through what you're seeing in the hiring environment? Any trouble getting people on board? Any better or worse retention within your employee base?

**Dharmesh Shah**

*Co-founder, Director & Chief Technology Officer, HubSpot, Inc.*

A

Thanks for your question. So, we're really pleased with the kind of long-term investments we've made in culture and employer brand that has really paid off now in these tough times. So we haven't seen a direct impact of the so-called kind of great resignation, but we know that there's some activity going out there in the world at large. But we continue to have a very strong employer brand. We leaned in even pre-pandemic into this notion of a hybrid and remote workforce, which we're even better at now.

So personally, I feel we're coming from a position of strength even more so than we were before. I think the value of our culture, the value of the flexibility we have in our workforce is appreciated. We've long said that we think of

culture as a second product that we build. And that product, including our main product is actually doing very well. So thanks for the question.

**Operator:** Your next question comes from the line of Parker Lane with Stifel. Your line is open.

**Jeffrey Parker Lane**

*Analyst, Stifel, Nicolaus & Co., Inc.*

Q

Yeah. Hi. Thanks for taking my question. At the Analyst Day, you mentioned about 60% of the business is coming direct versus the remainder coming from solution partners. Wondering if you could break down what the composition of that looks like in the enterprise customer tier, particularly with some of the go-to-market investments you've made there over the past year?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yeah. Parker, thanks a lot for the question. Broadly speaking, that's right. I think – but if you kind of break it down between our segments, partners focus much more on upmarket for all the obvious reasons. More customer – more integration, more CRM implementations, more customization. And so it's weighted a little bit higher towards the upmarket segment.

And look, our strategy has been very, very clear in terms of working with our solution partner ecosystem. If you historically look at the solution partner ecosystem, it's about 4,000 strong. They were marketing agencies, but we have done a lot of investments to diversify that solution partner ecosystem, and we're very pleased with the level of expertise in helping our upmarket customers. It's one of those competitive moats for us. They do a fantastic job of understanding our customers as well as our products. And when partners get engaged, we see high customer dollar retention as well as revenue retention.

And we understand that, we had an event right after INBOUND for partners where we talked about the our strategy and doubling down in our strategy of selling and servicing with them, and we're making pretty hefty investments in enabling partners, matching partners with customers and building expertise within the solution partner base. And so, we're excited to see that ecosystem thrive.

**Operator:** Your next question comes from the line of Rishi Jaluria with RBC Markets. Your line is open.

**Rishi Jaluria**

*Analyst, RBC Capital Markets LLC*

Q

Hi, guys. Thanks so much for taking my question. Just one from my end, I wanted to drill back on to some of the upmarket penetration. Yamini, I think that 81% increase in large deals year-over-year in Q3 really, really impressive and great to see that. Maybe can you help us understand with this upmarket penetration? How you're kind of balancing the investments that you're making there with wanting to keep that same e-commerce-type approach and self-service approach that has worked for you historically?

And maybe directionally, can you give us a sense for with these larger customers, what sort of impact that tends to have on your net dollar retention? Thank you so much.

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Rishi, thanks for the question. I think it really goes back to our strategic pillar, which is strengthening our segmentation approach. So both at the Analyst Day as well as prepared remarks, we talked about the investments we are making to make sure that, every one of our segments are optimized.

We have broadly three segments. You've heard us speak about this, one to 20 segments where we are investing in product-led growth. The 20 to 200 segment, which is our traditional sweet spot from both a product and go-to-market perspective and the up-market segment, which is the 200 to 2,000 segment, where we're making a lot of investments.

And as we've mentioned before, we are being very thoughtful and deliberate in making product as well as go-to-market investments. Our clear view is that both of these need to be in complete lockstep in terms of execution.

So the success that you're seeing within up-market is one because of the product. We have worked on the product extensively. And we've talked about wanting to maintain a consumer-grade look and feel while investing in powerful features and that is beginning to work. And in terms of go-to-market, we have invested in sales enablement, partner enablement as well as brand marketing efforts.

And so, the results of our segmentation strategy, is what is reflected both in terms of customer dollar retention as well as revenue retention. And this is kind of what Kate mentioned earlier in her comments about revenue retention.

.....  
**Operator:** Your next question comes from the line of Ryan MacDonald with Needham & Company. Your line is open.

**Ryan MacDonald**

*Analyst, Needham & Company, LLC*

Q

Hi. Thanks for taking my question. Yamini, in the last, I guess, two questions, you've talked about sort of the upmarket motion here. And I wanted to focus in on the partner channel and how that's driving upmarket deals? And you announced the launch of Operations Hub. It's only been a whole two days since it's officially launched. But just curious, since the announcement at INBOUND, what sort of feedback you've gotten from the partner channel on that offering? And how you think that can continue to maybe unlock the higher end or the upper market segment of your business over time?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Thank you so much, Ryan, for the question. Yes, the Operations Hub Enterprise was just launched this week. And as you all know, we launched Operations Hub Starter as well as Pro earlier this year in April. And that's actually an example of one of the hubs where we co-launched it with partners. Our partner community has been just incredibly involved in terms of the beta program. They were incredibly involved in terms of identifying early use cases.

And we co-launched Operations Hub. In fact, that launch event was probably the highest NPS partner event that we have had all year. And the feedback from partners in terms of Operations Hub has been very, very promising as well as positive. Now the broader point in terms of how we are enabling go-to-market with partners upmarket. As we optimize our product investments as well as go-to-market investments, we've been working hand-in-hand with partners, in driving expertise within the partner ecosystem to enable them to take more complex

implementations and that's beginning to work. And I'm very pleased with how our direct teams as well as the partner teams have been working collaboratively this year.

**Operator:** Your next question comes from the line of Arjun Bhatia with William Blair. Your line is open.

**Arjun Bhatia**

*Analyst, William Blair & Co. LLC*

Q

Yes. Thank you for taking my question. Kate, maybe one for you. It seems like a lot of the trends that we've been talking about with ACV expansion, including multi-hub adoption, upsell, suite adoption. Those don't necessarily seem like temporary trends. So when we look out, maybe beyond Q4, should we think of the model as having structurally shifted where ACV growth can remain in that mid, high single-digit range, not just in Q4, but in 2022 and beyond as well?

**Kate Bueker**

*Chief Financial Officer, HubSpot, Inc.*

A

Yes. Thanks for the question. I think what we have shared, Arjun, is that we feel like the trends that we saw in Q2 and in Q3 are going to continue into Q4. In terms of longer term, these are not metrics that we manage the business against. And you heard Yamini talk about the segmentation strategy where we intend to innovate both at that upmarket, but also with the Velocity segment that is more lower end. And as we innovate at one end or another, you're going to continue to see movement in both of those KPIs. So I think it's fair to say that in the short term. But over the longer term, we're going to continue to see a little bit more volatility.

**Operator:** Your next question comes from the line of Kirk Materne with Evercore. Your line is open.

**Stewart Kirk Materne III**

*Analyst, Evercore ISI*

Q

Hi. Thanks very much. I was wondering if you could just talk about whether any of the trends that you're seeing in the upper part of your business – upper market part of your business are different if you looked at the US versus maybe internationally? I'm just kind of curious if uptake of service cloud, content management, are those products being taken up internationally at the same rate in the US? Or is it similar to what we've seen in other SaaS companies where international tends to follow the US? I know you all are much more balanced. So I was just curious on that. Thanks.

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

Yes, we've been very, very balanced in terms of both international growth as well as North America growth. And as you heard us talk about, international is about 46% of our revenue and consistently growing really well.

In terms of adoption trends, it's quite similar in a lot of international markets. They are still a bit earlier in terms of digital transformation and adoption of the digital products. But overall, for example, Operations Hub has done really well there. And going multi-hub with CMS and marketing has done quite well there. And so the trends are pretty consistent across both of the markets.

**Operator:** Your next question comes from the line of Siti Panigrahi with Mizuho. Your line is open.

**Matt Diamond**

*Analyst, Mizuho Securities*

Q

Hey, guys. This is actually Matt Diamond on Siti's behalf. One quick one, I'm curious about the magnitude of customer engagement that came after the INBOUND conference. If you could compare that to years past, that'd be super helpful?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

That's a good question. Overall, INBOUND, the product announcements, very, very favorable, positive feedback from customers. We had really good engagement both in terms of the breakouts as well as the spotlight sessions, and the NPS for some of the sessions were better than even last year.

So overall, INBOUND landed really well. The engagement of our customers has been really good and the feedback in terms of the announcements there, Operations Hub Enterprise, sandbox business units, the feedback for a lot of those features that we announced at INBOUND has been very, very positive.

It's still early days. It's just been a couple of weeks since INBOUND. And so we'll likely see more momentum in Q4 based on the announcements at INBOUND.

**Operator:** Your next question comes from the line of Robert D (sic) [Terry Tillman] (65:27) with Truist. Your line is open.

**Joseph Meares**

*Analyst, Truist Securities, Inc.*

Q

Hey, guys. This is actually Joe Meares on for Terry Tillman. You talked a lot about the product announcements, I think, on the call, but I'm just wondering from a very high level of the three major announcements that you guys made which have customers made the most noise about in the last three weeks since the Analyst Day?

**Yamini Rangan**

*Chief Executive Officer & Director, HubSpot, Inc.*

A

That's a good question. I think I broadly categorized our product announcements in three areas. The first one is Operations Hub Enterprise that we just launched in November, really positive feedback. We've seen very good momentum, not just for the Enterprise product, but also for the Pro as well as Starter releases earlier this year. So we're seeing consistent good feedback there.

I think the second class is just a lot of the upmarket-related big powerhouse features that we launched, right? So you heard us talk about business units, which, again, is another domino feature within Marketing Hub Enterprise. You heard us talk about sandboxes and forecasting, which is pretty big in terms of sales.

So a lot of customers that have been looking or will need this in the future are excited about that category of features. And then Payments, Payments is early days, but a lot of customers are engaged in conversations in terms of how they can create new revenue streams and – as well as enable consumer-like buying experiences. And so those three, I would say, are probably the big categories of interactions with customers.

**Operator:** There are no further questions at this time, Yamini Rangan. I turn the call back over to you.

## Yamini Rangan

*Chief Executive Officer & Director, HubSpot, Inc.*

Thank you so much. It was great seeing a lot of you at INBOUND, be well and do great work in Q4. We'll see you in the New Year.

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**Operator:** This concludes today's conference call. You may now disconnect.

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